

JEFFERIES GROUP INC /DE/

FORM 10-K (Annual Report)

Filed 02/29/08 for the Period Ending 12/31/07

Address	520 MADISON AVENUE 12TH FLOOR NEW YORK, NY 10022
Telephone	212-284-2550
CIK	0001084580
Symbol	JEF
SIC Code	6211 - Security Brokers, Dealers, and Flotation Companies
Industry	Investment Services
Sector	Technology
Fiscal Year	12/31

Table of Contents

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

Form 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the fiscal year ended December 31, 2007

OR

[] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.

For the transition period from _____ to _____

Commission File Number: 1-14947

JEFFERIES GROUP, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

95-4719745
(I.R.S. Employer
Identification No.)

520 Madison Avenue, 12th Floor
New York, New York
(Address of principal executive offices)

10022
(Zip Code)

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

Securities registered pursuant to Section 12(b) of the Act:

Title of each class:

Name of each exchange on which registered :

Common Stock, \$.0001 par value

New York Stock Exchange

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes [X] No []

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act.

Yes [] No [X]

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No []

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K, or any amendment to this Form 10-K. [X]

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. (Check one):

Large accelerated filer [X] Accelerated filer [] 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 [X]

State the aggregate market value of the voting and non-voting common equity held by non-affiliates computed by reference to the price at

which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter. \$3,038,203,420 as of June 29, 2007.

Indicate the number of shares outstanding of the registrant's class of common stock, as of the latest practicable date. 125,870,368 shares as of the close of business February 5, 2008.

DOCUMENTS INCORPORATED BY REFERENCE

Information from the Registrant's Definitive Proxy Statement with respect to the 2008 Annual Meeting of Stockholders to be held on May 19, 2008 to be filed with the SEC is incorporated by reference into Part III of this Form 10-K.

LOCATION OF EXHIBIT INDEX

The index of exhibits is contained in Part IV herein on page 97.

JEFFERIES GROUP, INC.
2007 FORM 10-K ANNUAL REPORT
TABLE OF CONTENTS

	<u>Page</u>
PART I	
Item 1. Business	1
Item 1A. Risk Factors	9
Item 1B. Unresolved Staff Comments	13
Item 2. Properties	13
Item 3. Legal Proceedings	13
Item 4. Submission of Matters to a Vote of Security Holders	13
PART II	
Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities	14
Item 6. Selected Financial Data	16
Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations	17
Item 7A. Quantitative and Qualitative Disclosures About Market Risk	39
Item 8. Financial Statements and Supplementary Data	43
Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	96
Item 9A. Controls and Procedures	96
Item 9B. Other Information	96
PART III	
Item 10. Directors, Executive Officers and Corporate Governance	96
Item 11. Executive Compensation	96
Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters	96
Item 13. Certain Relationships and Related Transactions, and Director Independence	96
Item 14. Principal Accountant Fees and Services	97
PART IV	
Item 15. Exhibits and Financial Statement Schedules	97
EXHIBIT 2	
EXHIBIT 10.6	
EXHIBIT 10.7	
EXHIBIT 10.12	
EXHIBIT 12.1	
EXHIBIT 21	
EXHIBIT 23	
EXHIBIT 31.1	
EXHIBIT 31.2	
EXHIBIT 32	

Exhibit Index located on page 97 of this report.

PART I

Item 1. Business.

Introduction

Jefferies Group, Inc. and its subsidiaries (“we” or “us”) operate as a full-service global investment bank and institutional securities firm serving dynamic companies and their investors. We offer these companies capital markets, merger and acquisition, restructuring and other financial advisory services, and provide investors fundamental research and trade execution in equity, equity-linked, high yield and investment grade fixed income securities, as well as commodities and derivatives. We also provide asset management services and products to institutions and other investors.

Our principal operating subsidiary, Jefferies & Company, Inc. (“Jefferies”), was founded in 1962. Since 2000, we have pursued a strategy of continuing growth and diversification, whereby we have sought to increase our market share in each of the markets we serve and the products and services we offer, while at the same time expanding the breadth of our activities in an effort to mitigate the cyclical nature of the financial markets in which we operate. Our growth plan has been achieved through internal growth supported by the ongoing addition of experienced personnel in targeted areas, as well as the acquisition from time to time of complementary businesses. More recently, we have increased our global focus on serving companies and investors in Europe, the Middle East, Latin America and Asia.

As of December 31, 2007, we had 2,568 employees. We maintain offices throughout the world and have our executive offices located at 520 Madison Avenue, New York, New York 10022. Our telephone number is (212) 284-2550 and our Internet address is www.jefferies.com.

We make available free of charge on our Internet website the following documents and reports, including amendments (the reports are made available as soon as reasonably practicable after such materials are filed with or furnished to the SEC pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934):

- Code of Ethics;
- Reportable waivers, if any, from our Code of Ethics by our executive officers;
- Board of Directors Corporate Governance Guidelines;
- Charter of the Audit Committee of the Board of Directors;
- Charter of the Corporate Governance and Nominating Committee of the Board of Directors;
- Charter of the Compensation Committee of the Board of Directors;
- Annual reports on Form 10-K;
- Quarterly reports on Form 10-Q;
- Current reports on Form 8-K; and
- Beneficial ownership reports on Forms 3, 4 and 5.

Shareholders may also obtain free of charge a printed copy of any of these documents or reports by sending a request to Investor Relations, Jefferies & Company, Inc., 520 Madison Avenue, 12th Floor, New York, NY 10022, by calling 203-708-5975 or by sending an email to info@jefferies.com.

Table of Contents

Business Segments

We currently operate in two business segments, Capital Markets and Asset Management. The Capital Markets reportable segment includes our securities trading, including the results of our recently reorganized high yield secondary market trading activities, and investment banking activities. The Capital Markets reportable segment is managed as a single operating segment that provides the research, sales, trading and origination effort for various fixed income, equity and advisory products and services. The Capital Markets segment comprises a number of interrelated divisions. The Asset Management segment is primarily comprised of operating activities related to our asset management businesses. Beginning in the second quarter of 2007, our international convertible bond funds are included within the results of the Asset Management segment. Previously, operations from our international convertible bond funds were included in the Capital Markets segment. Prior period disclosures have been adjusted to conform to the current period's presentation. This change was made in order to reflect the manner in which these segments are currently managed.

Financial information regarding our reportable business segments as of December 31, 2007, December 31, 2006, and December 31, 2005 is set forth in note 19 of the Notes to Consolidated Financial Statements, titled "Segment Reporting" and is incorporated herein by reference.

Our Businesses

Capital Markets

Our Capital Markets activity includes our securities execution activities, including sales, trading and research in equity, equity derivatives, convertible, high yield and investment grade fixed income securities, and prime brokerage, and our investment banking activities which include capital markets transactions, mergers and acquisitions and other advisory transactions. In addition, our Capital Markets activities include securities lending and our proprietary trading activities as well as commodity-related trading. We are primarily focused on serving corporations and institutional investors.

Investment Banking

Our Investment Banking Division offers our clients, primarily growing and mid-sized companies, a full range of financial advisory services, as well as debt, equity, and convertible capital raising services.

Underwriting

Equity and Equity-Linked Financing — We offer direct placements, private equity, private placements, initial public offerings, and follow-on offerings of equity and equity-linked convertible securities.

Leveraged Finance — We offer a range of debt financing for growing and middle market companies and sponsors. We focus on structuring and distributing public and private debt in leveraged finance transactions, including leveraged buy-outs, acquisitions, growth capital financings, recapitalizations, and Chapter 11 exit financings. Our joint venture loan finance company, Jefferies Finance LLC, has the ability to commit capital for transactions that range between \$50 million and \$500 million.

Table of Contents

Advisory Services

Mergers & Acquisitions — We advise buyers and sellers on sales, divestitures, acquisitions, mergers, tender offers, joint ventures, strategic alliances and takeover defenses. We can facilitate and finance acquisitions and recapitalizations on both buy-side and sell-side mandates. Our service to our clients includes leveraging our industry knowledge, extensive relationships, and capital markets and restructuring expertise.

Restructuring & Recapitalization — We offer advisory services in connection with exchange offers, consent solicitations, capital raising, recapitalization, restructuring and distressed M&A activity. We provide advice and support in the structuring, valuation and placement of securities issued in recapitalizations and restructurings. We represent issuers, bondholders and creditors, as well as buyers and sellers of assets.

Fund Placement — Helix Associates, our fund placement group, is a placement agent serving private equity fund sponsors and sophisticated investors throughout North America, Europe, the Middle East, Japan and Australia.

Our 539 investment banking professionals operate throughout the United States, Europe and Asia, and are organized into industry, product and geographic coverage groups. Industry coverage groups include Jefferies Quarterdeck for Aerospace and Defense, CleanTech, Jefferies Randall & Dewey for Energy, Gaming and Leisure, Healthcare, Industrial, Private Equity and Venture Capital Sponsors, Retail & Consumer, Jefferies Broadview for Technology, Oil Service & Infrastructure, Media and Communications and Putnam Lovell Investment Banking Business for Financial Services. The division has experienced substantial growth over the last six years both organically and through acquisitions.

Equities

Our Equities Division consists of equity research, sales and trading, electronic execution services, equity derivatives, securities lending and prime brokerage.

Equity Sales and Trading

Our equity research, sales and trading unit is one of the primary foundations of our platform. We have an over forty-year history in equity trading. Our equity sales representatives connect a network of institutional investors around the globe and provide execution with a focus on minimal market impact. We provide listed block trades, NASDAQ market making, bulletin board trading, capital markets/origination, risk arbitrage, statistical arbitrage, special situations, pair trades, relative value, and portfolio and electronic trading, as well as trading in American Depository Receipts (“ADR”) and Ordinary Shares. Our clients include domestic and international investors such as investment advisors, banks, mutual funds, insurance companies, hedge funds, and pension and profit sharing plans. We have a small, but growing Private Client Services group that focuses on serving smaller institutions, family offices and high net worth individuals.

Execution

Through our Jefferies Execution subsidiary, we provide agency-only execution services for stocks and options listed on the NYSE, AMEX, and all other major exchanges, as well as OTC. In 2007, the firm traded over 33 billion shares utilizing its execution platform which includes floor brokerage, electronic connectivity, direct access and listed options trading. In addition, we offer quantitative and algorithmic trading solutions as well as access to liquidity in order to access the global markets. We leverage our portfolio management systems, analysis and benchmark auto-trading strategies to deliver our execution services to our institutional customers.

Equity Research

Encompassed within equity sales and trading is research and research sales. We provide long- and short-term investment ideas. Our analysts use a variety of quantitative and qualitative tools, integrating field analysis, proprietary channel checks and ongoing dialogue with the managements of the companies they cover.

Equity Derivatives

We offer equity derivatives for investors seeking to manage risk and optimize returns within the equities market. Our professionals have expertise in listed and over-the-counter transactions and products. We focus on serving the diverse needs of our institutional, corporate and private client base across multiple product lines, offering listed options, ETFs and OTC options and swaps.

Securities Lending

In connection with both trading and brokerage activities, we borrow securities to cover short sales and to complete transactions in which customers have failed to deliver securities by the required settlement date, and lend securities to other brokers and dealers for similar purposes. We have an active securities borrowed and lending matched book business in which we borrow securities from one party and lend them to another party. When we borrow securities, we generally provide cash to the lender as collateral, which is reflected in our Consolidated Statements of Financial Condition as securities borrowed. We earn interest revenues on this cash collateral. Similarly, when we lend securities to another party, that party provides cash to us as collateral, which is reflected in our Consolidated Statements of Financial Condition as securities loaned. We pay interest expense on the cash collateral received from the party borrowing the securities. A substantial portion of our interest revenues and interest expenses results from this matched book activity. The initial collateral advanced or received approximates or is greater than, the fair value of the securities borrowed or loaned. We monitor the fair value of the securities borrowed and loaned on a daily basis and request additional collateral or return excess collateral, as appropriate. In 2007 and 2006, we expanded our securities lending focus internationally, with additional professionals in London and New York. In addition to our securities lending activities, we are a participant in the U.S. and international repurchase agreement (“repo”) markets, providing secured financing for our clients in those regions.

Prime Brokerage

We offer prime brokerage services to hedge funds, money managers, and registered investment advisors.

Fixed Income and Commodities

Our Fixed Income and Commodities activities consist of our high yield secondary market activities, convertibles department, investment grade fixed income department, research and our commodity trading group.

High Yield Secondary Market Activities

In January 2000, we created three broker-dealer entities that employed a trading and investment strategy substantially similar to that historically employed by our High Yield division. Two of these entities, the Jefferies Partners Opportunity Fund and the Jefferies Partners Opportunity Fund II, were principally capitalized with equity contributions from institutional and high net worth investors. The third fund, Jefferies Employees Opportunity Fund (and collectively with the two Jefferies Partners Opportunity Funds, referred to as the “High Yield Funds”), was principally capitalized with equity investments from our employees and was therefore consolidated into our Consolidated Financial Statements. The High Yield division and each of the funds shared gains or losses on trading and investment activities of the High Yield division on the basis of a pre-established sharing arrangement related to the amount of capital each had committed.

On April 2, 2007, we reorganized Jefferies High Yield Trading, LLC (“JHYT”) to conduct the secondary market trading activities previously performed by the High Yield division of Jefferies and the High Yield Funds. The activities of JHYT are overseen by Richard Handler, our Chief Executive Officer, and the same long-standing team previously responsible for these trading activities. JHYT is a registered broker-dealer engaged in the secondary sales and trading of high yield securities and special situation securities, including bank debt, post-reorganization equity, public and private equity, equity derivatives, credit default swaps and other financial instruments. JHYT makes markets in high yield and distressed securities and provides research coverage on these types of securities. JHYT is a wholly-owned subsidiary of Jefferies High Yield Holdings, LLC (“JHYH”).

Table of Contents

We and Leucadia National Corporation (“Leucadia”) expect to increase our respective investments in JHYH to \$600 million each over time. We and Leucadia each have the right to nominate two of a total of four directors to JHYH’s board of directors, and each respectively own 50% of the voting securities of JHYH. JHYH provides the opportunity for additional capital investments over time from third party investors through two funds managed by us, Jefferies Special Opportunities Fund (“JSOP”) and Jefferies Employees Special Opportunities Fund (“JESOP”). The term of the arrangement is for six years, with an option to extend.

Convertibles

Our personnel in the U.S., London, Tokyo, and Zurich serve the geographically diverse global convertible markets. We offer sales, trading and analysis of U.S. domestic and international convertible bonds, convertible preferred shares, closed-end funds, warrants and structured products.

Investment Grade Fixed Income

We provide fixed income transaction execution for institutions acting as principal through a combination of sales and trading coverage, and a technology trading platform. The division trades corporate bonds, U.S. Treasury securities, U.S. government agency securities, mortgage-backed securities, municipal bonds and emerging markets debt.

Fixed Income Research

We have expanded our research platform over the last few years and provide long- and short-term investment ideas. Our analysts use a variety of quantitative and qualitative tools, integrating field analysis, proprietary channel checks and ongoing dialogue with the managements of the companies they cover.

Commodities

Our commodities group, Jefferies Financial Products, LLC (“JFP”), offers swaps, options and other derivatives typically linked to various commodity indexes and is a significant provider of liquidity in exchange-traded commodity index contracts. JFP provides financial products and commodity index knowledge to pension funds, mutual funds, sovereigns, foundations, endowments and other institutional investors seeking exposure to commodities as an asset class. In 2005, JFP worked with Reuters to modify the benchmark CRB Index, now renamed the Reuters Jefferies CRB Index. In addition, JFP offers proprietary commodity indexes, such as the Jefferies Commodity Performance Index, which are designed to outperform standard benchmark indexes.

Asset Management

We provide investment management services to various private investment funds. In the United States, investment management services are provided through Jefferies Asset Management, LLC (“JAM”) and Jefferies Capital Management, Inc. (“JCM”). Each of JAM and JCM is registered as an investment adviser with the SEC. Our private fund products consist of long-short equity and fixed income funds, including CLO’s, that focus on specific strategies. These funds are not registered under federal or state securities laws, are made available only to certain sophisticated investors and are not offered or sold to the general public.

Our Asset Management business is primarily comprised of operating activities related to our private investment funds.

In Europe, we offer investment solutions for long-only strategies in global convertible bonds to pension funds, insurance companies and private banking clients in Switzerland, France and Germany.

Table of Contents

Our Sources of Revenues

Commissions

A substantial portion of our revenues is derived from customer commissions and commission equivalents. We charge fees for assisting our domestic and international clients with purchasing and selling equity, debt and convertible securities as well as ADRs, options, preferred stocks, financial futures and other similar products.

Principal Transactions

In the regular course of our business, we take securities positions as a market maker to facilitate customer transactions and for proprietary risk trading. Trading profits or losses and changes in market prices of our proprietary positions are also recorded as principal transactions revenues.

Investment Banking

Investment banking revenues are generated by fees from capital markets activities which include debt, equity, and convertible underwriting and placement services, and fees from financial advisory activities including M&A and restructuring services.

Interest

We derive a substantial portion of our interest revenues in connection with our securities borrowed / securities lending and repo activity. We also earn interest on our securities portfolio, on our operating and segregated balances, on our margin lending activity and on certain of our investments, including our investment in short-term bond funds.

Competition

As a global investment bank and securities firm, all aspects of our business are intensely competitive. We compete directly with numerous domestic and international competitors, including firms included on the AMEX Securities Broker/Dealer Index and with other brokers and dealers, investment banking firms, investment advisors, mutual funds, hedge funds and commercial banks. Many of our competitors have substantially greater capital and resources than we do and offer a broader range of financial products. In addition to competition from firms currently in the securities business, there has been increasing competition from others offering financial services. These developments and others have resulted, and may continue to result, in significant additional competition for us. We believe that the principal factors affecting competition involve market focus, reputation, the abilities of professional personnel, the relative price of the service and products being offered and the quality of service.

Regulation

The securities industry in the United States is subject to extensive regulation under both federal and state laws. The Securities and Exchange Commission is the federal agency responsible for the administration of federal securities laws. In addition, self-regulatory organizations, principally Financial Industry Regulatory Authority ("FINRA"), are actively involved in the regulation of broker-dealers. These self-regulatory organizations conduct periodic examinations of member broker-dealers in accordance with rules they have adopted and amended from time to time, subject to approval by the SEC. Securities firms are also subject to regulation by foreign regulatory bodies, state securities commissions and state attorneys general in those jurisdictions and states in which they do business.

Table of Contents

Broker-dealers are subject to regulations which cover all aspects of the securities business, including sales methods, trade practices among broker-dealers, use and safekeeping of customers' funds and securities, capital structure of securities firms, anti-money laundering, record-keeping and the conduct of directors, officers and employees. Additional legislation, changes in rules promulgated by the SEC and self-regulatory organizations, or changes in the interpretation or enforcement of existing laws and rules, may directly affect the mode of operation and profitability of broker-dealers. Broker-dealers that engage in commodities and futures transactions are also subject to regulation by the Commodity Futures Trading Commission ("CFTC") and the National Futures Association ("NFA"). The SEC, self-regulatory organizations, state securities commissions, state attorneys general, the CFTC and the NFA may conduct administrative proceedings which can result in censure, fine, suspension, expulsion of a broker-dealer, its officers or employees, or revocation of broker-dealer licenses. The principal purpose of regulation and discipline of broker-dealers is the protection of customers and the securities markets, rather than protection of creditors and stockholders of broker-dealers.

As registered broker-dealers, Jefferies, JHYT and Jefferies Execution are required by law to belong to the Securities Investor Protection Corporation ("SIPC"). In the event of a member's insolvency, the SIPC fund provides protection for customer accounts up to \$500,000 per customer, with a limitation of \$100,000 on claims for cash balances. We carry an excess policy that provides additional protection for securities of up to \$24.5 million per customer with an aggregate limit of \$100 million.

Net Capital Requirements. U.S. registered broker-dealers doing business with the public are subject to the SEC's Uniform Net Capital Rule (the "Rule"), which specifies minimum net capital requirements. Jefferies Group is not a registered broker-dealer and is therefore not subject to the Rule; however, its United States broker-dealer subsidiaries are registered and are subject to the Rule.

The Rule provides that a broker-dealer doing business with the public shall not permit its aggregate indebtedness to exceed 15 times its adjusted net capital (the "basic method") or, alternatively, that it not permit its adjusted net capital to be less than the greater of 2% of its aggregate debit balances (primarily receivables from customers and broker-dealers) or \$250,000 computed in accordance with such Rule (the "alternative method"). Jefferies, Jefferies Execution and JHYT use the alternative method of calculation.

Compliance with applicable net capital rules could limit operations of Jefferies, such as underwriting and trading activities, that require the use of significant amounts of capital, and may also restrict loans, advances, dividends and other payments by Jefferies, Jefferies Execution, or JHYT to us.

As of December 31, 2007, Jefferies, Jefferies Execution and JHYT's net capital and excess net capital were as follows (in thousands of dollars):

	Net Capital	Excess Net Capital
Jefferies	\$505,080	\$483,108
Jefferies Execution	\$ 30,297	\$ 30,047
JHYT	\$558,087	\$557,837

NYSE Regulations. Our common stock is listed on the New York Stock Exchange ("NYSE"). As a listed company, we are required to comply with the NYSE's rules and regulations, including rules pertaining to corporate governance matters. As required by the NYSE on an annual basis, in 2007 our Chief Executive Officer, Richard Handler, certified to the NYSE that he was not aware of any violation by us of the NYSE's corporate governance listing standards.

Regulation Outside the United States. We are an active participant in the international fixed income and equity markets and also provide investment banking services outside of the United States. Many of our principal subsidiaries that participate in these markets and provide these services are subject to comprehensive regulations in the United States and elsewhere that include some form of capital adequacy rules, other customer protection rules and compliance with other applicable regulations. We provide investment services in and from the United Kingdom under the regulation of the Financial Services Authority ("FSA").

Business Risks

As a global investment bank and securities firm, risk is an inherent part of our businesses. Capital markets, by their nature, are prone to uncertainty and subject participants to a variety of risks. We have developed policies and procedures designed to identify, measure and monitor each of the risks involved in our trading, brokerage and investment banking activities on a global basis. Our principal risks are market, credit, operational, legal and compliance, new business risks. Risk management is considered to be of paramount importance to our day-to-day operations. Consequently, we devote significant resources (including investments in personnel and technology) to the measurement, analysis and management of risk.

We seek to reduce risk through the diversification of our businesses, counterparties and activities. We accomplish this objective by monitoring the usage of capital to each of our businesses, establishing trading limits and setting credit limits for individual counterparties. We seek to achieve adequate returns from each of our businesses commensurate with the risks assumed. Nonetheless, the effectiveness of our policies and procedures for managing risk exposure can never be completely or accurately predicted or fully assured. For example, unexpectedly large or rapid movements or disruptions in one or more markets or other unforeseen developments can have an adverse effect on our results of operations and financial condition. The consequences of these developments can include losses due to adverse changes in inventory values, decreases in the liquidity of trading positions, higher volatility in our earnings, increases in our credit exposure to customers and counterparties and increases in general systemic risk. If any of our strategies used to hedge or otherwise mitigate exposures to the various types of risks described above are not effective, we could incur losses. Additionally, business continuity plans have been developed and are periodically tested for critical processes and systems, and controls have been implemented to provide oversight of the activities.

Margin Risk

Customers' transactions are executed on either a cash or margin basis. In a margin transaction, we extend credit to the customer, collateralized by securities and cash in the customer's account, for a portion of the purchase price, and receive income from interest charged on such extensions of credit. In permitting a customer to purchase securities on margin, we are subject to the risk that a market decline could reduce the value of its collateral below the amount of the customer's indebtedness and that the customer might otherwise be unable to repay the indebtedness.

In addition to monitoring the creditworthiness of our customers, we also consider the trading liquidity and volatility of the securities we accept as collateral for margin loans. Trading liquidity and volatility may be dependent, in part, upon the market in which the security is traded, the number of outstanding shares of the issuer, events affecting the issuer and/or securities markets in general, and whether or not there are any legal restrictions on the sale of the securities. Certain types of securities have historical trading patterns, which may assist us in making this evaluation. Historical trading patterns, however, may not be good indicators over relatively short time periods or in markets which are affected by unusual or unexpected developments. We consider all of these factors at the time we agree to extend credit to customers and continue to review extensions of credit on an ongoing basis.

The majority of our margin loans are made to United States citizens or to corporations which are domiciled in the United States. We may extend credit to investors or corporations who are citizens of foreign countries or who may reside outside the United States. We believe that should such foreign investors default upon their loans and should the collateral for those loans be insufficient to satisfy the investors' obligations, it may be more difficult to collect such investors' outstanding indebtedness than would be the case if investors were citizens or residents of the United States.

Although we attempt to minimize the risk associated with the extension of credit in margin accounts, there is no assurance that the assumptions on which we base our decisions will be correct or that we are in a position to predict factors or events which will have an adverse impact on any individual customer or issuer, or the securities markets in general.

Underwriting Risk

Investment banking activity involves both economic and regulatory risks. An underwriter may incur losses if it is unable to sell the securities it is committed to purchase or if it is forced to liquidate its commitments at less than the agreed upon purchase price. In addition, under the federal securities laws and other laws and court decisions with respect to underwriters' liability and limitations on indemnification of underwriters by issuers, an underwriter is subject to substantial potential liability for material misstatements or omissions in prospectuses and other communications with respect to underwritten offerings. Further, underwriting commitments constitute a charge against net capital and our underwriting commitments may be limited by the requirement that our broker-dealers must, at all times, be in compliance with the Uniform Net Capital Rule 15c3-1 of the Securities Exchange Act of 1934. We intend to continue to pursue opportunities for our corporate customers, which may require us to finance and/or underwrite the issuance of securities. Under circumstances where we are required to act as an underwriter or to take a position in the securities of our customers, we may assume greater risk than would normally be assumed in our normal trading activity.

Item 1A. Risk Factors.

Factors Affecting Our Business

The following factors describe some of the assumptions, risks, uncertainties and other factors that could adversely affect our business or that could otherwise result in changes that differ materially from our expectations. In addition to the factors mentioned in this report, we may also be affected by changes in general economic and business conditions, acts of war, terrorism and natural disasters.

Changing conditions in financial markets and the economy could result in decreased revenues.

Our net revenues are directly related to the number and size of the transactions in which we participate and therefore were adversely affected in the second half of 2007 by the equity and credit market turmoil, and may be further impacted by continued or further credit market dislocations or sustained market downturns. As an investment banking and securities firm, changes in the financial markets or economic conditions in the United States and elsewhere in the world could adversely affect our business in many ways, including the following:

- A market downturn could lead to a decline in the volume of transactions executed for customers and, therefore, to a decline in the revenues we receive from commissions and spreads.
- Unfavorable financial or economic conditions could likely reduce the number and size of transactions in which we provide underwriting, financial advisory and other services. Our investment banking revenues, in the form of financial advisory and underwriting or placement fees, are directly related to the number and size of the transactions in which we participate and could therefore be adversely affected by unfavorable financial or economic conditions.
- Adverse changes in the market could lead to a reduction in revenues from principal transactions and commissions.
- Adverse changes in the market could also lead to a reduction in revenues from asset management fees and investment income from managed funds and losses from managed funds. Continued increases in our asset management business, especially increases in the amount of our investments in managed funds, would make us more susceptible to adverse changes in the market. Even in the absence of a market downturn, below-market investment performance by our funds and portfolio managers could reduce asset management revenues and assets under management and result in reputational damage that might make it more difficult to attract new investors.
- Increases in interest rates or credit spreads, as well as limitations on the availability of credit, such as occurred in the second half of 2007, can affect our ability to borrow on a secured or unsecured basis, which may adversely affect our liquidity and results of operations.

Our principal trading and investments expose us to risk of loss.

A considerable portion of our revenues is derived from trading in which we act as principal. Although a significant portion of our principal trading is “riskless principal” in nature, we may incur trading losses relating to the purchase, sale or short sale of high yield, international, convertible, and equity securities and futures and commodities for our own account and from other program or principal trading. Additionally, we have made substantial investments of our capital in debt securities, equity securities and commodities, including investments managed by us and investments managed by third parties. In any period, we may experience losses as a result of price declines, lack of trading volume, and illiquidity. From time to time, we may engage in a large block trade in a single security or maintain large position concentrations in a single security, securities of a single issuer, or securities of issuers engaged in a specific industry. In general, because our inventory is marked to market on a daily basis, any downward price movement in these securities could result in a reduction of our revenues and profits. In addition, we may engage in hedging transactions that if not successful, could result in losses.

Increased competition may adversely affect our revenues and profitability.

All aspects of our business are intensely competitive. We compete directly with numerous other brokers and dealers, investment banking firms and banks. In addition to competition from firms currently in the securities business, there has been increasing competition from others offering financial services, including automated trading and other services based on technological innovations. We believe that the principal factors affecting competition involve market focus, reputation, the abilities of professional personnel, the ability to execute the transaction, relative price of the service and products being offered and the quality of service. Increased competition or an adverse change in our competitive position could lead to a reduction of business and therefore a reduction of revenues and profits. Competition also extends to the hiring and retention of highly skilled employees. A competitor may be successful in hiring away an employee or group of employees, which may result in our losing business formerly serviced by such employee or employees. Competition can also raise our costs of hiring and retaining the key employees we need to effectively execute our business plan.

Operational risks may disrupt our business, result in regulatory action against us or limit our growth.

Our businesses are highly dependent on our ability to process, on a daily basis, a large number of transactions across numerous and diverse markets in many currencies, and the transactions we process have become increasingly complex. If any of our financial, accounting or other data processing systems do not operate properly or are disabled or if there are other shortcomings or failures in our internal processes, people or systems, we could suffer an impairment to our liquidity, financial loss, a disruption of our businesses, liability to clients, regulatory intervention or reputational damage. These systems may fail to operate properly or become disabled as a result of events that are wholly or partially beyond our control, including a disruption of electrical or communications services or our inability to occupy one or more of our buildings. The inability of our systems to accommodate an increasing volume of transactions could also constrain our ability to expand our businesses.

We also face the risk of operational failure or termination of any of the clearing agents, exchanges, clearing houses or other financial intermediaries we use to facilitate our securities transactions. Any such failure or termination could adversely affect our ability to effect transactions and manage our exposure to risk.

In addition, despite the contingency plans we have in place, our ability to conduct business may be adversely impacted by a disruption in the infrastructure that supports our businesses and the communities in which they are located. This may include a disruption involving electrical, communications, transportation or other services used by us or third parties with which we conduct business.

Table of Contents

Our operations rely on the secure processing, storage and transmission of confidential and other information in our computer systems and networks. Although we take protective measures and endeavor to modify them as circumstances warrant, our computer systems, software and networks may be vulnerable to unauthorized access, computer viruses or other malicious code, and other events that could have a security impact. If one or more of such events occur, this potentially could jeopardize our or our clients' or counterparties' confidential and other information processed and stored in, and transmitted through, our computer systems and networks, or otherwise cause interruptions or malfunctions in our, our clients', our counterparties' or third parties' operations. We may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures, and we may be subject to litigation and financial losses that are either not insured against or not fully covered through any insurance maintained by us.

Asset management revenue is subject to variability based on market and economic factors and the amount of assets under management.

Asset management revenue includes revenues we receive from management, administrative and performance fees from funds managed by us, revenues from asset management and performance fees we receive from third-party managed funds, and investment income from our investments in these funds. These revenues are dependent upon the amount of assets under management and the performance of the funds. If these funds do not perform as well as our asset management clients expect, our clients may withdraw their assets from these funds, which would reduce our revenues. Some of our revenues are derived from our own investments in these funds. We experience significant fluctuations in our quarterly operating results due to the nature of our asset management business and therefore may fail to meet revenue expectations. Even in the absence of a market downturn, below-market investment performance by our funds and portfolio managers could reduce asset management revenues and assets under management and result in reputational damage that might make it more difficult to attract new investors.

We face numerous risks and uncertainties as we expand our business.

We expect the growth of our business to come primarily from internal expansion and through acquisitions and strategic partnering. As we expand our business, there can be no assurance that our financial controls, the level and knowledge of our personnel, our operational abilities, our legal and compliance controls and our other corporate support systems will be adequate to manage our business and our growth. The ineffectiveness of any of these controls or systems could adversely affect our business and prospects. In addition, as we acquire new businesses, we face numerous risks and uncertainties integrating their controls and systems into ours, including financial controls, accounting and data processing systems, management controls and other operations. A failure to integrate these systems and controls, and even an inefficient integration of these systems and controls, could adversely affect our business and prospects.

Our business depends on our ability to maintain adequate levels of personnel.

We have made substantial increases in personnel. If a significant number of our key personnel leave, or if our business volume increases significantly over current volume, we could be compelled to hire additional personnel. At that time, there could be a shortage of qualified and, in some cases, licensed personnel whom we could hire. This could hinder our ability to expand or cause a backlog in our ability to conduct our business, including the handling of investment banking transactions and the processing of brokerage orders, all of which could harm our business, financial condition and operating results.

Table of Contents

Extensive regulation of our business limits our activities, and, if we violate these regulations, we may be subject to significant penalties.

The securities industry in the United States is subject to extensive regulation under both federal and state laws. The SEC is the federal agency responsible for the administration of federal securities laws. In addition, self-regulatory organizations, principally FINRA and the securities exchanges, are actively involved in the regulation of broker-dealers. Securities firms are also subject to regulation by regulatory bodies, state securities commissions and state attorneys general in those foreign jurisdictions and states in which they do business. Broker-dealers are subject to regulations which cover all aspects of the securities business, including sales methods, trade practices among broker-dealers, use and safekeeping of customers' funds and securities, capital structure of securities firms, anti-money laundering, record-keeping and the conduct of directors, officers and employees. Broker-dealers that engage in commodities and futures transactions are also subject to regulation by the CFTC and the NFA. The SEC, self-regulatory organizations, state securities commissions, state attorneys general, the CFTC and the NFA may conduct administrative proceedings which can result in censure, fine, suspension, expulsion of a broker-dealer or its officers or employees, or revocation of broker-dealer licenses. Additional legislation, changes in rules or changes in the interpretation or enforcement of existing laws and rules, may directly affect our mode of operation and our profitability. Continued efforts by market regulators to increase transparency and reduce the transaction costs for investors, such as decimalization and FINRA's Trade Reporting and Compliance Engine, or TRACE, has affected and could continue to affect our trading revenue.

Our business is substantially dependent on our Chief Executive Officer.

Our future success depends to a significant degree on the skills, experience and efforts of Richard Handler, our Chief Executive Officer. We do not have an employment agreement with Mr. Handler which provides for his continued employment. The loss of his services could compromise our ability to effectively operate our business. In addition, in the event that Mr. Handler ceases to actively manage the high yield fund, investors would have the right to withdraw from the fund. Although we have substantial key man life insurance covering Mr. Handler, the proceeds from the policy may not be sufficient to offset any loss in business.

Legal liability may harm our business.

Many aspects of our business involve substantial risks of liability, and in the normal course of business, we have been named as a defendant or co-defendant in lawsuits involving primarily claims for damages. The risks associated with potential legal liabilities often may be difficult to assess or quantify and their existence and magnitude often remain unknown for substantial periods of time. Private Client Services involves an aspect of the business that has historically had more risk of litigation than our institutional business. Additionally, the expansion of our business, including increases in the number and size of investment banking transactions and our expansion into new areas, imposes greater risks of liability. In addition, unauthorized or illegal acts of our employees could result in substantial liability to us. Substantial legal liability could have a material adverse financial effect or cause us significant reputational harm, which in turn could seriously harm our business and our prospects.

Our business is subject to significant credit risk.

In the normal course of our businesses, we are involved in the execution, settlement and financing of various customer and principal securities and derivative transactions. These activities are transacted on a cash, margin or delivery-versus-payment basis and are subject to the risk of counterparty or customer nonperformance. Although transactions are generally collateralized by the underlying security or other securities, we still face the risks associated with changes in the market value of the collateral through settlement date or during the time when margin is extended. We may also incur credit risk in our derivative transactions to the extent such transactions result in uncollateralized credit exposure to our counterparties.

Table of Contents

We seek to control the risk associated with these transactions by establishing and monitoring credit limits and by monitoring collateral and transaction levels daily. We may require counterparties to deposit additional collateral or return collateral pledged. In the case of aged securities failed to receive, we may, under industry regulations, purchase the underlying securities in the market and seek reimbursement for any losses from the counterparty.

Derivative transactions may expose us to unexpected risk and potential losses.

We are party to a large number of derivative transactions that require us to deliver to the counterparty the underlying security, loan or other obligation in order to receive payment. In a number of cases, we do not hold the underlying security, loan or other obligation and may have difficulty obtaining, or be unable to obtain, the underlying security, loan or other obligation through the physical settlement of other transactions. As a result, we are subject to the risk that we may not be able to obtain the security, loan or other obligation within the required contractual time frame for delivery, particularly if default rates increase as we have seen for the second half of 2007 and through the beginning of 2008. This could cause us to forfeit the payments due to us under these contracts or result in settlement delays with the attendant credit and operational risk as well as increased costs to the firm.

Item 1B. Unresolved Staff Comments.

None.

Item 2. Properties.

Our executive offices and principal administrative offices are located at 520 Madison Avenue, New York, New York under an operating lease arrangement. We maintain offices throughout the world including New York, Stamford, Jersey City, London, Los Angeles, and Zurich. In addition, we maintain back-up facilities with redundant technologies in Dallas. We lease all of our office space which management believes is adequate for our business. For information concerning leasehold improvements and rental expense, see notes 1, 6 and 14 of the Notes to Consolidated Financial Statements.

Item 3. Legal Proceedings.

Many aspects of our business involve substantial risks of legal liability. In the normal course of business, we have been named as defendants or co-defendants in lawsuits involving primarily claims for damages. We are also involved in a number of judicial and regulatory matters arising out of the conduct of our business. Our management, based on currently available information, does not believe that any matter will have a material adverse effect on our financial condition, although, depending on our results for a particular period, an adverse determination could be material for a particular period.

Item 4. Submission of Matters to a Vote of Security Holders.

None.

PART II

Item 5. Market for Registrant’s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.

Our common stock trades on the NYSE under the symbol JEF. On April 18, 2006, we declared a 2-for-1 split of all outstanding shares of our common stock, payable May 15, 2006 to stockholders of record as of April 28, 2006. The stock split was effected as a stock dividend of one share for each one share outstanding on the record date. All prior period share, share price and per share information has been restated to retroactively reflect the effect of the 2-for-1 stock split.

The following table sets forth for the periods indicated the range of high and low sales prices per share of our common stock as reported by the NYSE, adjusted for the 2-for-1 stock split as appropriate.

	<u>High</u>	<u>Low</u>
2007		
Fourth Quarter	\$29.67	\$22.15
Third Quarter	30.98	22.40
Second Quarter	33.80	25.92
First Quarter	30.42	23.90
2006		
Fourth Quarter	\$31.76	\$26.41
Third Quarter	30.50	21.45
Second Quarter	34.80	24.73
First Quarter	29.58	22.38

There were approximately 900 holders of record of our common stock at February 7, 2008.

In 1988, we instituted a policy of paying regular quarterly cash dividends. The only restrictions on our present ability to pay dividends on our common stock are the dividend preference terms of our Series A convertible preferred stock and the governing provisions of the Delaware General Corporation Law.

In the second quarter of 2006, we announced a 67% increase in our quarterly dividend to \$0.125 per share.

Dividends per share of common stock (declared and paid):

	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
2007	\$0.125	\$0.125	\$0.125	\$0.125
2006	\$0.075	\$0.125	\$0.125	\$0.125

Table of Contents

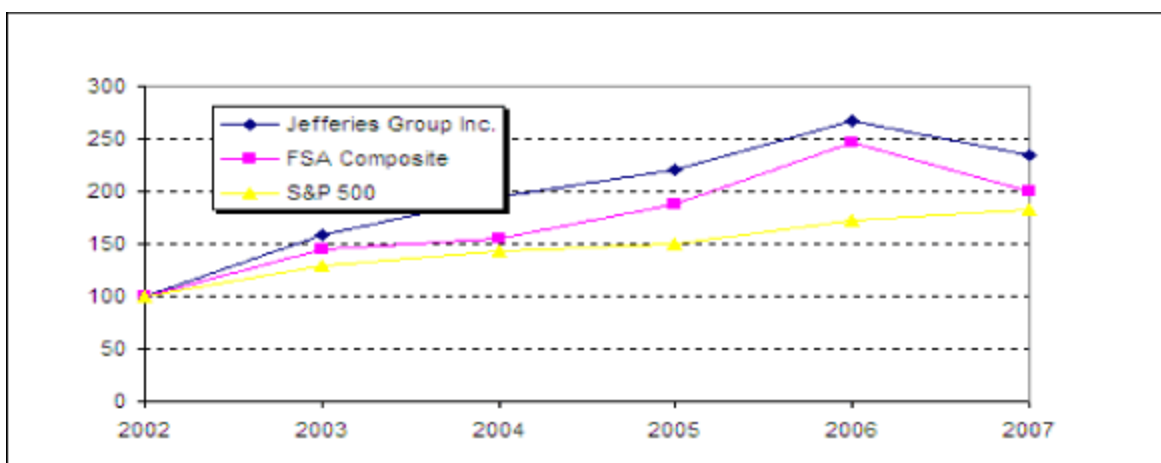
Issuer Purchases of Equity Securities

Period	(a) Total Number of Shares Purchased (1)	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs (2)(3)	(d) Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
October 1 - October 31, 2007	1,753,435	24.90	1,704,700	2,752,578
November 1 - November 30, 2007	1,739,490	23.56	1,671,200	1,081,378
December 1 - December 31, 2007	58,419	24.01	—	1,081,378
Total	3,551,344	24.23	3,375,900	

- (1) We repurchased an aggregate of 175,444 shares other than as part of a publicly announced plan or program. We repurchased these securities in connection with our stock compensation plans which allow participants to use shares to pay the exercise price of options exercised and to use shares to satisfy tax liabilities arising from the exercise of options or the vesting of restricted stock. The number above does not include unvested shares forfeited back to us pursuant to the terms of our stock compensation plans.
- (2) On July 26, 2005, we issued a press release announcing the authorization by our Board of Directors to repurchase, from time to time, up to an aggregate of 3,000,000 shares of our common stock. After giving effect to the 2-for-1 stock split effected as a stock dividend on May 15, 2006, this authorization increased to 6,000,000 shares.
- (3) On January 23, 2008, we issued a press release announcing the authorization by our Board of Directors to repurchase, from time to time, up to an additional 15,000,000 shares of our common stock

Shareholder Return Performance Presentation

Set forth below is a line graph comparing the yearly change in the cumulative total shareholder return on our common stock, after consideration of all relevant stock splits during the period, against the cumulative total return of the Financial Service Analytics Brokerage (“FSA Composite”) and Standard & Poor’s 500 Indices for the period of five fiscal years, commencing January 1, 2003 (based on prices at December 31, 2002), and ending December 31, 2007 (normalized so that the value of our common stock and each index was \$100 on December 31, 2002).



	2002	2003	2004	2005	2006	2007
Jefferies Group Inc.	100	159	195	221	268	235
FSA Composite	100	144	156	188	247	200
S&P 500	100	129	143	150	173	183

Table of Contents

Item 6. Selected Financial Data.

The selected data presented below as of and for each of the years in the five-year period ended December 31, 2007, are derived from the Consolidated Financial Statements of Jefferies Group, Inc. and its subsidiaries. The data should be read in connection with the Consolidated Financial Statements including the related notes contained on pages 43 through 95. On July 14, 2003, we declared a 2-for-1 split of all outstanding shares of common stock, payable August 15, 2003 to stockholders of record as of July 31, 2003. On April 18, 2006, we declared a 2-for-1 split of all outstanding shares of common stock, payable May 15, 2006 to stockholders of record as of April 28, 2006. The stock splits were effected as a stock dividend of one share for each one share outstanding on the record date. All share, share price and per share information has been restated to retroactively reflect the effect of the two-for-one stock splits. Certain reclassifications have been made to the prior period amounts to conform to the current period's presentation.

	Year Ended December 31,				
	2007	2006	2005	2004	2003
	(In Thousands, Except Per Share Amounts)				
Earnings Statement Data					
Revenues:					
Commissions	\$ 355,601	\$ 280,681	\$ 246,943	\$ 258,838	\$ 250,191
Principal transactions	390,374	468,002	349,489	358,213	301,299
Investment banking	750,192	540,596	495,014	352,804	229,608
Asset management fees and investment income from managed funds	23,534	109,550	82,052	81,184	32,769
Interest	1,174,883	528,882	304,053	134,450	102,403
Other	24,311	35,497	20,322	13,150	10,446
Total revenues	2,718,895	1,963,208	1,497,873	1,198,639	926,716
Interest expense	1,150,805	505,606	293,173	140,394	97,102
Revenues, net of interest expense	1,568,090	1,457,602	1,204,700	1,058,245	829,614
Non-interest expenses:					
Compensation and benefits	946,309	791,255	669,957	595,887	474,709
Floor brokerage and clearing fees	71,851	62,564	46,644	52,922	48,217
Technology and communications	103,763	80,840	67,666	64,555	58,581
Occupancy and equipment rental	76,765	59,792	47,040	39,553	32,534
Business development	56,594	48,634	42,512	35,006	26,481
Other	67,074	65,863	62,474	43,333	44,559
Total non-interest expenses	1,322,356	1,108,948	936,293	831,256	685,081
Earnings before income taxes, minority interest, and cumulative effect of change in accounting principle	245,734	348,654	268,407	226,989	144,533
Income taxes	93,178	137,541	104,089	83,955	52,851
Earnings before minority interest and cumulative effect of change in accounting principle	152,556	211,113	164,318	143,034	91,682
Minority interest in earnings of consolidated subsidiaries, net	7,891	6,969	6,875	11,668	7,631
Earnings before cumulative effect of change in accounting principle, net	144,665	204,144	157,443	131,366	84,051
Cumulative effect of change in accounting principle, net	—	1,606	—	—	—
Net earnings	\$ 144,665	\$ 205,750	\$ 157,443	\$ 131,366	\$ 84,051
Earnings per share of Common Stock:					
Basic-					
Earnings before cumulative effect of change in accounting principle, net	\$ 1.02	\$ 1.53	\$ 1.27	\$ 1.14	\$ 0.79
Cumulative effect of change in accounting principle, net	—	0.01	—	—	—
Net earnings	\$ 1.02	\$ 1.54	\$ 1.27	\$ 1.14	\$ 0.79
Diluted-					
Earnings before cumulative effect of change in accounting principle, net	\$ 0.97	\$ 1.41	\$ 1.16	\$ 1.03	\$ 0.71
Cumulative effect of change in accounting principle, net	—	0.01	—	—	—
Net earnings	\$ 0.97	\$ 1.42	\$ 1.16	\$ 1.03	\$ 0.71
Weighted average shares of Common Stock:					
Basic	141,515	133,898	123,646	114,906	106,179
Diluted	153,807	147,531	135,569	127,815	118,531
Cash dividends per common share	\$ 0.50	\$ 0.42	\$ 0.26	\$ 0.18	\$ 0.11

Selected Balance Sheet Data

Total assets	\$29,793,817	\$17,825,457	\$12,780,931	\$13,824,628	\$10,992,283
Long-term debt	\$ 1,764,067	\$ 1,168,562	\$ 779,873	\$ 789,067	\$ 443,148
Mandatorily redeemable convertible preferred stock	\$ 125,000	\$ 125,000	—	—	—
Total stockholders' equity	\$ 1,761,544	\$ 1,581,087	\$ 1,286,850	\$ 1,039,133	\$ 838,371
Shares outstanding	124,453	119,547	116,220	114,578	113,404
Other Data (Unaudited)					
Book value per share of Common Stock	\$ 14.15	\$ 13.23	\$ 11.07	\$ 9.07	\$ 7.40
Fixed charge coverage ratio (1)	3.0X	4.5X	5.5X	5.6X	5.6X

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- (1) The ratio of earnings to fixed charges is computed by dividing (a) income from continuing operations before income taxes plus fixed charges by (b) fixed charges. Fixed charges consist of interest expense on all long-term indebtedness and the portion of operating lease rental expense that is representative of the interest factor (deemed to be one-third of operating lease rentals).

Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

This report contains or incorporates by reference “forward-looking statements” within the meaning of the safe harbor provisions of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements include statements about our future and statements that are not historical facts. These forward-looking statements are usually preceded by the words “believe,” “intend,” “may,” “will,” or similar expressions. Forward-looking statements may contain expectations regarding revenues, earnings, operations and other financial projections, and may include statements of future performance, plans and objectives. Forward-looking statements also include statements pertaining to our strategies for future development of our business and products. Forward-looking statements represent only our belief regarding future events, many of which by their nature are inherently uncertain and outside of our control. It is possible that the actual results may differ, possibly materially, from the anticipated results indicated in these forward-looking statements. Information regarding important factors that could cause actual results to differ, perhaps materially, from those in our forward-looking statements is contained in this report and other documents we file. You should read and interpret any forward-looking statement together with these documents, including the following:

- the description of our business contained in this report under the caption “Business”;
- the risk factors contained in this report under the caption “Risk Factors”;
- the discussion of our analysis of financial condition and results of operations contained in this report under the caption “Management’s Discussion and Analysis of Financial Condition and Results of Operations”;
- the discussion of our risk management policies, procedures and methodologies contained in this report under the caption “Risk Management” included within Management’s Discussion and Analysis of Financial Condition and Results of Operations;
- the notes to the Consolidated Financial Statements contained in this report; and
- cautionary statements we make in our public documents, reports and announcements.

Any forward-looking statement speaks only as of the date on which that statement is made. We will not update any forward-looking statement to reflect events or circumstances that occur after the date on which the statement is made.

Critical Accounting Policies

The Consolidated Financial Statements are prepared in conformity with U.S. generally accepted accounting principles, which require management to make estimates and assumptions that affect the amounts reported in the Consolidated Financial Statements and related notes. Actual results can and will differ from estimates. These differences could be material to the financial statements.

We believe our application of accounting policies and the estimates required therein are reasonable. These accounting policies and estimates are constantly re-evaluated, and adjustments are made when facts and circumstances dictate a change. Historically, we have found our application of accounting policies to be appropriate, and actual results have not differed materially from those determined using necessary estimates.

Our management believes our critical accounting policies (policies that are both material to the financial condition and results of operations and require management’s most difficult, subjective or complex judgments) are our valuation of financial instruments, impairment of goodwill assessment and our use of estimates related to compensation and benefits during the year.

Table of Contents

Valuation of Financial Instruments

Definition of Fair Value - Our financial instruments are primarily recorded at fair value. The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (the exit price). The use of fair value to measure financial instruments is fundamental to our financial statements and is a critical accounting policy. Unrealized gains or losses are generally recognized in principal transactions in our Consolidated Statements of Earnings. Financial instruments are valued at quoted market prices, if available. For financial instruments that do not have readily determinable fair values through quoted market prices, the determination of fair value is based upon consideration of available information, including types of financial instruments, current financial information, restrictions on dispositions, fair values of underlying financial instruments and quotations for similar instruments. Certain financial instruments have bid and ask prices that can be observed in the marketplace. Bid prices reflect the highest price that we and others are willing to pay for an asset. Ask prices represent the lowest price that we and others are willing to accept for an asset. For financial instruments whose inputs are based on bid-ask prices, the Company does not require that fair value always be a predetermined point in the bid-ask range. Our policy is to allow for mid-market pricing and adjusting to the point within the bid-ask range that meets our best estimate of fair value. For offsetting positions in the same financial instrument, the same price within the bid-ask spread is used to measure both the long and short positions.

Fair Value Hierarchy - We adopted FASB 157, *Fair Value Measurements* (“FASB 157”), as of the beginning of 2007. FASB 157 defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the inputs used to measure fair value and enhances disclosure requirements for fair value measurements. FASB 157 establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of us. Unobservable inputs are inputs that reflect our assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

- Level 1: Quoted prices are available in active markets for identical assets or liabilities as of the reported date. The type of financial instruments included in Level 1 are highly liquid cash instruments with quoted prices such as G-7 government, agency securities, listed equities and money market securities, as well as listed derivative instruments;
- Level 2: Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these financial instruments include cash instruments for which quoted prices are available but traded less frequently, derivative instruments whose fair value have been derived using a model where inputs to the model are directly observable in the market, or can be derived principally from or corroborated by observable market data, and instruments that are fair valued using other financial instruments, the parameters of which can be directly observed. Instruments which are generally included in this category are corporate bonds, convertible bonds, municipal bonds and OTC derivatives;
- Level 3: Instruments that have little to no pricing observability as of the reported date. These financial instruments do not have two-way markets and are measured using management’s best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation. Instruments that are included in this category generally include certain illiquid equity securities, commercial loans and loan commitments, investments, distressed debt, as well as certain highly structured OTC derivative contracts.

Table of Contents

Valuation Process for Financial Instruments - The overall valuation process for financial instruments may include adjustments to valuations derived from pricing models. These adjustments may be made when, in management's judgment, either the size of the position in the financial instrument or other features of the financial instrument such as its complexity, or the market in which the financial instrument is traded (such as counterparty, credit, concentration or liquidity) require that an adjustment be made to the value derived from the pricing models. An adjustment may be made if a trade of a financial instrument is subject to sales restrictions that would result in a price less than the computed fair value measurement from a quoted market price. Additionally, an adjustment from the price derived from a model typically reflects management's judgment that other participants in the market for the financial instrument being measured at fair value would also consider such an adjustment in pricing that same financial instrument.

Valuation Models Used to Determine Fair Value - Non-derivative financial assets and liabilities presented at fair value and categorized as Level 3 are generally those that are based on an assessment of each underlying investment, incorporating valuations that consider the evaluation of financing and sale transactions with third parties, expected cash flows models, market-based information, including comparable company transactions, performance multiples and changes in market outlook, among other factors. Derivative financial instruments are generally those that are marked-to-model using relevant empirical data to estimate fair value. The models' inputs reflect assumptions that market participants would use in pricing the instrument in a current period transaction and outcomes from the models represent an exit price and expected future cash flows. Our valuation models are calibrated to the market on a frequent basis. The parameters and inputs are adjusted for assumptions about risk and current market conditions. Changes to inputs in valuation models are not changes to valuation methodologies; rather, the inputs are modified to reflect direct or indirect impacts on asset classes from changes in market conditions. Accordingly, results from valuation models in one period may not be indicative of future period measurements.

Controls Over Valuation of Financial Instruments — Our Risk Management Department, independent of the trading function, plays an important role in asserting that our financial instruments are appropriately valued and that fair value measurements are reliable. This is particularly important where prices or valuations that require inputs are less observable. In the event that observable inputs are not available, the control processes are designed to assure that the valuation approach utilized is appropriate and consistently applied and that the assumptions are reasonable. These control processes include reviews of the pricing model's theoretical soundness and appropriateness by risk management personnel with relevant expertise who are independent from the trading desks. Where a pricing model is used to determine fair value, recently executed comparable transactions and other observable market data are considered for purposes of validating assumptions underlying the model.

Compensation and Benefits

The use of estimates is important in determining compensation and benefits expenses for interim and year end periods. A substantial portion of our compensation and benefits represents discretionary bonuses, which are finalized at year end. In addition to the level of net revenues, our overall compensation expense in any given year is influenced by prevailing labor markets, revenue mix and our use of equity-based compensation programs. We believe the most appropriate way to allocate estimated annual discretionary bonuses among interim periods is in proportion to projected net revenues earned. Consequently, we have generally accrued interim compensation and benefits based on annual targeted compensation ratios, taking into account the guidance contained in FASB 123R regarding the timing of expense recognition for non-retirement-eligible and retirement-eligible employees. Our fourth quarter reflects the difference between the compensation and benefits we determine at year end and the accruals recorded through the end of the third quarter.

Goodwill Impairment

At least annually, we are required to assess whether goodwill has been impaired by comparing the estimated fair value, calculated based on earnings and book value multiples, of each business segment with its estimated net book value, by estimating the amount of stockholders' equity required to support each reporting unit. Periodically estimating the fair value of a reporting unit requires significant judgment and often involves the use of significant estimates and assumptions. These estimates and assumptions could have a significant effect on whether or not an

Table of Contents

impairment charge is recorded and the magnitude of such a charge. We completed our last impairment test on goodwill as of September 30, 2007, and no impairment was identified.

However, our Jefferies Execution subsidiary recorded a goodwill impairment charge of \$26 million during the fourth quarter of 2007. Jefferies Execution is a registered broker-dealer. Therefore, goodwill relating to the acquisition of Jefferies Execution in 2001, formerly Helfant Group, Inc., was “pushed down” from us to Jefferies Execution in accordance with Emerging Issues Task Force Issue No. D-97, *Push Down Accounting* .

We have two reporting units, Capital Markets and Asset Management, as defined by FASB 142, *Goodwill and Other Intangible Assets* . Jefferies Execution is not a reporting unit of ours and we have not recorded this \$26 million goodwill impairment charge to our Consolidated Financial Statements.

Revenues by Source

The Capital Markets reportable segment includes our securities trading, including the results of our recently reorganized high yield secondary market trading activities, and investment banking activities. The Capital Markets reportable segment is managed as a single operating segment that provides the sales, trading and origination effort for various fixed income, equity and advisory products and services. The Capital Markets segment comprises many divisions, with interactions among each. In addition, we choose to voluntarily disclose the Asset Management segment even though it is currently an “immaterial non-reportable” segment as defined by FASB 131, *Disclosures about Segments of an Enterprise and Related Information* .

For presentation purposes, the remainder of “Results of Operations” is presented on a detailed product and expense basis rather than on a business segment basis because the Asset Management segment is immaterial as compared to the consolidated Results of Operations.

Our earnings are subject to wide fluctuations since many factors over which we have little or no control, particularly the overall volume of trading, the volatility and general level of market prices, and the number and size of investment banking transactions may significantly affect our operations.

Table of Contents

The following provides a summary of revenues by source for the past three years:

	Year Ended December 31,					
	2007		2006		2005	
	Amount	% of Net Revenues	Amount (Dollars in Thousands)	% of Net Revenues	Amount	% of Net Revenues
Equity	\$ 597,164	38%	\$ 538,891	37%	\$ 438,080	36%
Fixed income and commodities:						
Fixed income (excluding high yield) and commodities (1)	139,274	9	165,170	11	116,801	10
High yield (2)	33,848	2	80,119	6	61,873	5
Total	173,122	11	245,289	17	178,674	15
Investment banking	750,192	48	540,596	37	495,014	41
Asset management fees and investment income from managed funds (3):						
Asset management fees	28,533	2	55,462	4	50,943	4
Investment income (loss) from managed funds	(4,999)	(1)	54,088	4	31,109	3
Total	23,534	1	109,550	8	82,052	7
Interest	1,174,883	75	528,882	36	304,053	25
Total revenues	\$ 2,718,895	173%	\$1,963,208	135%	\$1,497,873	124%
Interest expense	(1,150,805)	(73)	(505,606)	(35)	(293,173)	(24)
Net revenues	<u>\$ 1,568,090</u>	100%	<u>\$1,457,602</u>	100%	<u>\$1,204,700</u>	100%

- (1) Fixed income and commodities revenue is primarily comprised of investment grade fixed income, convertible and commodities product revenue.
- (2) High yield revenue is comprised of revenue generated by our reorganized high yield secondary market trading activities during the second, third, and fourth quarter of 2007 and revenue generated by our pari passu share of high yield revenue during the first quarter of 2007 and the full year of 2006. For the prior year, we recorded 100% of the revenue related to our pari passu share of our high yield revenue.
- (3) First quarter 2007 and prior period amounts include asset management revenue from high yield funds. Effective April 2, 2007, with the commencement of our reorganized high yield secondary market trading activities, we do not record asset management revenue associated with these activities.

Consolidated Results of Operations

2007 Compared to 2006

Net Revenues

Net revenues increased \$110.5 million, or 8%, to \$1,568.1 million, compared to \$1,457.6 million for 2006. The increase was primarily due to a \$209.6 million, or 39%, increase in investment banking revenues and a \$58.3 million, or 11%, increase in equity product revenues; partially offset by a \$25.9 million, or 16%, decrease in fixed income (excluding high yield) and commodities revenues, a \$46.3 million, or 58%, decrease in high yield revenues and a \$86.0 million, or 79%, decrease in asset management fees and investment income (loss) from managed funds.

Equity Product Revenue

Equity product revenue is comprised of equity (including principal transactions and commission revenue), correspondent clearing and prime brokerage, and execution product revenues. Equity product revenue was \$597.2 million, up 11% from 2006 primarily attributable to strong contributions from our U.S. and international agency cash equity and derivative products offset by principal trading losses from certain derivative and cash proprietary equity trading activities for the later half of the year. These principal trading losses were caused by illiquidity and volatility in the U.S. equity marketplace.

Table of Contents

Fixed Income and Commodities Revenue

Fixed income and commodities revenue is primarily comprised of high yield secondary market trading activities, investment grade fixed income, convertible and commodities product revenue. Fixed income and commodities revenue was \$173.1 million, down 29% over 2006. The decrease was driven by (1) extremely challenging and illiquid U.S. high yield credit markets for the latter half characterized by wider spreads and reduced levels of liquidity, and (2) strong prior period performance in high yield secondary market trading; offset by (1) consistent contributions throughout 2007 from our investment grade fixed income products despite a severe decline in fixed income liquidity and (2) a strong fourth quarter 2007 performance from JFP due to volatility in energy related commodities markets.

Investment Banking Product Revenue

	Year Ended		Percentage Change
	December 31, 2007	December 31, 2006	
	(Dollars in Thousands)		
Capital markets	\$ 388,675	\$ 231,261	68%
Advisory	361,517	309,335	17%
Total	<u>\$ 750,192</u>	<u>\$ 540,596</u>	<u>39%</u>

Capital markets revenues, which consists primarily of debt, equity and convertible financing services, were \$388.7 million, an increase of 68% from 2006. The increase in capital markets revenues was a result of increased U.S. and international debt underwritings and increased activity from our leverage finance group.

Revenues from advisory activities were \$361.5 million, an increase of 17% from 2006. The increase in advisory revenues was led by services rendered on assignments in the technology, industrial, energy, maritime and shipping, healthcare and aerospace and defense sectors.

Asset Management Fees and Investment Income from Managed Funds

Asset management revenue includes revenues from management, administrative and performance fees from funds managed by us, revenues from asset management and performance fees from third-party managed funds, and investment revenue from our investments in these funds. Asset management revenues were \$23.5 million, down \$86.0 million over 2006. The decrease in asset management revenue was a result of a strong prior period performance from our High Yield Funds, which are no longer included in asset management effective April 2, 2007 and weaker operating performance from our equity funds and managed CLO's offset by strong operating performance and increased assets under managements from our international global convertible funds.

Changes in Assets under Management

Dollars In millions	Year Ended December 31, 2007	Year Ended December 31, 2006	Percent Change
Balance, beginning of period	\$ 5,282	\$ 4,031	31%
Net cash flow in	269	792	
Net market appreciation	224	459	
	493	1,251	
Balance, end of period	<u>\$ 5,775</u>	<u>\$ 5,282</u>	<u>9%</u>

The net cash inflow during 2007 is primarily due to the commencement of the Clear Lake CLO and St. James River CLO, Ltd., partially offset by the liquidation of our managed high yield funds due to the commencement of our reorganized high yield secondary market trading activities (which are no longer included in assets under management) and the liquidation of the Jefferies Paragon Fund in June 2007.

Net Interest

Interest income increased \$646.0 million primarily as a result of increased stock borrowing, securities purchased under agreements to resell activities and increases in interest rates; and interest expense increased by \$645.2 million primarily as a result of increased stock lending and securities sold under agreements to repurchase activities, increases in interest rates and the issuance of our \$600 million of senior unsecured debentures in June 2007.

Compensation and Benefits

Compensation and benefits increased \$155.1 million, or 20%, while net revenues increased 8%. The ratio of compensation to net revenues was approximately 60.3% for 2007 as compared to 54.3% for 2006. Average employee headcount increased 12% from 2,140 during 2006 to 2,394 during 2007. Employee headcount increased 13% from 2,275 as of December 31, 2006 to 2,568 as of December 31, 2007.

Cash Compensation

Cash compensation and benefits increased \$95.7 million, or 14%, while net revenues increased 8%. The ratio of cash compensation to net revenues was approximately 51% for 2007 as compared to 48% for 2006. The ratio of cash compensation to average employee headcount was approximately \$334 thousand for 2007 as compared to \$329 thousand for 2006. The increase in cash compensation is primarily due to increased business activities and growth initiatives, both domestically and internationally. Specifically, during 2007 we hired numerous senior level employees as part of our growth initiatives requiring us to incur significant upfront cash compensation outflows including sign-on and guaranteed bonuses.

Issuance of Stock-Based Compensation to Employees

Restricted stock and restricted stock units (“RSU”s) are an important component of employee compensation. We believe they motivate employees and encourage long-term commitment to us. Restricted stock and RSU’s are awarded to employees subject to risk of forfeiture and/or vesting conditions. Typically the vesting occurs over a prescribed period of time and requires continued service and employment by the recipient. Restricted stock and RSU’s are valued at the date of grant and are amortized over the requisite service period which is typically five years.

Table of Contents

The following table summarizes selected financial ratios related to the issuance of stock-based compensation to our employees (dollars in thousands):

	2007	2006
Stock based compensation (1)	\$ 145,839	\$ 86,190
Net revenues	\$1,568,090	\$1,457,602
Compensation and benefits	\$ 946,309	\$ 791,255
Stock based compensation / net revenues	9%	6%
Stock based compensation / compensation and benefits	15%	11%

(1) Stock based compensation is the pre-tax expense associated with all of our employee stock-based compensation plans, including the discount on DCP deferred shares, restricted stock amortization, discounts on employee stock purchase plans and ESOP contributions.

The increase in stock-based compensation/net revenues and stock-based compensation/total compensation is primarily due to the increase in the amortization of stock-based awards from prior years. The increase in stock-based compensation is consistent with our change in compensation policies initiated during 2005 whereby we issue greater amounts of stock-based compensation to senior level employees as compared to cash compensation.

The following table summarizes estimated future amortization expense related to the issuance of stock-based awards to our employees prior to January 1, 2008. This table does not reflect the potential impact of future grants, modifications, if any, or actual forfeitures (in millions):

2008	\$104.8
2009	81.5
2010	63.1
2011	35.1
2012	13.2
Total	297.7

On January 22, 2008 we granted \$180 million of RSU's and restricted stock to our employees. These stock-based awards will generally be amortized into compensation and benefits expense on a straight-line basis over their five year vesting period.

Additional information relating to issuances pursuant to our employee stock-based compensation plans is contained in Consolidated Statements of Changes in Stockholders' Equity and Comprehensive Income (Loss) on page 50, Stock-Based Compensation included in note 1 of the Notes to the Consolidated Financial Statements, and Defined Benefit Plan included in note 11 of the Notes to the Consolidated Financial Statements.

Non-Personnel Expenses

Non-personnel expense was \$376.0 million for 2007 versus \$317.7 million for 2006 or 24.0% of net revenues for 2007 versus 21.8% of net revenues for 2006. The increase in non-personnel expenses is consistent with our revenue growth and primarily attributable to increased compliance, technology and communications costs as well as increased occupancy related to the expansion of our London and New York offices.

Earnings before Income Taxes, Minority Interest, and Cumulative Effect of Change in Accounting Principle, Net

Earnings before income taxes, minority interest and cumulative effect of change in accounting principle, net, were down \$102.9 million, or 29.5%, to \$245.7 million, compared to \$348.7 million for 2006. The effective tax rates were approximately 37.9% for 2007 and 39.4% for 2006. The lower effective tax rate is due to (1) the minority interest holdings in JHYH which are not taxed at the Jefferies Group level (2) a decrease in state and local income taxes and (3) return to provision adjustments for amounts previously deemed to be non-deductible.

Minority Interest

Minority interest consists of third party interests in JHYH (effective April 2, 2007) and our consolidated asset management funds. Minority interest was \$7.9 million compared to \$7.0 million for 2006. The increase is due to the commencement of JHYH. We now consolidate 100% of the operations of JHYH for financial reporting purposes beginning with the second quarter of 2007.

Earnings per Share

Diluted net earnings per share were \$0.97 for 2007 on 153,807,000 shares compared to \$1.42 for 2006 on 147,531,000 shares. The diluted earnings per share calculation for 2007 and 2006 includes an addition of \$4.1 and \$3.5 million, respectively, to net earnings for preferred dividends.

Basic net earnings per share were \$1.02 for 2007 on 141,515,000 shares compared to \$1.54 for 2006 on 133,898,000 shares.

2006 Compared to 2005

Net Revenues

Net revenues increased \$252.9 million, or 21%, to \$1,457.6 million, compared to \$1,204.7 million for 2005. The increase was primarily due to a \$167.4 million, or 27%, increase in equity and fixed income and commodities revenues, a \$27.5 million, or 34%, increase in asset management fees and investment income from managed funds and a \$45.6 million, or 9%, increase in investment banking revenue. The 2006 results included an after-tax gain of \$1.6 million, or \$0.01 per diluted common share, as a cumulative effect of change in accounting principle associated with our adoption of FASB 123R on January 1, 2006.

Equity Product Revenue

Equity product revenue is comprised of equity (including principal transactions and commission revenue), correspondent clearing and prime brokerage, and execution product revenues. Equity product revenue was \$538.9 million, up 23% from 2005 reflecting higher revenues across most of our core equity businesses. The increase in equity product revenue was due to moderate volatility in the market, several large block and proprietary trading opportunities generated from our investment banking relationships and the continued expansion of our secondary trading activity generated off of our capital markets platform.

Fixed Income and Commodities Revenue

Fixed income and commodities revenue is comprised of high yield, investment grade fixed income, convertible and commodities product revenue. Fixed income and commodities revenue was \$245.3 million, up 37% over last year driven by increased activity in the high yield, investment grade corporate bond and commodity markets. High Yield revenues increased primarily due to energy related proprietary trading. Investment grade fixed income revenues increased primarily as a result of increased activity in the trading of corporate bonds. The increase in commodities revenue was due to the overall expansion of JFP, as well as, increased activity in most commodities, including energy related commodities markets.

Investment Banking Product Revenue

	Year Ended		Percentage Change
	December 31, 2006	December 31, 2005	
	(Dollars in Thousands)		
Capital markets	\$ 231,261	\$ 221,479	4%
Advisory	309,335	273,535	13%
Total	\$ 540,596	\$ 495,014	9%

Capital markets revenues, which consist primarily of debt, equity and convertible financing services were \$231.3 million, an increase of 4% from 2005. The increase in capital markets revenues is primarily attributable to increases in revenue from equity and convertible underwritings, offset by the decrease in revenue generated from high yield underwritings.

Revenues from advisory activities were \$309.3 million, an increase of 13% from 2005. The increase is primarily attributable to services rendered on assignments in the technology, aerospace and defense, industrial and energy sectors.

Asset Management Fees and Investment Income from Managed Funds

Asset management revenue includes revenues from management, administrative and performance fees from funds managed by us, revenues from asset management and performance fees from third-party managed funds, and investment revenue from our investments in these funds. Asset management revenues were \$109.6 million, up 34% over 2005. The increase in asset management revenue was a result of solid performance and expansion of the JAM platform along with strong 2006 results from our High Yield Funds. During 2006, we formed a total of four new funds, one focused on distressed debt and risk arbitrage, two technology-oriented long-short equity funds, and one financial services long-short equity fund. In addition, we launched the Summit Lake CLO and Diamond Lake CLO.

Changes in Assets under Management (1)

Dollars In millions	Year Ended December 31, 2006	Year Ended December 31, 2005	Percent Change
Balance, beginning of period	\$ 4,031	\$ 3,287	23%
Net cash flow in	792	556	
Net market appreciation	459	188	
	1,251	744	
Balance, end of period	\$ 5,282	\$ 4,031	31%

(1) Excludes certain third party managed funds that are no longer considered assets under management.

Net Interest

Interest income increased \$224.8 million primarily as a result of increased stock borrowing activity and increases in interest rates, and interest expense increased by \$212.4 million primarily as a result of increased stock lending activity, increases in interest rates, the issuance of our \$500 million of senior unsecured debentures and our \$125 million in Series A Mandatorily Convertible Preferred Stock.

Compensation and Benefits

Compensation and benefits, including the amortization of previously awarded equity awards, increased \$121.3 million, or 18%, versus the 21% increase in net revenues. The increase was consistent with our increase in headcount and change to our revenue mix offset by changes to FASB 123R guidance regarding the timing of expense recognition for non-retirement-eligible employees. Under FASB 123 we defined the service period (over which compensation costs should be recognized) to generally include the year prior to the grant and the subsequent vesting periods. With the adoption of FASB 123R, our policy regarding the timing of expense recognition for non retirement-eligible employees changed to recognize compensation cost over the period from the service inception date which is the grant date through the date the employee is no longer required to provide service to earn the award.

Average employee headcount increased 10% from 1,937 during 2005 to 2,140 during 2006. The ratio of compensation to net revenues was approximately 54.3% for 2006 as compared to 55.6% for 2005.

Non-Personnel Expenses

Non-personnel expense was \$317.7 million or 21.8% of net revenues for 2006 versus \$266.3 or 22.1% of net revenues for 2005. The increase in non-personnel expenses is consistent with our revenue growth and primarily attributable to increased technology and communications, occupancy, legal and compliance and other costs associated with higher levels of business activity.

Earnings before Income Taxes, Minority Interest, and Cumulative Effect of Change in Accounting Principle, Net

Earnings before income taxes, minority interest and cumulative effect of change in accounting principle, net, were up \$80.2 million, or 30%, to \$348.7 million, compared to \$268.4 million for 2005. The effective tax rates were approximately 39.4% for 2006 and 38.8% for 2005. The 2006 basic and diluted calculations included an additional \$0.01 per share related to the cumulative effect of the change in accounting principle, net.

Minority Interest

Minority interest was \$7.0 million compared to \$6.9 million for 2005.

Earnings per Share

Diluted net earnings per share were \$1.42 for 2006 on 147,531,000 shares compared to \$1.16 in 2005 on 135,569,000 shares. The diluted earnings per share calculation for 2006 includes an addition of \$3.5 million to net earnings for preferred dividends.

Basic net earnings per share were \$1.54 for 2006 on 133,898,000 shares compared to \$1.27 in 2005 on 123,646,000 shares.

Both the 2006 basic and diluted calculations included an additional \$0.01 per share related to the cumulative effect of the change in accounting principle, net.

Liquidity, Financial Condition and Capital Resources

Our Chief Financial Officer and Treasurer are responsible for developing and implementing our liquidity, funding and capital management strategies. These policies are determined by the nature of our day-to-day business operations, business growth possibilities, regulatory obligations, and liquidity requirements.

Our actual level of capital, total assets, and financial leverage are a function of a number of factors, including, asset composition, business initiatives, regulatory requirements and cost availability of both long-term and short-term funding. We have historically maintained a highly liquid balance sheet, with a substantial portion of our total assets consisting of cash, highly liquid marketable securities and short-term receivables, arising principally from traditional securities brokerage activity. The highly liquid nature of these assets provides us with flexibility in financing and managing our business.

Liquidity

The following are financial instruments that are cash and cash equivalents or are deemed by management to be generally readily convertible into cash, marginable or accessible for liquidity purposes within a relatively short period of time (in thousands of dollars):

	<u>December 31, 2007</u>	<u>December 31, 2006</u>
Cash and cash equivalents:		
Cash in banks	\$ 248,174	\$ 107,488
Money market investments	649,698	405,553
Total cash and cash equivalents	897,872	513,041
Cash and securities segregated (1)	659,219	508,303
Other (2)	—	71,160
	<u>\$ 1,557,091</u>	<u>\$ 1,092,504</u>

- (1) In accordance with Rule 15c3-3 of the Securities Exchange Act of 1934, Jefferies, as a broker-dealer carrying client accounts, is subject to requirements related to maintaining cash or qualified securities in a segregated reserve account for the exclusive benefit of its clients.
- (2) Items are financial instruments utilized in our overall cash management activities and are readily convertible to cash in normal market conditions.

Bank loans represent short-term borrowings that are payable on demand and generally bear interest at a spread over the federal funds rate. We had no outstanding secured bank loans as of December 31, 2007 and 2006. Unsecured bank loans are typically overnight loans used to finance financial instruments owned or clearing related balances. We had \$280.4 million and \$0 of outstanding unsecured bank loans as of December 31, 2007 and 2006, respectively. Average daily bank loans for the years ended December 31, 2007 and 2006 were \$267.1 million and \$12.4 million, respectively.

A substantial portion of our assets are liquid, consisting of cash or assets readily convertible into cash. The majority of securities positions (both long and short) in our trading accounts are readily marketable and actively traded. In addition, receivables from brokers and dealers are primarily current open transactions or securities borrowed transactions, which are typically settled or closed out within a few days. Receivable from customers includes margin balances and amounts due on transactions in the process of settlement. Most of our receivables are secured by marketable securities.

Table of Contents

Our assets are funded by equity capital, senior debt, mandatorily redeemable convertible preferred stock, securities loaned, securities sold under agreements to repurchase, customer free credit balances, bank loans and other payables. Bank loans represent temporary (usually overnight) secured and unsecured short-term borrowings, which are generally payable on demand. We have arrangements with banks for unsecured financing of up to \$877.0 million. Secured bank loans are collateralized by a combination of customer, non-customer and firm securities. We have always been able to obtain necessary short-term borrowings in the past and believe that we will continue to be able to do so in the future. Additionally, we have \$308.0 million in letters of credit outstanding as of December 31, 2007, which are used in the normal course of business mostly to satisfy various collateral requirements in lieu of depositing cash or securities.

Excess Liquidity

Our policy is to maintain excess liquidity to cover all expected cash outflows for one year in a stressed liquidity environment. Liquid resources consist of unrestricted cash and unencumbered assets that are readily convertible into cash on a secured basis on short notice. Certain investments are also readily convertible to cash. In addition, we have \$1,185.0 million of unsecured, uncommitted lines of credit with various banks.

Management believes these resources provide sufficient excess liquidity to cover all expected cash outflows for one year during a stressed liquidity environment. Expected cash outflows include:

- The payment of interest expense (including dividends on our mandatorily redeemable convertible preferred stock) on our long-term debt;
- The anticipated funding of outstanding investment commitments;
- The anticipated fixed costs over the next 12 months;
- Potential stock repurchases; and
- Certain accrued expenses and other liabilities.

Analysis of Financial Condition and Capital Resources

Financial Condition

As previously discussed, we have historically maintained a highly liquid balance sheet, with a substantial portion of our total assets consisting of cash, highly liquid marketable securities and short-term receivables, arising principally from traditional securities brokerage activity. Total assets increased \$11,968.4 million, or 67%, from \$17,825.5 million at December 31, 2006 to \$29,793.8 million at December 31, 2007 primarily due to increased repo activity. Our financial instruments owned, including securities pledged to creditors, increased \$1,092.5 million, while our financial instruments sold, not yet purchased decreased \$266.2 million. Our securities borrowed and securities purchased under agreements to resell increased \$9,856.4 million, while our securities loaned and securities sold under agreements to repurchase increased \$10,119.6 million.

Level 3 assets, as defined by FASB 157, decreased to approximately 6.1% of total financial instruments owned as of December 31, 2007, compared to approximately 7.4% in the trailing quarter. The decrease in Level 3 assets resulted largely from the repayment of \$148.1 million in bridge loans from investment-banking clients in acquisition-finance transactions.

Table of Contents

The following table sets forth book value, pro forma book value, tangible book value and pro forma tangible book value per share (dollars in thousands, except per share data):

	December 31, 2007	December 31, 2006
Stockholders' equity	\$ 1,761,544	\$ 1,581,087
Less: Goodwill	<u>(344,063)</u>	<u>(257,321)</u>
Tangible stockholders' equity	\$ 1,417,481	\$ 1,323,766
Stockholders' equity	\$ 1,761,544	\$ 1,581,087
Add: Projected tax benefit on vested portion of restricted stock	<u>84,729</u>	<u>130,700</u>
Pro forma stockholders' equity	\$ 1,846,273	\$ 1,711,787
Tangible stockholders' equity	\$ 1,417,481	\$ 1,323,766
Add: Projected tax benefit on vested portion of restricted stock	<u>84,729</u>	<u>130,700</u>
Pro forma tangible stockholders' equity	\$ 1,502,210	\$ 1,454,466
Shares outstanding	124,453,174	119,546,914
Add: Shares not issued, to the extent of related expense amortization	<u>22,577,007</u>	<u>24,139,907</u>
Less: Shares issued, to the extent related expense has not been amortized	<u>(4,439,790)</u>	<u>(1,813,423)</u>
Adjusted shares outstanding	142,590,391	141,873,398
Book value per share (1)	<u>\$ 14.15</u>	<u>\$ 13.23</u>
Pro forma book value per share (2)	<u>\$ 12.95</u>	<u>\$ 12.07</u>
Tangible book value per share (3)	<u>\$ 11.39</u>	<u>\$ 11.07</u>
Pro forma tangible book value per share (4)	<u>\$ 10.54</u>	<u>\$ 10.25</u>

- (1) Book value per share equals stockholders' equity divided by common shares outstanding.
- (2) Pro forma book value per share equals stockholders' equity plus the projected deferred tax benefit on the amortized portion of restricted stock and RSUs divided by common shares outstanding adjusted for shares not yet issued to the extent of the related expense amortization and shares issued to the extent the related expense has not been amortized.
- (3) Tangible book value per share equals tangible stockholders' equity divided by common shares outstanding.
- (4) Pro forma tangible book value per share equals tangible stockholders' equity plus the projected deferred tax benefit on the amortized portion of restricted stock and RSUs divided by common shares outstanding adjusted for shares not yet issued to the extent of the related expense amortization and shares issued to the extent the related expense has not been amortized.

Tangible stockholders' equity, pro forma book value per share, tangible book value per share and pro forma tangible book value per share are "non-GAAP financial measures." A "non-GAAP financial measure" is a numerical measure of financial performance that includes adjustments to the most directly comparable measure calculated and presented in accordance with GAAP, or for which there is no specific GAAP guidance. We calculate tangible stockholders' equity as stockholders' equity less intangible assets. We calculate pro forma book value per share as stockholders' equity plus the projected deferred tax benefit on the vested portion of restricted stock and RSUs divided by common shares outstanding adjusted for shares not yet issued to the extent of the related expense amortization and shares issued to the extent the related expense has not been amortized. We calculate tangible book value per share by dividing tangible stockholders' equity by common stock outstanding. We calculate pro forma tangible book value per share by dividing tangible stockholders' equity plus the projected deferred tax benefit on the vested portion of restricted stock and RSUs by common shares outstanding adjusted for shares not yet issued to the extent of the related expense amortization and shares issued to the extent the related expense has not been amortized. We consider these ratios as meaningful measurements of our financial condition and believe they provide investors with additional metrics to comparatively assess the fair value of our stock.

Table of Contents

Capital Resources

We had total long-term capital of \$3.7 billion and \$2.9 billion resulting in a long-term debt to total capital ratio of 48% and 41%, at year end 2007 and 2006, respectively. Our total capital base as of December 31, 2007 and 2006 was as follows (in thousands):

	December 31, 2007	December 31, 2006
Long-Term Debt	\$1,764,067	\$1,168,562
Mandatorily Redeemable Convertible Preferred Stock	125,000	125,000
Total Stockholders' Equity	1,761,544	1,581,087
Total Capital	\$3,650,611	\$2,874,649

Our ability to support increases in total assets is largely a function of our ability to obtain short-term secured and unsecured funding, primarily through securities lending, and through our \$1,185.0 million of uncommitted unsecured bank lines. Our ability is further enhanced by the cash proceeds from the \$500 million senior unsecured bonds and \$125 million in series A preferred stock, both issued in the first quarter of 2006; as well as cash proceeds from our \$600 million senior unsecured debt issuance in June 2007.

At December 31, 2007, our senior long-term debt, net of unamortized discount, consisted of contractual principal payments (adjusted for amortization) of \$492.3 million, \$346.2 million, \$348.5 million, \$248.4 million and \$328.6 million due in 2036, 2027, 2016, 2014 and 2012, respectively.

We rely upon our cash holdings and external sources to finance a significant portion of our day-to-day operations. Access to these external sources, as well as the cost of that financing, is dependent upon various factors, including our debt ratings. Our current debt ratings are dependent upon many factors, including operating results, operating margins, earnings trend and volatility, balance sheet composition, liquidity and liquidity management, our capital structure, our overall risk management, business diversification and our market share and competitive position in the markets in which we operate.

Our long-term debt ratings are as follows:

	Rating
Moody's Investors Services	Baa1
Standard and Poor's	BBB+
Fitch Ratings	BBB+

Net Capital

Jefferies, Jefferies Execution and Jefferies High Yield Trading are subject to the net capital requirements of the SEC and other regulators, which are designed to measure the general financial soundness and liquidity of broker-dealers. Jefferies, Jefferies Execution and Jefferies High Yield Trading use the alternative method of calculation.

Table of Contents

As of December 31, 2007, Jefferies, Jefferies Execution and Jefferies High Yield Trading's net capital and excess net capital were as follows (in thousands of dollars):

	Net Capital	Excess Net Capital
Jefferies	\$505,080	\$483,108
Jefferies Execution	\$ 30,297	\$ 30,047
Jefferies High Yield Trading	\$558,087	\$557,837

Guarantees

As of December 31, 2007, we had outstanding guarantees of \$20.0 million relating to an undrawn bank credit obligation of an associated investment fund in which we have an interest. In addition, we guarantee up to an aggregate of approximately \$36.0 million in bank loans committed to an employee parallel fund of Jefferies Capital Partners IV L.P. ("Fund IV").

We have guaranteed the performance of JIL and JFP to their trading counterparties and various banks and other entities, which provide clearing and credit services to JIL and JFP. Also, we have provided a guarantee to a third-party bank in connection with the bank's extension of 500 million Japanese yen (approximately \$4.5 million) to Jefferies (Japan) Limited. In addition, as of December 31, 2007, we had commitments to invest up to \$500.1 million in various investments, including \$195.0 million in Jefferies Finance LLC, \$18.0 million in Babson-Jefferies Loan Opportunity CLO, \$25.9 million in Fund IV, \$250.0 million in JHYH and \$11.2 million in other investments.

Leverage Ratios

The following table presents total assets, adjusted assets, total stockholders' equity and tangible stockholders' equity with the resulting leverage ratios as of December 31, 2007 and December 31, 2006:

	December 31, 2007	December 31, 2006
Total assets	\$ 29,793,817	\$ 17,825,457
Deduct: Securities borrowed	(16,422,130)	(9,711,894)
Securities purchased under agreements to resell	(3,372,294)	(226,176)
Add: Financial instruments sold, not yet purchased	3,334,678	3,600,869
Less derivative liabilities	(331,788)	(240,231)
Subtotal	3,002,890	3,360,638
Deduct: Cash and securities segregated and on deposit for regulatory purposes or deposited with clearing and depository organizations	(659,219)	(508,303)
Goodwill	(344,063)	(257,321)
Adjusted assets	<u>11,999,001</u>	<u>10,482,401</u>
Total stockholders' equity	\$ 1,761,544	\$ 1,581,087
Deduct: Goodwill	(344,063)	(257,321)
Tangible stockholders' equity	<u>1,417,481</u>	<u>1,323,766</u>
Leverage ratio (1)	<u>16.9</u>	<u>11.3</u>
Adjusted leverage ratio (2)	<u>8.5</u>	<u>7.9</u>

(1) Leverage ratio equals total assets divided by total stockholders' equity.

(2) Adjusted leverage ratio equals adjusted assets divided by tangible stockholders' equity.

Table of Contents

Commitments

The tables below provide information about our commitments related to debt obligations, leases, guarantees, letters of credit and investments as of December 31, 2007. For debt obligations, leases and investments, the table presents principal cash flows with expected maturity dates. For guarantees and letters of credit, the table presents notional amounts with expected maturity dates.

	Expected Maturity Date						Total
	2008	2009	2010	2011	2012	After 2012	
	(Dollars in Millions)						
Debt obligations							
Senior notes	—	—	—	—	\$ 325.0	\$ 1,450.0	\$ 1,775.0
Mandatorily redeemable convertible preferred stock	—	—	—	—	—	\$ 125.0	\$ 125.0
Leases							
Gross lease commitments	\$ 47.5	\$ 48.0	\$ 45.8	\$ 43.6	\$ 37.5	\$ 149.9	\$ 372.3
Sub-leases	10.6	10.7	10.4	10.0	6.7	14.7	63.1
Net lease commitments	\$ 36.9	37.3	\$ 35.4	\$ 33.6	\$ 30.8	\$ 135.2	\$ 309.2
Guarantees	\$ 20.0	—	—	—	\$ 36.0	\$ 4.5	\$ 60.5
Letters of credit	\$ 307.7	\$ 0.1	\$ 0.2	—	—	—	\$ 308.0
Commitments to invest	—	\$ 0.1	—	\$ 0.9	\$ 0.4	\$ 498.7	\$ 500.1
High yield loan commitment	—	—	\$ 5.0	—	—	—	\$ 5.0
Derivative contracts	\$ 392.5	—	—	—	\$ 5.0	—	\$ 397.5

Off Balance Sheet Arrangements

Information concerning our off balance sheet arrangements are included in note 18 of the Notes to Consolidated Financial Statements. Such information is hereby incorporated by reference.

Effects of Changes in Foreign Currency Rates

We maintain a foreign securities business in our foreign offices (London, Paris, Tokyo and Zurich) as well as in some of our domestic offices. Most of these activities are hedged by related foreign currency liabilities or by forward exchange contracts. However, we are still subject to some foreign currency risk. A change in the foreign currency rates could create either a foreign currency transaction gain/loss (recorded in our Consolidated Statements of Earnings) or a foreign currency translation adjustment to the stockholders' equity section of our Consolidated Statements of Financial Condition.

Effects of Inflation

Based on today's modest inflationary rates and because our assets are primarily monetary in nature, consisting of cash and cash equivalents, financial instruments and receivables, we believe that our assets are not significantly affected by inflation. The rate of inflation, however, can affect various expenses, including employee compensation, communications and technology and occupancy, which may not be readily recoverable in charges for services provided by us.

Risk Management

Risk is an inherent part of our business and activities. The extent to which we properly and effectively identify, assess, monitor and manage each of the various types of risk involved in our activities is critical to our financial soundness and profitability. We seek to identify, assess, monitor and manage the following principal risks involved in our business activities: market, credit, operational, legal and compliance, new business, reputational and other. Risk management is a multi-faceted process that requires communication, judgment and knowledge of financial products and markets. Senior management takes an active role in the risk management process and requires specific administrative and business functions to assist in the identification, assessment and control of various risks. Our risk management policies, procedures and methodologies are fluid in nature and are subject to ongoing review and modification.

Market Risk. The potential for changes in the value of financial instruments is referred to as market risk. Our market risk generally represents the risk of loss that may result from a change in the value of a financial instrument as a result of fluctuations in interest rates, credit spreads, equity prices, commodity prices and foreign exchange rates, along with the level of volatility. Interest rate risks result primarily from exposure to changes in the yield curve, the volatility of interest rates, and credit spreads. Equity price risks result from exposure to changes in prices and volatilities of individual equities, equity baskets and equity indices. Commodity price risks result from exposure to the changes in prices and volatilities of individual commodities, commodity baskets and commodity indices. We make dealer markets in equity securities, debt securities and commodities. We attempt to hedge our exposure to market risk by managing our net long or short positions. Due to imperfections in correlations, gains and losses can occur even for positions that are hedged. Position limits in trading and inventory accounts are established and monitored on an ongoing basis. Each day, consolidated position and exposure reports are prepared and distributed to various levels of management, which enable management to monitor inventory levels and results of the trading groups.

Credit Risk. Credit risk represents the loss that we would incur if a client, counterparty or issuer of financial instruments, such as securities and derivatives, held by us fails to perform its contractual obligations. We follow industry practices to reduce credit risk related to various trading, investing and financing activities by obtaining and maintaining collateral. We adjust margin requirements if we believe the risk exposure is not appropriate based on market conditions. Liabilities to other brokers and dealers related to unsettled transactions (i.e., securities failed-to-receive) are recorded at the amount for which the securities were purchased, and are paid upon receipt of the securities from other brokers or dealers. In the case of aged securities failed-to-receive, we may purchase the underlying security in the market and seek reimbursement for losses from the counterparty in accordance with standard industry practices.

Operational Risk. Operational risk generally refers to the risk of loss resulting from our operations, including, but not limited to, improper or unauthorized execution and processing of transactions, deficiencies in our operating systems, business disruptions and inadequacies or breaches in our internal control processes. Our businesses are highly dependent on our ability to process, on a daily basis, a large number of transactions across numerous and diverse markets in many currencies. In addition, the transactions we process have become increasingly complex. If any of our financial, accounting or other data processing systems do not operate properly or are disabled or if there are other shortcomings or failures in our internal processes, people or systems, we could suffer an impairment to our liquidity, financial loss, a disruption of our businesses, liability to clients, regulatory intervention or reputational damage. These systems may fail to operate properly or become disabled as a result of events that are wholly or partially beyond our control, including a disruption of electrical or communications services or our inability to occupy one or more of our buildings. The inability of our systems to accommodate an increasing volume of transactions could also constrain our ability to expand our businesses.

We also face the risk of operational failure or termination of any of the clearing agents, exchanges, clearing houses or other financial intermediaries we use to facilitate our securities transactions. Any such failure or termination could adversely affect our ability to effect transactions and manage our exposure to risk.

Table of Contents

In addition, despite the contingency plans we have in place, our ability to conduct business may be adversely impacted by a disruption in the infrastructure that supports our businesses and the communities in which they are located. This may include a disruption involving electrical, communications, transportation or other services used by us or third parties with which we conduct business.

Our operations rely on the secure processing, storage and transmission of confidential and other information in our computer systems and networks. Although we take protective measures and endeavor to modify them as circumstances warrant, our computer systems, software and networks may be vulnerable to unauthorized access, computer viruses or other malicious code, and other events that could have a security impact. If one or more of such events occur, this potentially could jeopardize our or our clients' or counterparties' confidential and other information processed and stored in, and transmitted through, our computer systems and networks, or otherwise cause interruptions or malfunctions in our, our clients', our counterparties' or third parties' operations. We may be required to expend significant additional resources to modify our protective measures or to investigate and remediate vulnerabilities or other exposures, and we may be subject to litigation and financial losses that are either not insured against or not fully covered through any insurance maintained by us.

Legal and Compliance Risk . Legal and compliance risk includes the risk of non-compliance with applicable legal and regulatory requirements. We are subject to extensive regulation in the different jurisdictions in which we conduct our business. We have various procedures addressing issues such as regulatory capital requirements, sales and trading practices, use of and safekeeping of customer funds, credit granting, collection activities, anti-money laundering and record keeping. We also maintain an anonymous hotline for employees or others to report suspected inappropriate actions by us or by our employees or agents.

New Business Risk . New business risk refers to the risks of entering into a new line of business or offering a new product. By entering a new line of business or offering a new product, we may face risks that we are unaccustomed to dealing with and may increase the magnitude of the risks we currently face. We review proposals for new businesses and new products to determine if we are prepared to handle the additional or increased risks associated with entering into such activities.

Reputational Risk . We recognize that maintaining our reputation among clients, investors, regulators and the general public is an important aspect of minimizing legal and operational risks. Maintaining our reputation depends on a large number of factors, including the selection of our clients and the conduct of our business activities. We seek to maintain our reputation by screening potential clients and by conducting our business activities in accordance with high ethical standards.

Other Risk . Other risks encountered by us include political, regulatory and tax risks. These risks reflect the potential impact that changes in local and international laws and tax statutes have on the economics and viability of current or future transactions. In an effort to mitigate these risks, we continuously review new and pending regulations and legislation and participate in various industry interest groups.

Accounting and Regulatory Developments

FASB Interpretation No. 48 . In July 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (“FIN 48”). FIN 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. We adopted FIN 48 as of the beginning of 2007. The transition adjustment to beginning retained earnings was a reduction of approximately \$0.4 million.

FASB 157 . In September 2006, the FASB issued FASB 157, *Fair Value Measurements* (“FASB 157”). FASB 157 clarifies that fair value is the amount that would be exchanged to sell an asset or transfer a liability, in an orderly transaction between market participants. FASB 157 reverses the consensus reached in EITF Issue No. 02-3 prohibiting the recognition of day one gain or loss on derivative contracts where we cannot verify all of the significant model inputs to observable market data and verify the model to market transactions. However, FASB 157 requires that a fair value measurement technique include an adjustment for risks inherent in a particular valuation technique (such as a pricing model) and/or the risks inherent in the inputs to the model, if market participants would also include such an adjustment. In addition, FASB 157 prohibits the recognition of “block discounts” for large holdings of unrestricted financial instruments where quoted prices are readily and regularly available in an active market. The provisions of FASB 157 are to be applied prospectively, except for changes in fair value measurements that result from the initial application of FASB 157 to existing derivative financial instruments measured under EITF Issue No. 02-3 and block discounts, which are to be recorded as an adjustment to opening retained earnings in the year of adoption. FASB 157 is effective for fiscal years beginning after November 15, 2007. We adopted FASB 157 as of the beginning of 2007. To determine the transition adjustment to opening retained earnings, we performed an analysis of existing derivative instruments measured under EITF Issue 02-3 and block discounts, and determined that there was no transition adjustment to opening retained earnings as of January 1, 2007.

FASB 158. In September 2006, the FASB issued Statement No. 158, *Accounting for Uncertainty in Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)* (“FASB 158”). FASB 158 improves financial reporting by requiring an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. This Statement also improves financial reporting by requiring an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. An employer with publicly traded equity securities is required to initially recognize the funded status of a defined benefit postretirement plan and to provide the required disclosures as of the end of the fiscal year ending after December 15, 2006. The requirement to measure plan assets and benefit obligations as of the date of the employer’s fiscal year-end statement of financial position is effective for fiscal years ending after December 15, 2008. On December 31, 2006, we adopted the recognition and disclosure provisions of FASB 158. FASB 158 required us to recognize the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of our benefit plan on our December 31, 2006 Consolidated Statement of Financial Condition, with a corresponding adjustment to accumulated other comprehensive income, net of tax. As a result of the pension plan being frozen, the projected benefit obligation was equal to the accumulated benefit obligation. Consequently, no additional adjustment to accumulated other comprehensive income was necessary as of December 31, 2006.

FASB 159. In February 2007, the FASB issued FASB 159, *The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of FASB Statement No. 115* (“FASB 159”). This standard permits an entity to measure financial instruments and certain other items at estimated fair value. Most of the provisions of FASB 159 are elective; however, the amendment to FASB 115, *Accounting for Certain Investments in Debt and Equity Securities* , applies to all entities that own trading and available-for-sale securities. The fair value option created by FASB 159 permits an entity to measure eligible items at fair value as of specified election dates. The fair value option (a) may generally be applied instrument by instrument, (b) is irrevocable unless a new election date occurs, and (c) must be applied to the entire instrument and not to only a portion of the instrument. FASB 159

allows for a one-time election for existing positions upon adoption, with the transition adjustment recorded to opening retained earnings. FASB 159 is effective as of the beginning of the first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of the previous fiscal year provided that the entity (i) makes that choice in the first 120 days of that year, (ii) has not yet issued financial statements for any interim period of such year, and (iii) elects to apply the provisions of FASB 157. We adopted FASB 159 as of the beginning of 2007. We elected to apply the fair value option on loans and loan commitments made in connection with our investment banking activities (“loans and loan commitments”). Loans and loan commitments are included in financial instruments owned on the Consolidated Statement of Financial Condition. At the time of adoption, we did not have such loans and loan commitments outstanding, therefore there was no transition adjustment recorded to opening retained earnings. In addition, we elected to apply the fair value option on certain investments held by subsidiaries that are not registered broker-dealers as defined in the AICPA Audit and Accounting Guide, *Brokers and Dealers in Securities*. These investments had been accounted for by us at fair value prior to the adoption of FASB 159; therefore, there was no transition adjustment recorded to opening retained earnings related to these investments. The fair value option was elected for loans and loan commitments and investments held by subsidiaries that are not registered broker-dealers because they are risk managed by us on a fair value basis.

FSP FIN 39-1. In April 2007, the FASB issued a Staff Position (“FSP”) FIN No. 39-1, *Amendment of FASB Interpretation No. 39*. FSP FIN No. 39-1 defines “right of setoff” and specifies what conditions must be met for a derivative contract to qualify for this right of setoff. It also addresses the applicability of a right of setoff to derivative instruments and clarifies the circumstances in which it is appropriate to offset amounts recognized for those instruments in the statement of financial position. In addition, this FSP permits offsetting of fair value amounts recognized for multiple derivative instruments executed with the same counterparty under a master netting arrangement and fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) arising from the same master netting arrangement as the derivative instruments. The provisions of this FSP are consistent with our current accounting practice. This interpretation is effective for fiscal years beginning after November 15, 2007, with early application permitted. The adoption of FSP FIN 39-1 on January 1, 2008 did not have a material impact on our Consolidated Financial Statements.

EITF Issue No. 06-11. In June 2007, the FASB ratified the consensus reached by the Emerging Issues Task Force on Issue 06-11, *Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards* (“EITF 06-11”). EITF 06-11 requires that the tax benefit related to dividends or dividend equivalents that are charged to retained earnings and are paid to employees for equity classified nonvested equity shares, nonvested equity share units, and outstanding equity share options be recorded as an increase in additional paid-in capital. We currently account for this tax benefit as a reduction to income tax expense. EITF 06-11 is to be applied prospectively for tax benefits on dividends declared in fiscal years beginning after December 15, 2007. We intend to adopt EITF 06-11 in the first quarter of 2008. We are currently evaluating the impact of EITF 06-11 on our results of operations for the first quarter of 2008.

SOP No. 07-1 and FSP FIN No. 46R-7. In June 2007, the American Institute of Certified Public Accountants issued Statement of Position No. 07-1, *Clarification of the Scope of the Audit and Accounting Guide ‘Audits of Investment Companies’ and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies* (“SOP 07-1”). SOP 07-1 clarifies the scope of when an entity may apply the provisions of the AICPA Audit and Accounting Guide Investment Companies (“the Guide”). SOP 07-1 also provides guidance for determining whether the specialized industry accounting principles of the Guide should be retained in the financial statements of a parent company of an investment company or an equity method investor in an investment company, and includes certain disclosure requirements. In May 2007, the FASB issued FSP FIN 46R-7, *Application of FIN 46R to Investment Companies* (“FSP FIN 46R-7”). FSP FIN 46R-7 amends FIN 46R to make permanent the temporary deferral of the application of FIN 46R to entities within the scope of the revised Guide under SOP 07-1. FSP FIN 46R-7 is effective upon the adoption of SOP 07-1. In November 2007, the FASB issued a proposed FSP SOP No. 07-1-a, *The Effective Date of AICPA Statement of Position 07-1*, which proposes to indefinitely defer the effective date for SOP 07-1 and, consequently, FSP FIN 46R-7. We are currently evaluating the potential impact of adopting SOP 07-1 and FSP FIN 46R-7 in light of the proposed FSP SOP No. 07-1-a.

FASB 141(R). In December 2007, the FASB issued FASB 141 (revised 2007), *Business Combinations* (“FASB 141R”). Under FASB 141R, an entity is required to recognize the assets acquired, liabilities assumed, contractual

Table of Contents

contingencies and contingent consideration measured at their fair value at the acquisition date for any business combination consummated after the effective date. It further requires that acquisition-related costs are to be recognized separately from the acquisition and expensed as incurred. This statement is effective for financial statements issued for fiscal years beginning after December 15, 2008. Accordingly, we will adopt FASB 141R effective January 1, 2009.

FASB 160. In December 2007, the FASB issued FASB 160, *Noncontrolling Interests in Consolidated Financial Statements — an amendment of ARB No. 51* (“FASB 160”). FASB 160 requires an entity to clearly identify and present ownership interests in subsidiaries held by parties other than the entity in the Consolidated Financial Statements within the equity section but separate from the entity’s equity. It also requires the amount of consolidated net income attributable to the parent and to the noncontrolling interest be clearly identified and presented on the face of the consolidated statement of income; changes in ownership interest be accounted for similarly, as equity transactions; and when a subsidiary is deconsolidated, any retained noncontrolling equity investment in the former subsidiary and the gain or loss on the deconsolidation of the subsidiary be measured at fair value. This statement is effective for financial statements issued for fiscal years beginning after December 15, 2008. Accordingly, we will adopt FASB 160 effective January 1, 2009. We are currently evaluating the impact of FASB 160 on our Consolidated Financial Statements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk.

We use a number of quantitative tools to manage our exposure to market risk. These tools include:

- inventory position and exposure limits, on a gross and net basis;
- scenario analyses, stress tests and other analytical tools that measure the potential effects on our trading net revenues of various market events, including, but not limited to, a large widening of credit spreads, a substantial decline in equities markets and significant moves in selected emerging markets; and
- risk limits based on a summary measure of risk exposure referred to as Value-at-Risk (“VaR”).

Value-at-Risk

In general, VaR measures potential loss of trading revenues at a given confidence level over a specified time horizon. We calculate VaR over a one day holding period measured at a 95% confidence level which implies the potential loss of daily trading revenue is expected to be at least as large as the VaR amount on one out of every twenty trading days.

VaR is one measurement of potential loss in trading revenues that may result from adverse market movements over a specified period of time with a selected likelihood of occurrence. As with all measures of VaR, our estimate has substantial limitations due to our reliance on historical performance, which is not necessarily a predictor of the future. Consequently, this VaR estimate is only one of a number of tools we use in our daily risk management activities.

The VaR numbers below are shown separately for interest rate, equity, currency and commodity products, as well as for our overall trading positions, excluding corporate investments in asset management positions, using a historical simulation approach. The aggregated VaR presented here is less than the sum of the individual components (i.e., interest rate risk, foreign exchange rate risk, equity risk and commodity price risk) due to the benefit of diversification among the risk categories. Diversification benefit equals the difference between aggregated VaR and the sum of VaRs for the four risk categories. The following table illustrates the VaR for each component of market risk:

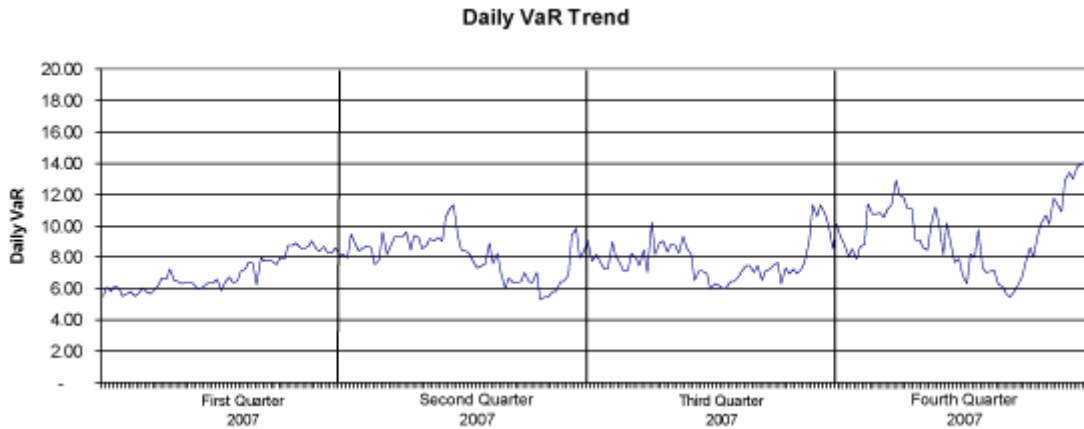
Risk Categories	Daily VaR (1) (in millions)							
	Value-at-Risk in trading portfolios							
	VaR at		Year Ended 12/31/2007			Year Ended 12/31/2006		
	12/31/07	12/31/06	Average	High	Low	Average	High	Low
Interest Rates	\$ 1.70	\$ 1.39	\$ 1.60	\$ 2.24	\$0.97	\$ 0.81	\$ 1.50	\$0.41
Equity Prices	\$16.73	\$ 6.37	\$ 8.42	\$17.01	\$4.94	\$ 4.35	\$13.30	\$1.10
Currency Rates	\$ 0.47	\$ 0.34	\$ 0.41	\$ 1.06	\$0.13	\$ 0.37	\$ 0.53	\$0.24
Commodity Prices	\$ 2.07	\$ 0.80	\$ 1.22	\$ 2.36	\$0.27	\$ 1.98	\$ 4.87	\$0.61
Diversification Effect (2)	\$(7.24)	\$(3.36)	\$(3.53)			\$(2.76)		
Firmwide	\$13.73	\$ 5.54	\$ 8.12	\$14.02	\$5.31	\$ 4.75	\$13.90	\$1.95

- (1) VaR is the potential loss in value of our trading positions due to adverse market movements over a defined time horizon with a specific confidence level. For the VaR numbers reported above, a one-day time horizon and 95% confidence level were used.
- (2) Equals the difference between firmwide VaR and the sum of the VaRs by risk categories. This effect is due to the market categories not being perfectly correlated.

Table of Contents

Average firmwide VaR of \$8.12 million during 2007 increased from the \$4.75 million average during 2006 primarily due to an increase in exposure to equity prices, and interest rates.

The following table presents our daily VaR over the last four quarters:



VaR Back-Testing

The comparison of daily actual revenue fluctuations with the daily VaR estimate is the primary method used to test the efficacy of the VaR model. A back-testing exception occurs when the daily loss exceeds the daily VaR estimate. Results of the process at the aggregate level demonstrated nineteen outliers when comparing the 95% one-day VaR with the back-testing profit and loss in 2007. Ten of the outliers occurred during the third quarter as result of increased market volatility. A 95% confidence one-day VaR model should not have more than twelve (1 out of 20 days) back-testing exceptions on an annual basis under normal market conditions. Back-testing profit and loss is a subset of actual trading revenue and includes the profit and loss effects relevant to the VaR model, excluding fees, commissions and certain provisions. We compare the trading revenue with VaR for back-testing purposes because VaR assesses only the potential change in position value due to overnight movements in financial market variables such as prices, interest rates and volatilities under normal market conditions. The graph below illustrates the relationship between daily back-testing profit and loss and daily VaR for us in 2007.

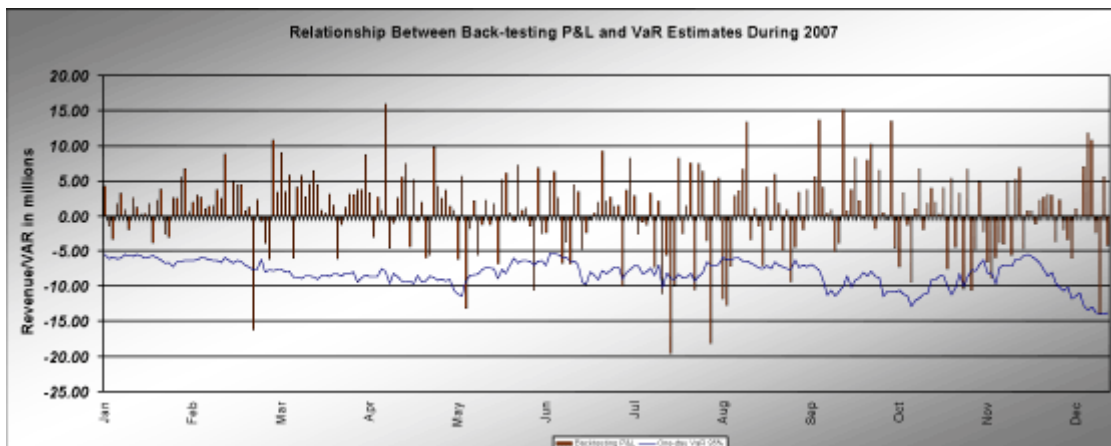
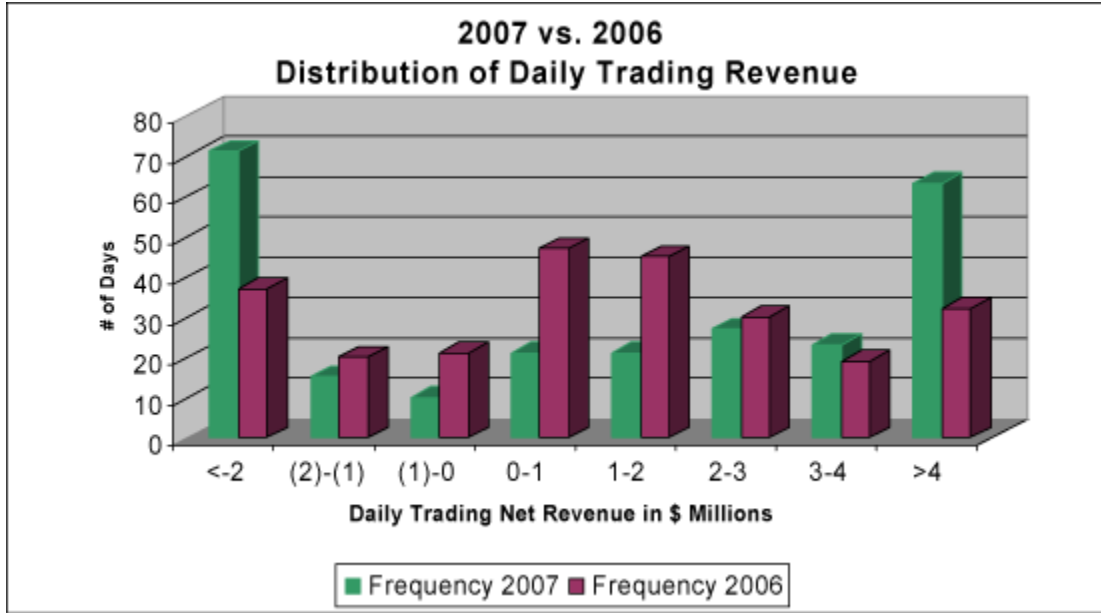


Table of Contents

VaR is a model that estimates the future risk based on historical data. We could incur losses greater than the reported VaR because the historical market prices and rates changes may not be an accurate measure of future market events and conditions. In addition, the VaR model measures the risk of a current static position over a one-day horizon and might not predict the future position. When comparing our VaR numbers to those of other firms, it is important to remember that different methodologies could produce significantly different results.

Daily Trading Net Revenue (\$ in millions)



Trading revenue used in the histogram below entitled “2007 vs. 2006 Distribution of Daily Trading Revenue” is the actual daily trading revenue which is excluding fees, commissions and certain provisions. The histogram below shows the distribution of daily trading revenue for our trading activities:

Maturity Data

At December 31, 2007, we had \$1,775.0 million aggregate principal amount of senior notes outstanding, with fixed interest rates. We previously entered into a fair value hedge with no ineffectiveness using interest rate swaps in order to convert \$200 million aggregate principal amount of unsecured 7 3/4% senior notes due March 15, 2012 into floating rates based upon LIBOR. During the third quarter of 2007, we terminated these interest rate swaps and received cash consideration less accrued interest of \$8.5 million. The \$8.5 million basis difference related to the fair value of the interest rate swaps at the time of the termination is being amortized as a reduction in interest expense of approximately \$1.9 million per year over the remaining life of the notes through March 2012.

The table below provides information about our OTC derivative financial instruments and other financial instruments that are sensitive to changes in interest rates, exchange rates and price movements. For debt obligations and mandatorily redeemable convertible preferred stock, the table presents principal cash flows with expected maturity dates. For OTC derivative financial instruments, the table presents fair value amounts with expected maturity dates.

	Expected Maturity Date					After 2012	Total	Fair Value
	2008	2009	2010	2011	2012			
	(Dollars in Millions)							
Debt obligations								
7.75% Senior notes	—	—	—	—	\$325.0	—	\$ 325.0	\$ 352.9
5.875% Senior notes	—	—	—	—	—	\$250.0	\$ 250.0	\$ 251.5
5.5% Senior notes	—	—	—	—	—	\$350.0	\$ 350.0	\$ 333.8
6.45% Senior notes	—	—	—	—	—	\$350.0	\$ 350.0	\$ 324.2
6.25% Senior notes	—	—	—	—	—	\$500.0	\$ 500.0	\$ 446.9
Mandatorily redeemable convertible preferred stock								
	—	—	—	—	—	\$125.0	\$ 125.0	\$ 113.9
OTC derivatives								
Commodity swaps	\$ (405.7)	\$ (0.8)	\$ (0.6)	—	\$ (0.1)	—	\$ (407.2)	\$ (407.2)
Commodity options	\$ (20.1)	\$ (29.7)	\$ (6.7)	\$ (28.6)	\$ (1.2)	—	\$ (86.3)	\$ (86.3)
Equity options	\$ (10.6)	\$ (0.9)	—	—	—	\$ (22.4)	\$ (33.9)	\$ (33.9)
Credit default swaps	\$ (0.4)	—	—	—	\$ 2.3	\$ 0.1	\$ 2.0	\$ 2.0
Total return swaps	\$ (9.4)	—	—	—	—	—	\$ (9.4)	\$ (9.4)
Forward contracts	\$ (0.3)	—	—	\$ 0.5	—	—	\$ 0.2	\$ 0.2

Table of Contents

Item 8. Financial Statements and Supplementary Data.

INDEX TO FINANCIAL STATEMENTS

	<u>Page</u>
Management's Report on Internal Control over Financial Reporting	44
Report of Independent Registered Public Accounting Firm	45
Report of Independent Registered Public Accounting Firm	46
Consolidated Statements of Financial Condition as of December 31, 2007 and 2006	47
Consolidated Statements of Earnings for Each of the Years in the Three-Year Period Ended December 31, 2007	49
Consolidated Statements of Changes in Stockholders' Equity and Comprehensive Income for Each of the Years in the Three-Year Period Ended December 31, 2007	50
Consolidated Statements of Cash Flows for Each of the Years in the Three-Year Period Ended December 31, 2007	51
Notes to Consolidated Financial Statements	53

Management's Report on Internal Control over Financial Reporting

Our management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management evaluated our internal control over financial reporting as of December 31, 2007. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in *Internal Control — Integrated Framework*. As a result of this assessment and based on the criteria in this framework, management has concluded that, as of December 31, 2007, our internal control over financial reporting was effective.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

JEFFERIES GROUP, INC. :

We have audited the accompanying consolidated statements of financial condition of Jefferies Group, Inc. and subsidiaries (the Company) as of December 31, 2007 and 2006, and the related consolidated statements of earnings, changes in stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2007. These Consolidated Financial Statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these Consolidated Financial Statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the Consolidated Financial Statements referred to above present fairly, in all material respects, the financial position of Jefferies Group, Inc. and subsidiaries as of December 31, 2007 and 2006, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2007, in conformity with U.S. generally accepted accounting principles.

As more fully described in note 1 to the Consolidated Financial Statements, in 2006 the company changed its method of accounting for share based payments.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Jefferies Group, Inc.'s internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated February 28, 2008 expressed an unqualified opinion on the effectiveness of the Company's internal control over financial reporting.

/s/ KPMG LLP

KPMG LLP
New York, New York
February 28, 2008

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders

JEFFERIES GROUP, INC.:

We have audited Jefferies Group, Inc. and subsidiaries (the Company) internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying *Management's Report on Internal Control over Financial Reporting*. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Jefferies Group, Inc. and subsidiaries maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated statements of financial condition of Jefferies Group, Inc. and subsidiaries as of December 31, 2007 and 2006, and the related consolidated statements of earnings, changes in stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2007, and our report dated February 28, 2008 expressed an unqualified opinion on those Consolidated Financial Statements.

/s/ KPMG LLP

KPMG LLP
New York, New York
February 28, 2008

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Consolidated Statements of Financial Condition
December 31, 2007 and 2006
(Dollars in thousands, except per share amounts)**

	December 31, 2007	December 31, 2006
ASSETS		
Cash and cash equivalents	\$ 897,872	\$ 513,041
Cash and securities segregated and on deposit for regulatory purposes or deposited with clearing and depository organizations	659,219	508,303
Financial instruments owned, including securities pledged to creditors of \$1,087,906 and \$1,481,098 in 2007 and 2006, respectively:		
Corporate equity securities	2,266,679	1,737,174
Corporate debt securities	2,162,893	1,918,829
U.S. Government and agency obligations	730,921	592,374
Mortgage-backed securities	26,895	85,040
Asset-backed securities	—	28,009
Derivatives	501,502	234,646
Investments at fair value	104,199	97,289
Other	2,889	10,151
Total financial instruments owned	5,795,978	4,703,512
Investments in managed funds	293,523	372,869
Other investments	78,715	28,244
Securities borrowed	16,422,130	9,711,894
Securities purchased under agreements to resell	3,372,294	226,176
Receivable from brokers, dealers and clearing organizations	508,926	254,580
Receivable from customers	764,833	663,552
Premises and equipment	141,472	91,375
Goodwill	344,063	257,321
Other assets	514,792	494,590
Total Assets	<u>\$29,793,817</u>	<u>\$17,825,457</u>

See accompanying notes to Consolidated Financial Statements.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Consolidated Statements of Financial Condition — (Continued)
December 31, 2007 and 2006
(Dollars in thousands, except per share amounts)**

	December 31, 2007	December 31, 2006
LIABILITIES AND STOCKHOLDERS' EQUITY		
Bank loans and current portion of long-term debt	\$ 280,378	\$ 99,981
Financial instruments sold, not yet purchased:		
Corporate equity securities	1,389,099	1,835,046
Corporate debt securities	1,407,387	1,185,400
U.S. Government and agency obligations	206,090	339,891
Derivatives	331,788	240,231
Other	314	301
Total financial instruments sold, not yet purchased	3,334,678	3,600,869
Securities loaned	7,681,464	6,794,554
Securities sold under agreements to repurchase	11,325,562	2,092,838
Payable to brokers, dealers and clearing organizations	874,028	669,196
Payable to customers	1,415,803	1,010,486
Accrued expenses and other liabilities	627,597	650,974
	<u>25,539,510</u>	<u>14,918,898</u>
Long-term debt	1,764,067	1,168,562
Mandatorily redeemable convertible preferred stock	125,000	125,000
Minority interest	603,696	31,910
Total Liabilities	<u>28,032,273</u>	<u>16,244,370</u>
STOCKHOLDERS' EQUITY		
Common stock, \$.0001 par value. Authorized 500,000,000 shares; issued 155,375,808 shares in 2007 and 145,628,024 shares in 2006	16	14
Additional paid-in capital	1,115,011	876,393
Retained earnings	1,031,764	952,263
Less:		
Treasury stock, at cost, 30,922,634 shares in 2007 and 26,081,110 shares in 2006	(394,406)	(254,437)
Accumulated other comprehensive gain:		
Currency translation adjustments	10,986	9,764
Additional minimum pension liability	(1,827)	(2,910)
Total accumulated other comprehensive gain	<u>9,159</u>	<u>6,854</u>
Total stockholders' equity	<u>1,761,544</u>	<u>1,581,087</u>
Total Liabilities and Stockholders' Equity	<u>\$29,793,817</u>	<u>\$17,825,457</u>

See accompanying notes to Consolidated Financial Statements.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Consolidated Statements of Earnings
For each of the years in the three-year period ended December 31, 2007
(In thousands, except per share amounts)**

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Revenues:			
Commissions	\$ 355,601	\$ 280,681	\$ 246,943
Principal transactions	390,374	468,002	349,489
Investment banking	750,192	540,596	495,014
Asset management fees and investment income from managed funds	23,534	109,550	82,052
Interest	1,174,883	528,882	304,053
Other	24,311	35,497	20,322
Total revenues	<u>2,718,895</u>	<u>1,963,208</u>	<u>1,497,873</u>
Interest expense	<u>1,150,805</u>	<u>505,606</u>	<u>293,173</u>
Revenues, net of interest expense	<u>1,568,090</u>	<u>1,457,602</u>	<u>1,204,700</u>
Non-interest expenses:			
Compensation and benefits	946,309	791,255	669,957
Floor brokerage and clearing fees	71,851	62,564	46,644
Technology and communications	103,763	80,840	67,666
Occupancy and equipment rental	76,765	59,792	47,040
Business development	56,594	48,634	42,512
Other	67,074	65,863	62,474
Total non-interest expenses	<u>1,322,356</u>	<u>1,108,948</u>	<u>936,293</u>
Earnings before income taxes, minority interest and cumulative effect of change in accounting principle	245,734	348,654	268,407
Income taxes	93,178	137,541	104,089
Earnings before minority interest and cumulative effect of change in accounting principle	152,556	211,113	164,318
Minority interest in earnings of consolidated subsidiaries, net	7,891	6,969	6,875
Earnings before cumulative effect of change in accounting principle, net	144,665	204,144	157,443
Cumulative effect of change in accounting principle, net	—	1,606	—
Net earnings	<u>\$ 144,665</u>	<u>\$ 205,750</u>	<u>\$ 157,443</u>
Earnings per share:			
Basic-			
Earnings before cumulative effect of change in accounting principle, net	\$ 1.02	\$ 1.53	\$ 1.27
Cumulative effect of change in accounting principle, net	—	0.01	—
Net earnings	<u>\$ 1.02</u>	<u>\$ 1.54</u>	<u>\$ 1.27</u>
Diluted-			
Earnings before cumulative effect of change in accounting principle, net	\$ 0.97	\$ 1.41	\$ 1.16
Cumulative effect of change in accounting principle, net	—	0.01	—
Net earnings	<u>\$ 0.97</u>	<u>\$ 1.42</u>	<u>\$ 1.16</u>
Weighted average shares of common stock:			
Basic	141,515	133,898	123,646
Diluted	153,807	147,531	135,569

See accompanying notes to Consolidated Financial Statements.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

Consolidated Statements of Changes in Stockholders' Equity and Comprehensive Income
For each of the years in the three-year period ended December 31, 2007
(Dollars in thousands, except per share amounts)

	Year Ended December 31,		
	2007	2006	2005
Common stock, par value \$0.0001 per share			
Balance, beginning of year	14	7	7
Issued / stock dividend	2	7	—
Balance, end of year	<u>16</u>	<u>14</u>	<u>7</u>
Additional paid in capital			
Balance, beginning of year	876,393	709,447	508,221
Benefit plan share activity (1)	38,053	33,360	13,432
Share-based amortization expense	144,382	83,137	100,217
Proceeds from exercise of stock options	5,233	17,543	33,661
Acquisitions and contingent consideration	9,240	—	26,998
Tax benefits for issuance of stock-based awards	41,710	32,906	26,918
Balance, end of year	<u>1,115,011</u>	<u>876,393</u>	<u>709,447</u>
Retained earnings			
Balance, beginning of year	952,263	803,262	677,464
Cumulative effect of adjustment from adoption of FIN 48	(410)	—	—
Net earnings	144,665	205,750	157,443
Dividends	(64,754)	(56,749)	(31,645)
Balance, end of year	<u>1,031,764</u>	<u>952,263</u>	<u>803,262</u>
Treasury stock, at cost			
Balance, beginning of year	(254,437)	(220,703)	(149,039)
Purchases	(147,809)	(23,972)	(76,291)
Returns / forfeitures	(7,785)	(9,762)	(6,717)
Issued	15,625	—	11,344
Balance, end of year	<u>(394,406)</u>	<u>(254,437)</u>	<u>(220,703)</u>
Accumulated other comprehensive income (loss)			
Balance, beginning of year	6,854	(5,163)	2,480
Currency adjustment, net of tax	1,222	8,802	(8,386)
Pension adjustment, net of tax	1,083	3,215	743
Balance, end of year	<u>9,159</u>	<u>6,854</u>	<u>(5,163)</u>
Total stockholders' equity	<u>1,761,544</u>	<u>1,581,087</u>	<u>1,286,850</u>
Comprehensive income			
Net earnings	144,665	205,750	157,443
Other comprehensive income (loss), net of tax	2,305	12,017	(7,643)
Total comprehensive income	<u>146,970</u>	<u>217,767</u>	<u>149,800</u>

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

See accompanying notes to Consolidated Financial Statements.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

Consolidated Statements of Cash Flows
Three years ended December 31, 2007
(Dollars in thousands)

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Cash flows from operating activities:			
Net earnings	\$ 144,665	\$ 205,750	\$ 157,443
Adjustments to reconcile net earnings to net cash (used in) provided by operating activities:			
Cumulative effect of accounting change, net	—	(1,606)	—
Depreciation and amortization	27,863	19,891	15,556
Accruals related to various benefit plans, stock issuances, net of forfeitures	174,652	109,505	118,276
Deferred income taxes	(6,269)	(37,982)	(23,475)
Minority interest	7,891	6,969	6,875
(Increase) decrease in cash and securities segregated and on deposit for regulatory purposes or deposited with clearing and depository organizations	(150,883)	120,862	(75,640)
(Increase) decrease in receivables:			
Securities borrowed	(6,710,158)	(1,568,414)	2,089,418
Brokers, dealers and clearing organizations	(296,599)	149,026	(92,263)
Customers	(101,261)	(186,651)	(105,113)
Increase in financial instruments owned	(788,715)	(2,777,970)	(579,779)
Increase in other investments	(35,955)	(16,084)	(12,160)
Decrease (increase) in investments in managed funds	20,653	(94,753)	(82,134)
Increase in securities purchased under agreements to resell	(3,146,118)	(226,176)	—
Increase in other assets	(21,559)	(65,031)	(34,020)
Increase (decrease) in payables:			
Securities loaned	920,290	(934,990)	(1,601,436)
Brokers, dealers and clearing organizations	282,117	347,797	(58,856)
Customers	405,368	183,265	127,959
(Decrease) increase in financial instruments sold, not yet purchased	(336,498)	2,300,552	180,144
Increase in securities sold under agreements to repurchase	9,232,724	2,092,838	—
(Decrease) increase in accrued expenses and other liabilities	(51,785)	103,636	182,275
Net cash (used in) provided by operating activities	<u>(429,577)</u>	<u>(269,566)</u>	<u>213,070</u>
Cash flows from investing activities:			
Decrease (increase) in short-term bond funds	—	7,037	(176)
Purchase of premises and equipment	(76,893)	(39,342)	(27,186)
Business acquisitions, net of cash received	(33,437)	—	(53,030)
Cash paid for contingent consideration	(25,720)	(19,944)	(8,925)
Net cash flows used in investing activities	<u>(136,050)</u>	<u>(52,249)</u>	<u>(89,317)</u>

Continued on next page.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

Consolidated Statements of Cash Flows — (Continued)
Three years ended December 31, 2007
(Dollars in thousands)

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Cash flows from financing activities:			
Tax benefits from the issuance of stock-based awards	41,710	32,906	—
Proceeds from reorganization of high yield secondary market trading	361,735	—	—
Redemptions and distributions related to our reorganization of high yield secondary market trading	(31,858)	—	—
Repayment of long-term debt	(100,000)	—	—
Net proceeds from (payments on):			
Bank loans	280,386	—	(70,000)
Issuance of senior notes	593,176	492,155	—
Termination of interest rate swaps	8,452	—	—
Issuance of mandatorily redeemable convertible preferred stock	—	125,000	—
Minority interest holders of consolidated subsidiaries related to asset management activities	3,849	(11,553)	(5,467)
Repurchase of treasury stock	(147,809)	(23,972)	(76,291)
Dividends	(64,754)	(56,749)	(31,645)
Exercise of stock options, not including tax benefits	5,233	17,543	33,661
Net cash provided by (used in) financing activities	<u>950,120</u>	<u>575,330</u>	<u>(149,742)</u>
Effect of foreign currency translation on cash and cash equivalents			
Net increase (decrease) in cash and cash equivalents	<u>384,831</u>	<u>257,108</u>	<u>(28,178)</u>
Cash and cash equivalents at beginning of year	<u>513,041</u>	<u>255,933</u>	<u>284,111</u>
Cash and cash equivalents at end of year	<u>\$ 897,872</u>	<u>\$513,041</u>	<u>\$ 255,933</u>

Supplemental disclosures of cash flow information:

Cash paid during the year for:			
Interest	\$1,133,861	\$492,179	\$ 283,318
Income taxes	69,973	198,294	87,013
Acquisitions:			
Fair value of assets acquired, including goodwill	\$ 61,999		\$ 95,118
Liabilities assumed	(6,150)		(13,854)
Stock issued	(22,412)		(26,998)
Cash paid for acquisition	33,437		54,266
Cash acquired in acquisition	—		1,435
Net cash paid for acquisition	33,437		52,831

Supplemental disclosure of non-cash financing activities:

Non-cash proceeds from reorganization of high yield secondary market trading	230,169	—	—
------------------------------------------------------------------------------	---------	---	---

In 2005, the additional minimum pension liability included in stockholders' equity of \$6,125 resulted from a decrease of \$743 to accrued expenses and other liabilities and an offsetting increase in stockholders' equity. In 2006, the additional minimum pension liability included in stockholders' equity of \$2,910 resulted from a decrease of \$3,215 to accrued expenses and other liabilities and an offsetting increase in stockholders' equity. In 2007, the additional minimum pension liability included in stockholders' equity of \$1,827 resulted from a decrease of \$1,083 to accrued expenses and other liabilities and an offsetting increase in stockholders' equity.

See accompanying notes to Consolidated Financial Statements.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**
Notes to Consolidated Financial Statements
December 31, 2007 and 2006

Index

Note	Page
(1) Organization and Summary of Significant Accounting Policies	54
(2) Asset Management Fees and Investment Income From Managed Funds	65
(3) Cash, Cash Equivalents, and Short-Term Investments	67
(4) Receivable from, and Payable to, Customers	67
(5) Financial Instruments Owned and Financial Instruments Sold, Not Yet Purchased	68
(6) Premises and Equipment	70
(7) Short-Term Borrowings	70
(8) Long-Term Debt	70
(9) Mandatorily Redeemable Convertible Preferred Stock	71
(10) Income Taxes	71
(11) Defined Benefit Plan	74
(12) Minority Interest	76
(13) Earnings Per Share	77
(14) Leases	78
(15) Derivative Financial Instruments	78
(16) Other Comprehensive Income (Loss)	82
(17) Net Capital Requirements	83
(18) Commitments and Guarantees	83
(19) Segment Reporting	85
(20) Goodwill	87
(21) Quarterly Dividends	88
(22) Variable Interest Entities (“VIEs”)	88
(23) High Yield Secondary Market Trading	89
(24) Jefferies Finance LLC	89
(25) Stock-Based Compensation	90
(26) Selected Quarterly Financial Data (Unaudited)	95

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(1) Organization and Summary of Significant Accounting Policies

Organization

The accompanying audited Consolidated Financial Statements include the accounts of Jefferies Group, Inc. and all its subsidiaries (together, “we” or “us”), including Jefferies & Company, Inc. (“Jefferies”), Jefferies Execution Services, Inc., (“Jefferies Execution”), Jefferies International Limited, Jefferies Asset Management, LLC, Jefferies Financial Products, LLC and all other entities in which we have a controlling financial interest or are the “primary beneficiary”, including Jefferies High Yield Holdings, LLC (“JHYH”), Jefferies Special Opportunities Partners, LLC (“JSOP”) and Jefferies Employees Special Opportunities Partners, LLC (“JESOP”). The accompanying Consolidated Financial Statements have been prepared in accordance with U.S. generally accepted accounting principles for financial information and with the instructions to Form 10-K.

Reclassifications

Starting in the third quarter of 2007, we include investments and investments in managed funds as a component of cash flows from operating activities rather than cash flows from investing activities and accordingly have reclassified the prior period to be consistent with the current presentation. We believe that a change in classification of a cash flow item represents a reclassification of information and not a change in accounting principle. The amounts involved are immaterial to the Consolidated Financial Statements taken as a whole. In addition, the change only affects the presentation within the Consolidated Statements of Cash Flows and does not impact the Consolidated Statements of Financial Condition or the Consolidated Statements of Earnings, debt balances or compliance with debt covenants.

Certain other reclassifications have been made to previously reported balances to conform to the current presentation.

Common Stock

On April 18, 2006, we declared a 2-for-1 split of all outstanding shares of our common stock, payable May 15, 2006 to stockholders of record as of April 28, 2006. The stock split was effected as a stock dividend of one share for each one share outstanding on the record date. All share, share price and per share information included in this annual report, including the Consolidated Financial Statements and the notes thereto, have been restated to retroactively reflect the effect of the 2-for-1 stock split.

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements – (Continued)
December 31, 2007 and 2006

Summary of Significant Accounting Policies

Principles of Consolidation

Our policy is to consolidate all entities in which we own more than 50% of the outstanding voting stock and have control. In addition, in accordance with Financial Accounting Standards Board (“FASB”) Interpretation No. 46(R), *Consolidation of Variable Interest Entities* (“FIN 46(R)”), as revised, we consolidate entities which lack characteristics of an operating entity or business for which we are the primary beneficiary. Under FIN 46(R), the primary beneficiary is the party that absorbs a majority of the entity’s expected losses, receives a majority of its expected residual returns, or both, as a result of holding variable interests, direct or implied. In situations where we have significant influence but not control of an entity that does not qualify as a variable interest entity, we apply the equity method of accounting or fair value accounting. We also have formed nonconsolidated investment vehicles with third-party investors that are typically organized as limited partnerships. We act as general partner for these investment vehicles and have generally provided the third-party investors with termination or “kick-out” rights as defined by Emerging Issues Task Force (“EITF”) EITF 04-5, *Determining Whether a General Partner, or the General Partners as a Group, Controls a Limited Partnership or Similar Entity When the Limited Partners Have Certain Rights*.

All material intercompany accounts and transactions are eliminated in consolidation.

Revenue Recognition Policies

Commissions. All customer securities transactions are reported on the Consolidated Statement of Financial Condition on a settlement date basis with related income reported on a trade-date basis. Under clearing agreements, we clear trades for unaffiliated correspondent brokers and retain a portion of commissions as a fee for our services. Correspondent clearing revenues are included in Other revenue. We permit institutional customers to allocate a portion of their gross commissions to pay for research products and other services provided by third parties. The amounts allocated for those purposes are commonly referred to as soft dollar arrangements. Soft dollar expenses amounted to \$39.3 million, \$32.1 million and \$37.7 million for 2007, 2006 and 2005 respectively. We are accounting for the cost of these arrangements on an accrual basis. Our accounting for commission revenues includes the guidance contained in EITF 99-19, *Reporting Revenues Gross versus Net*, because we are not the primary obligor of such arrangements, and accordingly, expenses relating to soft dollars are netted against the commission revenues.

Principal Transactions. Financial instruments owned, securities pledged and financial instruments sold, but not yet purchased (all of which are recorded on a trade-date basis) are carried at fair value with unrealized gains and losses reflected in principal transactions in the Consolidated Statement of Earnings on a trade date basis.

Investment Banking. Underwriting revenues and fees from mergers and acquisitions, restructuring and other investment banking advisory assignments are recorded when the services related to the underlying transaction are completed under the terms of the assignment or engagement. Expenses associated with such transactions are deferred until reimbursed by the client, the related revenue is recognized or the engagement is otherwise concluded. Expenses are recorded net of client reimbursements. Revenues are presented net of related unreimbursed expenses. Unreimbursed expenses with no related revenues are included in business development in the consolidated statement of earnings. Reimbursed expenses totaled approximately \$11.2 million, \$17.9 million and \$16.3 million for the years ended December 31, 2007, 2006 and 2005 respectively.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

Asset Management Fees and Investment Income From Managed Funds. Asset management fees and investment income from managed funds include revenues we receive from management, administrative and performance fees from funds managed by us, revenues from management and performance fees we receive from third-party managed funds, and investment income from our investments in these funds. We receive fees in connection with management and investment advisory services performed for various funds and managed accounts. These fees are based on the value of assets under management and may include performance fees based upon the performance of the funds. Management and administrative fees are generally recognized over the period that the related service is provided based upon the beginning or ending Net Asset Value of the relevant period. Generally, performance fees are earned when the return on assets under management exceeds certain benchmark returns, “high-water marks”, or other performance targets. Performance fees are accrued on a monthly basis and are not subject to adjustment once the measurement period ends (annually) and performance fees have been realized.

Interest Revenue and Expense. We recognize contractual interest on financial instruments owned and financial instruments sold, but not yet purchased, on an accrual basis as a component of interest revenue and expense. Interest flows on derivative trading transactions and dividends are included as part of the mark-to-market valuation of these contracts in principal transactions in the Consolidated Statements of Earnings and are not recognized as a component of interest revenue or expense. We account for our short-term, long-term borrowings and our mandatorily redeemable convertible preferred stock on an accrual basis with related interest recorded as interest expense. In addition, we recognize interest revenue related to our securities borrowed activities and interest expense related to our securities loaned activities. See accounting policies related to securities borrowed and securities loaned for further explanation.

Cash Equivalents

Cash equivalents include highly liquid investments not held for resale with original maturities of three months or less.

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

In accordance with Rule 15c3-3 of the Securities Exchange Act of 1934, Jefferies & Company, Inc., as a broker-dealer carrying client accounts, is subject to requirements related to maintaining cash or qualified securities in a segregated reserve account for the exclusive benefit of its clients. In addition, certain financial instruments used for initial and variation margin purposes with clearing and depository organizations are recorded in this caption.

Foreign Currency Translation

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

Financial Instruments Owned and Financial Instruments Sold, not yet Purchased and Fair Value

Our financial instruments owned and financial instruments sold, not yet purchased are recorded at fair value, either through the fair value option election or as required by other accounting pronouncements. A description of our policies regarding fair value measurement and its application to these financial instruments follows. These instruments primarily represent our trading activities and include both cash and derivative products. Gains and losses on all of these instruments carried at fair value are reflected in principal transactions.

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

Definition of Fair Value

The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (the exit price). The use of fair value to measure financial instruments is fundamental to our financial statements and is a critical accounting policy. Unrealized gains or losses are generally recognized in principal transactions in our Consolidated Statements of Earnings. Financial instruments are valued at quoted market prices, if available. For financial instruments that do not have readily determinable fair values through quoted market prices, the determination of fair value is based upon consideration of available information, including types of financial instruments, current financial information, restrictions on dispositions, fair values of underlying financial instruments and quotations for similar instruments. Certain financial instruments have bid and ask prices that can be observed in the marketplace. Bid prices reflect the highest price that we and others are willing to pay for an asset. Ask prices represent the lowest price that we and others are willing to accept for an asset. For financial instruments whose inputs are based on bid-ask prices, we do not require that fair value always be a predetermined point in the bid-ask range. Our policy is to allow for mid-market pricing and adjusting to the point within the bid-ask range that meets our best estimate of fair value. For offsetting positions in the same financial instrument, the same price within the bid-ask spread is used to measure both the long and short positions.

Fair Value Hierarchy

We adopted FASB 157, *Fair Value Measurements* (“FASB 157”), as of the beginning of 2007. FASB 157 defines fair value, establishes a framework for measuring fair value, establishes a fair value hierarchy based on the inputs used to measure fair value and enhances disclosure requirements for fair value measurements. FASB 157 establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the observable inputs be used when available. Observable inputs are inputs that market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of us. Unobservable inputs are inputs that reflect our assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. The hierarchy is broken down into three levels based on the reliability of inputs as follows:

- Level 1: Quoted prices are available in active markets for identical assets or liabilities as of the reported date. The type of financial instruments included in Level 1 are highly liquid cash instruments with quoted prices such as G-7 government, agency securities, listed equities and money market securities, as well as listed derivative instruments;
- Level 2: Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these financial instruments include cash instruments for which quoted prices are available but traded less frequently, derivative instruments whose fair value have been derived using a model where inputs to the model are directly observable in the market, or can be derived principally from or corroborated by observable market data, and instruments that are fair valued using other financial instruments, the parameters of which can be directly observed. Instruments which are generally included in this category are corporate bonds, convertible bonds, municipal bonds and OTC derivatives;
- Level 3: Instruments that have little to no pricing observability as of the reported date. These financial instruments do not have two-way markets and are measured using management’s best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation. Instruments that are included in this category generally include certain illiquid equity securities, commercial loans and loan commitments, investments, distressed debt, as well as certain highly structured OTC derivative contracts.

Valuation Process for Financial Instruments

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

The overall valuation process for financial instruments may include adjustments to valuations derived from pricing models. These adjustments may be made when, in management's judgment, either the size of the position in the financial instrument or other features of the financial instrument such as its complexity, or the market in which the financial instrument is traded (such as counterparty, credit, concentration or liquidity) require that an adjustment be made to the value derived from the pricing models. An adjustment may be made if a trade of a financial instrument is subject to sales restrictions that would result in a price less than the computed fair value measurement from a quoted market price. Additionally, an adjustment from the price derived from a model typically reflects management's judgment that other participants in the market for the financial instrument being measured at fair value would also consider such an adjustment in pricing that same financial instrument.

Valuation Models Used to Determine Fair Value

Non-derivative financial assets and liabilities presented at fair value and categorized as Level 3 are generally those that are based on an assessment of each underlying investment, incorporating valuations that consider the evaluation of financing and sale transactions with third parties, expected cash flows models, market-based information, including comparable company transactions, performance multiples and changes in market outlook, among other factors. Derivative financial instruments are generally those that are marked-to-model using relevant empirical data to estimate fair value. The models' inputs reflect assumptions that market participants would use in pricing the instrument in a current period transaction and outcomes from the models represent an assumed exit price and expected future cash flows. Our valuation models are calibrated to the market on a frequent basis. The parameters and inputs are adjusted for assumptions about risk and current market conditions. Changes to inputs in valuation models are not necessarily changes to valuation methodologies; rather, the inputs are modified to reflect direct or indirect impacts on asset classes from changes in market conditions. Accordingly, results from valuation models in one period may not be indicative of future period measurements.

Derivatives

We have derivative financial instrument positions in exchange traded and over-the-counter option contracts, credit default swaps, foreign exchange forward contracts, index futures contracts, commodities swap and option contracts and commodities futures contracts, which are measured at fair value with gains and losses recognized in principal transactions. The gross contracted or notional amount of these contracts is not reflected in the Consolidated Statements of Financial Condition. We follow FIN 39, *Offsetting Amounts Related to Certain Contracts* ("FIN 39") and offset assets and liabilities in the Consolidated Statements of Financial Condition provided that the legal right of offset exists under a master netting agreement and that other requirements of FIN 39 are met. We also offset payables or receivables relating to the fair value of cash collateral received or paid associated with our derivative inventory, on a counterparty basis provided that all FIN 39 criteria are met.

Prior to the adoption of FASB 157, *Fair Value Measurements* ("FASB 157"), we followed Emerging Issues Task Force Statement No. 02-3, *Issues Involved in Accounting for Derivative Contracts Held for Trading Purposes and Contracts Involved in Energy Trading and Risk Management Activities* ("EITF 02-3"). This guidance generally prohibited recognizing profit at the inception of a derivative contract unless the fair value of the derivative was obtained from a quoted market price in an active market or was otherwise evidenced by comparison to other observable current market transactions or based on a valuation technique that incorporates observable market data. Subsequent to the transaction date, we recognized trading profits deferred at inception of the derivative transaction in the period in which the valuation of an instrument became observable. With the adoption of FASB 157, we are no longer applying the revenue recognition criteria of EITF 02-3. However, FASB 157 requires that a fair value measurement reflect the assumptions market participants would use in pricing an asset or liability based on the best information available, which includes the transaction exit price, and therefore this change did not have a significant impact on our results of operations.

Investments in Managed Funds

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

Investments in managed funds includes our investments in funds managed by us and our investments in third-party managed funds in which we are entitled to a portion of the management and/or performance fees. Investments in managed funds are accounted for on the equity method. Gains or losses on our investments in managed funds are included in asset management fees and investment income from managed funds in the Consolidated Statements of Earnings.

Other Investments

Other investments includes investments entered into where we exercise significant influence over operating and capital decisions in private equity and other operating entities in connection with our capital market activities. Other investments are accounted for on the equity method.

Receivable from, and Payable to, Customers

Receivable from, and payable to, customers includes amounts receivable and payable on cash and margin transactions. Securities owned by customers and held as collateral for these receivables are not reflected in the accompanying Consolidated Financial Statements. Receivable from officers and directors represents balances arising from their individual security transactions. These transactions are subject to the same regulations as customer transactions and are provided on substantially the same terms.

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

Securities Borrowed and Securities Loaned

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

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

Due to their short-term nature, Securities purchased under agreements to resell and securities sold under agreements to repurchase (“repos”) are carried at cost which approximates fair value. Repos are treated as collateralized financing transactions and are recorded at their contracted repurchase amount which approximates fair value. We earn net interest revenues from this activity which is reflected in our Consolidated Statements of Operations.

We monitor the fair value of the repos daily versus the related receivable or payable balances. Should the fair value of the repos decline or increase, additional collateral is requested or excess collateral is returned, as appropriate.

We carry repos on a net basis when permitted under the provisions of FASB Interpretation No. 41, *Offsetting of Amounts Related to Certain Repurchase and Reverse Repurchase Agreements* (“FIN 41”).

Premises and Equipment

Premises and equipment are depreciated using the straight-line method over the estimated useful lives of the related assets (generally three to ten years). Leasehold improvements are amortized using the straight-line method over the term of the related leases or the estimated useful lives of the assets, whichever is shorter.

Goodwill

At least annually, we assess whether goodwill has been impaired by comparing the estimated fair value, calculated based on earnings and book value multiples, of each business segment with its estimated net book value, by estimating the amount of stockholders’ equity required to support each business segment. Periodically estimating the fair value of a reporting unit requires significant judgment and often involves the use of significant estimates and assumptions. These estimates and assumptions could have a significant effect on whether or not an impairment charge is recorded and the magnitude of such a charge. We completed our last impairment test on goodwill as of September 30, 2007, and no impairment was identified.

Our Jefferies Execution subsidiary recorded a goodwill impairment charge of \$26 million during the fourth quarter of 2007. Jefferies Execution is a registered broker-dealer. Therefore, goodwill relating to the acquisition of Jefferies Execution in 2001, formerly Helfant Group, Inc., was “pushed down” from us to Jefferies Execution in accordance with Emerging Issues Task Force Issue No. D-97, *Push Down Accounting*.

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

We have two reporting units, Capital Markets and Asset Management, as defined by FASB 142, *Goodwill and Other Intangible Assets*. Jefferies Execution is not a reporting unit of ours and we have not recorded this \$26 million goodwill impairment charge to our Consolidated Financial Statements.

Income Taxes

We file a consolidated U.S. Federal income tax return, which includes all of our qualifying subsidiaries. We also are subject to income tax in various states and municipalities and those foreign jurisdictions in which we operate. Amounts provided for income taxes are based on income reported for financial statement purposes and do not necessarily represent amounts currently payable. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred income taxes are provided for temporary differences in reporting certain items, principally deferred compensation, unrealized gains and losses on investments, and tax amortization on intangible assets. The realization of deferred tax assets is assessed and a valuation allowance is recorded to the extent that it is more likely than not that any portion of the deferred tax asset will not be realized. Tax credits are recorded as a reduction of income taxes when realized.

Legal Reserves

We recognize a liability for a contingency when it is probable that a liability has been incurred and when the amount of loss can be reasonably estimated. When a range of probable loss can be estimated, we accrue the most likely amount of such loss, and if such amount is not determinable, then we accrue the minimum of the range of probable loss.

We record reserves related to legal proceedings in accrued expenses and other liabilities. Such reserves are established and maintained in accordance with FASB 5, *Accounting for Contingencies*, and FASB Interpretation No. 14, *Reasonable Estimation of the Amount of a Loss and Interpretation of FASB Statement No. 5*. The determination of these reserve amounts requires significant judgment on the part of management. Our management considers many factors including, but not limited to: the amount of the claim; the basis and validity of the claim; previous results in similar cases; and legal precedents and case law. Each legal proceeding is reviewed with counsel in each accounting period and the reserve is adjusted as deemed appropriate by management.

Stock-based Compensation

Under FASB 123, *Accounting for Stock-Based Compensation*, we defined the service period (over which compensation cost should be recognized) to generally include the year prior to the grant and the subsequent vesting period. With the adoption of FASB 123R on January 1, 2006, our policy regarding the timing of expense recognition for non-retirement eligible employees changed to recognize compensation cost over the period from the service inception date, which is the grant date, through the date the employee is no longer required to provide service to earn the award.

In addition, with the adoption of FASB 123R on January 1, 2006, the awards granted to retirement eligible employees where the award does not contain future service requirements must be either expensed on the date of grant or, in certain circumstances, may be accrued in the periods prior to the grant date. Subsequent to the adoption of FASB 123R, we made certain changes to the terms of certain new grants which effectively eliminated accelerated expense recognition upon retirement and/or increased the retirement eligibility age and years of service from those generally provided for in prior grants. During the fourth quarter of 2007, we undertook a comprehensive review of the retirement eligibility requirements of certain share-based awards, examining the impact to both us and our employees. Upon completion of this review during the fourth quarter of 2007, we determined that future share-based grants should contain more stringent provisions that include increased length of service requirements for

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

certain senior level employees to be eligible to retire and retain the award. As a result of this comprehensive review, we reversed \$8.2 million of previously accrued compensation and benefits expense during the fourth quarter of 2007. The \$8.2 million reversal will be amortized over the subsequent three year period.

Earnings per Common Share

Basic earnings per share of common stock are computed by dividing net earnings by the average number of shares outstanding and certain other shares committed to be, but not yet issued. Basic earnings per share include restricted stock and RSUs for which no future service is required. Diluted earnings per share of common stock are computed by dividing net earnings plus dividends on mandatorily redeemable convertible preferred stock divided by the average number of shares outstanding of common stock and all dilutive common stock equivalents outstanding during the period. Diluted earnings per share include the dilutive effects of restricted stock and RSUs for which future service is required.

Accounting and Regulatory Developments

FASB Interpretation No. 48 . In July 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (“FIN 48”). FIN 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. We adopted FIN 48 as of the beginning of 2007. The transition adjustment to beginning retained earnings was a reduction of approximately \$0.4 million.

FASB 157 . In September 2006, the FASB issued FASB 157, *Fair Value Measurements* (“FASB 157”). FASB 157 clarifies that fair value is the amount that would be exchanged to sell an asset or transfer a liability, in an orderly transaction between market participants. FASB 157 reverses the consensus reached in EITF Issue No. 02-3 prohibiting the recognition of day one gain or loss on derivative contracts where we cannot verify all of the significant model inputs to observable market data and verify the model to market transactions. However, FASB 157 requires that a fair value measurement technique include an adjustment for risks inherent in a particular valuation technique (such as a pricing model) and/or the risks inherent in the inputs to the model, if market participants would also include such an adjustment. In addition, FASB 157 prohibits the recognition of “block discounts” for large holdings of unrestricted financial instruments where quoted prices are readily and regularly available in an active market. The provisions of FASB 157 are to be applied prospectively, except for changes in fair value measurements that result from the initial application of FASB 157 to existing derivative financial instruments measured under EITF Issue No. 02-3 and block discounts, which are to be recorded as an adjustment to opening retained earnings in the year of adoption. FASB 157 is effective for fiscal years beginning after November 15, 2007. We adopted FASB 157 as of the beginning of 2007. To determine the transition adjustment to opening retained earnings, we performed an analysis of existing derivative instruments measured under EITF Issue 02-3 and block discounts, and determined that there was no transition adjustment to opening retained earnings as of January 1, 2007.

FASB 158. In September 2006, the FASB issued Statement No. 158, *Accounting for Uncertainty in Employers’ Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)* (“FASB 158”). FASB 158 improves financial reporting by requiring an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan (other than a multiemployer plan) as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. This Statement also improves financial reporting by requiring an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. An employer with publicly traded equity securities is required to initially recognize the funded status of a defined benefit postretirement plan and to provide the required disclosures as of the end of the fiscal year ending after December 15, 2006. The requirement to measure plan assets and benefit obligations as of the date of the employer’s fiscal year-end statement of financial position is effective for fiscal

JEFFERIES GROUP, INC.
AND SUBSIDIARIESNotes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

years ending after December 15, 2008. On December 31, 2006, we adopted the recognition and disclosure provisions of FASB 158. FASB 158 required us to recognize the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of our benefit plan on our December 31, 2006 Consolidated Statement of Financial Condition, with a corresponding adjustment to accumulated other comprehensive income, net of tax. As a result of the pension plan being frozen, the projected benefit obligation was equal to the accumulated benefit obligation. Consequently, no additional adjustment to accumulated other comprehensive income was necessary as of December 31, 2006.

FASB 159. In February 2007, the FASB issued FASB 159, *The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of FASB Statement No. 115* (“FASB 159”). This standard permits an entity to measure financial instruments and certain other items at estimated fair value. Most of the provisions of FASB 159 are elective; however, the amendment to FASB 115, *Accounting for Certain Investments in Debt and Equity Securities*, applies to all entities that own trading and available-for-sale securities. The fair value option created by FASB 159 permits an entity to measure eligible items at fair value as of specified election dates. The fair value option (a) may generally be applied instrument by instrument, (b) is irrevocable unless a new election date occurs, and (c) must be applied to the entire instrument and not to only a portion of the instrument. FASB 159 allows for a one-time election for existing positions upon adoption, with the transition adjustment recorded to opening retained earnings. FASB 159 is effective as of the beginning of the first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of the previous fiscal year provided that the entity (i) makes that choice in the first 120 days of that year, (ii) has not yet issued financial statements for any interim period of such year, and (iii) elects to apply the provisions of FASB 157. We adopted FASB 159 as of the beginning of 2007. We elected to apply the fair value option on loans and loan commitments made in connection with our investment banking activities (“loans and loan commitments”). Loans and loan commitments are included in financial instruments owned on the Consolidated Statement of Financial Condition. At the time of adoption, we did not have such loans and loan commitments outstanding, therefore there was no transition adjustment recorded to opening retained earnings. In addition, we elected to apply the fair value option on certain investments held by subsidiaries that are not registered broker-dealers as defined in the AICPA Audit and Accounting Guide, *Brokers and Dealers in Securities*. These investments had been accounted for by us at fair value prior to the adoption of FASB 159; therefore, there was no transition adjustment recorded to opening retained earnings related to these investments. The fair value option was elected for loans and loan commitments and investments held by subsidiaries that are not registered broker-dealers because they are risk managed by us on a fair value basis.

FSP FIN 39-1. In April 2007, the FASB issued a Staff Position (“FSP”) FIN 39-1, *Amendment of FASB Interpretation No. 39*. FSP FIN No. 39-1 defines “right of setoff” and specifies what conditions must be met for a derivative contract to qualify for this right of setoff. It also addresses the applicability of a right of setoff to derivative instruments and clarifies the circumstances in which it is appropriate to offset amounts recognized for those instruments in the statement of financial position. In addition, this FSP permits offsetting of fair value amounts recognized for multiple derivative instruments executed with the same counterparty under a master netting arrangement and fair value amounts recognized for the right to reclaim cash collateral (a receivable) or the obligation to return cash collateral (a payable) arising from the same master netting arrangement as the derivative instruments. The provisions of this FSP are consistent with our current accounting practice. This interpretation is effective for fiscal years beginning after November 15, 2007, with early application permitted. The adoption of FSP FIN No. 39-1 on January 1, 2008 did not have a material impact on our Consolidated Financial Statements.

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

EITF Issue No. 06-11. In June 2007, the FASB ratified the consensus reached by the Emerging Issues Task Force on Issue 06-11, *Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards* (“EITF 06-11”). EITF 06-11 requires that the tax benefit related to dividends or dividend equivalents that are charged to retained earnings and are paid to employees for equity classified nonvested equity shares, nonvested equity share units, and outstanding equity share options be recorded as an increase in additional paid-in capital. We currently account for this tax benefit as a reduction to income tax expense. EITF 06-11 is to be applied prospectively for tax benefits on dividends declared in fiscal years beginning after December 15, 2007. We intend to adopt EITF 06-11 in the first quarter of 2008. We are currently evaluating the impact of EITF 06-11 on our results of operations for the first quarter of 2008.

SOP No. 07-1 and FSP FIN No. 46R-7. In June 2007, the American Institute of Certified Public Accountants issued Statement of Position No. 07-1, *Clarification of the Scope of the Audit and Accounting Guide ‘Audits of Investment Companies’ and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies* (“SOP 07-1”). SOP 07-1 clarifies the scope of when an entity may apply the provisions of the AICPA Audit and Accounting Guide Investment Companies (“the Guide”). SOP 07-1 also provides guidance for determining whether the specialized industry accounting principles of the Guide should be retained in the financial statements of a parent company of an investment company or an equity method investor in an investment company, and includes certain disclosure requirements. In May 2007, the FASB issued FSP FIN No. 46R-7, *Application of FIN 46R to Investment Companies* (“FSP FIN 46R-7”). FSP FIN 46R-7 amends FIN 46R to make permanent the temporary deferral of the application of FIN 46R to entities within the scope of the revised Guide under SOP 07-1. FSP FIN 46R-7 is effective upon the adoption of SOP 07-1. In November, the FASB issued a proposed FSP SOP No. 07-1-a, *The Effective Date of AICPA Statement of Position 07-1*, which proposes to indefinitely defer the effective date for SOP 07-1 and, consequently, FSP FIN 46R-7. We are currently evaluating the potential impact of adopting SOP 07-1 and FSP FIN 46R-7 in light of the proposed FSP SOP No. 07-1-a.

FASB 141(R). In December 2007, the FASB issued FASB 141 (revised 2007), *Business Combinations* (“FASB 141R”). Under FASB 141R, an entity is required to recognize the assets acquired, liabilities assumed, contractual contingencies and contingent consideration measured at their fair value at the acquisition date for any business combination consummated after the effective date. It further requires that acquisition-related costs are to be recognized separately from the acquisition and expensed as incurred. This statement is effective for financial statements issued for fiscal years beginning after December 15, 2008. Accordingly, we will adopt FASB 141R effective January 1, 2009.

FASB 160. In December 2007, the FASB issued FASB 160, *Noncontrolling Interests in Consolidated Financial Statements — an amendment of ARB No. 51* (“FASB 160”). FASB 160 requires an entity to clearly identify and present ownership interests in subsidiaries held by parties other than the entity in the Consolidated Financial Statements within the equity section but separate from the entity’s equity. It also requires the amount of consolidated net income attributable to the parent and to the noncontrolling interest be clearly identified and presented on the face of the consolidated statement of income; changes in ownership interest be accounted for similarly, as equity transactions; and when a subsidiary is deconsolidated, any retained noncontrolling equity investment in the former subsidiary and the gain or loss on the deconsolidation of the subsidiary be measured at fair value. This statement is effective for financial statements issued for fiscal years beginning after December 15, 2008. Accordingly, we will adopt FASB 160 effective January 1, 2009. We are currently evaluating the impact of FASB 160 on our Consolidated Financial Statements.

Use of Estimates

Our management has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in conformity with U.S. generally accepted accounting principles. The most important of these estimates and assumptions relate to fair value measurements and compensation and benefits. Although these and other estimates and assumptions are based on the best available information, actual results could be materially different from these estimates.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(2) Asset Management Fees and Investment Income From Managed Funds

Period end assets under management by predominant asset strategy were as follows (in millions of dollars):

	December 31, 2007	December 31, 2006
Assets under management:		
Fixed Income (1)	\$ 1,802	\$ 1,439
Equities	295	475
Convertibles	2,872	2,486
	<u>4,969</u>	<u>4,400</u>
Assets under management by third parties (2):		
Equities, Convertibles and Fixed Income	206	282
Private Equity	600	600
	<u>806</u>	<u>882</u>
Total	<u>\$ 5,775</u>	<u>\$ 5,282</u>

- (1) With the reorganization of our high yield secondary market trading activities, we no longer include high yield assets as assets under management as of April 2, 2007. Prior period amounts include \$447 million in assets under management from our high yield funds.
- (2) Third party managed funds in which we have a 50% or less interest in the entities that manage these assets or otherwise receive a portion of the management fees.

The following summarizes revenues from asset management fees and investment income from managed funds relating to funds managed by us and funds managed by third parties for the years ended December 31, 2007, 2006 and 2005 (in thousands of dollars):

	2007	2006	2005
Asset management fees:			
Fixed Income (1)	\$ 12,129	\$ 24,604	\$ 19,556
Equities	4,140	16,366	15,415
Convertibles	12,264	12,256	7,516
Real Assets	—	2,236	8,456
	<u>28,533</u>	<u>55,462</u>	<u>50,943</u>
Investment income (loss) from managed funds(1)	(4,999)	54,088	31,109
Total	<u>\$ 23,534</u>	<u>\$ 109,550</u>	<u>\$ 82,052</u>

- (1) With the reorganization of our high yield secondary market trading activities, we no longer record asset management fees and investment income from managed funds related to these activities as of April 2, 2007. For the years ended December 31, 2007, 2006 and 2005, asset management fees and investment income from managed funds related to our high yield funds amounted to \$3.9 million, \$37.5 million and \$31.1 million, respectively.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

The following tables detail our average investment in managed funds, investment income from managed funds, investment income from managed funds – minority interest portion and net investment income from managed funds relating to funds managed by us and funds managed by third parties for the years ended December 31, 2007 and 2006 (in millions of dollars):

Year Ended December 31, 2007

	Average Investment (2)	Investment Income (Loss) from Managed Funds	Investment Income from Managed Funds - Minority Interest Portion	Net Investment Income (Loss) from Managed Funds
Fixed Income (1)	\$ 241.1	\$ (10.0)	\$ 0.4	\$ (10.4)
Equities	172.9	3.8	0.9	2.9
Convertibles	34.3	1.2	—	1.2
Total	<u>\$ 448.3</u>	<u>\$ (5.0)</u>	<u>\$ 1.3</u>	<u>\$ (6.3)</u>

(1) Excludes high yield secondary market trading activities for the nine month period ended December 31, 2007.

(2) Includes our average investment in consolidated asset management entities of \$112.3 million for which we are not recognizing asset management fees. Because these entities are consolidated, the financial instruments are reflected in financial instruments owned or financial instruments sold, not yet purchased, in our Consolidated Financial Statements.

Year Ended December 31, 2006

	Average Investment (3)	Investment Income from Managed Funds	Investment Income from Managed Funds - Minority Interest Portion	Net Investment Income from Managed Funds
Fixed Income	\$ 198.8	\$ 41.4	\$ 6.9	\$ 34.5
Equities	89.6	10.5	0.2	10.3
Convertibles	12.8	1.5	—	1.5
Real Assets	3.5	0.7	—	0.7
Total	<u>\$ 304.7</u>	<u>\$ 54.1</u>	<u>\$ 7.1</u>	<u>\$ 47.0</u>

(3) Includes our average investment in consolidated asset management entities of \$59.5 million and non-consolidated high yield funds of \$52.5 million for which we are not recognizing asset management fees. Because these entities are consolidated, the financial instruments are reflected in financial instruments owned or financial instruments sold, not yet purchased, in our Consolidated Financial Statements.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(3) Cash, Cash Equivalents, and Short-Term Investments

We generally invest our excess cash in money market funds and other short-term investments. Cash equivalents include highly liquid investments not held for resale with original maturities of three months or less. The following are financial instruments that are cash and cash equivalents or are deemed by our management to be generally readily convertible into cash as of December 31, 2007 and 2006 (in thousands of dollars):

	<u>December 31, 2007</u>	<u>December 31, 2006</u>
Cash and cash equivalents:		
Cash in banks	\$ 248,174	\$ 107,488
Money market investments	649,698	405,553
Total cash and cash equivalents	897,872	513,041
Cash and securities segregated (1)	659,219	508,303
Other (2)	—	71,160
	<u>\$ 1,557,091</u>	<u>\$ 1,092,504</u>

- (1) In accordance with Rule 15c3-3 of the Securities Exchange Act of 1934, Jefferies, as a broker-dealer carrying client accounts, is subject to requirements related to maintaining cash or qualified securities in a segregated reserve account for the exclusive benefit of its clients.
- (2) Items are financial instruments utilized in our overall cash management activities and are readily convertible to cash, marginable or accessible for liquidity purposes and are included in financial instruments owned.

(4) Receivable from, and Payable to, Customers

The following is a summary of the major categories of receivables from customers as of December 31, 2007 and 2006 (in thousands of dollars):

	<u>2007</u>	<u>2006</u>
Customers (net of allowance for uncollectible accounts of \$1,493 in 2007 and \$1,402 in 2006)	\$754,472	\$650,590
Officers and directors	10,361	12,962
	<u>\$764,833</u>	<u>\$663,552</u>

Receivable from officers and directors represents standard margin loan balances arising from their individual security transactions. These transactions are subject to the same terms and conditions as customer transactions.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(5) Financial Instruments Owned and Financial Instruments Sold, Not Yet Purchased

The following is a summary of the fair value of major categories of financial instruments owned and financial instruments sold, not yet purchased, as of December 31, 2007 and 2006 (in thousands of dollars):

	December 31, 2007		December 31, 2006	
	Financial Instruments Owned	Financial Instruments Sold, Not Yet Purchased	Financial Instruments Owned	Financial Instruments Sold, Not Yet Purchased
Corporate equity securities	\$2,266,679	\$1,389,099	\$1,737,174	\$1,835,046
Corporate debt securities	2,162,893	1,407,387	1,918,829	1,185,400
U.S. Government and agency obligations	730,921	206,090	592,374	339,891
Mortgage-backed securities	26,895	—	85,040	—
Asset-backed securities	—	—	28,009	—
Derivatives	501,502	331,788	234,646	240,231
Investments at fair value	104,199	—	97,289	—
Other	2,889	314	10,151	301
	<u>\$5,795,978</u>	<u>\$3,334,678</u>	<u>\$4,703,512</u>	<u>\$3,600,869</u>

Financial instruments owned includes securities pledged to creditors. The following is a summary of the fair value of major categories of securities pledged to creditors as of December 31, 2007 and 2006 (in thousands of dollars):

	December 31, 2007	December 31, 2006
Corporate equity securities	\$ 985,783	\$ 1,068,498
Corporate debt securities	102,123	412,600
	<u>\$ 1,087,906</u>	<u>\$ 1,481,098</u>

At December 31, 2007 and 2006, the approximate fair value of collateral received by us that may be sold or repledged by us was \$19.8 billion and \$9.8 billion, respectively. This collateral was received in connection with resale agreements and securities borrowings. At December 31, 2007 and 2006, a substantial portion of this collateral received by us had been sold or repledged.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

The following is a summary of our financial assets and liabilities that are accounted for at fair value as of December 31, 2007 by level within the fair value hierarchy (in thousands of dollars):

	Level 1	Level 2	Level 3	Counterparty and Cash Collateral Netting	Total
Assets:					
Financial instruments owned:					
Securities	\$2,122,640	\$2,819,240	\$ 248,397	\$ —	\$5,190,277
Derivative instruments	763,529	118,905	—	(380,932)	501,502
Investments at fair value	—	—	104,199	—	104,199
Total financial instruments owned	2,886,169	2,938,145	352,596	(380,932)	5,795,978
Level 3 assets for which the firm does not bear economic exposure (1)			(106,106)		
Level 3 assets for which the firm bears economic exposure			246,490		
Liabilities:					
Financial instruments sold, not yet purchased:					
Securities	1,425,789	1,568,398	8,703	—	3,002,890
Derivative instruments	532,895	642,507	12,929	(856,543)	331,788
Total financial instruments sold, not yet purchased	1,958,684	2,210,905	21,632	(856,543)	3,334,678

(1) Consists of level 3 assets which are attributable to minority investors or attributable to employee interests in certain consolidated funds.

The following is a summary of changes in fair value of our financial assets and liabilities that have been classified as Level 3 for year ended December 31, 2007 (in thousands of dollars):

	Non-derivative instruments - Assets	Non-derivative instruments - Liabilities	Derivative instruments - Liabilities	Investments
Balance, December 31, 2006	\$ 205,278	\$ —	\$ —	\$ 97,289
Total gains/ (losses) (realized and unrealized) (1)	(6,139)	(46)	(22,962)	23,494
Purchases, sales, settlements, and Issuances	(13,492)	(9,154)	26,385	(16,584)
Net transfers in and/or out of Level 3	62,750	497	(16,352)	—
Balance, December 31, 2007	<u>\$ 248,397</u>	<u>\$ (8,703)</u>	<u>\$ (12,929)</u>	<u>\$ 104,199</u>
Change in unrealized gains/ (losses) relating to instruments still held at December 31, 2007 (1)	\$ (7,866)	\$ —	\$ (7,384)	\$ 23,474

(1) Realized and unrealized gains/ losses are reported in principal transactions in the Consolidated Statements of Earnings.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(6) Premises and Equipment

The following is a summary of premises and equipment as of December 31, 2007 and 2006 (in thousands of dollars):

	<u>2007</u>	<u>2006</u>
Furniture, fixtures and equipment	\$189,376	\$147,868
Leasehold improvements	109,895	81,923
Total	299,271	229,791
Less accumulated depreciation and amortization	157,799	138,416
	<u>\$141,472</u>	<u>\$ 91,375</u>

Depreciation and amortization expense amounted to \$27,047,000, \$18,902,000 and \$14,705,000 for the years ended December 31, 2007, 2006 and 2005, respectively.

(7) Short-Term Borrowings

Bank loans represent short-term borrowings that are payable on demand and generally bear interest at a spread over the federal funds rate. We had no outstanding secured bank loans as of December 31, 2007 and 2006. Unsecured bank loans are typically overnight loans used to finance securities owned or clearing related balances. We had \$280.4 million and \$0 of outstanding unsecured bank loans as of December 31, 2007 and 2006, respectively. Average daily bank loans for the years ended December 31, 2007 and 2006 were \$267.1 million and \$12.4 million, respectively.

(8) Long-Term Debt

The following summarizes long-term debt outstanding at December 31, 2007 and 2006 (in thousands of dollars):

	<u>2007</u>	<u>2006</u>
7.75% Senior Notes, due 2012, net of unamortized discount of \$3,933 (2007)	328,594	328,003
5.875% Senior Notes, due 2014, net of unamortized discount of \$1,598 (2007)	248,402	—
5.5% Senior Notes, due 2016, net of unamortized discount of \$1,499 (2007)	348,501	348,320
6.45% Senior Debentures, due 2027, net of unamortized discount of \$3,764 (2007)	346,236	—
6.25% Senior Debentures, due 2036, net of unamortized discount of \$7,666 (2007)	492,334	492,239
	<u>\$1,764,067</u>	<u>\$1,168,562</u>

We previously entered into a fair value hedge with no ineffectiveness using interest rate swaps in order to convert \$200 million aggregate principal amount of unsecured 7.75% senior notes due March 15, 2012 into floating rates based upon LIBOR. During the third quarter of 2007 we terminated these interest rate swaps and received cash consideration less accrued interest of \$8.5 million. The \$8.5 million basis difference related to the fair value of the interest rate swaps at the time of the termination is being amortized as a reduction in interest expense of \$1.9 million per year over the remaining life of the notes through March 2012.

In January 2006, we sold in a registered public offering \$500.0 million aggregate principal amount of our unsecured 6.25% 30-year senior debentures due January 15, 2036.

In June 2007, we sold in a registered public offering \$600.0 million aggregate principal amount of our senior debt, consisting of \$250.0 million of 5.875% senior notes due June 8, 2014 and \$350.0 million of 6.45% senior debentures due June 8, 2027.

(9) Mandatorily Redeemable Convertible Preferred Stock

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

In February 2006, Massachusetts Mutual Life Insurance Company (“MassMutual”) purchased in a private placement \$125.0 million of our Series A convertible preferred stock. Our Series A convertible preferred stock has a 3.25% annual, cumulative cash dividend and is currently convertible into 4,082,538 shares of our common stock at an effective conversion price of approximately \$30.62 per share. The preferred stock is callable beginning in 2016 and will mature in 2036. As of December 31, 2007, 10,000,000 shares of preferred stock were authorized and 125,000 shares of preferred stock were issued and outstanding. The dividend is recorded as a component of interest expense as the Series A convertible preferred stock is treated as debt for accounting purposes. The dividend is not deductible for tax purposes because the Series A convertible preferred stock is considered “equity” for tax purposes.

(10) Income Taxes

Total income taxes for the years ended December 31, 2007, 2006 and 2005 were allocated as follows (in thousands of dollars):

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Earnings	\$ 93,178	\$137,541	\$104,089
Stockholders’ equity, for compensation expense for tax purposes in excess of amounts recognized for financial reporting purposes	<u>(41,710)</u>	<u>(32,906)</u>	<u>(26,918)</u>
	<u>\$ 51,468</u>	<u>\$104,635</u>	<u>\$ 77,171</u>

Income taxes (benefits) for the years ended December 31, 2007, 2006 and 2005 consist of the following (in thousands of dollars):

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Current:			
Federal	\$ 78,715	\$129,648	\$ 95,341
State and city	9,379	31,557	24,771
Foreign	<u>11,353</u>	<u>14,318</u>	<u>7,452</u>
	<u>99,447</u>	<u>175,523</u>	<u>127,564</u>
Deferred:			
Federal	(13,030)	(29,414)	(14,251)
State and city	4,218	(6,938)	(6,344)
Foreign	<u>2,543</u>	<u>(1,630)</u>	<u>(2,880)</u>
	<u>(6,269)</u>	<u>(37,982)</u>	<u>(23,475)</u>
	<u>\$ 93,178</u>	<u>\$137,541</u>	<u>\$104,089</u>

Income taxes differed from the amounts computed by applying the Federal income tax rate of 35% for 2007, 2006 and 2005 as a result of the following (in thousands of dollars):

	<u>2007</u>		<u>2006</u>		<u>2005</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
Computed expected income taxes	\$86,007	35.0%	\$122,029	35.0%	\$ 93,944	35.0%
Increase (decrease) in income taxes resulting from:						
State and city income taxes, net of Federal income tax benefit	8,838	3.6	16,002	4.6	11,977	4.5
Limited deductibility of meals and entertainment	1,801	0.7	1,972	0.5	1,634	0.6
Minority interest, not subject to tax	(2,762)	(1.1)	(2,439)	(0.7)	(2,887)	(1.1)
Foreign income	2,593	1.1	(143)	(0.1)	(1,086)	(0.4)
Other, net	<u>(3,299)</u>	<u>(1.4)</u>	<u>120</u>	<u>0.1</u>	<u>507</u>	<u>0.2</u>
Total income taxes	<u>\$93,178</u>	<u>37.9%</u>	<u>\$137,541</u>	<u>39.4%</u>	<u>\$104,089</u>	<u>38.8%</u>

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

The following table presents a reconciliation of gross unrecognized tax benefits between January 1, 2007 and December 31, 2007 (in thousands of dollars):

Balance at January 1, 2007	\$ 5,114
Additions for tax positions related to current year	2,167
Additions for tax positions related to prior year	2,839
Reductions for tax positions related to prior year	(153)
Settlements	<u>(1,142)</u>
Balance at December 31, 2007	<u>\$ 8,825</u>

The total amount of unrecognized benefits that, if recognized, would affect the effective tax rate was \$5.7 million (net of federal benefit of state issues) at December 31, 2007. We recognize interest accrued related to unrecognized tax benefits in interest expense. Penalties, if any, are recognized in other general and administrative expenses. During the years ended December 31, 2007 and 2006, we recognized approximately \$1.0 million and \$0.3 million, respectively, in interest. We had approximately \$1.4 million and \$1.0 million for the payment of interest and penalties accrued at December 31, 2007, and 2006, respectively.

We are subject to U.S. federal income tax as well as income tax in multiple state and foreign jurisdictions. We have concluded all U.S. federal income tax matters for the years through 2000. Substantially all material state and local, and foreign income tax matters have been concluded for the years through 1999. New York State and New York City income tax returns for the years 2001 through 2004 and 2000 through 2003, respectively, are currently under examination. The final outcome of these examinations is not yet determinable. We do not expect that unrecognized tax benefits for tax positions taken with respect to 2007 and prior years will significantly change in 2008.

The cumulative tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities at December 31, 2007 and 2006 are presented below (in thousands of dollars):

	<u>2007</u>	<u>2006</u>
Deferred tax assets:		
Long-term compensation	\$225,803	\$195,079
State income taxes	652	6,359
Pension	1,241	2,102
Net operating loss	5,326	1,483
Other	2,417	5,415
Sub-total	<u>235,439</u>	<u>210,438</u>
Valuation allowance	<u>(2,294)</u>	<u>(1,483)</u>
Total deferred tax assets	<u>\$233,145</u>	<u>\$208,955</u>
Deferred tax liabilities:		
Premises and equipment	2,467	2,787
Goodwill amortization	18,480	13,917
Investments	11,600	5,108
Other	4,041	2,906
Total deferred tax liabilities	<u>\$ 36,588</u>	<u>\$ 24,718</u>
Net deferred tax asset, included in other assets	<u>\$196,557</u>	<u>\$184,237</u>

A valuation allowance of \$2.3 million and \$1.5 million was recorded at December 31, 2007 and 2006, respectively, and represents the portion of our deferred tax assets for which it is more likely than not that the benefit of such items will not be realized. Such valuation allowance increased by approximately \$0.8 million and \$1.5 million for the years ended December 31, 2007 and 2006, respectively. We believe it is more likely than not that we will realize our other deferred tax assets through future earnings.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

As of December 31, 2007 we have net operating losses in certain foreign jurisdictions totaling approximately \$16.2 million. These losses begin to expire in the year 2013.

The current tax receivable, included in other assets, was \$37,267,000 and \$28,044,000 as of December 31, 2007 and 2006, respectively.

Withholding and U.S. taxes have not been provided on approximately \$66.0 million of unremitted earnings of certain non-U.S. subsidiaries because we reinvested these earnings permanently in such operations. Such earnings would become taxable upon the sale or liquidation of these non- U.S. subsidiaries or upon the remittance of dividends; however, management does not believe the related tax on such taxable amounts would be material.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(11) Defined Benefit Plan*Pension Plan*

We have a defined benefit pension plan which covers certain of our employees. The plan is subject to the provisions of the Employee Retirement Income Security Act of 1974. Benefits are based on years of service and the employee's career average pay. Our funding policy is to contribute to the plan at least the minimum amount that can be deducted for Federal income tax purposes. Differences in each year, if any, between expected and actual returns in excess of a 10% corridor (as defined in FASB 87, *Employers' Accounting for Pensions*) are amortized in net periodic pension calculations. Effective December 31, 2005, benefits under the pension plan have been frozen. Accordingly, there will be no further benefit accruals for future service after December 31, 2005.

On December 31, 2006, we adopted the recognition and disclosure provisions of FASB 158. FASB 158 required us to recognize the funded status (i.e., the difference between the fair value of plan assets and the projected benefit obligations) of our benefit plan in the December 31, 2006 Consolidated Statement of Financial Condition, with a corresponding adjustment to accumulated other comprehensive income, net of tax. As a result of the pension plan being frozen, the projected benefit obligation was equal to the accumulated benefit obligation. Consequently, no additional adjustment to accumulated other comprehensive income was necessary.

The following tables set forth the plan's funded status and amounts recognized in our accompanying consolidated statements of financial condition and consolidated statements of earnings (in thousands of dollars):

	December 31		
	2007	2006	
Accumulated benefit obligation	\$ 40,828	\$ 42,892	
Projected benefit obligation for service rendered to date	\$ 40,828	\$ 42,892	
Plan assets, at fair value	41,634	39,484	
Funded status	\$ 806	\$ (3,408)	
Unrecognized net loss	3,068	5,013	
Prepaid benefit cost	\$ 3,874	\$ 1,605	
Adjustment to recognize minimum asset (liability)	(3,068)	(5,013)	
Pension asset (liability)	\$ 806	\$ (3,408)	
	Year ended December 31		
	2007	2006	2005
Net pension cost included the following components:			
Service cost — benefits earned during the period	\$ 275	\$ 275	\$ 2,077
Interest cost on projected benefit obligation	2,378	2,361	2,551
Expected return on plan assets	(2,923)	(2,514)	(2,239)
Net amortization	—	562	1,008
Net periodic pension (income) cost	\$ (270)	\$ 684	\$ 3,397

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

	<u>Year ended December 31</u>	
	<u>2007</u>	<u>2006</u>
Fair value of assets, beginning of year	\$ 39,484	\$ 33,062
Employer contributions	2,000	2,000
Benefit payments made	(2,394)	(1,061)
Administrative expenses paid	(174)	(267)
Total investment return	2,718	5,750
Fair value of assets, end of year	<u>\$ 41,634</u>	<u>\$ 39,484</u>

	<u>Year ended December 31</u>	
	<u>2007</u>	<u>2006</u>
Projected benefit obligation, beginning of year	\$ 42,892	\$ 43,287
Service cost	275	275
Interest cost	2,378	2,361
Actuarial gains and losses	(2,149)	(1,703)
Administrative expenses paid	(174)	(267)
Benefits paid	(2,394)	(1,061)
Projected benefit obligation, end of year	<u>\$ 40,828</u>	<u>\$ 42,892</u>

The plan assets consist of approximately 56% equities, 41% fixed income and 3% other securities in 2007 versus approximately 60% equities and 40% fixed income in 2006. The target allocation of plan assets for 2008 is approximately 60% equities and 40% fixed income securities.

The weighted average discount rate and the rate of increase in future compensation levels used in determining the actuarial present value of the projected benefit obligation were 6.25% and 0.00%, respectively, in 2007, 5.90% and 0.00%, respectively, in 2006, and 5.55% and 4.00%, respectively, in 2005. The expected long-term rate of return on assets was 7.5% in 2007, 2006 and 2005.

The expected long-term rate of return assumption is based on an analysis of historical experience of the portfolio and the summation of prospective returns for each asset class in proportion to the fund's current asset allocation. The target asset allocation was determined based on the risk tolerance characteristics of the plan and, at times, may be adjusted to achieve the plan's investment objective and to minimize any concentration of investment risk.

We have contributed \$2.0 million to our pension plan during 2007. Effective December 31, 2005, benefits under the pension plan have been frozen. There will be no further benefit accruals for service after December 31, 2005. The amounts in accumulated other comprehensive income that have not yet been recognized as components of net periodic benefit cost include \$3,068,000 and \$5,013,000 as of December 31, 2007 and 2006, respectively.

During 2008, we do not expect to recognize an amortization of net loss as a component of net periodic benefit cost.

Expected benefit payments through December 31, 2017 are as follows (in thousands of dollars):

2008	\$ 1,967
2009	2,130
2010	3,126
2011	1,389
2012	2,971
2013 through 2017	12,091

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

(12) Minority Interest

Under FASB 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity* (“FASB 150”), certain minority interests in consolidated entities may meet the standard’s definition of a mandatorily redeemable financial instrument and thus require reclassification as liabilities and remeasurement at the estimated amount of cash that would be due and payable to settle such minority interests under the applicable entity’s organization agreement, assuming an orderly liquidation of the entity, net of estimated liquidation costs. Our Consolidated Financial Statements include certain minority interests that meet the standard’s definition of mandatorily redeemable financial instruments. These mandatorily redeemable minority interests represent interests held by third parties in Jefferies High Yield Holdings, LLC (“JHYH”). The mandatorily redeemable minority interests are entitled to a pro rata share of the profits of JHYH, as set forth in JHYH’s organization agreements, and are scheduled to terminate in 2013, with an option to extend up to three additional one-year periods. The carrying amount of these mandatorily redeemable minority interests are approximately \$607.6 million at December 31, 2007, which represents the initial capital and the pro rata share of the profits of JHYH assigned to the holder of the mandatorily redeemable minority interests. A certain portion of these mandatorily redeemable minority interests represents investments from Jefferies Special Opportunities Partners (“JSOP”) and Jefferies Employees Special Opportunities Partners (“JESOP”), and are eliminated in consolidation. The carrying amount of these mandatorily redeemable minority interests eliminated in consolidation is approximately \$253.3 million at December 31, 2007, resulting in minority interest related to JHYH on a consolidated basis of approximately \$354.3 million at December 31, 2007.

Minority interest also includes the minority equity holders’ proportionate share of the equity of JSOP and JESOP. At December 31, 2007, minority interest related to JSOP and JESOP was approximately \$212.1 million and \$26.5 million, respectively.

At December 31, 2007, we had other minority interests of approximately \$10.8 million primarily related to our start-up asset management funds.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(13) Earnings per Share

The following is a reconciliation of the numerators and denominators of the basic and diluted earnings per share computations for the years 2007, 2006 and 2005 (in thousands, except per share amounts):

	Year Ended December 31,		
	2007	2006	2005
Earnings:			
Earnings before cumulative effect of change in accounting principle, net	\$144,665	\$204,144	\$157,443
Cumulative effect of change in accounting principle, net	—	1,606	—
Net earnings	\$144,665	\$205,750	\$157,443
Add: Convertible preferred stock dividends	4,063	3,543	—
Net earnings for diluted earnings per share	<u>\$148,728</u>	<u>\$209,293</u>	<u>\$157,443</u>
Shares:			
Average shares used in basic computation	141,515	133,898	123,646
Stock options	388	1,251	2,747
Mandatorily redeemable convertible preferred stock	4,068	3,521	—
Unvested restricted stock / restricted stock units	7,836	8,861	9,176
Average shares used in diluted computation	<u>153,807</u>	<u>147,531</u>	<u>135,569</u>
Earnings per share:			
Basic-			
Earnings before cumulative effect of change in accounting principle, net	\$ 1.02	\$ 1.53	\$ 1.27
Cumulative effect of change in accounting principle, net	—	0.01	—
Net earnings	<u>\$ 1.02</u>	<u>\$ 1.54</u>	<u>\$ 1.27</u>
Diluted-			
Earnings before cumulative effect of change in accounting principle, net	\$ 0.97	\$ 1.41	\$ 1.16
Cumulative effect of change in accounting principle, net	—	0.01	—
Net earnings	<u>\$ 0.97</u>	<u>\$ 1.42</u>	<u>\$ 1.16</u>

We had no anti-dilutive securities for purposes of the annual earnings per share computations in 2007, 2006 and 2005.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(14) Leases

As lessee, we lease certain premises and equipment under noncancelable agreements expiring at various dates through 2022 which are operating leases. Future minimum lease payments for all noncancelable operating leases at December 31, 2007 are as follows (in thousands of dollars):

	Gross	Sub-leases	Net
2008	\$ 47,494	\$10,609	\$ 36,885
2009	48,043	10,667	37,376
2010	45,841	10,427	35,414
2011	43,561	10,002	33,559
2012	37,500	6,716	30,784
Thereafter	149,947	14,704	135,243

Rental expense amounted to \$50,443,000, \$43,406,000 and \$34,959,000, in 2007, 2006 and 2005, respectively.

(15) Derivative Financial Instruments*Off-Balance Sheet Risk*

We have contractual commitments arising in the ordinary course of business for securities loaned or purchased under agreements to sell, financial instruments sold but not yet purchased, repurchase agreements, future purchases and sales of foreign currencies, securities transactions on a when-issued basis, options contracts, futures index contracts, commodities futures contracts and underwriting. Each of these financial instruments and activities contains varying degrees of off-balance sheet risk whereby the fair values of the securities underlying the financial instruments may be in excess of, or less than, the contract amount. The settlement of these transactions is not expected to have a material effect upon our Consolidated Financial Statements.

Derivative Financial Instruments

Our derivative activities are recorded at fair value in the Consolidated Statements of Financial Condition. Acting in a trading capacity, we may enter into derivative transactions to satisfy the needs of our clients and to manage our own exposure to market and credit risks resulting from our trading activities.

Derivatives are subject to various risks similar to other financial instruments, including market, credit and operational risk. In addition, we may be exposed to legal risks related to derivative activities. The risks of derivatives should not be viewed in isolation, but rather should be considered on an aggregate basis along with our other trading-related activities. We manage the risks associated with derivatives on an aggregate basis along with the risks associated with proprietary trading as part of our firmwide risk management policies.

We record trading derivative contracts at fair value with realized and unrealized gains and losses recognized in principal transactions in the Consolidated Statements of Earnings on a trade date basis and as a component of cash flows from operating activities in the Consolidated Statements of Cash Flows.

We previously entered into a fair value hedge with no ineffectiveness using interest rate swaps in order to convert \$200 million aggregate principal amount of unsecured 7 3/4% senior notes due March 15, 2012 into floating rates based upon LIBOR. During the third quarter of 2007 we terminated these interest rate swaps and received cash consideration less accrued interest of \$8.5 million. The \$8.5 million basis difference related to the fair value of the interest rate swaps at the time of the termination is being amortized as a reduction in interest expense of approximately \$1.9 million per year over the remaining life of the notes through March 2012.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

The following table presents the fair value of derivatives at December 31, 2007 and 2006. The fair value of assets/liabilities related to derivative contracts at December 31, 2007 and 2006 represent our receivable/payable for derivative financial instruments, gross of related collateral received and pledged:

(in thousands)	<u>December 31, 2007</u>		<u>December 31, 2006</u>	
	<u>Assets</u>	<u>Liabilities</u>	<u>Assets</u>	<u>Liabilities</u>
Derivative instruments included in financial instruments owned and financial instruments sold, not yet purchased:				
Exchange traded futures	\$162,723	\$ 4,712	\$ 19,724	\$ 2,116
Swaps (1)	2,424	417,020	173,821	20,251
Option contracts (1)	355,119	404,525	152,361	238,115
Forward contracts	3,348	3,254	820	—
Total	\$523,614	\$829,511	\$346,726	\$260,482
Derivative instruments included in other assets:				
Interest rate swaps	—	—	7,690	—

- (1) Option and swap contracts in the table above are gross of collateral received and/ or collateral pledged. Option and swap contracts are recorded net of collateral received and/ or collateral pledged on the Consolidated Statement of Financial Condition. At December 31, 2007, collateral received and collateral pledged were \$22.1 million and \$497.7 million, respectively. At December 31, 2006, collateral received and collateral pledged were \$112.1 million and \$20.3 million, respectively.

The following table set forth the fair value of OTC derivative assets and liabilities by contract type as of December 31, 2007:

(in millions)	<u>0 – 12</u>	<u>1 – 5</u>	<u>5 – 10</u>	<u>Total</u>
	<u>Months</u>	<u>Years</u>	<u>Years</u>	
Commodity swaps	\$ (405.7)	\$ (1.5)	\$ —	\$ (407.2)
Commodity options	(20.1)	(66.2)	—	(86.3)
Equity options	(10.6)	(23.3)	—	(33.9)
Credit default swaps	(0.4)	2.4	—	2.0
Total return swaps	(9.4)	—	—	(9.4)
Forward contracts	(0.3)	0.5	—	0.2
Total	\$ (446.5)	\$ (88.1)	\$ —	\$ (534.6)

At December 31, 2007, the counterparty credit quality with respect to the fair value of our OTC derivatives was as follows:

(in millions)	<u>December 31,</u> <u>2007</u>
Counterparty credit quality:	
A or higher	\$ (491.4)
B to BBB	(22.4)
Lower than B	—
Unrated	(20.8)
Total	\$ (534.6)

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

Jefferies Financial Products, LLC

Jefferies Financial Products, LLC (“JFP”), a wholly-owned subsidiary of ours, was formed as a limited liability company in November 2003. JFP is a market maker in commodity index products and a trader in commodities futures and options. JFP offers customers exposure to over-the-counter commodity indices and other commodity baskets in the form of fixed-for-floating swaps (“swaps”) and options, where the return is based on a specific commodity or basket of commodities (e.g., Jefferies Commodity Performance Index (“JCPI”). The primary end users in this market are highly rated institutional investors, such as pension funds, mutual funds, foundations, endowments, and insurance companies. These investors generally seek exposure to commodities in order to diversify their existing stock and bond portfolios. Generally, JFP will enter into swaps whereby JFP receives a stream of fixed cash flows against paying the return of a given commodity or index plus a spread or fee (“fee”). The fee is meant to compensate JFP for the costs of replicating the commodity or index exposure in the underlying exchange traded futures markets. The floating return can be either the total return on the index (inclusive of implied collateral yield) or the excess return. JFP also enters into swap, forward and option transactions on foreign exchange, individual commodities and commodity indices.

Generally, the swap and option contract tenors range from 1 month to 2 years, and in some transactions both parties may settle the changes in the mark-to-market value of the transaction on a monthly basis. Where appropriate, JFP utilizes various credit enhancements, including guarantees, collateral and margin agreements to mitigate the credit exposure relating to these swaps and options. JFP establishes credit limits based on, among other things, the creditworthiness of the counterparties, the transaction’s size and tenor, and estimated potential exposure. In addition, swap and option transactions are generally documented under International Swaps and Derivatives Association Master Agreements. We believe that such agreements provide for legally enforceable set-off and close-out netting of exposures to specific counterparties. Under such agreements, in connection with an early termination of a transaction, JFP is permitted to set-off its receivables from a counterparty against its payables to the same counterparty arising out of all included transactions. As a result, the fair value represents the net sum of estimated fair values after the application of such netting. JFP has determined that the fair value of its swaps and options approximated \$(407.2) million and \$(84.0) million, respectively at December 31, 2007 and \$156.1 million and \$(125.4) million, respectively at December 31, 2006.

The following table sets forth the fair value of JFP’s outstanding OTC positions and exchange-traded futures and options by remaining contractual maturity as of December 31, 2007:

(in millions)	0 – 12 Months	1 – 5 Years	5 – 10 Years	Total
Swaps	\$ (405.7)	\$ (1.5)	\$ —	\$ (407.2)
Options	(16.3)	(67.7)	—	(84.0)
FX forwards	0.6	0.5	—	1.1
Exchange-traded futures	296.4	(133.9)	—	162.5
Total	\$ (125.0)	\$ (202.6)	\$ —	\$ (327.6)

In July 2004, JFP entered into a credit intermediation facility with an AA-rated European bank (the “Bank”). This facility allows JFP customers that require a counterparty with a high credit rating for commodity index transactions to transact with the Bank. The Bank simultaneously enters into a back-to-back transaction with JFP and receives a fee from JFP for providing credit support. Subject to the terms of the agreement between JFP and the Bank, JFP is generally responsible to the Bank for the performance of JFP’s customers. We guarantee the performance of JFP to the Bank under the credit intermediation facility. JFP also provides commodity index pricing to the Bank’s customers and JFP earns revenue from the Bank’s hedging of its customer transactions with JFP.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

At December 31, 2007 and 2006, the counterparty credit quality with respect to the fair value of commodities and foreign exchange futures, options and swap portfolios were as follows:

(in millions)	Fair Value	
	December 31, 2007	December 31, 2006
Counterparty credit quality:		
A or higher	\$ (494.4)	\$ 37.5
Exchange-traded futures and options (1)	166.8	13.4
Total	<u>\$ (327.6)</u>	<u>\$ 50.9</u>

(1) Exchange-traded commodities and foreign exchange futures and options are not deemed to have significant credit exposures as the exchanges guarantee that every contract will be properly settled on a daily basis.

At December 31, 2007 and 2006 the counterparty breakdown by industry with respect to the fair value of JFP's commodities and foreign exchange futures, options and swap portfolio was as follows:

(in millions)	Fair Value	
	December 31, 2007	December 31, 2006
Foundations, trusts and endowments	\$ (47.8)	\$ (6.4)
Financial services	(223.8)	4.7
Sovereign entity	(32.5)	—
Collective investment vehicles (including pension plans, mutual funds and other institutional counterparties)	(190.3)	39.2
Exchanges (1)	166.8	13.4
Total	<u>\$ (327.6)</u>	<u>\$ 50.9</u>

(1) Exchange-traded commodities and foreign exchange futures and options are not deemed to have significant credit exposures as the exchanges guarantee that every contract will be properly settled on a daily basis.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(16) Other Comprehensive Income (Loss)

The following summarizes other comprehensive income and accumulated other comprehensive income (loss) at December 31, 2007 and for the year then ended (in thousands of dollars):

	<u>Before-Tax Amount</u>	<u>Income Tax or Benefit</u>	<u>Net-of-Tax Amount</u>
Currency translation adjustments	\$ 1,222	\$ —	\$ 1,222
Minimum pension liability adjustment	1,945	(862)	1,083
Other comprehensive income	<u>\$ 3,167</u>	<u>\$ (862)</u>	<u>\$ 2,305</u>

	<u>Currency Translation Adjustments</u>	<u>Minimum Pension Liability Adjustment</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>
Beginning balance	\$ 9,764	\$ (2,910)	\$ 6,854
Change in 2007	1,222	1,083	2,305
Ending balance	<u>\$ 10,986</u>	<u>\$ (1,827)</u>	<u>\$ 9,159</u>

The following summarizes other comprehensive income and accumulated other comprehensive income (loss) at December 31, 2006 and for the year then ended (in thousands of dollars):

	<u>Before-Tax Amount</u>	<u>Income Tax or Benefit</u>	<u>Net-of-Tax Amount</u>
Currency translation adjustments	\$ 8,802	\$ —	\$ 8,802
Minimum pension liability adjustment	5,502	(2,287)	3,215
Other comprehensive income	<u>\$ 14,304</u>	<u>\$ (2,287)</u>	<u>\$ 12,017</u>

	<u>Currency Translation Adjustments</u>	<u>Minimum Pension Liability Adjustment</u>	<u>Accumulated Other Comprehensive Income (Loss)</u>
Beginning balance	\$ 962	\$ (6,125)	\$ (5,163)
Change in 2006	8,802	3,215	12,017
Ending balance	<u>\$ 9,764</u>	<u>\$ (2,910)</u>	<u>\$ 6,854</u>

The following summarizes other comprehensive loss and accumulated other comprehensive income (loss) at December 31, 2005 and for the year then ended (in thousands of dollars):

	<u>Before-Tax Amount</u>	<u>Income Tax or Benefit</u>	<u>Net-of-Tax Amount</u>
Currency translation adjustments	\$ (8,386)	\$ —	\$ (8,386)
Minimum pension liability adjustment	1,276	(533)	743
Other comprehensive loss	<u>\$ (7,110)</u>	<u>\$ (533)</u>	<u>\$ (7,643)</u>

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

Equity Commitments. On October 7, 2004, we entered into an agreement with Babson Capital and MassMutual to form Jefferies Finance LLC, a joint venture entity created for the purpose of offering senior loans to middle market and growth companies. In February 2006, we and MassMutual reached an agreement to double our equity commitments to Jefferies Finance LLC. With an incremental \$125 million from each partner, the total committed equity capitalization of Jefferies Finance LLC is \$500 million as of December 31, 2007. Loans are originated primarily through the investment banking efforts of Jefferies & Company, Inc. with Babson Capital providing primary credit analytics and portfolio management services. As of December 31, 2007, we have funded \$55.0 million of our aggregate \$250.0 million commitment leaving \$195.0 million unfunded.

As of December 31, 2007, we have an aggregate capital commitment to invest in Babson-Jefferies Loan Opportunity CLO, Ltd. of approximately \$18.0 million (see note 21 of the Notes to Consolidated Financial Statements for more information related to our commitment to invest in Babson-Jefferies Loan Opportunity CLO, Ltd.).

As of December 31, 2007, we have an aggregate commitment to invest in Jefferies Capital Partners IV L.P. and its related parallel fund of approximately \$25.9 million, a private equity fund managed by a team led by Messrs. Friedman and Luikart.

As of December 31, 2007, we have funded approximately \$350.0 million of our aggregate commitment in JHYH leaving approximately \$250.0 million unfunded (see note 22 of the Notes to Consolidated Financial Statements for more information related to our commitment to invest in JHYH).

As of December 31, 2007, we had other equity commitments to invest up to \$11.2 million in various other investments.

Derivative Contracts. In accordance with FASB Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others* ("FIN 45"), we disclose certain derivative contracts meeting the FIN 45 definition of a guarantee. Such derivative contracts include credit default swaps (whereby a default or significant change in the credit quality of the underlying financial instrument may obligate us to make a payment) and written equity put options. At December 31, 2007, the maximum payout value of derivative contracts deemed to meet the FIN 45 definition of a guarantee was approximately \$397.5 million. For purposes of determining maximum payout, notional values are used; however, we believe the fair value of these contracts is a more relevant measure of these obligations because we believe the notional amounts greatly overstate our expected payout. At December 31, 2007, the fair value of such derivative contracts approximated \$13.6 million. In addition, the derivative contracts deemed to meet the FIN 45 definition of a guarantee are before consideration of hedging transactions. We substantially mitigate our risk on these contracts through hedges, such as other derivative contracts and/or cash instruments. We manage risk associated with derivative guarantees consistent with our risk management policies.

High Yield Loan Commitments. From time to time we make commitments to extend credit to investment-banking clients in loan syndication and acquisition-finance transactions. These commitments and any related drawdowns of these facilities typically have fixed maturity dates and are contingent on certain representations, warranties and contractual conditions applicable to the borrower. We define high yield (non-investment grade) as debt securities or loan commitments to companies rated BB+ or lower or equivalent ratings by recognized credit rating agencies, as well as non-rated securities or loans that, in management's opinion, are non-investment grade. As of December 31, 2007 we had \$5.0 million of high yield loan commitments outstanding.

Jefferies Financial Products, LLC. In July 2004, JFP entered into a credit intermediation facility with an "AA"-rated European bank (the "Bank"). This facility allows JFP customers that require a counterparty with a high credit rating for commodity index transactions to transact with the Bank. The Bank simultaneously enters into a back-to-back transaction with JFP and receives a fee from JFP for providing credit support. Subject to the terms of the agreement between JFP and the Bank, JFP is responsible to the Bank for the performance of JFP's customers.

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

We guarantee the performance of JFP to the Bank under the credit intermediation facility. JFP will also provide commodity index pricing to the Bank's customers and JFP will earn revenue from the Bank's hedging of its customer transactions with JFP. Also, we guarantee the performance of JFP to its trading counterparties and various banks and other entities, which provide clearing and credit services to JFP.

Other Guarantees . In the normal course of business we provide guarantees to securities clearinghouses and exchanges. These guarantees generally are required under the standard membership agreements, such that members are required to guarantee the performance of other members. To mitigate these performance risks, the exchanges and clearinghouses often require members to post collateral. Our obligations under such guarantees could exceed the collateral amounts posted; however, the potential for us to be required to make payments under such guarantees is deemed remote. Also, we have guaranteed obligations of Jefferies International Limited ("JIL") to various banks which provide clearing and credit services to JIL and to counterparties of JIL.

(19) Segment Reporting

Beginning in the second quarter of 2007, our international convertible bond funds are included within the results of the Asset Management segment. Previously, operations from our international convertible bond funds were included in the Capital Markets segment. Prior period disclosures have been adjusted to conform to the current quarter's presentation. The above change was made in order to reflect the manner in which these segments are currently managed.

The Capital Markets reportable segment includes our traditional securities brokerage, including the results of our recently reorganized high yield secondary market trading activities and investment banking activities. The Capital Markets reportable segment is managed as a single operating segment that provides the sales, trading and origination effort for various fixed income, equity and advisory products and services. The Capital Markets segment comprises a number of interrelated divisions. In addition, we choose to voluntarily disclose the Asset Management segment even though it is currently an "immaterial non-reportable" segment as defined by FASB 131, *Disclosures about Segments of an Enterprise and Related Information* .

Our reportable business segment information is prepared using the following methodologies:

- Net revenues and expenses directly associated with each reportable business segment are included in determining earnings before taxes.
- Net revenues and expenses not directly associated with specific reportable business segments are allocated based on the most relevant measures applicable, including each reportable business segment's net revenues, headcount and other factors.
- Reportable business segment assets include an allocation of indirect corporate assets that have been fully allocated to our reportable business segments, generally based on each reportable business segment's capital utilization.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

Our net revenues, expenses, income before income taxes and total assets by segment are summarized below (amounts in millions):

	<u>Capital Markets</u>	<u>Asset Management</u>	<u>Eliminating Items</u>	<u>Total</u>
Twelve months ended December 31, 2007				
Net revenues	\$ 1,547.5	\$ 20.6	\$ —	\$ 1,568.1
Expenses	<u>1,301.7(1)</u>	<u>46.7</u>	<u>(26.0)(1)</u>	<u>1,322.4</u>
Income before taxes	<u>\$ 245.8</u>	<u>\$ (26.1)</u>	<u>\$ 26.0</u>	<u>\$ 245.7</u>
Segment assets	<u>\$29,417.2</u>	<u>\$ 350.6</u>	<u>\$ 26.0(1)</u>	<u>\$29,793.8</u>
Twelve months ended December 31, 2006				
Net revenues	\$ 1,389.5	\$ 68.1	\$ —	\$ 1,457.6
Expenses	<u>1,059.6</u>	<u>49.3</u>	<u>—</u>	<u>1,108.9</u>
Income before taxes	<u>\$ 329.9</u>	<u>\$ 18.8</u>	<u>\$ —</u>	<u>\$ 348.7</u>
Segment assets	<u>\$17,676.9</u>	<u>\$ 148.6</u>	<u>\$ —</u>	<u>\$17,825.5</u>
Twelve months ended December 31, 2005				
Net revenues	\$ 1,156.1	\$ 48.6	\$ —	\$ 1,204.7
Expenses	<u>904.4</u>	<u>31.9</u>	<u>—</u>	<u>936.3</u>
Income before taxes	<u>\$ 251.7</u>	<u>\$ 16.7</u>	<u>\$ —</u>	<u>\$ 268.4</u>
Segment assets	<u>\$12,762.2</u>	<u>\$ 18.7</u>	<u>\$ —</u>	<u>\$12,780.9</u>

- (1) Our Jefferies Execution subsidiary recorded a goodwill impairment charge of \$26 million during the fourth quarter of 2007. Jefferies Execution is a registered broker-dealer. Therefore, goodwill relating to the acquisition of Jefferies Execution in 2001, formerly Helfant Group, Inc., was “pushed down” from us to Jefferies Execution in accordance with Emerging Issues Task Force Issue No. D-97, *Push Down Accounting*.

Jefferies Execution is not one of our “reporting units” as defined by FASB 142, *Goodwill and Other Intangible Assets* and therefore we have not recorded this \$26 million goodwill impairment charge to our Consolidated Financial Statements.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

Net Revenues by Geographic Region

Net revenues are recorded in the geographic region in which the senior coverage banker is located in the case of investment banking, or where the position was risk-managed within Capital Markets or the location of the investment advisor in the case of Asset Management. In addition, certain revenues associated with U.S. financial instruments and services that result from relationships with non-U.S. clients have been classified as non-U.S. revenues using an allocation consistent with our internal reporting. The following table presents net revenues by geographic region for the years ended December 31, 2007, 2006 and 2005 (amounts in thousands):

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Americas (1)	\$1,357,991	\$1,333,745	\$1,140,991
Europe	194,034	117,524	51,530
Asia (including Middle East)	16,065	6,333	12,179
Net Revenues	<u>\$1,568,090</u>	<u>\$1,457,602</u>	<u>\$1,204,700</u>

(1) Substantially all relates to U.S. results.

(20) Goodwill

We acquired LongAcre Partners Limited in May 2007. The LongAcre Partners Limited acquisition contained a five-year contingency for additional consideration to the selling owners, based on future revenues.

We acquired Putnam Lovell investment banking business (“Putnam”) in July 2007. The purchase price of the Putnam acquisition was \$14.7 million in cash and the acquisition did not contain any contingencies related to additional consideration.

The following is a summary of goodwill activity for the year ended December 31, 2007 (in thousands of dollars):

	Year Ended December 31, 2007
Balance, at December 31, 2006	\$ 257,321
Add: Acquisition(s)	44,235
Add: Accrued contingent consideration	42,507
Balance, at December 31, 2007	<u>\$ 344,063</u>

The acquisitions of LongAcre Partners Limited, Helix Associates, Randall & Dewey, and Quarterdeck Investment Partners, LLC (expired December 31, 2007) all contained a five-year contingency for additional consideration to the selling owners, based on future revenues. This additional consideration is paid in cash annually. There is no contractual dollar limit to the potential of additional consideration. During the quarter ended June 30, 2007, the Broadview International LLC contingency for additional consideration was modified and all remaining contingencies have been accrued for as of June 30, 2007. During the year ended December 31, 2007, we paid approximately \$25.7 million in cash related to contingent consideration that had been earned during the current year or prior periods.

None of the acquisitions listed above were considered material based on the small percentage each represents of our total assets, equity, revenues and net earnings.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

(21) Quarterly Dividends

The only restrictions on our present ability to pay dividends on our common stock are the dividend preference terms of our Series A convertible preferred stock and the governing provisions of the Delaware General Corporation Law.

Dividends per Common Share (declared and paid):

	<u>1st Quarter</u>	<u>2nd Quarter</u>	<u>3rd Quarter</u>	<u>4th Quarter</u>
2007	\$0.125	\$0.125	\$0.125	\$0.125
2006	\$0.075	\$0.125	\$0.125	\$0.125

On April 18, 2006, we declared a 2-for-1 stock split of all outstanding shares of common stock. The stock split was paid May 15, 2006 to stockholders of record as of April 28, 2006 and was effected as a stock dividend of one share of common stock for each one share outstanding on the record date. We also announced an increase to our quarterly dividend to \$0.125 per post-split share, which at the time represented a 67% increase from the previous dividend of \$0.075 per post split share.

(22) Variable Interest Entities (“VIEs”)*Jefferies High Yield Holdings*

Under the provisions of FIN 46(R) we determined that Jefferies High Yield Holdings and Jefferies Employees Special Opportunities Partners meet the definition of a VIE. We are the primary beneficiary of JHYH, and we and our employees (related parties) are the primary beneficiaries of JESOP. Therefore, we consolidate both JHYH and JESOP.

Managed CLO’s

We also own significant variable interests in various managed CLO’s and for which we are not the primary beneficiary and therefore do not consolidate these entities. In aggregate, these variable interest entities have assets approximating \$1.4 billion as of December 31, 2007. Our exposure to loss is limited to our capital contributions. The carrying value of our aggregate investment in these variable interest entities is \$16.7 million at December 31, 2007 and is included in Investments in Managed Funds on our Consolidated Statements of Financial Condition.

Third Party Managed Warehouse/Special Purpose Entity

We own a significant variable interest in Babson-Jefferies Loan Opportunity CLO, Ltd., a third party managed warehouse/special purpose entity, in which we have a 33% direct economic interest and a 17% indirect economic interest via Jefferies Finance LLC which we are not the primary beneficiary and therefore do not consolidate this entity. This variable interest entity has assets of approximately \$461.9 million as of December 31, 2007. The fair value of our direct and indirect interest in this variable interest entity is \$49.2 million (\$32.8 million direct interest and \$16.4 million indirect interest) at December 31, 2007. The investment in this entity is accounted for at fair value in accordance with FASB 157.

JEFFERIES GROUP, INC.
AND SUBSIDIARIES

Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006

(23) High Yield Secondary Market Trading

In January 2000, we created three broker-dealer entities that employed a trading and investment strategy substantially similar to that historically employed by our High Yield division. Two of these entities, the Jefferies Partners Opportunity Fund and the Jefferies Partners Opportunity Fund II, were principally capitalized with equity contributions from institutional and high net worth investors. The third fund, Jefferies Employees Opportunity Fund (and collectively with the two Jefferies Partners Opportunity Funds, referred to as the “High Yield Funds”), was principally capitalized with equity investments from our employees and was therefore consolidated into our Consolidated Financial Statements. The High Yield division and each of the funds shared gains or losses on trading and investment activities of the High Yield division on the basis of a pre-established sharing arrangement related to the amount of capital each had committed.

On April 2, 2007 we reorganized Jefferies High Yield Trading, LLC (“JHYT”) to conduct the secondary market trading activities previously performed by the High Yield division of Jefferies and the High Yield Funds. The activities of JHYT are overseen by Richard Handler, our Chief Executive Officer, and the same long-standing team previously responsible for these trading activities. JHYT is a registered broker-dealer engaged in the secondary sales and trading of high yield securities and special situation securities, including bank debt, post-reorganization equity, public and private equity, equity derivatives, credit default swaps and other financial instruments. JHYT makes markets in high yield and distressed securities and provides research coverage on these types of securities. JHYT is a wholly-owned subsidiary of Jefferies High Yield Holdings, LLC (“JHYH”).

We and Leucadia National Corporation (“Leucadia”) expect to increase our respective investments in JHYH to \$600 million each over time. We and Leucadia each have the right to nominate two of a total of four directors to JHYH’s board of directors, and each respectively own 50% of the voting securities of JHYH. JHYH provides the opportunity for additional capital investments over time from third party investors through two funds managed by us, Jefferies Special Opportunities Fund (“JSOP”) and Jefferies Employees Special Opportunities Fund (“JESOP”). The term of the arrangement is for six years, with an option to extend.

Under the provisions of FASB Interpretation No. 46(R), *Consolidation of Variable Interest Entities*, we determined that JHYH meets the definition of a variable interest entity. We are the primary beneficiary and consolidate JHYH.

Assets of JHYH were \$1.2 billion as of December 31, 2007. JHYH’s net revenue and formula-determined non-interest expenses for the nine month period ended December 31, 2007 (April 2, 2007, date of commencement, to December 31, 2007) amounted to \$44.7 million and \$30.3 million, respectively. These formula-determined non-interest expenses do not necessarily reflect the actual expenses of operating JHYH.

(24) Jefferies Finance LLC

On October 7, 2004, we entered into an agreement with Babson Capital and MassMutual to form Jefferies Finance LLC (“JFIN”), a joint venture entity created for the purpose of offering senior loans to middle market and growth companies. JFIN is a commercial finance company that provides a broad array of financial products to small and medium-sized businesses. JFIN’s primary focus is the origination and syndication of senior secured debt in the form of term and revolving loans. JFIN can also originate various other debt products such as second lien term, bridge and mezzanine loans as well as related equity co-investments. JFIN also purchases syndicated loans in the secondary market, including loans that are performing, stressed and distressed loan obligations.

In February 2006, we and MassMutual reached an agreement to double our equity commitments to JFIN. With an incremental \$125 million from each partner, the new total committed equity capitalization of JFIN is \$500 million. Loans are originated primarily through the investment banking efforts of Jefferies & Company, Inc. with Babson Capital providing primary credit analytics and portfolio management services. As of December 31, 2007, we have funded \$55.0 million of our aggregate \$250.0 million commitment leaving \$195.0 million unfunded. Our investment

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

in JFIN is accounted for under the equity method of accounting and is included in other investments in the Consolidated Statements of Financial Condition. Equity method gains and losses on JFIN are included in principal transactions in the Consolidated Statements of Earnings.

The following is a summary of selected financial information for JFIN as of and for each of the years in the three-year period ended December 31, 2007 (in millions):

	2007	2006	2005
Balance Sheet			
Total assets	\$1,007.5	\$309.9	\$139.7
Total liabilities	884.1	253.4	115.4
Total equity	123.4	56.5	24.3
Jefferies share of total equity	61.7	28.2	12.1

(25) Stock-based Compensation

We sponsor the following non-share based employee incentive plans:

Employee Stock Ownership Plan. We have an Employee Stock Ownership Plan (“ESOP”) which was established in 1988. We had no contributions and no compensation cost related to the ESOP in 2007, 2006 and 2005.

Profit Sharing Plan. We have a profit sharing plan, covering substantially all employees, which includes a salary reduction feature designed to qualify under Section 401(k) of the Internal Revenue Code. The compensation cost related to this plan was \$8,876,000, \$3,774,000, and \$3,230,000 in 2007, 2006 and 2005, respectively.

We sponsor the following share based employee incentive plans:

Incentive Compensation Plan. We have an Incentive Compensation Plan (“Incentive Plan”) which allows awards in the form of incentive stock options (within the meaning of Section 422 of the Internal Revenue Code), nonqualified stock options, stock appreciation rights, restricted stock, unrestricted stock, performance awards, dividend equivalents or other stock-based awards. The plan imposes a limit on the number of shares of our common stock that may be subject to awards. An award relating to shares may be granted if the aggregate number of shares subject to then-outstanding awards plus the number of shares subject to the award being granted do not exceed 30% of the number of shares issued and outstanding immediately prior to the grant.

The Incentive Plan allows for grants of restricted stock awards, whereby employees are granted restricted shares of common stock subject to forfeiture until the requisite service has been provided. Grants of restricted stock are generally subject to annual ratable vesting over a five year period (i.e., 20% of the number of shares granted vests each year for a five year award) with provisions related to retirement eligibility. In addition, vested shares are subject to transferability restrictions that lapse at the end of the award term. With certain exceptions, the employee must remain with us for several years after the date of grant to receive the full number of shares granted. The Incentive Plan also allows for grants of restricted stock units. Restricted stock units give a participant the right to receive fully vested shares at the end of a specified deferral period. Restricted stock units are generally subject to forfeiture conditions similar to those of our restricted stock awards. One advantage of restricted stock units, as compared to restricted stock, is that the period during which the award is deferred as to settlement can be extended past the date the award becomes non-forfeitable, allowing a participant to hold an interest tied to common stock on a tax deferred basis. Prior to settlement, restricted stock units carry no voting or dividend rights associated with the stock ownership, but dividend equivalents are paid or accrued.

Director Plan. We also have a Directors’ Stock Compensation Plan (“Directors’ Plan”) which provides for an annual grant to each non-employee director of \$100,000 of restricted stock or deferred shares (which are similar to restricted stock units). These grants are made automatically on the date directors are elected or reelected at our

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

annual shareholders' meeting. These grants vest three years after the date of grant and are expensed over the requisite service period.

Additionally, the Directors' Plan permits each non-employee director to elect to be paid annual retainer fees, meeting fees and fees for service as chairman of a Board committee in the form of cash, deferred cash or deferred shares. If deferred cash is elected, interest is credited to such deferred cash at the prime interest rate in effect at the date of each annual meeting of stockholders. If deferred shares are elected, dividend equivalents equal to dividends declared and paid on our common stock are credited to a Director's account and reinvested as additional deferred shares.

A total of 2,000,000 shares of our common stock is reserved under the Directors' Plan.

Employee Stock Purchase Plan. We also have an Employee Stock Purchase Plan ("ESPP") which we consider non-compensatory effective January 1, 2007. All regular full-time employees and employees who work part-time over 20 hours per week are eligible for the ESPP. Annual employee contributions are limited to \$21,250, are voluntary and are made via payroll deduction. The employee contributions are used to purchase our common stock. The stock price used is 95% of the closing price of our common stock on the last day of the applicable session (monthly).

The compensation cost related to these plans was \$0, \$1,604,000 and \$1,800,000 in 2007, 2006 and 2005, respectively.

Deferred Compensation Plan. We also have a Deferred Compensation Plan which was established in 2001. In 2007, 2006 and 2005, employees with annual compensation of \$200,000 or more were eligible to defer compensation by investing it in the Company's common stock ("DCP shares"), stock options (prior to 2004) or other alternatives on a pre-tax basis. The compensation deferred by our employees is expensed in the period earned. The Company's common stock can be invested in at a 10% discount through the Deferred Compensation Plan. The Company recognizes additional compensation cost related to this discount. This compensation cost was \$1,457,000, \$1,449,000 and \$1,329,000 for the years ended December 31, 2007, 2006 and 2005, respectively. A total of 16,000,000 shares of our common stock is reserved under the Deferred Compensation Plan. As of December 31, 2007, there were 6,011,000 DCP shares outstanding under the Plan.

The following table details the activity of DCP shares:

	Year Ended December 31,		
	2007	2006	2005
			(Shares in 000s)
DCP deferred shares			
Balance, beginning of year	6,730	7,356	6,810
Credits	673	717	552
Withdrawals	(1,392)	(1,343)	(6)
Balance, end of year	6,011	6,730	7,356

Adoption of FASB 123R

We adopted the fair value recognition provisions for share based awards pursuant to FASB 123R effective January 1, 2006. See Note 1 "Summary of Significant Accounting Policies" for a further discussion. The following disclosures are also being provided pursuant to the requirements of FASB 123R.

Prior to the adoption of FASB 123R, we presented all tax benefits resulting from share based compensation as cash flows from operating activities in the consolidated statements of cash flows. FASB 123R requires cash flows

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

resulting from tax deductions in excess of the grant-date fair value of share based awards to be included in cash flows from financing activities. Accordingly, we reflected the excess tax benefit of \$41.7 million and \$32.9 million related to share based compensation in cash flows from financing activities in the years ended December 31, 2007 and 2006, respectively.

In accordance with FASB 123R, the fair value of share based awards is estimated on the date of grant based on the market price of our common stock less the impact of selling restrictions subsequent to vesting, if any, and is amortized as compensation expense on a straight-line basis over the related requisite service periods, which are generally five years. As of December 31, 2007, there was \$313.3 million of total unrecognized compensation cost related to nonvested share based awards, which is expected to be recognized over a remaining weighted-average vesting period of approximately 3.7 years. The unrecognized compensation cost related to nonvested share based awards was recorded as unearned compensation in stockholders' equity at December 31, 2005. As part of the adoption of FASB 123R, the additional paid-in capital was reduced by the amount of unrecognized compensation cost related to nonvested share based awards granted prior to January 1, 2006.

The total compensation cost of all share based awards, including awards under the Deferred Compensation Plan, was \$145.8 million, \$86.2 million and \$82.9 million for the years ended December 31, 2007, 2006 and 2005, respectively.

We have historically and generally expect to issue new shares of common stock when satisfying our issuance obligations pursuant to share based awards, as opposed to reissuing common stock from treasury.

During the year ended December 31, 2007, we granted stock-based awards with a fair value of \$9.2 million, which was accrued in the year prior to the grant date.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

Restricted Stock and Restricted Stock Units (“Share Based Awards”)

The following tables detail the activity of restricted stock and restricted stock units:

	Year Ended December 31,		
	2007	2006	2005
	(Shares in 000s)		
Restricted stock			
Balance, beginning of year	4,336	7,358	10,541
Grants	5,417	395	2,597
Forfeited	(476)	(836)	(620)
RSU conversion	—	—	(3,112)
Vested	(1,960)	(2,581)	(2,048)
Balance, end of year	<u>7,317</u>	<u>4,336</u>	<u>7,358</u>

Restricted stock units (RSU)

Balance, beginning of year	28,718	24,662	12,058
Grants, includes dividends	5,723	4,403	9,477
Restricted stock conversion	—	—	3,112
Deferral expiration	(2,060)	(669)	(536)
Forfeited	(862)	(365)	(118)
Deferral of option gains	606	687	669
Balance, end of year	<u>32,125</u>	<u>28,718</u>	<u>24,662</u>

	Year Ended	Weighted
	December 31, 2007	Average Grant
	(Shares in 000s)	
	Date Fair Value	
Restricted stock		
Balance, beginning of year	4,336	\$18.54
Grants	5,417	\$28.06
Forfeited	(476)	\$25.03
Vested	(1,960)	\$18.09
Balance, end of period	<u>7,317</u>	\$25.34

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

	Year Ended December 31, 2007		Weighted Average Grant Date Fair Value	
	(Shares in 000s)		Future Service Required	No Future Service Required
	Future Service Required	No Future Service Required (2)		
Restricted stock units				
Balance, beginning of year	14,813	13,905	\$19.18	\$ 8.33
Grants, includes dividends	5,198	525(1)	\$24.12	\$ —(1)
Deferral expiration	—	(2,060)	\$ —	\$12.78
Forfeited	(503)	(359)	\$21.10	\$18.57
Vested	(4,629)	4,629	\$18.22	\$18.22
Grants related to stock option exercises	—	606	\$ —	\$11.35
Balance, end of period	<u>14,879</u>	<u>17,246</u>	\$21.18	\$10.18

(1) Represents dividend equivalents on restricted stock units declared during the twelve month period ending December 31, 2007.

(2) Represents fully vested restricted stock units which are still subject to transferability restrictions.

The compensation cost associated with restricted stock and restricted stock units amounted to \$144,382,000, \$83,137,000, and \$79,762,000 in 2007, 2006, and 2005, respectively. The average fair value of the vested awards during 2007 was approximately \$27.25 per share. The conversion of restricted stock into restricted stock units in 2005 did not impact compensation expenses because such conversation is a result of employee deferral elections under Section 409A of the Internal Revenue Code.

Stock Options

The fair value of all option grants are estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted-average assumptions used for all fixed option grants in 2004: dividend yield of 0.9%; expected volatility of 32.6%; risk-free interest rates of 3.0%; and expected lives of 4.8 years. There were no option grants during 2007, 2006 or 2005. A summary of our stock option activity for the years ended December 31, 2007, 2006 and 2005 is presented below (shares in thousands):

	2007		2006		2005	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	1,688	\$11.02	4,533	\$ 9.75	9,782	\$8.87
Granted	—	—	—	—	—	—
Exercised	(1,484)	11.18	(2,826)	8.98	(4,988)	8.23
Canceled	—	—	(19)	11.53	(261)	5.99
Outstanding at end of year	<u>204</u>	9.87	<u>1,688</u>	11.02	<u>4,533</u>	9.75
Options exercisable at year-end	204	9.87	1,688	11.02	4,533	9.75

The total intrinsic value of stock options exercised during 2007, 2006 and 2005 was \$8.2 million, \$51.9 million and \$46.2 million, respectively. Cash received from the exercise of stock options during 2007, 2006 and 2005 totaled \$5.2 million, \$17.5 million and \$33.7 million, respectively, and the tax benefit realized from stock options exercised during 2007, 2006 and 2005 was \$3.3 million, \$18.1 million and \$18.3 million, respectively.

**JEFFERIES GROUP, INC.
AND SUBSIDIARIES**

**Notes to Consolidated Financial Statements — (Continued)
December 31, 2007 and 2006**

The table below provides additional information related to stock options outstanding at December 31, 2007:

Dollars and shares in thousands, except per share data

December 31, 2007	Outstanding Net of Expected Forfeitures	Options Exercisable
Number of options	204	204
Weighted-average exercise price	\$ 9.87	\$ 9.87
Aggregate intrinsic value	\$2,687	\$2,687
Weighted-average remaining contractual term, in years	2.45	2.45

At December 31, 2007, the intrinsic value of vested options was approximately \$2.7 million for which tax benefits expected to be recognized in equity upon exercise are approximately \$1.1 million.

(26) Selected Quarterly Financial Data (Unaudited)

The following is a summary of unaudited quarterly statements of earnings for the years ended December 31, 2007 and 2006 (in thousands of dollars, except per share amounts):

	March	June	September	December	Year
2007					
Revenues	\$623,284	\$766,345	\$666,964	\$662,302	\$2,718,895
Earnings/(loss) before income taxes, minority interest, and cumulative effect of change in accounting principle	103,493	128,391	55,321	(41,471)	245,734
Net earnings/ (loss)	62,259	67,835	38,773	(24,202)	144,665
Net earnings/ (loss) per share:					
Basic	<u>\$ 0.44</u>	<u>\$ 0.48</u>	<u>\$ 0.27</u>	<u>\$ (0.17)</u>	<u>\$ 1.02</u>
Diluted	<u>\$ 0.42</u>	<u>\$ 0.45</u>	<u>\$ 0.26</u>	<u>\$ (0.17)</u>	<u>\$ 0.97</u>
2006					
Revenues	\$524,077	\$457,119	\$468,664	\$513,348	\$1,963,208
Earnings before income taxes, minority interest, and cumulative effect of change in accounting principle	97,407	80,715	76,337	94,195	348,654
Net earnings	58,447	45,580	45,940	55,783	205,750
Net earnings per share:					
Basic	<u>\$ 0.45</u>	<u>\$ 0.34</u>	<u>\$ 0.34</u>	<u>\$ 0.41</u>	<u>\$ 1.54</u>
Diluted	<u>\$ 0.41</u>	<u>\$ 0.32</u>	<u>\$ 0.32</u>	<u>\$ 0.38</u>	<u>\$ 1.42</u>

Table of Contents

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure.

None

Item 9A. Controls and Procedures.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of December 31, 2007. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures as of December 31, 2007 are functioning effectively to provide reasonable assurance that the information required to be disclosed by us in reports filed under the Securities Exchange Act of 1934 is (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding disclosure. A controls system cannot provide absolute assurance, however, that the objectives of the controls system are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

No change in our internal control over financial reporting occurred during the fourth quarter of 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Management's annual report on internal control over financial reporting is contained in Part II, Item 8 of this report.

Our Chief Executive Officer and Chief Financial Officer filed with the SEC as exhibits to our Form 10-K for the year ended December 31, 2007 and are filing as exhibits to this report, the certifications required by Section 302 of the Sarbanes-Oxley Act of 2002 and Rule 13a-14 (a)/15d-14(a) of the Securities Exchange Act of 1934.

Item 9B. Other Information.

None

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

Information with respect to this item will be contained in the Proxy Statement for the 2008 Annual Meeting of Stockholders, which is incorporated herein by reference.

Item 11. Executive Compensation.

Information with respect to this item will be contained in the Proxy Statement for the 2008 Annual Meeting of Stockholders, which is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

Information with respect to this item will be contained in the Proxy Statement for the 2008 Annual Meeting of Stockholders, which is incorporated herein by reference.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

Information with respect to this item will be contained in the Proxy Statement for the 2008 Annual Meeting of Stockholders, which is incorporated herein by reference.

Table of Contents

Item 14. Principal Accountant Fees and Services.

Information with respect to this item will be contained in the Proxy Statement for the 2008 Annual Meeting of Stockholders, which is incorporated herein by reference.

PART IV

Item 15. Exhibits and Financial Statement Schedules.

	<u>Pages</u>
(a)1. Financial Statements	
Included in Part II of this report:	
Report of Independent Registered Public Accounting Firm	46
Consolidated Statements of Financial Condition	47
Consolidated Statements of Earnings	49
Consolidated Statements of Changes in Stockholders' Equity and Comprehensive Income	50
Consolidated Statements of Cash Flows	51
Notes to Consolidated Financial Statements	53
(a)2. Financial Statement Schedules	
All Schedules are omitted because they are not applicable or because the required information is shown in the Consolidated Financial Statements or notes thereto.	
(a)3. Exhibits	
2* Amendment No. 1 dated as of November 1, 2007 to the Share and Membership Interest Purchase Agreement dated as of July 18, 2005, among Brian P. Friedman, James L. Luikart, 2055 Partners L.P., Jefferies Capital Partners IV LLC, JCP IV LLC, and Jefferies Group, Inc.	
3.1 Registrant's Amended and Restated Certificate of Incorporation is incorporated by reference to Exhibit 3 of Registrant's Form 8-K filed on May 26, 2004.	
3.2 Registrant's Certificate of Designations of 3.25% Series A Cumulative Convertible Preferred Stock is incorporated by reference to Exhibit 3.1 of Registrant's Form 8-K filed on February 21, 2006.	
3.3 Registrant's By-Laws as amended and restated on December 3, 2007 are incorporated by reference to Exhibit 3 of Registrant's Form 8-K filed on December 4, 2007.	
4 Instruments defining the rights of holders of long-term debt securities of the Registrant and its subsidiaries are omitted pursuant to Item 601(b)(4)(iii) of Regulation S-K. Registrant hereby agrees to furnish copies of these instruments to the Commission upon request.	
10.1 Jefferies Group, Inc. Deferred Compensation Plan, as Amended and Restated as of January 1, 2003 is incorporated by reference to Exhibit 4.1 of Registrant's Form S-8 filed on July 14, 2003.	
10.2 Amendment No. 1, dated as of December 1, 2005, to the Jefferies Group, Inc. Deferred Compensation Plan, as Amended and Restated as of January 1, 2003 is incorporated by reference to Exhibit 10.2 of Registrant's Form 10-K filed on March 1, 2006.	
10.3 Jefferies Group, Inc. 2003 Incentive Compensation Plan is incorporated by reference to Appendix 4 of Registrant's Proxy Statement filed on April 4, 2003.	
10.4 Jefferies Group, Inc. Stock Option Gain and Stock Award Deferral Program effective as of January 21, 2003 is incorporated by reference to Exhibit 10.1 of Registrant's Form 10-Q filed on May 9, 2003.	
10.5 Jefferies Group, Inc. 1999 Directors' Stock Compensation Plan is incorporated by reference to Exhibit 10.2 of Registrant's Form 10 filed on April 20, 1999.	
10.6* Form of Restricted Stock Agreement pursuant to the Jefferies Group, Inc. 2003 Incentive Compensation Plan.	
10.7* Form of Restricted Stock Units Agreement pursuant to the Jefferies Group, Inc. 2003 Incentive Compensation Plan.	

Table of Contents

- 10.8 Summary of Non-Employee Director Compensation (as amended on January 17, 2006) pursuant to the Jefferies Group, Inc. 1999 Directors' Stock Compensation Plan is incorporated by reference to Exhibit 10 of Registrant's Form 8-K filed on January 18, 2006.
- 10.9 Summary of the 2007 and 2008 Executive Compensation for Messrs. Handler and Friedman is incorporated by reference to Exhibit 10 of Registrant's Form 8-K filed on August 25, 2006.
- 10.10 Summary of the 2007 Executive Compensation for Messrs. Schenk and Feller and Ms. Syrjamaki is incorporated herein by reference to Exhibit 10.2 of the Registrant's Form 10-Q filed on May 9, 2007.
- 10.11 Deferred Compensation Agreement, as amended and restated as of December 29, 2005, between Jefferies & Company, Inc. and Richard B. Handler is incorporated by reference to Exhibit 10.15 of Registrant's Form 10-K filed on March 1, 2006.
- 10.12* Letter Agreement dated October 8, 2007 between Peregrine C. Broadbent and Jefferies Group, Inc.
- 10.13 Letter agreement dated June 1, 2007 between Joseph A. Schenk and Jefferies Group, Inc. is incorporated herein by reference to Exhibit 10.3 of the Registrant's Form 10-Q filed on August 9, 2007.
- 10.14 Letter agreement dated April 16, 2007 between Maxine Syrjamaki and Jefferies Group, Inc. is incorporated herein by reference to Exhibit 10.4 of the Registrant's Form 10-Q filed on August 9, 2007.
- 10.15 Consulting Agreement dated August 1, 2007 between Maxine Syrjamaki and Jefferies Group, Inc. is incorporated herein by reference to Exhibit 10.5 of the Registrant's Form 10-Q filed on August 9, 2007.
- 10.16 Letter agreement dated April 19, 2006 between Charles J. Hendrickson and Jefferies Group, Inc. is incorporated herein by reference to Exhibit 10.6 of the Registrant's Form 10-Q filed on August 9, 2007.
- 10.17 Purchase Agreement dated June 4, 2007 among Jefferies Group, Inc., Jefferies & Company, Inc., Citigroup Global Markets Inc., Merrill Lynch, Pierce, Fenner & Smith Incorporated, BNP Paribas Securities Corp., BNY Capital Markets, Inc., Goldman, Sachs & Co., HSBC Securities (USA) Inc., J.P. Morgan Securities Inc., Greenwich Capital Markets, Inc., Banc of America Securities LLC, Fox-Pitt, Kelton Incorporated, Keefe, Bruyette & Woods, Inc., and SG Americas Securities, LLC is incorporated by reference to Exhibit 10.1 of Registrant's Form 8-K filed on June 5, 2007.
- 10.18 Master Agreement for the Formation of a Limited Liability Company, dated as of February 28, 2007 among Jefferies Group, Inc., Jefferies & Company, Inc. and Leucadia National Corporation is incorporated by reference to Exhibit 10.3 of Registrant's Form 10-Q filed on May 9, 2007.
- 12.1* Computation of Ratio of Earnings to Fixed Charges.
- 21* List of Subsidiaries.
- 23* Consent of KPMG LLP.
- 31.1* Rule 13a-14(a)/15d-14(a) Certification by Chief Financial Officer.
- 31.2* Rule 13a-14(a)/15d-14(a) Certification by Chief Executive Officer.
- 32* Rule 13a-14(b)/15d-14(b) and Section 1350 of Title 18 U.S.C. Certification by the Chief Executive Officer and Chief Financial Officer.

* Filed herewith.

Exhibits 10.1, 10.2, 10.3, 10.4, 10.5, 10.6, 10.7, 10.8, 10.9, 10.10, 10.11, 10.12, 10.13, 10.14, 10.15 and 10.16 are management contracts or compensatory plans or arrangements.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

JEFFERIES GROUP, INC.

By /s/ RICHARD B. HANDLER
 Richard B. Handler
 Chairman of the Board of Directors,
 Chief Executive Officer

Dated: February 28, 2008

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

Name	Title	Date
<u>/s/ RICHARD B. HANDLER</u> Richard B. Handler	Chairman of the Board of Directors, Chief Executive Officer	February 28, 2008
<u>/s/ PEREGRINE C. BROADBENT</u> Peregrine C. Broadbent	Executive Vice President and Chief Financial Officer	February 28, 2008
<u>/s/ BRIAN P. FRIEDMAN</u> Brian P. Friedman	Director and Chairman, Executive Committee	February 28, 2008
<u>/s/ W. PATRICK CAMPBELL</u> W. Patrick Campbell	Director	February 22, 2008
<u>/s/ RICHARD G. DOOLEY</u> Richard G. Dooley	Director	February 28, 2008
<u>/s/ ROBERT E. JOYAL</u> Robert E. Joyal	Director	February 26, 2008
<u>/s/ FRANK J. MACCHIAROLA</u> Frank J. Macchiarola	Director	February 24, 2008
<u>/s/ MICHAEL T. O'KANE</u> Michael T. O'Kane	Director	February 28, 2008

**AMENDMENT NO. 1
TO
SHARE AND MEMBERSHIP INTEREST PURCHASE AGREEMENT**

among

BRIAN P. FRIEDMAN

2055 PARTNERS L.P.

JAMES L. LUIKART

and

JEFFERIES GROUP, INC.

Dated as of November 1, 2007

LIST OF EXHIBITS

- Exhibit A — Share and Membership Interest Purchase Agreement dated as of July 18, 2005
 - Exhibit B — Amended and Restated Limited Liability Agreement of JCP IV LLC dated as of July 16, 2007
 - Exhibit B-1 — Member Register of JCP IV LLC with Respect to Fund IV As of July 16, 2007
 - Exhibit B-2 — Pro Forma Member Register of JCP IV LLC with Respect to Fund IV, as of November 1, 2007
 - Exhibit C — Schedule 1.4 — Jefferies Shares
 - Exhibit D — Cash Payment
 - Exhibit E — Previously Funded Capital Contributions
-

AMENDMENT NO. 1

TO

SHARE AND MEMBERSHIP INTEREST PURCHASE AGREEMENT

THIS AMENDMENT NO. 1 to SHARE AND MEMBERSHIP INTEREST PURCHASE AGREEMENT (this "Agreement") is made as of November 1, 2007, by and among Brian P. Friedman, an individual, James L. Luikart, an individual (Messrs. Friedman and Luikart are each a "Managing Member" and together are the "Managing Members"), 2055 Partners L.P., a Delaware limited partnership ("2055 Partners" and, together with the Managing Members, the "Selling Members"), Jefferies Capital Partners IV LLC (the "Manager"), a Delaware limited liability company, JCP IV LLC (the "GP" and, together with the Manager, the "Companies"), a Delaware limited liability company, and Jefferies Group Inc. ("Jefferies"), a Delaware corporation. Capitalized terms used but not otherwise defined herein shall have the respective meanings set forth in the Share and Membership Interest Purchase Agreement by and among the Selling Members, the Companies and Jefferies, dated as of July 18, 2005, a copy of which is attached as Exhibit A (the "Purchase Agreement").

RECITALS

WHEREAS, the Selling Members, the Companies and Jefferies desire to amend the Purchase Agreement in certain respects;

WHEREAS, the Limited Liability Company Agreement of the GP was amended and restated pursuant to the Amended and Restated Limited Liability Company Agreement of JCP IV LLC dated as of July 16, 2007;

WHEREAS, the aggregate amount of Committed Capital committed to Fund IV at the time of the Fund IV Final Closing was \$600 million;

WHEREAS, Jefferies is a limited partner in the Institutional Fund, with a capital commitment to the Institutional Fund in the amount of \$49 million;

WHEREAS, the parties desire to hold the Closing under the Purchase Agreement concurrently with the execution of this Agreement;

NOW, THEREFORE, in consideration of the agreements and obligations set forth herein and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereby agree as follows:

TERMS

1. Amendment of Certain Exhibits and Schedules .

(a) Exhibit B to the Purchase Agreement (i.e., the GP Operating Agreement) is hereby replaced in its entirety by the Amended and Restated Limited Liability Company Agreement of JCP IV LLC dated as of July 16, 2007, a copy of which is attached hereto as Exhibit B .

(b) Exhibit B-1 to the Purchase Agreement is hereby replaced in its entirety with Exhibit B-1 hereto.

(c) Exhibit B-2 to the Purchase Agreement is hereby replaced in its entirety with Exhibit B-2 hereto.

(d) Schedule 1.4 to the Purchase Agreement is hereby replaced in its entirety with Exhibit C hereto, which revised Schedule 1.4 reflects that a 2 for 1 stock split with respect to Group Shares occurred after June 30, 2005 as well as that at the time of the Fund IV Final Closing, Committed Capital to Fund IV was \$600 million.

2. Jefferies Shares; Earnout Shares . In lieu of the adjustment to the number of Jefferies Shares contemplated by the second sentence of Section 1.4 of the Purchase Agreement (but not in lieu of the adjustment for the 2 for 1 stock split, which adjustment is effected in Section 1(d) above), at the Closing under the Purchase Agreement, Jefferies shall pay to each Managing Member the amount set forth on Exhibit D hereto opposite the name of such Managing Member. Section 6.1 of the Purchase Agreement is hereby amended by adding at the end thereof a new paragraph as follows:

“(f) If any Earnout Shares are forfeited pursuant to this Section 6.1, each Managing Member shall pay to Jefferies an amount equal to \$0.15 for each Earnout Share so forfeited by such Managing Member (i.e., \$65,000 if all Earnout Shares are forfeited) (such a per share amount to be adjusted for any stock split, stock dividend or similar transaction with respect to Group Shares after November 1, 2007).”

3. Closing Date; Previously Funded Capital Contributions . The parties hereto agree that the Closing under the Purchase Agreement shall take place on November 1, 2007, concurrently with the execution hereof. As of November 1, 2007:

(a) The Managing Members have funded their respective Working Capital Commitments in the amounts set forth on Exhibit E hereto;

(b) The Selling Members have funded Capital Commitments (net of distributions) to the GP in the amounts set forth on Exhibit E hereto;
and

(c) Jefferies has funded Capital Commitments (net of distributions) to the Institutional Fund in the amount set forth on Exhibit E hereto.

Accordingly, and in accordance with Section 1.6 of the Purchase Agreement, at the Closing, Jefferies shall pay to the Managing Members and Selling Members the amounts set forth on Exhibit E hereto, and the Selling Members shall pay to Jefferies the amounts set forth on Exhibit E hereto, it being understood that as a matter of convenience, such amounts shall be set off against each other as appropriate with only the net amounts paid to the appropriate party, all as set forth and calculated in Exhibit E hereto.

4. Successors and Assigns. Except as otherwise provided herein or in the Manager Operating Agreement or the GP Operating Agreement, the terms and conditions of this Agreement shall inure to the benefit of and be binding upon the respective successors and assigns of the parties (including transferees of any Purchased Interests in accordance with the Manager Operating Agreement or the GP Operating Agreement). Nothing in this Agreement, express or implied, is intended to confer upon any party, other than the parties hereto or their respective successors and assigns, any rights, remedies, obligations or liabilities under or by reason of this Agreement, except as expressly provided in this Agreement.

5. Governing Law. This Agreement shall be governed by and construed under the laws of the State of New York as applied to agreements among New York residents entered into and to be performed entirely within New York.

6. Amendments and Waivers. Any term of this Agreement may be amended and the observance of any term of this Agreement may be waived (either generally or in a particular instance and either retroactively or prospectively) only with the written consent of each of the parties hereto. Any amendment or waiver affected in accordance with this paragraph shall be binding upon each of the parties.

7. Entire Agreement. This Agreement, the Purchase Agreement, the Manager Operating Agreement, the GP Operating Agreement and the documents referred to herein constitute the entire agreement among the parties with respect to the subject matter hereof and supersedes all prior and contemporaneous agreements and understandings with respect to the subject matter hereof. No party shall be liable or bound to any other party in any manner by any warranties, representations or covenants except as specifically set forth herein or in the Manager Operating Agreement or the GP Operating Agreement, as applicable. Each party acknowledges that there are no, and it is not relying upon any, representations or warranties by or on behalf of any other party hereto other than those expressly set forth herein. Except as expressly amended herein, the Purchase Agreement shall remain in full force and effect.

8. Counterparts. This Agreement may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument.

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

JEFFERIES GROUP, INC.

By: /s/ Joseph A. Schenk

Name: Joseph A. Schenk

Title: Chief Financial Officer

JEFFERIES CAPITAL PARTNERS IV LLC

By: /s/ Brian P. Friedman

Name:

Title:

JCP IV LLC

By: JEFFERIES CAPITAL PARTNERS IV LLC,
its Managing Member

By: /s/ Brian P. Friedman

Name:

Title: Managing Member

/s/ Brian P. Friedman

Brian P. Friedman

/s/ James L. Luikart

James L. Luikart

2055 PARTNERS, L.P.

By: /s/ Brian P. Friedman
its general partner

Exhibits Omitted

JEFFERIES GROUP, INC.
2003 INCENTIVE COMPENSATION PLAN
RESTRICTED STOCK AGREEMENT

AGREEMENT dated as of [insert grant date] (the “Grant Date”), between JEFFERIES GROUP, INC., a Delaware corporation (the “Company”), and [insert employee name] (“Employee”).

WHEREAS, the Compensation Committee of the Board of Directors (the “Committee”) has determined that the Company shall make a grant of Restricted Stock to Employee under the Company’s 2003 Incentive Compensation Plan (the “2003 Plan”), in furtherance of the purposes of the 2003 Plan and in recognition of Employee’s service as an employee of the Company and/or its subsidiaries; and

WHEREAS, the Company desires to confirm the grant of Restricted Stock, and to set forth the terms and conditions of such grant, and Employee desires to accept such grant and agree to the terms and conditions thereof, as set forth in this Restricted Stock Agreement (the “Agreement”).

NOW, THEREFORE, in consideration of the mutual covenants contained herein, the parties hereto agree as follows:

1. **Grant of Restricted Stock.** The Company hereby confirms the grant, under the 2003 Plan, to Employee on the Grant Date set forth above of [insert number of shares] shares of Restricted Stock (the “Restricted Stock”). The Restricted Stock is subject to all of the terms and conditions set forth in this Agreement, including the restrictions set forth in Section 3. The Company shall issue in the name of Employee, as promptly as practicable, one or more certificates representing the shares of Common Stock, \$.0001 par value (“Common Stock”), granted as Restricted Stock or shall instruct its transfer agent to issue Restricted Stock which shall be maintained in “book entry” form on the books of the transfer agent. The Restricted Stock shall bear the restrictive legend and be subject to the other terms set forth in Section 3. For purposes of this Agreement, each tranche of shares of Common Stock will remain Restricted Stock until the expiration of the Restrictions (as defined in Section 3) on such tranche or the forfeiture of the Restricted Stock, without regard to extraordinary transactions which may affect the Common Stock except as may be otherwise provided under the 2003 Plan and determinations of the Committee thereunder.

2. **Incorporation of 2003 Plan by Reference .** The Restricted Stock has been granted to Employee under the 2003 Plan. The 2003 Plan and information regarding the 2003 Plan, including documents that constitute the “Prospectus” for the 2003 Plan under the Securities Act of 1933, can be viewed and printed out from the Company’s secure Intranet website, www.corp.jefferies.com (go to People Services, then to Plan Documents). All of the terms, conditions, and other provisions of the 2003 Plan are hereby incorporated by reference into this Agreement. Capitalized terms used in this Agreement but not defined herein shall have the same meanings as in the 2003 Plan. If there is any conflict between the provisions of this Agreement and the provisions of the 2003 Plan, the provisions of the 2003 Plan shall govern. Employee hereby acknowledges that the 2003 Plan and information regarding the 2003 Plan has been made readily available to him and agrees to be bound by all the terms and provisions thereof (as presently in effect

or hereafter amended), rules and regulations adopted from time to time thereunder, and by all decisions and determinations of the Committee made from time to time thereunder.

3. Restrictions on Restricted Stock and Related Terms.

(a) Restrictions Generally. Until they expire in accordance with Section 3(b), the following restrictions (the “Restrictions”) shall apply to the Restricted Stock: (1) the Restricted Stock shall be subject to a risk of forfeiture as set forth in Section 3(b) (the “Risk of Forfeiture”), and (2) Employee shall not sell, transfer, assign, pledge, margin, or otherwise encumber or dispose of the Restricted Stock (except for transfers and forfeitures to the Company). Upon issuance of certificates or the transfer agent making the appropriate entry on its books representing the Restricted Stock in the name of Employee, which shall occur as promptly as practicable after the Grant Date, Employee shall be entitled to receive dividends on the Restricted Stock as provided in Section 3(e), shall be entitled to vote Restricted Stock on any matter submitted to a vote of holders of Common Stock, and shall have all other rights in connection with such Restricted Stock as would a holder of Common Stock except as otherwise expressly provided under this Section 3, and subject to the Committee’s authority (including authority to make adjustments to Awards) under the 2003 Plan.

(b) Risk of Forfeiture and Expiration Thereof. Unless otherwise determined by the Committee, if for any reason Employee’s employment by the Company or a subsidiary terminates prior to the expiration of the Restrictions, and immediately thereafter Employee is not employed by the Company or any direct or indirect subsidiary of Company (“Termination”), except as set forth below, all Restricted Stock as to which the Restrictions have not expired at or before the time of such Termination (and any related property resulting from Section 3(e)(iii)) shall be forfeited at the time of such Termination. Except as otherwise specifically set forth herein, the Restrictions shall expire as to [insert percentage to vest]% of the shares of Restricted Stock (and any related property) on each of [insert vesting dates] (each being a “Vesting Date,” at which date such Restricted Stock is deemed “vested”).

- (i) *Death or Disability*. If Employee dies or if such Termination is by reason of Employee’s Disability (as defined below), then such forfeiture shall not occur, and the Restrictions as to all of the shares of Restricted Stock shall immediately expire upon such death or Termination.
- (ii) *Retirement or Involuntary Termination by the Company not for Cause (and not subject to Section 3(b)(iii))*. In the event of Employee’s Retirement or an involuntary Termination of Employment by the Company not for Cause (other than a Termination not for Cause following a Change in Control), provided that the Employee executes a settlement agreement and release in such form as may be requested by the Company within 21 days (or such longer period as may be required by law) (and provided further that any period of revocation required by law has expired without Employee exercising his right to revoke his agreement to the settlement agreement and release), Restricted Stock not then or previously vested shall not then be forfeited, but thereafter shall be forfeited if there occurs a Forfeiture Event prior to the earlier of the Vesting Date for such Restricted Stock or Employee’s death. A “Forfeiture Event” shall be deemed to occur if, following

Employee's Retirement or Termination by the Company not for Cause, Employee renders services for any organization or engages (either as owner, investor, partner, stockholder, employer, employee, consultant, advisor, or director) directly or indirectly, in any business which is or becomes competitive with the Company, its subsidiaries or affiliates, or otherwise engaged in conduct violating Section 7.4(a), 7.4(b) or 7.4(c) of the Plan. However, following Employee's Retirement or Termination by the Company not for Cause, it shall not constitute a Forfeiture Event if Employee purchases stock or other securities of an organization or business so long as the stock or other securities are listed upon a recognized securities exchange or traded over-the-counter and such investment does not represent a greater than five percent equity interest in the organization or business. If Employee does not sign a settlement agreement and release within the time period requested by the Company (or signs and then timely revokes his agreement to the settlement agreement and release), all Restricted Stock which is not vested at the date of Termination will be forfeited.

- (iii) *Termination not for Cause Following a Change in Control* . If, following a Change in Control, Employee's employment is terminated not for Cause by the Company or its successor, Restrictions on all of the then-outstanding Restricted Stock not vested at the date of Termination will immediately expire and such Restricted Stock will immediately vest. If a Change in Control occurs followed by Termination of Employment by the Company not for Cause and a determination is made by the Company pursuant to Sections 280G and 4999 of the Code that a "golden parachute" excise tax will be payable in connection with compensation to Employee hereunder, Employee's right to accelerated vesting of the shares upon the Change in Control, to the extent such right results in "parachute payments" (as such term is defined in Code Section 280G), shall be limited to the extent just necessary to avoid the excise tax. This limitation shall be applied in a manner that maximizes the number of shares as to which accelerated vesting can apply (or, stated conversely, any limitation on acceleration of vesting shall apply first to those shares with the lengthiest remaining vesting period, which shares would result in the highest "parachute payments").
- (iv) *Termination by Employee for any reason or Termination by the Company for Cause* . In the event of Employee's Termination of Employment by Employee for any reason (other than due to Retirement, death or Disability) or by the Company for Cause, the portion of the then-outstanding Restricted Stock not vested at the date of termination will be forfeited.
- (c) Certain Definitions. The following definitions apply for purposes of this Agreement:
 - (i) "Cause" means Employee's:
Neglect, failure or refusal to timely perform the duties of Employee's employment (other than by reason of a physical or mental illness or impairment), or Employee's gross negligence in the performance of his or her duties;

Material breach of any agreements, covenants and representations made in any employment agreement or other agreement with the Company or any of its subsidiaries or affiliates or violation of internal policies or procedures as are in effect as of the date such action is taken, including but not limited to the Company's Code of Ethics, as amended from time to time;

Violation of any law, rule, regulation or by-law of any governmental authority (state, federal or foreign), any securities exchange or association or other regulatory or self-regulatory body or agency applicable to Employee, the Company, its subsidiaries or affiliates or any material general policy or directive of the Company, its subsidiaries or affiliates;

Conviction of, or plea of guilty or nolo contendere to, a crime involving moral turpitude, dishonesty, fraud or unethical business conduct, or any felony of any nature whatsoever;

Failure to obtain or maintain any registration, license or other authorization or approval that Employee is required to maintain or that the Company, its subsidiaries or affiliates reasonably believes is required in order for Employee to perform his or her duties, provided, however, that Employee shall be given written notice of any such registration, license or other authorization or approval that he or she is required to obtain and a reasonable period of time to obtain such registration, license, or other authorization or approval; or

Willful failure to execute a directive of the board of directors of the Company or any of its subsidiaries or affiliates, the Executive Committee of any of the Company's subsidiaries or affiliates, or Employee's supervisor (unless such directive would result in the commission of an act which is illegal or unethical) or commission of an act against the directive of such Board, such Executive Committee or Employee's supervisor.

- (ii) A "Change in Control" shall be deemed to have occurred if any of the following conditions shall have been satisfied after the Grant Date:

Any person (as defined in section 3(a)(9) of the Securities Exchange Act of 1934, as such term is modified in Section 13(d)), other than (i) an employee plan established by the Company or any of its subsidiaries or (ii) any group of Company employees holding shares subject to agreements relating to the voting of such shares, becomes a beneficial owner, directly or indirectly, of more than 51% of the voting stock of the Company;

The consummation of a merger or consolidation of the Company with any other corporation or any other entity, or the issuance of voting securities in connection with a merger or consolidation of the Company, if the holders of the Company's voting securities immediately prior to such transaction hold in the aggregate less than a majority of the then outstanding voting securities of the Company (or any successor

company or entity) entitled to vote generally in the election of the directors of the Company (or such other company or entity) after such transaction;

The sale or disposition by the Company of all or substantially all of its assets in which one person or more than one person acting as a group acquires assets from the Company that have a total gross fair market value equal to more than 50% of the total gross fair market value of all of the assets of the Company immediately prior to such acquisition; or

A change in the composition of the Board of Directors of the Company such that individuals who, as of the date of this agreement, constitute the Board of Directors of the Company (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board of Directors of the Company; provided, however, that any individual becoming a member of the Board of Directors of the Company subsequent to the date of this agreement whose election, or nomination for election by the shareholders of the Company, was approved by a vote of at least a majority of the directors then constituting the Incumbent Board shall be considered as if that individual were a member of the Incumbent Board.

- (iii) "Disability" means that Employee has commenced receipt of long-term disability benefits under the Company's long-term disability policy as in effect at the date of Employee's termination of employment.
- (iv) "Retirement" means retirement after attaining the age at which an Employee's age plus his years of service equals age [60] [62], provided, however, that (a) Employee has provided a minimum of 7.5 years of service to the Company, its subsidiaries or affiliates [and (b) such retirement is more than 36 months after the Grant Date]. For this purpose, years of service shall be credited for each twelve month period beginning on the date of Employee's commencement of employment with the Company and on each anniversary thereof during which the Employee was in active employment with the Company. [For the avoidance of doubt, Employee's retirement within 36 months of the Grant Date, shall not qualify as a Retirement hereunder.]
- (v) "Termination" or "Termination of Employment" means the event by which Employee ceases to be employed by the Company, its subsidiaries and affiliates and immediately thereafter is not employed by any other entity included within the Company.

(d) Evidence of Restricted Stock. Restricted Stock shall be evidenced either (i) by issuance of one or more certificates in the name of Employee or (ii) by an entry on the books of the Company's transfer agent. The Restricted Stock shall bear an appropriate legend referring to the terms, conditions, and Restrictions applicable hereunder in substantially the following form:

The shares of Common Stock represented by this certificate (the "Shares") have been granted by Jefferies Company, Inc. (the "Company") as Restricted Stock under the Company's 2003 Incentive Compensation Plan (the "2003 Plan") and the Restricted Stock Agreement (the

“Agreement”), dated as of [insert date of agreement] between the registered owner named hereon (“Employee”) and the Company. Under the 2003 Plan and the Agreement, copies of which may be examined at the office of the Secretary of the Company, until [insert last vesting date] (subject to acceleration in certain circumstances), Employee shall not sell, transfer, assign, pledge, margin, or otherwise encumber or dispose of the Shares (except for transfers and forfeitures to the Company), and Employee shall forfeit the Shares upon termination of Employee’s employment with the Company and its subsidiaries in certain circumstances. The Shares are subject to certain other terms and conditions set forth in the Agreement.

Unless otherwise determined by the Company, certificates representing Restricted Stock shall remain in the physical custody of the General Counsel of the Company or his designee until such time as Restrictions on such Restricted Stock have expired. In addition, Restricted Stock shall be subject to such stop-transfer orders and other restrictive measures as the General Counsel of the Company shall deem advisable under federal or state securities laws, rules and regulations thereunder, and the rules of the New York Stock Exchange (the “NYSE”) or any national securities exchange or automated quotation system on which Common Stock is then listed or quoted, or to implement the Restrictions.

(e) Dividends and Distributions; Stock Splits . Employee shall be entitled to receive dividends and distributions payable with respect to Restricted Stock if and to the extent that he or she is the record owner of such Restricted Stock on any record date for such a dividend or distribution and he or she has not forfeited such Restricted Stock on or before the payment date for such dividend or distribution, and Restricted Stock shall be subject to any stock split, subject to the following terms and conditions:

- (i) In the event of a cash dividend or distribution on Common Stock which is not a large, special and non-recurring dividend or distribution (as determined by the Board of Directors), such dividend or distribution shall be paid in cash to Employee;
- (ii) In the event of a large, special and non-recurring cash dividend payable on Common Stock, the Company shall retain the amount of such cash dividend and, in lieu of delivery thereof, shall grant to Employee additional shares of Restricted Stock having a fair market value (as determined by the Committee) at the payment date of the dividend or distribution equal to the amount of cash paid as a dividend or distribution on each share of Common Stock multiplied by the number of shares of Employee’s Restricted Stock. Such additional Restricted Stock will be subject to the same Restrictions and to such other terms and conditions as applied to the Restricted Stock;
- (iii) In the event of any non-cash dividend or distribution in the form of property other than Common Stock payable on Common Stock (including shares of a subsidiary of the Company distributed in a spin-off) (unless the Committee determines to make equitable adjustments under Section 5.3 of the 2003 Plan in lieu of the procedure specified in this Section 3(e)(iii)), the Company shall retain in its custody the property so distributed in respect of Employee’s Restricted Stock, which property

will be subject to the same Restrictions and to such other terms and conditions of the 2003 Plan and this Agreement as apply to the Restricted Stock with respect to which such property was distributed, until such time as the Restrictions expire or the Restricted Stock (together with such property) are forfeited. To the greatest extent practicable, such property will be treated the same as such Restricted Stock with respect to which the property was distributed, including in the event of any dividends or distributions paid in respect of such property or with respect to the placement of any legend on certificate(s) or documents representing such property.

(iv) In the event of a dividend or distribution in the form of Common Stock or split-up of shares, the Common Stock issued or delivered as such dividend or distribution or resulting from such split-up will be deemed to be additional Restricted Stock and will be subject to the same Restrictions and to such other terms and conditions of the 2003 Plan and this Agreement as applied to the Restricted Stock with respect to which such dividend or distribution was paid or which was subject to such split-up.

(f) Delivery of Certificates. Upon expiration of Restrictions on any Restricted Stock, the shares previously issued in the name of Employee as such Restricted Stock shall no longer be deemed to be Restricted Stock, and the Company shall, subject to the satisfactory payment of any federal, state or foreign taxes or other amounts referred to in Section 4, below, cause any legend referring to the Restrictions to be removed from the certificate(s) representing such shares and shall deliver such certificate(s) (together with any property resulting from Section 3(e)(iii)) to Employee.

(g) Stock Powers. Employee shall deliver to the General Counsel of the Company, at the time of execution of this Agreement and/or at such other time or times as the General Counsel may request, one or more executed stock powers, in the form attached hereto as Exhibit A or such other form as may be specified by the General Counsel, authorizing the transfer of the Restricted Stock to the Company upon forfeiture, and Employee shall take such other steps or perform such other actions as may be requested by the General Counsel to effect the transfer of any forfeited Restricted Stock (together with any property resulting from Section 3(e)(iii)) to the Company.

4. **Tax Withholding**. Employee understands and acknowledges that certain amounts must be withheld to satisfy federal, state, local, or foreign tax obligations associated with the grant of the Restricted Stock or the expiration of the Restrictions applicable to the Restricted Stock (and any property resulting from Section 3(e)(iii)) (“Withholdings”). Employee shall make arrangements satisfactory to the Company, in advance of any event triggering a Withholding obligation on the part of the Company or any affiliate of the Company that employs Employee, to provide for payment of all applicable Withholdings. If Employee has failed to make such arrangements or for any reason full payment of Withholdings is not made by Employee under such arrangements, Employee expressly authorizes the Company (and any such affiliated employer) to (1) withhold the applicable amount of Withholdings from any payment to Employee, including any payment relating to an Award or any payroll or other payment, and/or (2) withhold shares deliverable upon lapse of the Restrictions on the Restricted Stock having a fair market value (as determined by the Committee) equal to the amount of such tax liability required to be withheld as Withholdings in connection with the event triggering Withholding. If the Company (or such affiliated employer) elects to withhold shares to satisfy any Withholding obligation, the value of shares withheld shall not exceed the

minimum applicable withholding tax rate for federal (including FICA), state and local tax liabilities (interpreted in a manner consistent with applicable accounting rules). This provision does not obligate the Company or any affiliate to withhold shares to satisfy Withholding obligations. The Company may specify a reasonable deadline (for example, 90 days before lapse of Restrictions) by which Employee must make separate arrangements for the payment of Withholdings. In the event that Employee files, under Section 83(b) of the Code, an election to be taxed as having received ordinary income at the date of grant of the Restricted Stock, Employee shall at the time of such filing notify the Company of the making of such election and furnish a copy of the notice to the Company, and shall meet the other obligations under this Section 4 with respect to Withholding.

5. **Legal Compliance.** Employee agrees to take any action the Company reasonably deems necessary in order to comply with federal and state laws, or the rules and regulations of the NYSE, the Financial Industry Regulatory Authority, or any other stock exchange or self-regulatory organization, or any other obligation of the Company or Employee relating to the Restricted Stock or this Agreement.

6. **Governing Law.** THIS AGREEMENT SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NEW YORK, WITHOUT GIVING EFFECT TO CONFLICTS OF LAWS PRINCIPLES.

7. **Restricted Stock Agreement — Grantee's Acceptance .** The Employee hereby accepts the Restricted Stock described in this Agreement, and agrees to be bound by the terms and administrative provisions as set forth in the Plan and this Agreement. The Employee hereby further agrees that all the decisions and determinations of the Committee shall be final and binding.

8. **Miscellaneous.** This Agreement shall be binding upon the heirs, executors, administrators, and successors of the parties. This Agreement and the 2003 Plan constitute the entire agreement between the parties with respect to the Restricted Stock, and supersede any prior agreements or documents with respect thereto. No amendment, alteration, suspension, discontinuation, or termination of this Agreement which may impose any additional obligation upon the Company or materially impair the rights of Employee with respect to the Restricted Stock shall be valid unless in each instance such amendment, alteration, suspension, discontinuation, or termination is expressed in a written instrument duly executed in the name and on behalf of the Company and, if Employee's rights are being materially impaired, by Employee. Neither the Restricted Stock nor the granting thereof shall constitute or be evidence of any agreement or understanding, express or implied, that Employee has a right to continue as an officer or employee of the Company or any subsidiary for any period of time, or at any particular rate of compensation. Any waiver by the Company of a breach of any provision of this Agreement shall not operate or be construed as a waiver of any subsequent breach of such provision or any other provision hereof.

The Employee hereby acknowledges that the type and periods of restriction imposed in the provisions of this Agreement are fair and reasonable. The Employee hereby further acknowledges that the provisions of this Agreement shall be enforced to the fullest extent permissible under the laws and public policies applied in each jurisdiction in which enforcement is sought. Accordingly, the Employee agrees that if any particular provision of this Agreement shall be adjudicated to be

invalid or unenforceable, such provision shall be deemed amended to delete therefrom the portion thus adjudicated to be invalid or unenforceable, such deletion to apply only with respect to the operation of such provision in the particular jurisdiction in which such adjudication is made. In addition, if any one or more of the provisions contained in this Agreement shall for any reason be held to be excessively broad as to duration, geographical scope, activity or subject, it shall be construed by limiting and reducing it, so as to be enforceable to the extent compatible with the applicable law as it shall then appear. Any provision of this Agreement which is prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof, and any such prohibition or unenforceability in any jurisdiction shall not invalidate or render unenforceable such provision in any other jurisdiction.

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

Employee:

JEFFERIES GROUP, INC.

[Insert employee name]

By: _____

Judith O. Kester
Assistant Secretary

Social Sec. No.

Address:

[Insert employee address]

EXHIBIT A
STOCK POWER

FOR VALUE RECEIVED, the undersigned hereby sells, assigns and transfers unto Jefferies Group, Inc. [insert number of shares] shares of Common Stock, \$0.0001 par value per share, of Jefferies Group, Inc., a Delaware corporation (the "Corporation"), registered in the name of the undersigned on the books and records of the Corporation, and does hereby irrevocably constitute and appoint Lloyd H. Feller and Judith O. Kester, and each of them, attorneys, to transfer the Common Stock on the books of the Corporation, with full power of substitution in the premises.

(Signature should be in exact form as on Stock certificate)

Date

JEFFERIES GROUP, INC.
2003 Incentive Compensation Plan
Restricted Stock Units Agreement

This Restricted Stock Units Agreement (the "Agreement") confirms the grant on _____ (the "Grant Date") by Jefferies Group, Inc., a Delaware corporation (the "Company"), to _____ ("Employee") of Restricted Stock Units (the "Units"), including rights to Dividend Equivalents as specified herein, as follows:

Number granted: _____ Units

How Units Vest : ___% of the Units, if not previously forfeited, will vest on each of _____, provided that Employee continues to be employed by the Company or a subsidiary on each vesting date (each, a "Stated Vesting Date"). In addition, if not previously forfeited, the Units will become vested earlier upon the occurrence of certain events relating to Termination of Employment to the extent provided in Section 4 of the Terms and Conditions of Restricted Stock Units attached hereto (the "Terms and Conditions"). The terms "vest" and "vesting" mean that the Units have become non-forfeitable, except for forfeitures specified under Section 7.4 of the Plan. If Employee has a Termination of Employment prior to the Stated Vesting Date and the Units are not otherwise deemed vested by that date, the Units will be immediately forfeited except as otherwise provided in Section 4 of the Terms and Conditions.

Settlement : Settlement of vested Units will occur on _____, or as promptly as possible upon the death or Termination of Employment due to the Disability of Employee or Termination of Employment by the Company not for Cause following a Change in Control, except settlement shall be deferred in certain cases in accordance with Section 8(a) of the Terms and Conditions (the "Settlement Date"). Units granted hereunder will be settled by delivery of one Share for each Unit being settled (together with any cash or Shares resulting from Dividend Equivalents). Any settlement required to be made "promptly" under this Agreement shall in all cases be made not later than 60 days after the event that triggers such settlement.

The Units are subject to the terms and conditions of the 2003 Incentive Compensation Plan (the "Plan"), and this Agreement, including the Terms and Conditions attached hereto. The number of Units, the kind of shares deliverable in settlement of Units, and other terms relating to the Units are subject to adjustment in accordance with Section 5 of the Terms and Conditions and Section 5.3 of the Plan.

Employee acknowledges and agrees that (i) Units are nontransferable, except as provided in Section 3 of the Terms and Conditions and Section 9.2 of the Plan, (ii) Units, and certain amounts of gain realized upon settlement of Units, are subject to forfeiture, whether during employment or following a Termination of Employment, in the event Employee fails to meet applicable requirements relating to non-solicitation, confidentiality, and related matters with respect to the Company and its subsidiaries and affiliates (together, "Group," and each entity included in Group being a "Group Entity"), as set forth in Section 7.4 of the Plan and (iii) sales of shares delivered in settlement of Units will be subject to the Company's policies regulating trading by employees if the recipient is then an employee of the Company.

Employee hereby accepts the Units described in this Agreement, and agrees to be bound by the terms and administrative provisions set forth in the Plan and this Agreement. Employee

hereby further agrees that all the decisions and determinations of the Committee shall be final and binding.

IN WITNESS WHEREOF, JEFFERIES GROUP, INC. has caused this Agreement to be executed by its officer thereunto duly authorized, and Employee has duly executed this Agreement, by which each has agreed to the terms of this Agreement.

Employee

JEFFERIES GROUP, INC.

[Employee Name]

By: _____

TERMS AND CONDITIONS OF RESTRICTED STOCK UNITS

The following Terms and Conditions apply to the Units granted to Employee by JEFFERIES GROUP, INC. (the “Company”), and Units (if any) resulting from Dividend Equivalents, as specified in the Restricted Stock Units Agreement to which these Terms and Conditions are attached (and of which these Terms and Conditions form a part). Certain terms of the Units, including the number of Units granted, vesting date(s) and Settlement Date, are set forth on the preceding pages, referred to as the Cover Page in these Terms and Conditions. The Cover Page and these Terms and Conditions are collectively referred to as the “Agreement.”

1. **General** . The Units are granted to Employee under the Company’s 2003 Incentive Compensation Plan (the “Plan”). A copy of the Plan and information regarding the Plan, including documents that constitute the “Prospectus” for the Plan under the Securities Act of 1933, can be viewed and printed out from the Company’s secure Intranet website, www.corp.jefferies.com (go to People Services, then to Plan Documents). All of the applicable terms, conditions and other provisions of the Plan are incorporated by reference herein. Capitalized terms used in this Agreement but not defined herein shall have the same meanings as in the Plan. If there is any conflict between the provisions of this document and mandatory provisions of the Plan, the provisions of the Plan govern, otherwise, the terms of this document shall prevail. By accepting the grant of the Units, Employee agrees to be bound by all of the terms and provisions of the Plan (as presently in effect or later amended), the rules and regulations under the Plan adopted from time to time, and the decisions and determinations of the Company’s Compensation Committee (the “Committee”) made from time to time, provided that no such Plan amendment, rule or regulation or Committee decision or determination shall materially and adversely affect the rights of the Employee with respect to the Units.

2. **Account for Employee** . The Company shall maintain a bookkeeping account for Employee (the “Account”) reflecting the number of Units then credited to Employee hereunder as a result of such grant of Units and any crediting of additional Units to Employee pursuant to payments equivalent to dividends paid on Common Stock under Section 5 hereof (“Dividend Equivalents”).

3. **Nontransferability** . Until Units are settled in accordance with the terms of this Agreement, Employee may not sell, transfer, assign, pledge, margin or otherwise encumber or dispose of Units or any rights hereunder to any third party other than by will or the laws of descent and distribution, except for transfers to a Beneficiary or as otherwise permitted and subject to the conditions under Section 9.2 of the Plan.

4. **Termination Provisions** . The following provisions will govern the vesting and forfeiture of the Units in the event of Employee’s Termination of Employment and/or occurrence of a post-termination Forfeiture Event (as defined below), unless otherwise determined by the Committee (subject to Section 9(a) hereof):

(a) **Death or Disability** . In the event of Employee’s death or Termination of Employment due to Disability (as defined below), all Units then outstanding, if not previously vested, will immediately vest, and all Units (if not previously settled) will be settled in accordance with the settlement terms set out on the Cover Page, giving effect to any valid deferral election of Employee then in effect. The foregoing notwithstanding, any distribution resulting from a Disability will be subject to the six-month delay rule in Section 8(a)(i), if applicable. With respect to any RSUs which do not constitute a deferral of compensation for purposes of Section 409A of the Internal Revenue Code (the “Code”), only a termination elected by the Company will be deemed a Termination of Employment due to Disability.

(b) **Retirement or Involuntary Termination by the Company not for Cause (and not subject to Section 4(c))** . In the event of Employee’s Retirement or Termination of Employment

by the Company not for Cause (other than a Termination not for Cause following a Change in Control), Units not previously vested shall not then be forfeited provided that Employee executes a settlement agreement and release in such form as may be requested by the Company within 21 days or such longer period as may be required by law (and provided further that any period of revocation required by law has expired without Employee exercising his right to revoke his agreement to the settlement agreement and release), but thereafter all unvested Units shall be forfeited if there occurs a Forfeiture Event prior to the Settlement Date which would have applied in the absence of such Retirement or Termination of Employment. Upon such a Retirement or Termination of Employment, the then-outstanding Units that are vested at the date of Termination (if not already settled) and that become vested thereafter will be settled in accordance with the settlement terms set out on the Cover Page, giving effect to any valid deferral election of Employee then in effect. A “Forfeiture Event” shall be deemed to occur if, following Employee’s Retirement or Termination by the Company not for Cause, Employee renders services for any organization or engages (either as owner, investor, partner, stockholder, employer, employee, consultant, advisor, or director) directly or indirectly, in any business which is or becomes competitive with the Company, its subsidiaries or affiliates, or otherwise engaged in conduct violating Section 7.4(a), 7.4(b) or 7.4(c) of the Plan. However, following Employee’s Retirement or Termination by the Company not for Cause, Employee shall be free to purchase stock or other securities of an organization or business so long as it is listed upon a recognized securities exchange or traded over-the-counter and such investment does not represent a greater than five percent equity interest in the organization or business. If Employee does not sign a settlement agreement and release within the time period requested by the Company (or signs and then timely revokes his agreement to the settlement agreement and release), all Units which are not vested at the date of Termination will be forfeited.

(c) *Termination Following a Change in Control* . If, following a Change in Control, Employee’s employment is terminated not for Cause by the Company or its successor, all of the then-outstanding Units not vested at the date of Termination will immediately vest and will be settled promptly thereafter, subject to the six-month delay rule in Section 8(a)(i), if applicable. If a Change in Control occurs followed by Termination of Employment by the Company not for Cause and a determination is made by the Company pursuant to Sections 280G and 4999 of the Code that a “golden parachute” excise tax will be payable in connection with compensation to Employee hereunder, Employee’s right to accelerated vesting of the Units upon the Change in Control, to the extent such right results in “parachute payments” (as such term is defined in Code Section 280G), shall be limited to the extent just necessary to avoid the excise tax. This limitation shall be applied in a manner that maximizes the number of Units as to which accelerated vesting can apply (or, stated conversely, any limitation on acceleration of vesting shall apply first to those Units with the lengthiest remaining vesting period, which Units would result in the highest “parachute payments”).

(d) *Termination by Employee for any Reason or by the Company for Cause*. In the event of a Termination of Employment by the Employee for any reason (other than due to Retirement, death or Disability) or by the Company for Cause, the portion of the then-outstanding Units not vested at the date of Termination will be forfeited, and the portion of the then-outstanding Units that is vested at the date of Termination (if not already settled) will be settled on the Settlement Date specified on the Cover Page unless forfeited pursuant to the provisions of Section 7.4 of the Plan, except that any valid deferral election of Employee shall be given effect.

(e) *Certain Definitions* . The following definitions apply for purposes of this Agreement, whether or not Employee has an employment agreement or other agreement with the Company, or any of its subsidiaries or affiliates (the Company and any subsidiary or affiliate each being a “Group Entity”) containing the same or similar defined terms:

(i) "Cause" means Employee's:

Neglect, failure or refusal to timely perform the duties of Employee's employment (other than by reason of a physical or mental illness or impairment), or Employee's gross negligence in the performance of his or her duties;

Material breach of any agreements, covenants and representations made in any employment agreement or other agreement with the Company or any of its subsidiaries or affiliates or violation of internal policies or procedures as are in effect as of the date such action is taken, including but not limited to the Company's Code of Ethics, as amended from time to time;

Violation of any law, rule, regulation or by-law of any governmental authority (state, federal or foreign), any securities exchange or association or other regulatory or self-regulatory body or agency applicable to Employee, the Company, its subsidiaries or affiliates or any material general policy or directive of the Company, its subsidiaries or affiliates;

Conviction of, or plea of guilty or nolo contendere to, a crime involving moral turpitude, dishonesty, fraud or unethical business conduct, or any felony of any nature whatsoever;

Failure to obtain or maintain any registration, license or other authorization or approval that Employee is required to maintain or that the Company, its subsidiaries or affiliates reasonably believes is required in order for Employee to perform his or her duties, provided, however, that Employee shall be given written notice of any such registration, license or other authorization or approval that he or she is required to obtain and a reasonable period of time to obtain such registration, license, or other authorization or approval; or

Willful failure to execute a directive of the board of directors of the Company or any of its subsidiaries or affiliates, the Executive Committee of any of the Company's subsidiaries or affiliates, or Employee's supervisor (unless such directive would result in the commission of an act which is illegal or unethical) or commission of an act against the directive of such Board, such Executive Committee or Employee's supervisor.

(ii) A "Change in Control" shall be deemed to have occurred if any of the following conditions shall have been satisfied after the Grant Date:

Any person (as defined in section 3(a)(9) of the Securities Exchange Act of 1934, as such term is modified in Section 13(d)), other than (i) an employee plan established by the Company or any of its subsidiaries or (ii) any group of Company employees holding shares subject to agreements relating to the voting of such shares, becomes a beneficial owner, directly or indirectly, of more than 51% of the voting stock of the Company;

The consummation of a merger or consolidation of the Company with any other corporation or any other entity, or the issuance of voting securities in connection with a merger or consolidation of the Company, if the holders of the Company's voting securities immediately prior to such transaction hold in the aggregate less than a majority of the then outstanding voting securities of the Company (or any successor company or entity) entitled to vote generally in the election of the directors of the Company (or such other company or entity) after such transaction;

The sale or disposition by the Company of all or substantially all of its assets in which one person or more than one person acting as a group acquires assets from the Company that have a total gross fair market value equal to more than 50% of the total gross fair market value of all of the assets of the Company immediately prior to such acquisition; or

A change in the composition of the Board of Directors of the Company such that individuals who, as of the date of this agreement, constitute the Board of Directors of the Company (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board of Directors of the Company; provided, however, that any individual becoming a member of the Board of Directors of the Company subsequent to the date of this agreement whose election, or nomination for election by the shareholders of the Company, was approved by a vote of at least a majority of the directors then constituting the Incumbent Board shall be considered as if that individual were a member of the Incumbent Board.

(iii) "Disability" means that Employee has commenced receipt of long-term disability benefits under the Company's long-term disability policy as in effect at the date of Employee's termination of employment.

(iv) "Retirement" means retirement after attaining the age at which an Employee's age plus his years of service equals age [60] [62], provided, however, that (a) Employee has provided a minimum of 7.5 years of service to the Company, its subsidiaries or affiliates and [(b) such retirement is more than 36 months after the Grant Date]. For this purpose, years of service shall be credited for each twelve month period beginning on the date of Employee's commencement of employment with the Company and on each anniversary thereof during which the Employee was in active employment with the Company. [For the avoidance of doubt, Employee's retirement within 36 months of the Grant Date shall not qualify as a Retirement hereunder.]

(v) "Termination" or "Termination of Employment" means the event by which Employee ceases to be employed by a Group Entity and immediately thereafter is not employed by any other Group Entity.

5 . *Dividend Equivalents and Adjustments* .

(a) *Dividend Equivalents* . Subject to Section 5(d), Dividend Equivalents will be credited on Units (other than Units that, at the relevant record date, previously have been settled or forfeited) and deemed reinvested in additional Units, to the extent and in the manner as follows:

(i) *Cash Dividends* . If the Company declares and pays a dividend or distribution on Shares in the form of cash, then a number of additional Units shall be credited to Employee's Account as of the last day of the calendar quarter in which such dividend or distribution was paid equal to the number of Units credited to the Account as of the record date for such dividend or distribution multiplied by cash amount of the dividend or distribution paid on each outstanding share of Common Stock at such payment date, divided by the Fair Market Value of a share of Common Stock at the date of such crediting; provided, however, that in the case of an extraordinary cash dividend or distribution the Company may provide for such crediting at the dividend or distribution payment date instead of the last day of the calendar quarter.

(ii) *Non-Common Stock Dividends* . If the Company declares and pays a dividend or distribution on Common Stock in the form of property other than shares of Common Stock, then a number of additional Units shall be credited to Employee's Account as of the payment date for such dividend or distribution equal to the number of Units credited to the Account as of the record date for such dividend or distribution multiplied by the Fair Market Value of such property actually paid as a dividend or distribution on each outstanding share of Common Stock at such payment date, divided by the Fair Market Value of a share of Common Stock at such payment date.

(iii) *Common Stock Dividends and Splits* . If the Company declares and pays a dividend or distribution on Common Stock in the form of additional shares of Common Stock, or there occurs a forward split of Common Stock, then a number of additional Units shall be credited to Employee's Account as of the payment date for such dividend or distribution or forward split equal to the number of Units credited to the Account as of the record date for such dividend or distribution or split multiplied by the number of additional shares of Common Stock actually paid as a dividend or distribution or issued in such split in respect of each outstanding share of Common Stock.

(b) *Adjustments* . The number of Units credited to Employee's Account shall be appropriately adjusted, in order to prevent dilution or enlargement of Employee's rights with respect to Units or to reflect any changes in the number of outstanding shares of Common Stock resulting from any event referred to in Section 5.3 of the Plan, taking into account any Units credited to Employee in connection with such event under Section 5(a) hereof, and any performance conditions relating to the Units may be likewise adjusted in the discretion of the Committee.

(c) *Risk of Forfeiture and Settlement of Units Resulting from Dividend Equivalents and Adjustments*. Units which directly or indirectly result from Dividend Equivalents on or adjustments to a Unit granted hereunder and which do not result from a dividend or distribution on Shares in the form of cash shall be subject to the same risk of forfeiture (including Section 7.4 of the Plan) as applies to the granted Unit and, if not forfeited, will be settled at the same time as the granted Unit. Units which directly or indirectly result from Dividend Equivalents on or adjustments to a Unit granted hereunder and which result from an ordinary dividend or distribution on Shares in the form of cash shall not be subject to forfeiture and will be settled at the same time as the granted Unit (or if the granted Unit is forfeited, then at the time the granted Unit would have been settled if it were not forfeited). Units which directly or indirectly result from Dividend Equivalents on or adjustments to a Unit granted hereunder and which result from an extraordinary dividend or distribution on Shares in the form of cash shall, unless otherwise determined by the Company at the time of such extraordinary dividend or distribution, be subject to the same risk of forfeiture (including additional forfeiture terms of Section 7.4 of the Plan) as applies to the granted Unit and, if not forfeited, will be settled at the same time as the granted Unit.

(d) *Changes to Manner of Crediting Dividend Equivalents* . The provisions of Section 5(a) notwithstanding, the Company may vary the manner and timing of crediting dividend equivalents for administrative convenience, including, for example, by crediting cash dividend equivalents rather than additional Units.

6. **Additional Forfeiture Provisions.** Employee agrees that, by signing this Agreement and accepting the grant of the Units, the forfeiture conditions set forth in Section 7.4 of the Plan shall apply to all Units hereunder and to gains realized upon the settlement of the Units.

7. **Employee Representations and Warranties and Release** . As a condition to any non-forfeiture of the Units at or after Termination of Employment and to any settlement of the Units, the Company may require Employee (i) to make any representation or warranty to the Company as may be required under any applicable law or regulation, to make a representation and warranty that no Forfeiture Event has occurred or is contemplated, and that otherwise the requirements of Section 7.4(d) of the Plan and Section 7 above have been met, and (ii) to execute a release of claims against the Company arising before the date of such release, in such form as may be specified by the Company.

8. **Other Terms Relating to Units** .

(a) *Deferral of Settlement; Compliance with Code Section 409A* . Settlement of any Unit, which otherwise would occur at the Settlement Date, will be deferred in certain cases if and to the extent Employee is permitted to participate in the Stock Option Gain and Stock Award Deferral Program or otherwise permitted to defer the Units and Employee makes a valid deferral election relating to the Units. Deferrals, whether elective or mandatory under the terms of this Agreement, shall comply with requirements under Code Section 409A. Deferrals will be subject to such other restrictions and terms as may be specified by the Company prior to deferral. It is understood that Code Section 409A and regulations thereunder may require any elective deferral to comply with Section 409A(a)(4)(C). Other provisions of this Agreement notwithstanding, under U.S. federal income tax laws and Treasury Regulations (including proposed regulations) as presently in effect or hereafter implemented, with respect to Units other than those which are excluded from being deemed deferrals of compensation under 409A (i) a distribution in settlement of Units to Employee triggered by a Termination of Employment will occur only if the Termination constitutes a “separation from service” within the meaning of Code Section 409A(a)(2)(A)(i) and, if at the time of such separation from service Employee is a “specified employee” under Code Section 409A(a)(2)(B)(i) and a delay in distribution is required in order that Employee will not be subject to a tax penalty under Code Section 409A, such distribution in settlement of Units will occur at the date six months after Termination of Employment; and (ii) any rights of Employee or retained authority of the Company with respect to Units hereunder shall be automatically modified and limited to the extent necessary so that Employee will not be deemed to be in constructive receipt of income relating to the Units prior to the distribution and so that Employee shall not be subject to any penalty under Code Section 409A. Other provisions of this Agreement notwithstanding, if a separation from service occurs within less than six months before the fixed date specified as the Settlement Date and the six-month delay rule would apply to a settlement triggered by such separation from service, the settlement will not be made based on the separation from service, but instead the settlement shall be made based on the fixed date specified as the Settlement Date.

(b) *Fractional Units and Shares* . The number of Units credited to Employee’s Account shall include fractional Units calculated to at least three decimal places, unless otherwise determined by the Committee. Unless settlement is effected through a broker or agent that can accommodate fractional shares (without requiring issuance of a fractional share by the Company),

upon settlement of the Units Employee shall be paid, in cash, an amount equal to the value of any fractional share that would have otherwise been deliverable in settlement of such Units.

(c) *Tax Withholding* . Employee understands and acknowledges that certain amounts must be withheld to satisfy federal, state, local, or foreign tax obligations associated with the lapse of the risk of forfeiture and/or settlement of the Units (“Withholdings”). Employee shall make arrangements satisfactory to the Company, in advance of any event triggering a Withholding obligation on the part of the Company or a Group Entity that employs Employee, to provide for payment of all applicable Withholdings. If Employee has failed to make such arrangements or for any reason full payment of Withholdings is not made by Employee under such arrangements, Employee expressly authorizes the Company and any such Group Entity to (1) withhold the applicable amount of Withholdings from any payment to Employee, including any payment relating to an Award or any payroll or other payment, and/or (2) withhold shares deliverable in settlement of the Units having a fair market value (as determined by the Committee) equal to the amount of such tax liability required to be withheld as Withholdings in connection with the event triggering Withholding. If the Company or such Group Entity elects to withhold shares to satisfy any Withholding obligation, the value of shares withheld shall not exceed the minimum applicable withholding tax rate for federal (including FICA), state and local tax liabilities (interpreted in a manner consistent with applicable accounting rules). This provision does not obligate the Company or any Group Entity to withhold shares to satisfy Withholding obligations. The Company may specify a reasonable deadline (for example, 90 days before lapse of Restrictions) by which Employee must make separate arrangements for the payment of Withholdings.

(d) *Statements* . An individual statement of Employee’s Account will be issued to Employee at such times as may be determined by the Company. Such a statement shall reflect the number of Units credited to Employee’s Account, transactions therein during the period covered by the statement, and other information deemed relevant by the Committee. Such a statement may be combined with or include information regarding other plans and compensatory arrangements for employees. Employee’s statements shall be deemed a part of this Agreement, and shall evidence the Company’s obligations in respect of Units, including the number of Units credited as a result of Dividend Equivalents (if any). Any statement containing an error shall not, however, represent a binding obligation to the extent of such error, notwithstanding the inclusion of such statement as part of this Agreement.

9. *Miscellaneous* .

(a) *Binding Agreement; Written Amendments* . This Agreement shall be binding upon the heirs, executors, administrators, and successors of the parties. This Agreement and the Plan, and any deferral election separately filed with the Company relating to this Award, constitute the entire agreement between the parties with respect to the Units, and supersede any prior agreements or documents with respect thereto. No amendment, alteration, suspension, discontinuation, or termination of this Agreement which may impose any additional obligation upon the Company or materially impair the rights of Employee with respect to the Units shall be valid unless in each instance such amendment, alteration, suspension, discontinuation, or termination is expressed in a written instrument duly executed in the name and on behalf of the Company and, if Employee’s rights are being materially impaired, by Employee.

(b) *No Promise of Employment*. The Units and the granting thereof shall not constitute or be evidence of any agreement or understanding, express or implied, that Employee has a right to continue as an officer or employee of the Company for any period of time, or at any particular rate of compensation.

(c) *Unfunded Plan* . Any provision for distribution in settlement of Employee's Account hereunder shall be by means of bookkeeping entries on the books of the Company and shall not create in Employee or any Beneficiary any right to, or claim against any, specific assets of the Company, nor result in the creation of any trust or escrow account for Employee. With respect to any entitlement of Employee or any Beneficiary to any distribution hereunder, Employee or such Beneficiary shall be a general creditor of the Company.

(d) *Governing Law* . THIS AGREEMENT SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NEW YORK WITHOUT GIVING EFFECT TO CONFLICTS OF LAWS PRINCIPLES.

(e) *Legal Compliance*. Employee agrees to take any action the Company reasonably deems necessary in order to comply with federal and state laws, or the rules and regulations of the New York Stock Exchange, the Financial Industry Regulatory Authority, or any other stock exchange or self-regulatory organization, or any other obligation of the Company or Employee relating to the Units or this Agreement.

(f) *Notices* . Any notice to be given the Company under this Agreement shall be addressed to the Company at 520 Madison Avenue, 12th Floor, New York, NY 10022, attention: Corporate Secretary, and any notice to the Employee shall be addressed to the Employee at Employee's address as then appearing in the records of the Company.

October 8, 2007

Peregrine C. Broadbent
40 E. 94th Street, #17C
New York, New York 10128

Dear Peg:

On behalf of our Board of Directors, I am pleased to offer you the position of Executive Vice President and Chief Financial Officer of Jefferies Group, Inc. and Jefferies & Company, Inc. ("Jefferies"). The terms of our offer are conditioned only on you commencing your employment with us not later than January 7, 2008 and your successfully passing our normal background investigation and drug-screening test. This agreement will govern the terms of our relationship for the period from the commencement of your employment through December 31, 2008 (the "Term") and, where specifically provided herein, governs certain terms of our relationship following the Term.

I. EMPLOYEE'S REPRESENTATIONS AND WARRANTIES

You represent and warrant to Jefferies that:

- A. As of the date you sign this agreement, you have resigned as an employee of Morgan Stanley ("Morgan Stanley").
- B. You have not breached any contract or other agreement relating to your employment with Morgan Stanley.
- C. You made your decision to resign from Morgan Stanley prior to receiving this offer of employment.
- D. You are not the subject of any investigation, whether by any prior employer, any governmental or regulatory authority or any self-regulatory organization.
- E. You are not subject to any agreement with or policy of any previous employer that would prevent or restrict you from engaging in activities competitive with the activities of your previous employers or from directly or indirectly soliciting employees to leave the employ of such previous employers, or from directly or indirectly soliciting any clients or customers of such

previous employers to transfer its business away from such previous employers or, if you are subject to such an agreement or policy, you have complied and will comply with it.

F. To the best of your current knowledge and belief, your performance of all the terms of this Agreement and as an employee of Jefferies does not and will not breach any agreement to keep in confidence proprietary information, knowledge or data acquired by you in confidence or in trust prior to your employment hereunder, and that you will not disclose to Jefferies or induce Jefferies or any of its affiliates to use any confidential or proprietary information or material belonging to any previous employer or others.

G. You have not requested, solicited or encouraged, and you will not request, solicit or encourage, any employees, customers or clients of your previous employers to join Jefferies or to leave your previous employers in violation of any common law duties or other obligations to your previous employers.

H. You are not subject to any employment agreement with or policy of your previous employer that would require you to give notice to such previous employer of your resignation in order for such resignation to become effective, unless you have given, or will give, such notice, and any period of time required to elapse before such resignation becomes effective will have elapsed before you commence your employment with Jefferies.

I. You have not taken or retained (and will not take or retain) any documents or files, whether in hard copy or electronic form, which were created, collected or received by you in connection with your previous employment, except for documents and files relating solely to your compensation and benefits.

II. COMPENSATION

- A. During the Term of this Agreement, you will receive a salary at the rate of \$83,333.32 per month, to be paid in equal installments on approximately the 15th and 30th day of each month.
- B. For calendar year 2007, you will receive a cash bonus in the amount of \$1,300,000. The 2007 bonus will be paid on the later of (i) December 15, 2007 or (ii) five business days after the commencement of your employment. Subject to Section IV below, in order for the bonus described herein to be earned and received by you, you must be employed and in good standing on the date the bonus payments are to be paid by Jefferies.
- C. For calendar year 2008:

As an executive officer of Jefferies, you will also be eligible to receive performance based bonus compensation upon achievement of objective established by the compensation committee of the Board of Directors. The Compensation Committee has agreed that your target compensation for achievement of the targets that the Compensation Committee will establish in 2008 will be \$2,000,000 for 2008,

comprised of \$1,300,000 in cash and \$700,000 in restricted stock units in 2008, with a range of \$0 to \$2,750,000 possible depending on whether the actual results are above or below the targets for 2008, with the composition of such bonus in 2008 between the cash and stock components possible depending on whether the actual results are above or below the targets for 2008 being 65% in cash and 35% in restricted stock units. The performance criteria for you in 2008 will be based on the same grid that will be used for the other executive officers of the company that are subject to the provisions of Section 162(m) of the Internal Revenue Code. The restricted stock units granted pursuant to this Section shall be subject to the same vesting as the restricted stock units described in Section III below (i.e., 20% vesting each anniversary date of the grant), with the distribution to be made promptly following the final vesting date, or earlier upon death, termination due to Disability (as defined in the agreement governing the grant of the restricted stock units) or termination not for Cause following a Change of Control (as such terms are defined in this agreement) (subject to the six-month delay rule under Section 409A of the Internal Revenue Code, to the extent applicable) and terms other than those relating to distribution being substantially the same as the terms of awards of restricted stock units granted to other executive officers at the time). The terms will be substantially in the form of Exhibit B hereto.

Notwithstanding the foregoing, your bonus for 2008 will be not less than \$2,000,000, with the cash and restricted stock units in the percentages set forth above.

Subject to Section IV below, in order for any of the bonuses described above to be earned and received by you, you must be employed and in good standing on the date the bonus payments are to be paid by Jefferies.

- D. Other than the bonuses described in Sections II.B and II.C above, any other bonus during the time you are an employee of Jefferies, whether for calendar year 2007 or 2008 or any other period during which you are an employee of Jefferies, will be determined by Jefferies in its sole and absolute discretion, both in terms of amount and payment. In order for such bonus to be earned and received by you, you must be employed and in good standing on the date the bonus payments are to be paid by Jefferies.

III. RESTRICTED STOCK UNITS

In addition, to replace unvested stock that you will forfeit and to replace other long term compensation opportunities that you had at your former employer, the Compensation Committee of Jefferies has agreed that you will be granted \$6,350,000 in restricted stock units ("RSUs") when you commence your employment at Jefferies. The number of RSUs granted will be based on the closing price of Jefferies stock on the New York Stock Exchange on your first date of employment. The RSUs granted to you pursuant to this paragraph shall be granted on the same terms on which restricted stock units are generally granted to other executive officers of Jefferies in 2007.

Provided that you remain in the employ of Jefferies on the grant date and each of the vesting dates, the RSUs will vest as to 20% of the RSUs on each anniversary of the date of grant. However, the shares of common stock will not be distributed to you until approximately sixty (60) days following the last vesting date or such other later date as you may specify within the first thirty (30) days of your grant or such other period as may be permitted by applicable provisions of the Internal Revenue Code. The grant of the RSUs is subject to the execution of an agreement governing the grant, in such form as is requested by Jefferies

IV. TERMINATION

During the period you are employed by Jefferies (whether during or after the Term), you agree that you shall give Jefferies six months' notice of your intent to terminate your employment (the "Notice Period"). During the Notice Period, you will continue to be entitled to receive your salary (but not any bonus) at the regular payroll dates except in cases in which the six-month delay applies under Section 409A of the Internal Revenue Code ("409A") as provided below in this Section IV, your fiduciary duties and your obligations to Jefferies as an employee of Jefferies will continue, and you will cooperate in the transition of your responsibilities. Jefferies shall have the right, in its sole discretion, to direct that you no longer come in to the office during the Notice Period or to shorten the Notice Period. In determining whether to exercise this right, Jefferies will act solely in its own best interests, and under no circumstances will it take into consideration any request by you that Jefferies direct you to cease coming into the office or shorten the Notice Period.

This agreement may also be terminated by Jefferies for Cause without further obligation hereunder. "Cause" shall mean your:

- A. Material neglect, failure or refusal to timely perform the duties of your employment (other than by reason of a physical or mental illness or impairment), or your gross negligence in the performance of your duties; provided, however, that you shall be given written notice of any such neglect, failure or refusal to perform your duties and no Cause shall exist if you have corrected such neglect, failure or refusal to perform your duties within thirty (30) days of such notice;
- B. Material breach of any agreements, covenants or representations made in any employment agreement or other agreement with Jefferies or any subsidiary or affiliate of Jefferies or material violation of Jefferies internal policies or procedures as are in effect as of the date such action is taken or violation of Group's Code of Ethics, as amended from time to time;
- C. Conviction of, or plea of guilty or nolo contendere to, a crime involving moral turpitude, dishonesty, fraud or unethical business conduct, or any felony of any nature whatsoever; or
- D. Failure to obtain or maintain any registration, license or other authorization or approval that you are required to maintain or that Jefferies or any affiliate of Jefferies

reasonably believes is required in order for you to perform your duties; provided, however, that Jefferies shall give you at least ninety (90) days written notice of any such registration, license or other authorization or approval that you are required to obtain.

You agree that if Jefferies terminates your employment for Cause or you voluntarily leave Jefferies' employ prior to the date any payment which is due hereunder is made, Jefferies shall have no obligation whatsoever to make any further payments to you hereunder.

You acknowledge and agree that Jefferies' liability under this Agreement for any alleged termination of your employment without Cause or for any alleged wrongful termination of your employment if you terminate your employment for Good Reason shall be limited to the following: (i) if such termination is without Cause by Jefferies or by you for Good Reason, (a) Jefferies will pay you the salary described in Section II.A through the end of the Term to the extent such salary has not been paid to you, the 2007 bonus for 2007 described in Section II.B and the \$2,000,000 bonus described in Section II.C, to the extent, and only to the extent, that such bonuses have not been paid to you, and (b) the RSUs described in Section III which have not yet vested as of the time of such termination without Cause shall be vested and (ii) if such termination is without Cause by Jefferies or by you for Good Reason after the expiration of the Term, the RSUs described in Section III which have not yet vested as of the time of such termination without Cause shall be vested. The payments described in this paragraph and the vesting of the RSUs described in Section III are contingent upon your execution within 21 days (or such longer period as may be required by law) of a settlement agreement and release substantially in the form attached as Exhibit C hereto (provided that any period of revocation required by law has expired without you exercising your right to revoke your agreement to the settlement agreement and release). Such amounts shall be paid ten days after your release has become irrevocable, and such shares in settlement of such RSUs shall be distributed within 30 days after your release has become irrevocable except to the extent that the six-month delay applies under 409A as provided below in this Section IV. The settlement agreement and release will be substantially in the form attached hereto as Exhibit C.

For purposes of this Agreement, "Good Reason" means (i) a material diminution in your authority, duties or responsibilities, (ii) without your consent, you no longer report directly to Jefferies' Chief Executive Officer, Chairman, Executive Committee or President or (iii) without your consent, relocation outside the greater New York metropolitan area, it being understood that in the normal course of your activities, you may be require to travel and to spend periods of time away from your office in New York City, provided, however, that (a) you must give notice of the existence of the Good Reason condition within 90 days of its initial existence, by providing written notice to the General Counsel of Jefferies, (b) Jefferies shall have 60 days during which it may remedy or "cure" the circumstances giving rise to Good Reason and no Good Reason shall exist if Jefferies has remedied or cured the Good Reason during such time period, You must terminate your employment for Good Reason within one year of the initial existence of the Good Reason.

Each amount or benefit payable under this Section IV shall be deemed a separate payment for purposes of 409A, and such amounts or benefits shall be paid at the times specified above in this

Section IV to the maximum extent permissible under 409A without resulting in tax penalties to you. For this purpose, however, ***if all three of the following conditions are met***, those portions of such amounts and benefits constituting a “deferral of compensation” as specified below will be paid on the first business day of the seventh calendar month after your “separation from service” as defined in Treasury Regulation § 1.409A-1(h) (this is referred to as the “six-month delay” below):

- (i) At the time of your separation from service you were a “specified employee” as defined under 409A (including Treasury Regulation § 1.409A-1(i))
- (ii) At the time of your separation from service, the stock of the Company was publicly traded on an established securities market or otherwise
- (iii) A portion of the payments or benefits constitutes a “deferral of compensation” subject to 409A. For this purpose:
 - Any portion of the payments or benefits deemed payable solely due to involuntary separation from service that qualifies as a “short-term deferral” under Treasury Regulation § 1.409A-1(b)(4) will not be deemed a “deferral of compensation” and will be paid without the six-month delay
 - Any portion of the payments or benefits deemed payable solely due to involuntary separation from service up to the limit specified in Treasury Regulation § 1.409A-1(b)(9)(iii) will not be deemed a “deferral of compensation” and will be paid without the six-month delay
 - Any portion of the payments or benefits, whether or not separation from service is involuntary, up to the limit specified in Treasury Regulation § 1.409A-1(b)(9)(v)(D) (if this limited exclusion is not applied to payments apart from this Agreement) will not be deemed a “deferral of compensation” and will be paid without the six-month delay
 - Any portion of the payments or benefits that may be excluded from being deemed a “deferral of compensation” under any other applicable Treasury Regulation or Internal Revenue Service guidance will be paid without the six-month delay.

If the six-month delay is applicable to any payment, the payment shall be accelerated upon your death during the six-month delay period but not for any other reason (except that acceleration is permitted under Treasury Regulation § 1.409A-3(j)(4)(ii), (iii) and (iv)). For purposes of this Agreement, any payment that is not excluded from being deemed a “deferral of compensation” under 409A and is payable upon a “termination of employment” shall be payable only upon a “separation from service” as defined in Treasury Regulation § 1.409A-1(h) or, if the above rules apply, the specified date at least six months after such separation from service. Any other payments or benefits under this Agreement shall be paid at the times specified herein.

You understand and agree that the Company does not make any representations and is not providing any advice regarding the taxation of the payments hereunder, including but not limited to taxes, interest and penalties under 409A and similar liabilities under state tax laws. No indemnification or gross-up is payable under this Agreement with respect to any such tax, interest, penalty or similar liability, and no interest is payable on any payment or benefit which is subject to a six-month delay hereunder.

The terms of this Agreement relating to a deferral of compensation or compensation excluded from being a deferral under 409A, including any authority of the Company and your rights with respect thereto, shall be limited to those terms permitted under 409A, and any terms not permitted under 409A shall be modified and limited to the extent necessary to conform with 409A but only to the extent that such modification or limitation is permitted under 409A and the regulations and guidance issued thereunder.

V. ADDITIONAL OBLIGATIONS

A. Confidential Information . During and after your employment by Jefferies, you will not, directly or indirectly in one or a series of transactions, disclose to any person, or use or otherwise exploit for your own benefit or for the benefit of anyone other than Jefferies, any Confidential Information of Jefferies (as such term is defined in Exhibit A hereto), whether or not reduced to writing or physical embodiment and whether prepared by you or not. The terms of this Section V.A shall survive the termination of your employment with Jefferies, regardless of who terminates your employment, or the reasons therefor.

B. Non-Competition . While you are an employee of Jefferies, you shall not engage in Competitive Activity (as such term is defined in Exhibit A hereto).

C. Non-Solicitation . (i) While you are an employee of Jefferies and for a period of one year following any termination of your employment, you shall not, directly or indirectly, solicit any employees, contractors, or other persons who have rendered services to Jefferies and (ii) while you are an employee of Jefferies and for a period of three months following any termination of your employment, you shall not, directly or indirectly, solicit any customers or clients of Jefferies, all as more fully set forth in Exhibit A hereto.

D. If you breach your obligations in any material respect under this Section V, Jefferies, in addition to pursuing all available remedies, at law or otherwise, and without limiting its right to pursue the same, shall cease all payments to you under this Agreement.

VI. MISCELLANEOUS

You will be entitled to a benefits package commensurate with that received by all other similarly situated executive officers of Jefferies during your employment, including four weeks of vacation. The amounts referred to above are gross amounts and will be subject to all statutory and any voluntary deductions.

Jefferies will cooperate with you if any information or documentation is required by any local, state or federal agency to maintain your immigration status or to support your application for U.S. citizenship.

This agreement, together with Exhibits A, B and C hereto (it being understood that Exhibits B and C are subject to modification), constitutes the entire agreement of you and Jefferies with respect to the subject matters referred to herein, and supersedes all prior or contemporaneous negotiations, promises, covenants, agreements and representations of every kind or nature with respect thereto, all of which have become merged and finally integrated into this agreement.

This agreement shall be governed by, and construed in accordance with, the laws of the State of New York, without giving effect to its principles or rules of conflicts of laws, to the extent that such principles or rules would require or permit the application of the law of another jurisdiction. You hereby consent that any arbitration proceeding brought by you with respect to matters related to your employment or this agreement shall be brought before FINRA in the Borough of Manhattan in the State of New York, or if you are permitted to bring such action in a state or federal court, then you hereby consent to the personal jurisdiction of the state and federal courts sitting in the City and State of New York with respect to matters related to your employment or this agreement, and agree that any action with respect thereto shall be brought in such courts.

If the above terms are acceptable to you, I request that you signify your acceptance of the terms of this letter by signing and dating the copy enclosed and returning it to me.

Sincerely,

/s/ Brian P. Friedman

Brian P. Friedman
Chairman, Executive Committee

AGREED TO AND ACCEPTED BY:

/s/ Peregrine C. Broadbent

Peregrine C. Broadbent

Dated: 8 October, 2007

EXHIBIT A

1. CONFIDENTIAL INFORMATION

“Confidential Information” means research, processes, procedures, marketing techniques, marketing and business development plans, client data and financial information. Confidential Information may be disclosed in good faith by you in connection with the performance of your duties under this Agreement. You shall have no obligation hereunder to keep any Confidential Information confidential if and to the extent disclosure of any thereof is specifically required by law; provided, however, that in the event disclosure is required by law, you shall provide Jefferies with prompt notice of such requirement, prior to making the disclosure, so that Jefferies may seek an appropriate protective order. The term “Confidential Information” shall not be deemed to include information publicly known in the trade at the time you first learn of the information or which later becomes commonly known in the trade (other than as a result of a disclosure by you); nor shall the term include general knowledge or general trade information which you independently learn nor information already in your possession prior to your employment by Jefferies.

2. COMPETITIVE ACTIVITY

“Competitive Activity” means that you, whether acting alone or in conjunction with others, directly or indirectly

- A. Are rendering services for any organization or engaging (either as owner, investor, partner, stockholder, employer, employee, consultant, advisor, or director) directly or indirectly, in any business which is or becomes competitive with the business of Jefferies, its subsidiaries or affiliates; or
- B. Are inducing any customer or client of Jefferies, its subsidiaries or affiliates with whom you have had contacts or relationships, directly or indirectly, during and within the scope of your employment with Jefferies or any of its subsidiaries or affiliates, to curtail, limit, or cancel their business with Jefferies, its subsidiaries or affiliates.

Notwithstanding the foregoing, following the termination of your employment with Jefferies, you shall be free to purchase stock or other securities of an organization or business so long as it is listed upon a recognized securities exchange or traded over-the-counter and such investment does not represent a greater than five percent equity interest in the organization or business.

3. NON-SOLICITATION

- A. While you are an employee of Jefferies and for a period of one year following any termination of your employment, you shall not, directly or indirectly:
 - i. Solicit, induce, or attempt to influence, any employee of Jefferies, its subsidiaries or affiliates to terminate their employment with Jefferies, its subsidiaries or affiliates; or
 - ii. Solicit, hire or retain as an employee or independent contractor, or assist any third party in the solicitation, hiring, or retention as an employee or independent contractor, any person who during the previous 12 months was an employee of

Jefferies, or any of its subsidiaries or affiliates.

- B. While you are an employee of Jefferies and for a period of three months following any termination of your employment, you shall not, directly or indirectly, solicit any customer or client of Jefferies, its subsidiaries or affiliates with whom you have had contacts or relationships, directly or indirectly, during and within the scope of your employment with Jefferies or any of its subsidiaries or affiliates, for the purpose or with the intent of encouraging or inducing such customer or client to curtail, limit, or cancel their business with Jefferies, its subsidiaries or affiliates.

4. ACKNOWLEDGMENTS AND REPRESENTATIONS

You acknowledge and agree that the time periods referred to in the paragraphs above are reasonable and valid in duration and scope and in all other respects. You also represent that your financial resources, experience and capabilities are such that the enforcement of the foregoing covenants will not prevent you from earning a livelihood, and acknowledge that it would cause Jefferies serious and irreparable injury and cost if you were to use your ability and knowledge in competition with Jefferies or to otherwise breach the obligations contained in this Agreement. If the scope of any of the restrictions set forth above are deemed by any arbitration panel, court or other tribunal to be too broad to permit enforcement of such restriction to its full extent, then such restriction shall be enforced to the maximum extent permitted by law, and you hereby consent and agree that such scope may be judicially modified accordingly in any proceeding brought to enforce such restriction.

5. WORKS FOR HIRE

You acknowledge and agree that all copyrightable material and other intellectual property developed or prepared for Jefferies by you during your employment by Jefferies, including without limitation (a) all computer software and all elements thereof and (b) all inventions, improvements, discoveries, designs, documents, and other data (whether or not patentable or copyrightable) made, developed, or first reduced to practice by you for Jefferies, whether solely or jointly with others, during the period of your employment by Jefferies, are deemed to be developed and prepared for the sole and exclusive benefit of Jefferies, and all copyrightable material shall constitute works for hire. Jefferies shall have all right, title, and interest in such material and shall be the author thereof for all purposes under the copyright laws. In the event that any copyrightable material is deemed not to be works for hire, you hereby assign such works to Jefferies and agree, without further compensation or consideration, to immediately take such actions to effect such assignment as may be requested by Jefferies.

EXHIBIT B

**JEFFERIES GROUP, INC.
2003 Incentive Compensation Plan
Restricted Stock Units Agreement**

This Restricted Stock Units Agreement (the "Agreement") confirms the grant on _____ (the "Grant Date") by Jefferies Group, Inc., a Delaware corporation (the "Company"), to _____ ("Employee") of Restricted Stock Units (the "Units"), including rights to Dividend Equivalents as specified herein, as follows:

Number granted: _____ Units

How Units Vest : ____% of the Units, if not previously forfeited, will vest on each of _____, provided that Employee continues to be employed by the Company or a subsidiary on each vesting date (each, a "Stated Vesting Date"). In addition, if not previously forfeited, the Units will become vested earlier upon the occurrence of certain events relating to Termination of Employment to the extent provided in Section 4 of the Terms and Conditions of Restricted Stock Units attached hereto (the "Terms and Conditions"). The terms "vest" and "vesting" mean that the Units have become non-forfeitable, except for forfeitures specified under Section 7.4 of the Plan. If Employee has a Termination of Employment prior to the Stated Vesting Date and the Units are not otherwise deemed vested by that date, the Units will be immediately forfeited except as otherwise provided in Section 4 of the Terms and Conditions.

Settlement : Settlement of vested Units will occur on _____, or as promptly as possible upon the death or Termination of Employment due to the Disability of Employee or Termination of Employment by the Company not for Cause following a Change in Control, except settlement shall be deferred in certain cases in accordance with Section 8(a) of the Terms and Conditions (the "Settlement Date"). Units granted hereunder will be settled by delivery of one Share for each Unit being settled (together with any cash or Shares resulting from Dividend Equivalents). Any settlement required to be made "promptly" under this Agreement shall in all cases be made not later than 60 days after the event that triggers such settlement.

The Units are subject to the terms and conditions of the 2003 Incentive Compensation Plan (the "Plan"), and this Agreement, including the Terms and Conditions attached hereto. The number of Units, the kind of shares deliverable in settlement of Units, and other terms relating to the Units are subject to adjustment in accordance with Section 5 of the Terms and Conditions and Section 5.3 of the Plan.

Employee acknowledges and agrees that (i) Units are nontransferable, except as provided in Section 3 of the Terms and Conditions and Section 9.2 of the Plan, (ii) Units, and certain amounts of gain realized upon settlement of Units, are subject to forfeiture, whether during employment or following a Termination of Employment, in the event Employee fails to meet applicable requirements relating to non-solicitation, confidentiality, and related matters with respect to the Company and its subsidiaries and affiliates (together, "Group," and each entity included in Group being a "Group Entity"), as set forth in Section 7.4 of the Plan

and (iii) sales of shares delivered in settlement of Units will be subject to the Company's policies regulating trading by employees if the recipient is then an employee of the Company.

IN WITNESS WHEREOF, JEFFERIES GROUP, INC. has caused this Agreement to be executed by its officer thereunto duly authorized, and Employee has duly executed this Agreement, by which each has agreed to the terms of this Agreement.

Employee

JEFFERIES GROUP, INC.

[Employee Name]

By: _____

TERMS AND CONDITIONS OF RESTRICTED STOCK UNITS

The following Terms and Conditions apply to the Units granted to Employee by JEFFERIES GROUP, INC. (the “Company”), and Units (if any) resulting from Dividend Equivalents, as specified in the Restricted Stock Units Agreement to which these Terms and Conditions are attached (and of which these Terms and Conditions form a part). Certain terms of the Units, including the number of Units granted, vesting date(s) and Settlement Date, are set forth on the preceding pages, referred to as the Cover Page in these Terms and Conditions. The Cover Page and these Terms and Conditions are collectively referred to as the “Agreement.”

1. **General** . The Units are granted to Employee under the Company’s 2003 Incentive Compensation Plan (the “Plan”). A copy of the Plan and information regarding the Plan, including documents that constitute the “Prospectus” for the Plan under the Securities Act of 1933, can be viewed and printed out from the Company’s secure Intranet website, www.corp.jefferies.com (go to People Services, then to Plan Documents). All of the applicable terms, conditions and other provisions of the Plan are incorporated by reference herein. Capitalized terms used in this Agreement but not defined herein shall have the same meanings as in the Plan. If there is any conflict between the provisions of this document and mandatory provisions of the Plan, the provisions of the Plan govern, otherwise, the terms of this document shall prevail. By accepting the grant of the Units, Employee agrees to be bound by all of the terms and provisions of the Plan (as presently in effect or later amended), the rules and regulations under the Plan adopted from time to time, and the decisions and determinations of the Company’s Compensation Committee (the “Committee”) made from time to time, provided that no such Plan amendment, rule or regulation or Committee decision or determination shall materially and adversely affect the rights of the Employee with respect to the Units.

2. **Account for Employee** . The Company shall maintain a bookkeeping account for Employee (the “Account”) reflecting the number of Units then credited to Employee hereunder as a result of such grant of Units and any crediting of additional Units to Employee pursuant to payments equivalent to dividends paid on Common Stock under Section 5 hereof (“Dividend Equivalents”).

3. **Nontransferability** . Until Units are settled in accordance with the terms of this Agreement, Employee may not sell, transfer, assign, pledge, margin or otherwise encumber or dispose of Units or any rights hereunder to any third party other than by will or the laws of descent and distribution, except for transfers to a Beneficiary or as otherwise permitted and subject to the conditions under Section 9.2 of the Plan.

4. **Termination Provisions** . The following provisions will govern the vesting and forfeiture of the Units in the event of Employee’s Termination of Employment and/or occurrence of a post-termination Forfeiture Event (as defined below), unless otherwise determined by the Committee (subject to Section 9(a) hereof):

(a) **Death or Disability** . In the event of Employee’s death or Termination of Employment due to Disability (as defined below), all Units then outstanding, if not previously vested, will immediately vest, and all Units (if not previously settled) will be settled in accordance with the settlement terms set out on the Cover Page, giving effect to any valid deferral election of Employee then in effect. The foregoing notwithstanding, any distribution resulting from a Disability will be subject to the six-month delay rule in Section 8(a)(i), if applicable. With respect to any RSUs which do not constitute a deferral of compensation for purposes of Section 409A of the Internal Revenue Code (the “Code”), only a termination elected by the Company will be deemed a Termination of Employment due to Disability.

(b) *Retirement or Involuntary Termination by the Company not for Cause (and not subject to Section 4(c))* . In the event of Employee's Retirement or Termination of Employment by the Company not for Cause (other than a Termination not for Cause following a Change in Control), Units not previously vested shall not then be forfeited provided that Employee executes a settlement agreement and release in such form as may be requested by the Company (and provided further that any period of revocation required by law has expired without Employee exercising his right to revoke his agreement to the settlement agreement and release), but thereafter all unvested Units shall be forfeited if there occurs a Forfeiture Event prior to the Settlement Date which would have applied in the absence of such Retirement or Termination of Employment. Upon such a Retirement or Termination of Employment, the then-outstanding Units that are vested at the date of Termination (if not already settled) and that become vested thereafter will be settled in accordance with the settlement terms set out on the Cover Page, giving effect to any valid deferral election of Employee then in effect. A "Forfeiture Event" shall be deemed to occur if, following Employee's Retirement or Termination by the Company not for Cause, Employee renders services for any organization or engages (either as owner, investor, partner, stockholder, employer, employee, consultant, advisor, or director) directly or indirectly, in any business which is or becomes competitive with the Company, its subsidiaries or affiliates, or otherwise engaged in conduct violating Section 7.4(a), 7.4(b) or 7.4(c) of the Plan. However, following Employee's Retirement or Termination by the Company not for Cause, Employee shall be free to purchase stock or other securities of an organization or business so long as it is listed upon a recognized securities exchange or traded over-the-counter and such investment does not represent a greater than five percent equity interest in the organization or business.

(c) *Termination Following a Change in Control* . If, following a Change in Control, Employee's employment is terminated not for Cause by the Company or its successor, all of the then-outstanding Units not vested at the date of Termination will immediately vest and will be settled promptly thereafter, subject to the six-month delay rule in Section 8(a)(i), if applicable. If a Change in Control occurs followed by Termination of Employment by the Company not for Cause and a determination is made by the Company pursuant to Sections 280G and 4999 of the Code that a "golden parachute" excise tax will be payable in connection with compensation to Employee hereunder, Employee's right to accelerated vesting of the Units upon the Change in Control, to the extent such right results in "parachute payments" (as such term is defined in Code Section 280G), shall be limited to the extent just necessary to avoid the excise tax. This limitation shall be applied in a manner that maximizes the number of Units as to which accelerated vesting can apply (or, stated conversely, any limitation on acceleration of vesting shall apply first to those Units with the lengthiest remaining vesting period, which Units would result in the highest "parachute payments").

(d) *Termination by Employee for any Reason or by the Company for Cause*. In the event of a Termination of Employment by the Employee for any reason (other than due to Retirement, death or Disability) or by the Company for Cause, the portion of the then-outstanding Units not vested at the date of Termination will be forfeited, and the portion of the then-outstanding Units that is vested at the date of Termination (if not already settled) will be settled on the Settlement Date specified on the Cover Page unless forfeited pursuant to the provisions of Section 7.4 of the Plan, except that any valid deferral election of Employee shall be given effect.

(e) *Certain Definitions* . The following definitions apply for purposes of this Agreement, whether or not Employee has an employment agreement or other agreement with the Company, or any of its subsidiaries or affiliates (the Company and any subsidiary or affiliate each being a "Group

Entity”) containing the same or similar defined terms:

(i) “Cause” means Employee’s:

Neglect, failure or refusal to timely perform the duties of Employee’s employment (other than by reason of a physical or mental illness or impairment), or Employee’s gross negligence in the performance of his or her duties;

Material breach of any agreements, covenants and representations made in any employment agreement or other agreement with the Company or any of its subsidiaries or affiliates or violation of internal policies or procedures as are in effect as of the date such action is taken, including but not limited to the Company’s Code of Ethics, as amended from time to time;

Violation of any law, rule, regulation or by-law of any governmental authority (state, federal or foreign), any securities exchange or association or other regulatory or self-regulatory body or agency applicable to Employee, the Company, its subsidiaries or affiliates or any material general policy or directive of the Company, its subsidiaries or affiliates;

Conviction of, or plea of guilty or nolo contendere to, a crime involving moral turpitude, dishonesty, fraud or unethical business conduct, or any felony of any nature whatsoever;

Failure to obtain or maintain any registration, license or other authorization or approval that Employee is required to maintain or that the Company, its subsidiaries or affiliates reasonably believes is required in order for Employee to perform his or her duties, provided, however, that Employee shall be given written notice of any such registration, license or other authorization or approval that he or she is required to obtain and a reasonable period of time to obtain such registration, license, or other authorization or approval; or

Willful failure to execute a directive of the board of directors of the Company or any of its subsidiaries or affiliates, the Executive Committee of any of the Company’s subsidiaries or affiliates, or Employee’s supervisor (unless such directive would result in the commission of an act which is illegal or unethical) or commission of an act against the directive of such Board, such Executive Committee or Employee’s supervisor.

(ii) A “Change in Control” shall be deemed to have occurred if any of the following conditions shall have been satisfied after the Grant Date:

Any person (as defined in section 3(a)(9) of the Securities Exchange Act of 1934, as such term is modified in Section 13(d)), other than (i) an employee plan established by the Company or any of its subsidiaries or (ii) any group of Company employees holding shares subject to agreements relating to the

voting of such shares, becomes a beneficial owner, directly or indirectly, of more than 51% of the voting stock of the Company;

The consummation of a merger or consolidation of the Company with any other corporation or any other entity, or the issuance of voting securities in connection with a merger or consolidation of the Company, if the holders of the Company's voting securities immediately prior to such transaction hold in the aggregate less than a majority of the then outstanding voting securities of the Company (or any successor company or entity) entitled to vote generally in the election of the directors of the Company (or such other company or entity) after such transaction;

The sale or disposition by the Company of all or substantially all of its assets in which one person or more than one person acting as a group acquires assets from the Company that have a total gross fair market value equal to more than 50% of the total gross fair market value of all of the assets of the Company immediately prior to such acquisition; or

A change in the composition of the Board of Directors of the Company such that individuals who, as of the date of this agreement, constitute the Board of Directors of the Company (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board of Directors of the Company; provided, however, that any individual becoming a member of the Board of Directors of the Company subsequent to the date of this agreement whose election, or nomination for election by the shareholders of the Company, was approved by a vote of at least a majority of the directors then constituting the Incumbent Board shall be considered as if that individual were a member of the Incumbent Board.

(iii) "Disability" means that Employee has commenced receipt of long-term disability benefits under the Company's long-term disability policy as in effect at the date of Employee's termination of employment.

(iv) "Retirement" means retirement after attaining the age at which an Employee's age plus his years of service equals age 62, provided, however, that (a) Employee has provided a minimum of 7.5 years of service to the Company, its subsidiaries or affiliates and (b) such retirement is more than 12 months from the Grant Date. For this purpose, years of service shall be credited for each twelve month period beginning on the date of Employee's commencement of employment with the Company and on each anniversary thereof during which the Employee was in active employment with the Company. For the avoidance of doubt, Employee's retirement within 12 months of the Grant Date shall not qualify as a Retirement hereunder.

(v) "Termination" or "Termination of Employment" means the event by which Employee ceases to be employed by a Group Entity and immediately thereafter is not employed by any other Group Entity.

5 . *Dividend Equivalents and Adjustments* .

(a) *Dividend Equivalents* . Subject to Section 5(d), Dividend Equivalents will be credited on Units (other than Units that, at the relevant record date, previously have been settled or forfeited) and deemed reinvested in additional Units, to the extent and in the manner as follows:

(i) *Cash Dividends* . If the Company declares and pays a dividend or distribution on Shares in the form of cash, then a number of additional Units shall be credited to Employee's Account as of the last day of the calendar quarter in which such dividend or distribution was paid equal to the number of Units credited to the Account as of the record date for such dividend or distribution multiplied by cash amount of the dividend or distribution paid on each outstanding share of Common Stock at such payment date, divided by the Fair Market Value of a share of Common Stock at the date of such crediting; provided, however, that in the case of an extraordinary cash dividend or distribution the Company may provide for such crediting at the dividend or distribution payment date instead of the last day of the calendar quarter.

(ii) *Non-Common Stock Dividends* . If the Company declares and pays a dividend or distribution on Common Stock in the form of property other than shares of Common Stock, then a number of additional Units shall be credited to Employee's Account as of the payment date for such dividend or distribution equal to the number of Units credited to the Account as of the record date for such dividend or distribution multiplied by the Fair Market Value of such property actually paid as a dividend or distribution on each outstanding share of Common Stock at such payment date, divided by the Fair Market Value of a share of Common Stock at such payment date.

(iii) *Common Stock Dividends and Splits* . If the Company declares and pays a dividend or distribution on Common Stock in the form of additional shares of Common Stock, or there occurs a forward split of Common Stock, then a number of additional Units shall be credited to Employee's Account as of the payment date for such dividend or distribution or forward split equal to the number of Units credited to the Account as of the record date for such dividend or distribution or split multiplied by the number of additional shares of Common Stock actually paid as a dividend or distribution or issued in such split in respect of each outstanding share of Common Stock.

(b) *Adjustments* . The number of Units credited to Employee's Account shall be appropriately adjusted, in order to prevent dilution or enlargement of Employee's rights with respect to Units or to reflect any changes in the number of outstanding shares of Common Stock resulting from any event referred to in Section 5.3 of the Plan, taking into account any Units credited to Employee in connection with such event under Section 5(a) hereof, and any performance conditions relating to the Units may be likewise adjusted in the discretion of the Committee.

(c) *Risk of Forfeiture and Settlement of Units Resulting from Dividend Equivalents and Adjustments*. Units which directly or indirectly result from Dividend Equivalents on or adjustments to a Unit granted hereunder and which do not result from a dividend or distribution on Shares in the form of cash shall be subject to the same risk of forfeiture (including Section 7.4 of the Plan) as applies to the granted Unit and, if not forfeited, will be settled at the same time as the granted Unit. Units which directly or indirectly result from Dividend Equivalents on or adjustments to a Unit granted hereunder and which result from an ordinary dividend or distribution on Shares in the form of cash shall not be subject to forfeiture and will be settled at the same time as the granted Unit (or if the

granted Unit is forfeited, then at the time the granted Unit would have been settled if it were not forfeited). Units which directly or indirectly result from Dividend Equivalents on or adjustments to a Unit granted hereunder and which result from an extraordinary dividend or distribution on Shares in the form of cash shall, unless otherwise determined by the Company at the time of such extraordinary dividend or distribution, be subject to the same risk of forfeiture (including additional forfeiture terms of Section 7.4 of the Plan) as applies to the granted Unit and, if not forfeited, will be settled at the same time as the granted Unit.

(d) *Changes to Manner of Crediting Dividend Equivalents* . The provisions of Section 5(a) notwithstanding, the Company may vary the manner and timing of crediting dividend equivalents for administrative convenience, including, for example, by crediting cash dividend equivalents rather than additional Units.

6. **Additional Forfeiture Provisions.** Employee agrees that, by signing this Agreement and accepting the grant of the Units, the forfeiture conditions set forth in Section 7.4 of the Plan shall apply to all Units hereunder and to gains realized upon the settlement of the Units.

7. **Employee Representations and Warranties and Release** . As a condition to any non-forfeiture of the Units at or after Termination of Employment and to any settlement of the Units, the Company may require Employee (i) to make any representation or warranty to the Company as may be required under any applicable law or regulation, to make a representation and warranty that no Forfeiture Event has occurred or is contemplated, and that otherwise the requirements of Section 7.4(d) of the Plan and Section 7 above have been met, and (ii) to execute a release of claims against the Company arising before the date of such release, in such form as may be specified by the Company.

8. **Other Terms Relating to Units** .

(a) *Deferral of Settlement; Compliance with Code Section 409A* . Settlement of any Unit, which otherwise would occur at the Settlement Date, will be deferred in certain cases if and to the extent Employee is permitted to participate in the Stock Option Gain and Stock Award Deferral Program or otherwise permitted to defer the Units and Employee makes a valid deferral election relating to the Units. Deferrals, whether elective or mandatory under the terms of this Agreement, shall comply with requirements under Code Section 409A. Deferrals will be subject to such other restrictions and terms as may be specified by the Company prior to deferral. It is understood that Code Section 409A and regulations thereunder may require any elective deferral to comply with Section 409A(a)(4)(C). Other provisions of this Agreement notwithstanding, under U.S. federal income tax laws and Treasury Regulations (including proposed regulations) as presently in effect or hereafter implemented, with respect to Units other than those which are excluded from being deemed deferrals of compensation under 409A (*note: in some cases the final tranche may qualify for such an exclusion*) (i) a distribution in settlement of Units to Employee triggered by a Termination of Employment will occur only if the Termination constitutes a “separation from service” within the meaning of Code Section 409A(a)(2)(A)(i) and, if at the time of such separation from service Employee is a “specified employee” under Code Section 409A (a)(2)(B)(i) and a delay in distribution is required in order that Employee will not be subject to a tax penalty under Code Section 409A, such distribution in settlement of Units will occur at the date six months after Termination of Employment; and (ii) any rights of Employee or retained authority of the Company with respect to Units hereunder shall be automatically modified and limited to the extent necessary so that Employee will not be deemed to be in constructive receipt of income relating to the Units prior to the distribution and so that Employee shall not be subject to any penalty under Code Section 409A. Other provisions of this

Agreement notwithstanding, if a separation from service occurs within less than six months before the fixed date specified as the Settlement Date and the six-month delay rule would apply to a settlement triggered by such separation from service, the settlement will not be made based on the separation from service, but instead the settlement shall be made based on the fixed date specified as the Settlement Date.

(b) *Fractional Units and Shares* . The number of Units credited to Employee's Account shall include fractional Units calculated to at least three decimal places, unless otherwise determined by the Committee. Unless settlement is effected through a broker or agent that can accommodate fractional shares (without requiring issuance of a fractional share by the Company), upon settlement of the Units Employee shall be paid, in cash, an amount equal to the value of any fractional share that would have otherwise been deliverable in settlement of such Units.

(c) *Tax Withholding* . Employee shall make arrangements satisfactory to the Company, or, in the absence of such arrangements, a Group Entity may deduct from any payment to be made to Employee any amount necessary, to satisfy requirements of federal, state, local, or foreign tax law to withhold taxes or other amounts with respect to the lapse of the risk of forfeiture (including FICA due upon such lapse) or the settlement of the Units. Unless Employee has made separate arrangements satisfactory to the Company, the Company may elect to withhold shares deliverable in settlement of the Units having a fair market value (as determined by the Committee) equal to the amount of such tax liability required to be withheld in connection with the settlement of the Units, but the Company shall not be obligated to withhold such Shares. The Company may specify a reasonable deadline (for example, 90 days before the Settlement Date) by which separate arrangements must be made for payment of withholding taxes other than through withholding of shares.

(d) *Statements* . An individual statement of Employee's Account will be issued to Employee at such times as may be determined by the Company. Such a statement shall reflect the number of Units credited to Employee's Account, transactions therein during the period covered by the statement, and other information deemed relevant by the Committee. Such a statement may be combined with or include information regarding other plans and compensatory arrangements for employees. Employee's statements shall be deemed a part of this Agreement, and shall evidence the Company's obligations in respect of Units, including the number of Units credited as a result of Dividend Equivalents (if any). Any statement containing an error shall not, however, represent a binding obligation to the extent of such error, notwithstanding the inclusion of such statement as part of this Agreement.

9. *Miscellaneous* .

(a) *Binding Agreement; Written Amendments* . This Agreement shall be binding upon the heirs, executors, administrators, and successors of the parties. This Agreement and the Plan, and any deferral election separately filed with the Company relating to this Award, constitute the entire agreement between the parties with respect to the Units, and supersede any prior agreements or documents with respect thereto. No amendment, alteration, suspension, discontinuation, or termination of this Agreement which may impose any additional obligation upon the Company or materially impair the rights of Employee with respect to the Units shall be valid unless in each instance such amendment, alteration, suspension, discontinuation, or termination is expressed in a written instrument duly executed in the name and on behalf of the Company and, if Employee's rights are being materially impaired, by Employee.

(b) *No Promise of Employment.* The Units and the granting thereof shall not constitute or be evidence of any agreement or understanding, express or implied, that Employee has a right to continue as an officer or employee of the Company for any period of time, or at any particular rate of compensation.

(c) *Unfunded Plan.* Any provision for distribution in settlement of Employee's Account hereunder shall be by means of bookkeeping entries on the books of the Company and shall not create in Employee or any Beneficiary any right to, or claim against any, specific assets of the Company, nor result in the creation of any trust or escrow account for Employee. With respect to any entitlement of Employee or any Beneficiary to any distribution hereunder, Employee or such Beneficiary shall be a general creditor of the Company.

(d) *Governing Law.* THIS AGREEMENT SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NEW YORK WITHOUT GIVING EFFECT TO CONFLICTS OF LAWS PRINCIPLES.

(e) *Legal Compliance.* Employee agrees to take any action the Company reasonably deems necessary in order to comply with federal and state laws, or the rules and regulations of the New York Stock Exchange, FINRA, or any other stock exchange, or any other obligation of the Company or Employee relating to the Units or this Agreement.

(f) *Notices.* Any notice to be given the Company under this Agreement shall be addressed to the Company at 520 Madison Avenue, 12th Floor, New York, NY 10022, attention: Corporate Secretary, and any notice to the Employee shall be addressed to the Employee at Employee's address as then appearing in the records of the Company.

EXHIBIT C

[Date]

[Name]

[Address]

Dear [Name] :

This letter agreement and release (the "Agreement") confirms our understanding and agreement with regard to the termination of your employment with Jefferies & Company, Inc. (the "Company"):

1. Your employment with the Company was terminated effective **[Termination Date]** .
2. Your total and final payment and benefits from the Company shall be as follows:
 - (a) Regardless of whether you sign this Agreement:
 - (i) You have received your regular salary on a normal pay period cycle through and until **[Termination Date]** .
 - (ii) Your comprehensive life, accidental death and dismemberment and long and short term disability insurance benefits and all other benefits ceased as of **[Termination Date]** . You may have conversion privileges under some of these benefits programs. Please contact People Services for details.
 - (iii) Except as provided in Section 2(b)(ii), your coverage under the Company's group medical and dental insurance programs will cease as of **[Date]** . You may be eligible for continued coverage under these programs pursuant to COBRA at your own expense. Specific information regarding COBRA continuation will be sent to you separately.
 - (iv) You ceased participating in the Company's 401(k), profit-sharing, pension, ESOP, stock purchase plan, restricted stock award plan, deferred compensation plan and all similar plans in which you participated or for which you were eligible as of **[Termination Date]** . You retain your right to vested benefits you have earned and are entitled to, if any, through **[Termination Date]** . Specific information concerning those plans in which you participated will be forwarded to you separately.
 - (v) You will be reimbursed for all approved and authorized out-of-pocket expenses incurred through the date of termination of your

employment provided that you submit appropriate documentation by no later than X date.

(b) Provided that you execute this Agreement by **[Termination Date + 21 days]** and do not revoke it as provided in paragraph 19, and in consideration for your waiver and release in paragraph 4(a) below,

- (i) The Company will provide you with a lump sum payment of \$____.00 (the “Separation Payment”), less statutory deductions for all applicable federal and state taxes and withholding. The Separation Payment includes, but is not limited to, any severance payment to which you might otherwise have been entitled pursuant to Company policy, and any discretionary bonuses awarded to you through the effective date of the termination of your employment. The Separation Payment shall be made at the times specified in Section 2(c) below.
- (ii) You will be covered under the Company’s group medical and dental insurance through **[Date]** . Thereafter, you may be covered under COBRA. This continued coverage after **[Date]** shall be available at your own expense. This continued coverage shall be subject to and in accordance with the terms of the documents governing the program.
- (iii) The [insert number] of restricted stock units granted to you on [insert commencement date of employment] which remained unvested as of the date of termination of your employment are vested as of the effective date of this Agreement and shall be distributed to you in accordance with the Restricted Stock Units Agreement executed by you on [insert date].
- (iv) The following grants of restricted stock and restricted stock units (“RSUs”) of Jefferies Group, Inc. will not be forfeited upon the termination of your employment, but will continue to vest in accordance with the terms and conditions set forth in the Restricted Stock Agreement and the Restricted Stock Unit Agreements governing those grants subject to the following. The restricted stock and the RSUs will continue to vest provided (a) there is no breach of the terms and conditions of the Restricted Stock Agreement or the Restricted Stock Unit Agreements and (b) the conditions set forth therein for the continued vesting of the restricted stock and the RSUs are complied with through the respective vesting dates of the restricted stock and the RSUs. For the avoidance of doubt, if there is a Forfeiture Event as defined in the Restricted Stock Agreement or the Terms and Conditions of Restricted Stock Units (including but not limited to your going to

work for a competitor of the Company) prior to the time the restricted stock and the RSUs described herein have fully vested, all restricted stock and RSUs which have not yet vested as of the date of such Forfeiture Event will be forfeited. You acknowledge and agree that you are responsible for the payment of all taxes and withholding on the RSUs/shares which have vested and/or are distributed to you. Provided that the conditions set forth herein are complied with, the restricted stock and RSUs which are eligible to continue to vest are as follows:

[Insert details of additional RSU/restricted stock grants that allow for continued vesting upon a termination of employment not for Cause]

(c) Each element of the Separation Payment, including any portion representing severance to which you would have been entitled under any Company policy, any bonus payment, and any other portion of the Separation Payment, shall be deemed a separate payment for purposes of Section 409A of the Internal Revenue Code (“409A”). These portions comprising the Separation Payment, to the maximum extent permissible under 409A without resulting in tax penalties to you, will be paid ten days after this Agreement becomes effective in accordance with paragraph 19. [For this purpose, however, ***because the following three conditions are met***, those portions of the Separation Payment constituting a “deferral of compensation” as specified below will be paid on the first business day of the seventh calendar month after your “separation from service” as defined in Treasury Regulation § 1.409A-1(h) (this is referred to as the “six-month delay” below):

- (i) At the time of your separation from service you were a “specified employee” as defined under 409A (including Treasury Regulation § 1.409A-1(i))
- (ii) At the time of your separation from service, the stock of the Company was publicly traded on an established securities market or otherwise
- (iii) A portion of the Separation Payment, in the amount of \$____, constitutes a “deferral of compensation” subject to 409A. For this purpose:
 - Any portion of the Separation Payment deemed payable solely due to involuntary separation from service that qualifies as a “short-term deferral” under Treasury Regulation § 1.409A-1(b)(4) will not be deemed a “deferral of compensation” and shall be paid without the six-month delay;
 - Any portion of the Separation Payment deemed payable solely due to involuntary separation from service up to the limit specified in Treasury Regulation § 1.409A-1(b)(9)(iii) will not be deemed a “deferral of compensation” and shall be paid without the six-month delay
 - Any portion of the Separation Payment, whether or not separation from service is involuntary, up to the limit specified in Treasury Regulation § 1.409A-1(b)(9)(v)(D) (if this limited exclusion is not applied to payments apart from this Agreement) will not be deemed a “deferral of compensation” and may be paid without the six-month delay

- Any portion of the Separation Payment that may be excluded from being deemed a “deferral of compensation” under any other applicable Treasury Regulation or Internal Revenue Service guidance may be paid without the six-month delay.

If the six-month delay is applicable to any payment, the payment shall be accelerated upon the your death during the six-month delay period but not for any other reason. For purposes of this Agreement, any payment that is not excluded from being deemed a “deferral of compensation” under 409A shall be payable only upon a “separation from service” as defined in Treasury Regulation § 1.409A-1(h) or, if the six-month delay applies, the specified date at least six months after such separation from service. Any other payments or benefits under this Agreement shall be paid at the times specified herein, except that the rules set forth above shall apply to such payments and benefits (in addition to their application to Separation Payments) so that such payments and benefits will not be provided during the six months following separation from service to the extent necessary to comply with applicable requirements under Treasury Regulation § 1.409A-1(i)(2) (without affecting the timing of payments and benefits to be provided after such six-month delay period.)]

(d) You understand and agree that the Company does not make any representations and is not providing any advice regarding the taxation of the payments hereunder, including but not limited to taxes, interest and penalties under 409A and similar liabilities under state tax laws. No indemnification or gross-up is payable under this Agreement with respect to any such tax, interest, penalty or similar liability, and no interest is payable on any payment or benefit which is subject to a six-month delay hereunder. You hereby release the Company from any and all claims related to the imposition of taxes on the amounts payable hereunder and hold the Company harmless in the event of any claims made against you related to taxes due upon the amounts payable hereunder.

(e) The terms of this Agreement relating to a deferral of compensation or compensation excluded from being a deferral under 409A, including any authority of the Company and your rights with respect thereto, shall be limited to those terms permitted under 409A, and any terms not permitted under 409A shall be modified and limited to the extent necessary to conform with 409A but only to the extent that such modification or limitation is permitted under 409A and the regulations and guidance issued thereunder.

3. You understand and agree that you are receiving compensation, payments and/or benefits under this Agreement which are in excess of those to which you are now or in the future may be entitled from the Company or Releasees (as defined in paragraph 4(c) below). You further understand and agree that the foregoing consideration provided to you under the terms of this Agreement is in addition to anything of value to which you are otherwise entitled. You represent, warrant and acknowledge that the Company or Releasees (as defined in paragraph 4(c) below) owe you no wages, commissions, bonuses, sick pay, personal leave pay, severance pay, vacation pay, or other compensation or payments or form of remuneration of any kind or nature, other than that specifically provided for in this Agreement.

4. In exchange for the compensation, payments, benefits and other consideration provided to you pursuant to this Agreement, you agree as follows:

(a) To the fullest extent permitted by law, you waive, release and forever discharge the Company and Releasees (as defined in paragraph 4(c) below) from any and all legally waivable claims, grievances, injuries, controversies, agreements, covenants, promises, debts, accounts, actions, causes of action, suits, arbitrations, sums of money, wages, attorneys' fees, costs, damages, or any right to any monetary recovery or any other personal relief, whether known or unknown, in law or in equity, by contract, tort, law of trust or pursuant to federal, state or local statute, regulation, ordinance or common law, which you now have, ever have had, or may hereafter have, based upon or arising from any fact or set of facts, whether known or unknown to you, from the beginning of time until the date of execution of this Agreement, arising out of or relating in any way to your employment relationship with the Company and Releasees or other associations with the Company and Releasees or any termination thereof. Without limiting the generality of the foregoing, this waiver, release, and discharge includes any claim or right based upon or arising under any federal, state or local fair employment practices or equal opportunity laws, including, but not limited to, the Age Discrimination in Employment Act (29 U.S.C. Section 621, et seq.) ("ADEA"), the Older Workers' Benefits Protection Act, the Rehabilitation Act of 1973, the Worker Adjustment and Retraining Notification Act, 42 U.S.C. Section 1981, Title VII of the Civil Rights Act of 1964, the Equal Pay Act, the Employee Retirement Income Security Act ("ERISA") (including, but not limited to, claims for breach of fiduciary duty under ERISA), the Americans With Disabilities Act, the Sarbanes-Oxley Act, the New York State Human Rights Law, the New York State Constitution, the New York Labor Law, the New York Civil Rights Law, the New York City Human Rights Law, the New York Executive Law, **[add any other relevant state laws]**, including all amendments to any of the foregoing.

(b) Notwithstanding the generality of the foregoing, nothing herein constitutes a release or waiver by you of: (i) any claim or right you may have under COBRA; (ii) any claim or right you may have for unemployment insurance benefits or Workers' Compensation benefits; (iii) any claim or right that may arise after the execution of this Agreement; (iv) any claim or right you may have under this Agreement; or (v) any vested benefits under the written terms of a qualified employee pension benefit plan.

(c) For purposes of this Agreement, the term "the Company and Releasees" includes the Company and the Company's parents, subsidiaries, related companies, partnerships and joint ventures, predecessors, and successors, and, with respect to each such entity, all of its past and present employees, officers, directors, shareholders, owners, representatives, agents, attorneys, assigns, insurers, employee benefits plans and such plans' administrators, fiduciaries, trustees, record keepers and service providers, and each of its and their respective successors and assigns, each and all of them in their personal and representative capacities, and any other persons or entities acting on behalf of any of these persons or entities.

5. Nothing contained in this Agreement shall be deemed to constitute an admission or evidence of any wrongdoing or liability on the part of you or the Company or Releasees, nor

of any violation of any federal, state or municipal statute, regulation or principle of common law or equity. The Company expressly denies any wrongdoing of any kind in regard to your employment or your termination.

6. Subject to paragraph 10 below:

(a) You agree to maintain in confidence and not publish, release or in any manner disclose this Agreement and all attachments hereto, the terms of this Agreement, or any communications relating to the execution of this Agreement; however, you may discuss the terms of this Agreement with your attorney, your financial advisors and your immediate family members, provided that you shall be responsible for any breach of confidentiality by any such individuals.

(b) Unless you shall first secure the Company's written consent, you shall not directly or indirectly publish, disclose, market or use, or authorize, advise, hire, counsel or otherwise procure any other person or entity, directly or indirectly, to publish, disclose, market or use, any trade secrets, proprietary computer software and programs, and other confidential and proprietary information and materials of or about the Company and Releasees and their operations and customers, including any confidential and proprietary information and materials of which you became aware or informed during your employment with the Company ("Company Proprietary Information"). Such Company Proprietary Information is and shall continue to be the exclusive proprietary property of the Company and Releasees.

7. You represent that you have returned to the Company any and all original and duplicate copies of all your work product and of files, calendars, books, records, notes, notebooks, customer lists and proposals to customers, manuals, computer disks, diskettes and any other magnetic and other media materials you have in your possession or under your control belonging to the Company or Releasees or containing confidential or proprietary information concerning the Company or Releasees or their customers or operations ("Company Information").

8. You acknowledge and agree that, by virtue of the various positions that you have held with the Company and Releasees, your assistance may be required, whether in connection with formal or informal investigations, court proceedings, arbitrations and other forms of actions, and whether by the Company and Releasees or any third party. Therefore, you agree to provide such assistance to the Company or Releasees in connection with such investigations, proceedings, arbitrations and actions as may be requested of you from time to time.

9. You agree to perform all acts and execute and deliver any documents that may be reasonably necessary to carry out the provisions of this Agreement.

10. Notwithstanding the foregoing, you understand that nothing in this Agreement shall prohibit or restrict any party or such party's attorneys from their rights to: (i) make any disclosure of relevant and necessary information or documents in any action, investigation, or proceeding relating to this Agreement, or as required by law or legal process; or (ii) participate, cooperate, or testify in any action, investigation, or proceeding with, or provide information to,

any governmental agency or legislative body, any self-regulatory organization, or the Company's Legal Department; provided that, to the extent permitted by law, upon receipt of any subpoena, court order or other legal process compelling the disclosure of any such information or documents, the disclosing party gives prompt written notice to the other party so as to permit such other party to protect such party's interests in confidentiality to the fullest extent possible. You acknowledge and agree, however, that should you or any person, organization, or entity file, charge, claim, sue, or cause or permit to be filed any action, investigation, or proceeding arising out of or related to your employment or termination of employment with the Company, pursuant to paragraph 4(a), you waive any right to any personal or monetary relief in any such action, investigation, or legal proceeding.

11. This Agreement may not be changed orally, and no modification, amendment or waiver of any of the provisions contained in this Agreement, nor any future representation, promise or condition in connection with the subject matter of this Agreement shall be binding upon any party hereto unless made in writing and signed by such party.

12. In the event you breach any of the provisions of paragraphs 6 through 9 of this Agreement, you agree that the Company will be entitled to all appropriate remedies and damages, including but not limited to seeking the return of all compensation, payments and benefits provided for in this Agreement. You recognize that money damages will not be adequate to compensate the Company or to protect and preserve the status quo. Therefore, you expressly consent to the issuance of a temporary restraining order and/or a preliminary injunction, by any court or arbitral forum of competent jurisdiction to prohibit the breach of those provisions of this Agreement.

13. Except as provided in paragraph 12 of this Agreement, any controversy or claim arising out of or relating to your employment or this Agreement will be settled by arbitration before FINRA in accordance with its rules. The award rendered in arbitration shall be final and binding, and judgment upon the award entered by the arbitrator(s) may be entered in any court of competent jurisdiction. In addition, you agree to stipulate, upon request by the Company, to expedited hearing procedures for such arbitration. You acknowledge that a court or an arbitration panel can issue an injunction to maintain the status quo pending the outcome of any arbitration proceeding that may be initiated, and further, that the propriety of temporary and preliminary injunctive relief will be decided by a court and not by an arbitration panel should the Company in its sole discretion elect to seek such relief in court. This arbitration agreement applies (but is not limited) to statutory discrimination, harassment, retaliation and whistleblower claims under Title VII of the Civil Rights Act of 1964, the ADEA, the Americans with Disabilities Act, or any other federal, state or local discrimination, wage payment, whistleblower or fair employment practices law, statute or regulation, or common law rules. You understand and agree that by entering into this agreement, you are waiving any right to file a lawsuit or to have a jury trial over any claim covered by this agreement, any right to bring or litigate any such claim as a class or collective action, and any right to act as a class representative or to participate as a member of a class of claimants with respect to any such claim.

14. This Agreement shall be subject to and governed by and interpreted in accordance with the laws of the State of New York without regard to conflicts of laws principles. This Agreement contains the entire agreement between us and supersedes and terminates any and all previous agreements between us, whether written or oral. All prior and contemporaneous discussions and negotiations have been and are merged and integrated into, and are superseded by, this Agreement.

15. In the event that, any one or more provisions (or portion thereof) of this Agreement is held to be invalid, illegal or unenforceable for any reason, you and the Company agree that the relevant provision (or portion thereof) shall be construed or modified so as to provide the Company with the maximum protection that is lawful and enforceable, consistent with the intent of the Company and you in entering into this Agreement. If the relevant provision (or portion thereof) cannot be construed or modified to render it lawful and enforceable, the unlawful or unenforceable provision shall be construed as narrowly as possible and shall be severed from the remainder of the relevant provision(s) and the remainder of this Agreement shall be given full force and effect. Notwithstanding the foregoing, if the waiver and release of claims set forth in paragraph 4 is held to be invalid, illegal or unenforceable, the Company shall be relieved of its obligations under paragraph 2(b).

16. This Agreement shall inure to the benefit of and shall be binding upon (a) the Company, its successors and assigns, and any company with which the Company may merge or consolidate or to which the Company may sell all or substantially all of its assets and (b) you and your executors, administrators, heirs and legal representatives. You may not sell or otherwise assign your rights, obligations, or benefits under this Agreement and any attempt to do so shall be void.

17. All notices in connection with or provided for under this Agreement shall be validly given or made only if made in writing and delivered personally or mailed by registered or certified mail, return receipt requested, postage prepaid, to the party entitled or required to receive the same, as follows:

If to you, addressed to:

[Name/Address]

If to the Company, addressed to:

Judith Kester
Jefferies & Company, Inc.
11100 Santa Monica Blvd, 11th Floor
Los Angeles, CA 90025

or at such other address as either party may designate to the other by notice similarly given. Notice shall be deemed to have been given upon receipt in the case of personal delivery and upon the date of mailing in the case of mail.

18. You acknowledge and agree that:

(a) The Company advises you to consult with an attorney before signing this Agreement.

(b) You have obtained independent legal advice from an attorney of your own choice with respect to this Agreement, or you have knowingly and voluntarily chosen not to do so.

(c) You have entered into this Agreement knowingly and voluntarily.

(d) You have read and understand this entire Agreement.

(e) Changes to the Company's offer contained in this Agreement whether material or immaterial will not restart the twenty-one (21) day consideration period provided for in paragraph 2(b) below.

(f) In exchange for your waivers, releases and commitments set forth herein, including your waiver and release of all claims arising under the ADEA, the payments, benefits and other considerations that you are receiving pursuant to this Agreement exceed any payment, benefit or other thing of value to which you would otherwise be entitled, and are just and sufficient consideration for the waivers, releases and commitments set forth herein

19. You further acknowledge and agree:

(a) You have been afforded at least twenty-one (21) days in which to consider this Agreement. You acknowledge that, if you elect to sign this Agreement, the executed Agreement must be returned to the Company by U.S. mail postmarked on or before the twenty-first day after you receive this Agreement to Judith Kester, at the address indicated above. If the twenty-first day referenced above falls on a Saturday, Sunday, or holiday, the 21-day time limit shall be extended to the next business day.

(b) Once you have signed the Agreement, you will then be permitted to revoke this Agreement at any time during the period of seven (7) days following its execution by delivering to Judith Kester at the address indicated above a written notice of revocation. If you wish to revoke this Agreement, the notice of revocation must be received by the Company no later than the eighth day following your execution of this Agreement. If the seventh day referenced above falls on a Saturday, Sunday, or holiday, the 7-day time limit shall be extended to the next business day. This Agreement will not be effective or enforceable and no benefits shall be provided hereunder unless and until the seven-day revocation period has expired without your having exercised your right of revocation.

(c) In the event that you fail to execute and return this Agreement on a timely basis, or you execute and then elect to revoke this Agreement, this Agreement will be of no force or effect, and neither you nor the Company will have any rights or obligations hereunder.

If this Agreement conforms to your understanding and is acceptable to you, please indicate your agreement by signing and dating the enclosed copy of this Agreement in the space provided

below and returning the executed Agreement to the Company as provided in paragraph 19 above. You must sign this Agreement before a notary. If you cannot locate a notary, please contact me and I will arrange either to have a notary present in my office when you wish to sign, or will give you an address at another Company location where notaries are available.

Sincerely,

JEFFERIES & COMPANY, INC.

By: _____
Company Representative
Title

ACCEPTED AND AGREED:

[Name]

Date

State of _____ :

_____ :

County of _____ :

On this ___ day of _____, before me personally came [Name] to me known and known to me to be the person described in and who executed the foregoing Agreement, and [he/she] duly acknowledged to me that [he/she] executed the same.

Notary Public

My commission expires:

JEFFERIES GROUP, INC. AND SUBSIDIARIES
COMPUTATION OF RATIO OF EARNINGS TO FIXED CHARGES
(Amounts in thousands, except for per share amounts)

	Year Ended December 31,				
	2007	2006	2005	2004	2003
Fixed Charges:					
Interest expense on long-term indebtedness	\$105,221	\$ 84,044	\$ 47,669	\$ 40,256	\$ 23,987
Interest portion of rent expense	16,814	14,469	11,653	9,437	7,636
Total fixed charges	<u>\$122,035</u>	<u>\$ 98,513</u>	<u>\$ 59,322</u>	<u>\$ 49,693</u>	<u>\$ 31,623</u>
Earnings:					
Earnings before income taxes, minority interest, and cumulative effect of change in accounting principle	\$245,734	\$348,654	\$268,407	\$226,989	\$144,533
Total fixed charges	<u>122,035</u>	<u>98,513</u>	<u>59,322</u>	<u>49,693</u>	<u>31,623</u>
Total earnings	<u>\$367,769</u>	<u>\$447,167</u>	<u>\$327,729</u>	<u>\$276,682</u>	<u>\$176,156</u>
Ratio of Earnings to Fixed Charges (1)	3.0	4.5	5.5	5.6	5.6

- (1) The ratio of earnings to fixed charges is computed by dividing (a) income from continuing operations before income taxes plus fixed charges by (b) fixed charges. Fixed charges consist of interest expense on all long-term indebtedness and the portion of operating lease rental expense that is representative of the interest factor (deemed to be one-third of operating lease rentals).

Subsidiaries of Jefferies Group, Inc.

(excludes certain subsidiaries pursuant to Item 601 of Regulation S-K)

<i>Name</i>	<i>Place of Formation / Incorporation</i>
Jefferies & Company, Inc.	Delaware
Jefferies Asset Management, LLC	Delaware
Jefferies Asset Management (Zurich)	Switzerland
Jefferies Asset Management Japan Limited	England & Wales
Jefferies Execution Services, Inc.	California
Jefferies Finance, LLC	Delaware
Jefferies Financial Products, LLC	Delaware
Jefferies High Yield Holdings, LLC	Delaware
Jefferies High Yield Trading, LLC	Delaware
Jefferies International Limited	England & Wales
Jefferies International (Holdings) Limited	England & Wales
Jefferies Investment Management Limited	England & Wales

Consent of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
JEFFERIES GROUP, INC.:

We consent to the incorporation by reference in the Registration Statements No. 333-84079 dated July 29, 1999, and No. 333-107014 dated July 14, 2003, on Form S-8, No. 333-74723 on Form S-4, No. 333-81354 dated January 24, 2002, and No. 333-107032 dated July 15, 2003 and August 22, 2003, on Form S-3, No. 333-130325 dated December 14, 2005 on Form S-3ASR, and No. 001-14947 dated April 20, 1999 on Form 10 of Jefferies Group, Inc. of our reports dated February 28, 2008, with respect to the consolidated statements of financial condition of Jefferies Group, Inc. and subsidiaries as of December 31, 2007 and 2006, and the related consolidated statements of earnings, changes in stockholders' equity, cash flows and comprehensive income for each of the years in the three-year period ended December 31, 2007, and the effectiveness of internal control over financial reporting as of December 31, 2007, which reports appear in the December 31, 2007 annual report on Form 10-K of Jefferies Group, Inc. Our report with respect to the Consolidated Financial Statements refers to a change in 2006 in accounting for share-based payments.

/s/ KPMG LLP

KPMG LLP

New York, New York
February 28, 2008

**RULE 13a-14(a)/15d-14(a)
CERTIFICATION BY CHIEF FINANCIAL OFFICER**

I, Peregrine C. Broadbent, certify that:

1. I have reviewed this annual report on Form 10-K of Jefferies Group, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 28, 2008

By: /s/ Peregrine C. Broadbent
Peregrine C. Broadbent
Chief Financial Officer

**RULE 13a-14(a)/15d-14(a)
CERTIFICATION BY CHIEF EXECUTIVE OFFICER**

I, Richard B. Handler, certify that:

1. I have reviewed this annual report on Form 10-K of Jefferies Group, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal controls over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: February 28, 2008

By: /s/ Richard B. Handler
Richard B. Handler
Chief Executive Officer

**Rule 13a-14(b)/15d-14(b) and Section 1350 of Title 18 U.S.C.
CERTIFICATION BY THE CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER**

I, Richard B. Handler, Chief Executive Officer, and I, Peregrine C. Broadbent, Chief Financial Officer, of Jefferies Group, Inc, a Delaware corporation (the "Company"), each hereby certifies, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that to my knowledge:

(1) The Company's periodic report on Form 10-K for the year ended December 31, 2007 (the "Form 10-K") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the Form 10-K fairly presents, in all material respects, the financial condition and results of operations of the Company.

* * *

CHIEF EXECUTIVE OFFICER

/s/ Richard B. Handler

Richard B. Handler

CHIEF FINANCIAL OFFICER

/s/ Peregrine C. Broadbent

Peregrine C. Broadbent

Date: February 28, 2008

Date: February 28, 2008

A signed original of this written statement required by Section 906 has been provided to Jefferies Group, Inc. and will be retained by Jefferies Group, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.