

**J.P. MORGAN SECURITIES PLC**  
(formerly known as J.P. MORGAN SECURITIES LTD.)

(Registered Number: 2711006)

Annual report for the year ended 31 December 2012

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# **J.P. MORGAN SECURITIES PLC**

## **Annual report for the year ended 31 December 2012**

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# **J.P. MORGAN SECURITIES PLC**

## **Directors' report for the year ended 31 December 2012**

The directors present their report and the audited financial statements of J P Morgan Securities plc ("the Company" or "JPMS plc") (formerly J P Morgan Securities Ltd ) for the year ended 31 December 2012. The Company's registered number is 2711006. The Company is part of JPMorgan Chase & Co group (together with its subsidiaries, "the Group").

### **Principal activity**

The Company is the principal investment bank subsidiary in EMEA and was authorised and regulated in the UK by the Financial Services Authority ("FSA") but since 1 April 2013 is now authorised by the Prudential Regulation Authority ("PRA") and regulated by the Financial Conduct Authority ("FCA") and the PRA. J P Morgan Securities plc's business focus is across Equities, Fixed Income, Commodities and Prime Brokerage. Within these lines of business its activities include underwriting government and corporate bonds, equities and other securities, arranging private placements of debt and convertible securities, trading in debt, equity securities, commodities, swaps and derivative trading and marketing, and providing investment banking, advisory, brokerage and clearing services for exchange traded future and options contracts.

The Company is a member of over twenty exchanges. It is also the vehicle for some European Commodity Derivative activities excluding oil and base metals. It has branches in Frankfurt, Paris, Milan, Madrid, Stockholm and Zurich.

### **Review of business**

The directors are satisfied with the performance of the Company.

The Company's core businesses continued to perform well with solid revenues and good client flow despite challenging market conditions during the year.

The Company benefited from strong trading results from its client flow activities within the Fixed Income and Equities lines of business. The Company's strength as a market maker, the positive market sentiments and improved Eurozone climate allowed the businesses to provide better investment opportunities to clients leading to increased client flow and continued investment growth. The Company also generated positive revenues from its corporate finance activities by providing comprehensive advisory services and raising funds in capital markets for a broad range of clients.

Below are the key events of 2012:

- On 28 May 2012, the Company sub-divided and reclassified 10 ordinary shares of \$10,000 each in the issued capital held by J P Morgan Chase International Holdings into 50,000 ordinary shares of \$2 each. The Company then redenominated these converted shares into 50,000 ordinary shares of £1.24 each. These steps were made in order to introduce the authorised minimum amount of £50,000 share capital denominated in sterling as required by sections 542(3) and 765 of the Companies Act 2006 prior to the re-registration of the Company as a public limited company.
- On 26 June 2012, the Company received an ordinary dividend of \$900,000,000 from its wholly-owned subsidiary, J P Morgan Europe Limited.
- On 29 June 2012, the Board approved the payment of interim dividends of \$569,921,615 on preference shares (2011: Nil), \$12,605,911 on preferred ordinary shares (2011: Nil) and \$317,472,474 on the ordinary shares of the Company (2011: Nil).
- On 6 July 2012, the Company re-registered to a public limited company and changed its name to J P Morgan Securities plc.
- On 16 August 2012 the shareholders of the Company approved the adoption of new Articles of Association, removing the right of the Preferred Ordinary shareholders to vote at a general meeting of the Company.

# J.P. MORGAN SECURITIES PLC

## Directors' report for the year ended 31 December 2012 (continued)

### Principal risks and uncertainties

Whilst management of the Company's risks and uncertainties is integrated with that of the wider group, the Company also manages its risks at a legal entity level. This includes, for example, the use of Company level risk policies, the ability to set separate risk limits at a Company level and report metrics at a Company level. Whilst the Company operates within Group wide policy, in addition the Company develops its own risk policies. Stress and scenario testing is also performed at a legal entity level.

Both the Group and the Company operate within a highly regulated industry, and the Company's business and results may be significantly affected by the laws and regulations to which it is subject.

Significant changes in the way that major financial services institutions are regulated are occurring in the UK, the rest of Europe, the US and worldwide. The reforms being discussed include several that contemplate restructuring of the financial services industry. Such measures will likely lead to stricter regulations of financial institutions generally, and heightened prudential requirements for systemically important firms in particular. Under consideration are reforms of the over-the-counter derivatives markets, such as mandated exchange clearing, position limits, margin, capital and registration requirements. Many of these reforms, if enacted, could affect the Group and the Company's business model.

From 1 April 2013, regulation of J.P. Morgan Securities plc has transitioned to the PRA, pursuant to the U.K. Government's plan under the Financial Services Act 2012 to restructure regulatory responsibility between the PRA (which is a subsidiary of the Bank of England having responsibility for prudential regulation of banks and other systemically important institutions) and the FCA (which regulates prudential matters for other firms and conduct matters for all participants).

In the EU, there is an extensive and complex program of proposed regulatory enhancement which reflects, in part, the EU's commitments to policies of the G-20 together with other plans specific to the EU. This program includes the European Market Infrastructure Regulation ("EMIR") which, among other things, would require central clearing of standardised derivatives and which is likely to be phased in starting in 2013. It also includes the revision of the existing Markets in Financial Instruments Directive ("MiFID II") to deliver, among other things, the G20 commitment to on-venue trading of derivatives. Both EMIR and MiFID II include many other regulatory requirements that may have wide ranging and material effects on the Company's business operations.

### Key performance indicators (KPIs)

The results are monitored against expectations of the business activities. The Board of directors monitors progress on the performance of the Company by reference to the following KPIs:

	2012	2011
<b>Earnings Growth</b>		
Operating Margin (%)	53.38%	28.80%
<b>Capital &amp; Balance Sheet</b>		
Tier 1 capital (US\$ '000)	19,878,053	19,418,268
Assets variation	8.9%	7.55%

A more detailed description of the Group key performance indicators may be found within the Group annual report.

# **J.P. MORGAN SECURITIES PLC**

## **Directors' report for the year ended 31 December 2012 (continued)**

### **Business environment, strategy and future outlook**

In 2012, the Company benefited from strong revenues across most of its dedicated business lines and the directors expect the diversified and expanding activities in 2013 to provide continued opportunities

The Company continues to focus on the organic growth of its existing core businesses and expansion of the Prime Services business. The local infrastructure is now in place to serve clients across the entire spectrum of cash and synthetic products, along with equity financing, securities lending, clearing, settlement and custodial services. The Company will look to continue to build up and expand its foot print in this business and to generate solid returns

There are a number of known regulatory changes occurring over the next two years and beyond which may affect the capital adequacy or business model of the Company. European legislation includes changes to the Basel and Capital Requirements Directive framework. US legislation is yet to be finalised on the extraterritorial application of Dodd Frank and Section 716, often referred to as "Swaps Pushout", which is likely to require specific transactions (as defined by the legislation) to be booked in an entity other than JPMorgan Chase Bank N A, a group company. The Company is undertaking an analysis of the potential impact of any additional derivatives business being booked in the Company, including capital modelling and the technology build required to support any booking model changes

The Company's net assets at 31 December 2012 were \$27,882,561,000 (2011 \$26,385,131,000). The position of the Company is set out on page 11

### **Results and dividends**

The results for the year are set out on page 10 and show the Company's profit for the financial year after taxation is \$2,381,416,000 (2011 \$1,105,690,000)

On 29 June 2012, the Board approved the payment of interim dividends of \$569,921,615 on preference shares (2011 nil), \$12,605,911 on preferred ordinary shares (2011 nil) and \$317,472,474 on the ordinary shares of the Company (2011 nil)

No final dividend was paid or proposed for 2012 (2011 nil)

### **Post balance sheet events**

On 8 April 2013, the Board approved interim dividends in aggregate of \$372,776,521 on the preference shares, \$7,065,700 on the preferred ordinary shares and \$470,157,779 on the ordinary shares of the Company

### **Financial risk management**

Risk management is an inherent part of the Group's (of which the Company is a part) business activities and the Company has adopted the same risk management policies and procedures as the Group as a whole. The Group and the Company's risk management framework and governance structure are intended to provide comprehensive controls and ongoing management of its major risks. The Company exercises oversight through the Board of Directors and delegation from the Board to various sub-committees which are organised in line with the Group risk management policy

An overview of the key aspects of risk management and use of financial instruments is provided below. A more detailed description of the policies and processes adopted by all Group companies may be found within the Group annual report

The Company's risk policy framework includes risk policies which are Group wide but are supplemented, as required, by Company specific policies which are approved by the Board of the Company

# **J.P. MORGAN SECURITIES PLC**

## **Directors' report for the year ended 31 December 2012 (continued)**

### **Liquidity risk**

Liquidity risk is the potential inability to meet financial obligations as they become due

The Group's liquidity risk management is intended to ensure that the Group has the appropriate amount, composition and tenor of funding and liquidity in support of its assets. The primary objective of effective liquidity management is to ensure that the Group's core businesses are able to operate in support of client needs and meet contractual and contingent obligations through normal economic cycles as well as during market stress and maintain debt ratings that enable the Group to optimise its funding mix and liquidity sources while minimising costs.

The liquidity policy for the Company is reviewed and approved in line with the Group liquidity risk governance framework. Specific risk committees responsible for liquidity risk governance for the Company include the Group Asset Liability Committee (ALCO) at the Group level and ALCO. The regional ALCO reports on liquidity risk matters to the Company's Risk Committee and the Company's Board and is chaired by the European Treasurer.

Management considers the Company's liquidity position to be strong as of December 31, 2012, and believes that the Company's unsecured and secured funding capacity is sufficient to meet its on and off-balance sheet obligations.

The Company is locally subject to the PRA liquidity regulations. The key elements of the regulations are to ensure the Company has adequate liquidity and self-sufficiency of liquidity resources, and that it has systems and controls in place to monitor this. The Company's funding strategy is intended to ensure that it will have sufficient liquidity and diversity of funding sources necessary to enable it to meet actual and contingent liabilities during both normal and stress periods. The Company reports its liquidity position against 'Individual Liquidity Guidance' provided by the PRA for regulatory purposes. The Company has established a daily monitoring process to monitor liquidity adequacy and ensure compliance with regulatory requirements.

The Company will also be subject to the Liquidity Coverage Ratio ("LCR") and Net Stable Funding Ratio ("NSFR") requirements once the Basel III regulations are locally adopted. The Company is monitoring the LCR, based on its current understanding of the requirements on a regular basis.

A regular internal assessment of the liquidity risk management framework is performed which informs the Board of liquidity risks resulting from business activities in addition to the current and future funding needs of the Company.

Further details on liquidity risk are provided in note 33 to the financial statements.

### **Credit risk**

Credit risk is the risk of loss arising from a borrower, counterparty or obligor failing to meet its contractual obligations.

Credit risk is managed by the Group on a global as well as at a Company level. The Group has developed policies and practices, that the Company is subject to, that are designed to preserve the independence and integrity of the approval and decision making of extending credit. These policies are intended to ensure that credit risks are assessed accurately, approved properly, monitored regularly and managed actively at both the transaction and portfolio levels. In addition, the Company has its own credit policy which contains standards pertaining to governance, management of concentrations, credit risk limits, new business initiative approvals and credit risk reporting which is distributed to the Board of the Company.

The Company has a designated Chief Risk Officer (CRO) who is also a Board member of the Company. Credit Executives within this Line of Business approve extensions of credit for the Company and ultimately report to the Head of Wholesale Credit Risk. Each Line of Business within the Group has its own independent credit risk management function, reporting to the Group Chief Risk Officer. The Company is exposed to credit risk through lending and capital markets activities.

The Company is subject to the policies and practices developed by the Group. The policy framework establishes credit approval authorities, risk-rating methodologies, portfolio review parameters and guidelines for management of distressed exposures. In addition certain models, assumptions and inputs used in evaluating and monitoring credit risk are independently validated by support functions that are independent from the businesses.

To enable monitoring of credit risk, aggregate credit exposure, concentration levels and risk profile changes are reported to senior credit risk management and to the Board of the Company.

Further details on credit risk are provided in note 33 to the financial statements.

# **J.P. MORGAN SECURITIES PLC**

## **Directors' report for the year ended 31 December 2012 (continued)**

### **Market risk**

Market risk is the exposure to an adverse change in the market value of portfolios and financial instruments caused by a change in market prices. The primary categories of market risk factors are

- Interest Rates - Interest rate risk primarily results from exposure to changes in the level, slope and curvature of the yield curve, the volatility of interest rates, and mortgage prepayment rates,
- Foreign Exchange Rates - Foreign exchange rate risk results from exposure to changes in prices and the volatility of currency rates,
- Equity Prices - Equity price risk arises from exposure to changes in prices and the volatility of individual equities, equity baskets and equity indices,
- Credit Spreads - Credit spreads are the difference between yields on corporate debt subject to default risk and government bonds free of such risk, and
- Commodity Prices - Commodity price risk results from exposure to changes in prices and the volatility of commodities, such as natural gas, crude oil, petroleum products, precious and base metals and electricity

### *Market risk management*

The Company's Board is ultimately responsible for managing market risk. The Company has a designated Chief Risk Officer who has responsibilities in relation to market risk management. The Market Risk management function is an independent risk management function that works in close partnership with the lines of business to identify and monitor market risks throughout the Group and to define market risk policies and procedures. The Market Risk function reports to the Group's Chief Risk Officer.

The Market Risk management function seeks to control risk, facilitate efficient risk/return decisions, reduce volatility in operating performance and provide transparency into the Group and the Company's market risk profile for senior management and the Board of Directors. The Market Risk management function is responsible for the following functions:

- Establishing a market risk policy framework,
- Independent measurement, monitoring and control of line of business market risk,
- Definition, approval and monitoring of limits, and
- Performance of stress testing and qualitative risk assessments

Market risk is controlled primarily through a series of limits. Limits reflect the Company's risk appetite in the context of the market environment and business strategy. The Market risk management function regularly reviews and updates risk limits, as a minimum on a semi-annual basis. The Company's board and the Chief Risk Officer are responsible for reviewing and approving certain risk limits on an ongoing basis. Any one-off limit exceptions require approval by the Company's Chief Executive Officer (CEO) on behalf of the Company's Board. In setting limits, the Company takes into consideration factors such as senior management risk appetite, market volatility, product liquidity, accommodation of client business and management experience.

Non-statistical risk measures, VaR trends and limit excesses are reported daily to the lines of business and to senior management. Further, monthly market risk updates are provided to the monthly EMEA Investment Banking Risk Committee meetings and then Company's quarterly Board meetings.

Further details on market risk are provided in note 33 to the financial statements.

# **J.P. MORGAN SECURITIES PLC**

## **Directors' report for the year ended 31 December 2012 (continued)**

### **Operational risk**

Operational risk is the risk of loss resulting from inadequate or failed processes or systems, human factors or external events

Operational risk is inherent in each of the Group and the Company's businesses and support activities. Operational risk can manifest itself in various ways, including errors, fraudulent acts, business interruptions, inappropriate behaviour of employees, or vendors that do not perform in accordance with their arrangements. These events could result in financial losses, including litigation and regulatory fines, as well as other damage to the Group, including reputational harm.

To monitor and control operating risk, the Group maintains an overall framework including strong oversight and governance, comprehensive policies, consistent practices and enterprise risk management tools intended to provide a sound and well-controlled operational environment. The framework clarifies:

- Ownership of the risk by businesses and functional areas
- Monitoring and validation by business Control Officers
- Oversight by independent risk management
- Governance through business risk and control committees
- Independent review by Internal Audit

The objective is to keep operational risk at appropriate levels, in light of the Company's financial strength, the characteristics of its businesses, the market in which it operates, and the competitive and regulatory environment to which it is subject.

### **Directors**

The directors of the Company who served during the year and up to the date of signing the financial statements were as follows:

T D Hoppe	Chairman & Non Executive Director
D E Pinto	Chief Executive Officer
A J A Cox	Director & Chief Risk Officer
L P Jackson	Non Executive Director
M S Garvin	Director
T J O Throsby	Director
S D Moeller	Non Executive Director (Appointed 27 July 2012)
D A Wallestad	Director (appointed 11 March 2013)

### **Directors' interests**

None of the directors has any beneficial interest in the Company. The Company is a wholly owned subsidiary of a company incorporated in Great Britain. The ultimate holding company is a body corporate incorporated outside Great Britain. The directors are not required to notify the Company of any interests in shares of that or any other body incorporated outside Great Britain.



# **J.P. MORGAN SECURITIES PLC**

## **Directors' report for the year ended 31 December 2012 (continued)**

### **Statement of directors' responsibilities**

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations

Company Law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company as at the end of the financial year and of the profit or loss of the Company for the year.

In preparing those financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and estimates that are reasonable and prudent,
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

### **Disclosure of information to auditors**

Each person who is a director of the Company at the date of approval of this report confirms that

- so far as the director is aware, there is no relevant audit information (as defined in the Companies Act 2006) of which the Company's auditors are unaware, and
- each director has taken all the steps that he or she ought to have taken as a director to make himself or herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

### **Qualifying third party indemnity provisions**

An indemnity is provided to the directors of the Company under the By-laws of JPMorgan Chase & Co against liabilities and associated costs which they could incur in the course of their duties to the Company. The indemnity remains in force at the date of these financial statements and a copy of the By-laws of JPMorgan Chase & Co is kept at the registered office of the Company.

### **Corporate employee policy**

It is the policy of the Company to ensure equal opportunity for all persons without discrimination on the basis of race, colour, religion, sex, national origin, age, handicap, veteran status, marital status or sexual orientation. This policy of equal opportunity applies to all employment practices including, but not limited to recruiting, hiring, promotion, training and compensation.

Where existing employees become disabled, it is the Company policy wherever practicable to provide continuing employment under normal terms and conditions and to provide training and career development and promotion wherever appropriate.

With the aim of ensuring that views are taken into account when decisions are made, employee consultation has continued at all levels where it is likely to affect their interests. All employees are aware of the financial and economic performance of their business units and of the Company as a whole. Communication with all employees continues through the intra-net and other forums.

JPMorgan Chase Bank, N.A. operates an employee share scheme for all employees of JPMorgan Chase & Co. and its subsidiaries, to acquire a proprietary and vested interest in the growth and performance of the Group.

# **J.P. MORGAN SECURITIES PLC**

## **Directors' report for the year ended 31 December 2012 (continued)**

### **Creditors payment policy**

The Group policy is to pay invoices (including those in respect of the Company) upon presentation, except where other arrangements have been negotiated with the supplier. It is the policy of the Company to abide by the terms of payment, provided the supplier performs according to the terms of the contract.

### **Company secretary**

The secretaries of the Company who served during the year were as follows:

M F Vance

J P Morgan Secretaries (UK) Limited

### **Registered address**

The current registered address is as follows:

25 Bank Street

Canary Wharf

E14 5JP

England

The former registered address is as follows:

125 London Wall

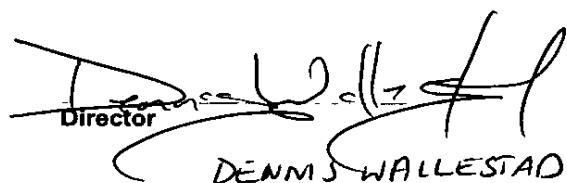
London

EC2Y 5AJ

### **Independent auditors**

A resolution to re-appoint PricewaterhouseCoopers LLP as auditors to the Company will be proposed at the Annual General Meeting.

### **By order of the Board**

  
Director  
DENNIS WALLESTAD

8/4/13

## **Independent auditors' report to the members of J.P. Morgan Securities plc (formerly known as J.P. Morgan Securities Ltd.)**

We have audited the financial statements of J P Morgan Securities plc for the year ended 31 December 2012 which comprise the profit and loss account, the statement of total recognised gains and losses, the balance sheet and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

### **Respective responsibilities of the directors and auditors**

As set out in the Statement of directors' responsibilities on page 7, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the Company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

### **Scope of the audit of the financial statements**

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates made by the directors, and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

### **Opinion on financial statements**

In our opinion the financial statements

- give a true and fair view of the state of the Company's affairs as at 31 December 2012 and of its profit for the year then ended,
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006.

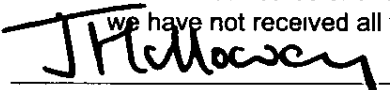
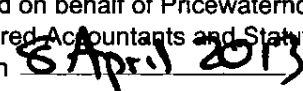
### **Opinion on other matter prescribed by the Companies Act 2006**

In our opinion the information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Matters on which we are required to report by exception**

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us, or
  - the financial statements are not in agreement with the accounting records and returns, or
  - certain disclosures of directors' remuneration specified by law are not made, or
- we have not received all the information and explanations we require for our audit.

  
Jonathan Holloway (Senior Statutory Auditor)  
For and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
London 

# J.P. MORGAN SECURITIES PLC

## Profit and loss account for the year ended 31 December 2012

		2012	2011
	Notes	\$'000	\$'000
Interest receivable and similar income	3	2,387,480	3,319,978
Interest payable and similar charges	4	(1,780,455)	(2,795,183)
<b>Net Interest Income</b>		<b>607,025</b>	<b>524,795</b>
Fees and commissions receivable		1,447,147	1,891,922
Trading profit		2,141,629	1,918,603
Other operating income		-	94,259
Foreign exchange translation gain/(loss)		30,381	(46,806)
Dividend income		900,000	-
<b>Total Operating Income</b>		<b>5,126,182</b>	<b>4,382,773</b>
Administrative expenses		(2,286,294)	(3,056,847)
Amortisation of intangible assets	17	(103,681)	(62,902)
Depreciation of tangible fixed assets	18	(316)	(837)
<b>Profit on ordinary activities before taxation</b>	6	<b>2,735,891</b>	<b>1,262,187</b>
Tax on profit on ordinary activities	7	(354,475)	(156,497)
<b>Profit for the financial year</b>		<b>2,381,416</b>	<b>1,105,690</b>

The profit for the year resulted from continuing operations

## Statement of total recognised gains and losses for the year ended 31 December 2012

		2012	2011
	Notes	\$'000	\$'000
Profit for the financial year		2,381,416	1,105,690
Actuarial gain/(loss) on pension schemes	31	(1,113)	(6,351)
Tax effect of movement in pension reserve	7	259	1,617
<b>Total recognised gains and losses for the year</b>		<b>2,380,562</b>	<b>1,100,956</b>

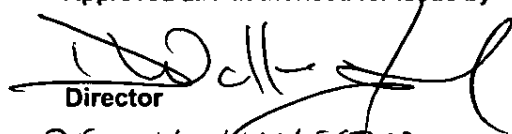
The notes on pages 12 - 52 form an integral part of these financial statements

# J.P. MORGAN SECURITIES PLC

## Balance sheet as at 31 December 2012

	Notes	2012 \$'000	2011 \$'000
<b>Assets</b>			
Cash and balances at central banks		35,156	28,175
Loans and advances to banks	8	15,468,005	19,632,290
Loans and advances to customers	9	1,099,819	160,177
Securities purchased under agreements to resell	10	108,043,553	100,094,752
Securities borrowed	11	19,020,210	23,092,244
Financial assets held for trading	12	156,174,562	136,856,987
Financial assets designated at fair value through profit or loss	13	16,222	16,523
Debtors	14	38,278,996	29,947,961
Other assets	15	851,300	871,652
Investments in Group undertakings	16	3,625,233	3,625,233
Intangible assets	17	1,817,461	1,921,142
Tangible fixed assets	18	1,463	1,733
<b>Total assets</b>		<b>344,431,980</b>	<b>316,248,869</b>
<b>Liabilities</b>			
Securities sold under agreements to repurchase	19	75,394,524	85,000,575
Securities loaned	20	20,448,502	19,565,299
Financial liabilities held for trading	21	101,795,834	98,297,855
Trade creditors	22	50,466,724	39,097,782
Amounts owed to Group undertakings		60,343,279	44,010,243
Other liabilities	22	8,100,556	3,891,984
<b>Total liabilities</b>		<b>316,549,419</b>	<b>289,863,738</b>
<b>Capital and reserves</b>			
Called-up share capital	23	15,505,750	15,505,750
Share premium account	25	4,646,581	4,646,581
Other reserves	25	1,647,100	1,631,086
Profit and loss account	25	6,083,130	4,601,714
<b>Total shareholders' funds</b>	26	<b>27,882,561</b>	<b>26,385,131</b>
<b>Total liabilities and shareholders' funds</b>		<b>344,431,980</b>	<b>316,248,869</b>

Approved and authorised for issue by the board of directors on 8 April 2013 and signed on its behalf by:

  
 Director  
 DENNIS KALLESTAD

The notes on pages 12 - 52 form an integral part of these financial statements

# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012**

### **1 Accounting policies**

#### **1.1 Accounting convention**

The financial statements have been prepared on the going concern basis under the historical cost convention, as modified by the revaluation of certain financial instruments, as explained in the accounting policies below. The financial statements have also been prepared in accordance with applicable accounting standards in the United Kingdom and the Companies Act 2006.

The principal accounting policies which have been consistently applied throughout the year are as set out below.

#### **1.2 Consolidation**

The Company is a wholly-owned subsidiary undertaking of J.P. Morgan Capital Holdings Limited, a company incorporated in Great Britain. The Company has elected not to prepare group financial statements in accordance with the dispensation set out in Section 400 of the Companies Act 2006.

#### **1.3 Cash flow statement**

The Company has taken advantage of the provisions of FRS 1, 'Cash Flow Statements (revised 1996)', which exempt the Company from preparation of a cash flow statement because it is at least a 90% owned subsidiary of JPMorgan Chase & Co (the Group), whose financial statements are publicly available.

#### **1.4 Related party transactions**

In accordance with the exemption afforded by FRS 8, 'Related Party Disclosures', certain details of transactions with parent and fellow subsidiary companies that are also wholly-owned within the Group, are not disclosed as they are included in the consolidated financial statements of the Group, which are publicly available.

#### **1.5 Income and expense recognition**

Interest receivable and payable are recognised on an effective interest rate basis.

Fees and commissions are recognised when the underlying contract becomes legally binding or at the agreed due date if later, unless a fee is received relating to work to be completed in the future in which case it is determined using the effective interest rate method. Effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount. Calculation of the effective interest rate takes into account fees receivable, that are an integral part of the instrument's yield, premiums or discounts on acquisition or issue, early redemption fees and transaction costs. All contractual terms of a financial instrument are considered when estimating future cash flows.

Profits and losses resulting from the purchase and sale of securities and the revaluation of financial instruments are recognised as trading gains or losses within operating income on a trade date basis.

Expenses are recognised when the underlying contract becomes legally binding or at the agreed due date if later.

#### **1.6 Dividend recognition**

Dividend income is recognised when the right to receive payment is established. Dividend distributions are recognised in the period in which they are declared and approved.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 1 Accounting policies (continued)

#### 1.7 Foreign currency translation

Monetary assets and liabilities in foreign currencies are translated into United States (US) Dollars at rates of exchange ruling on the balance sheet date. Income and expense items denominated in foreign currencies are translated into United States (US) Dollars at exchange rates prevailing at the date of the transactions. Any gains or losses arising on translation are taken directly to the profit and loss account.

Non-monetary items denominated in foreign currencies that are stated at historical cost are translated into United States (US) Dollars at the exchange rate ruling at the date of the transaction.

Non-monetary items denominated in foreign currencies that are stated at fair value are translated into US dollars at foreign exchange rates ruling at the dates when the fair values were determined. Translation differences arising on non-monetary items measured at fair value are recognised in profit and loss account except for differences arising on available-for-sale non-monetary financial assets, which are included in financial assets available-for-sale reserve.

The financial statements have been presented in United States (US) Dollars as the directors are of the opinion that this is the functional currency of the Company.

Year end exchange rate (USD/GBP)	1.61530	(2011: 1.53970)
Average rate for the year (USD/GBP)	1.59201	(2011: 1.60851)

#### 1.8 Tangible fixed assets and depreciation

Tangible fixed assets are stated at cost less accumulated depreciation. Tangible fixed assets are depreciated on a straight-line basis over their useful economic lives at the annual rates detailed below.

Leasehold improvements	10% or life of the lease if under 10 years
Computers and similar office equipment	33%
Fixtures and fittings	10%

The Company capitalises certain costs associated with the acquisition or development of software for internal use. Once the software is ready for its intended use, capitalised costs will be depreciated over an expected useful life of not more than five years.

The Company selects its depreciation rates carefully and reviews them regularly to take account of any changes in circumstances. When setting useful economic lives, the principal factors the Company takes into account are the expected rate of technological developments, expected market requirements for the equipment and the intensity at which the assets are expected to be used.

#### 1.9 Intangible fixed assets

Goodwill represents the excess of cost over the fair value of the identifiable net assets of businesses acquired. Goodwill is capitalised as an intangible fixed asset and amortised on a straight-line basis over the period that the directors estimate that the values of the underlying businesses acquired are expected to exceed the value of the underlying assets.

For the purpose of calculating goodwill, fair values of acquired assets and liabilities are determined by reference to market prices.

#### 1.10 Investments in Group undertakings

Investments in Group undertakings are stated at cost less provision for any impairment.

#### 1.11 Financial assets and financial liabilities

The Company classifies its financial assets and financial liabilities in the following categories: financial assets and financial liabilities held for trading, financial assets designated at fair value through profit or loss, loans and advances to customers and financial assets available-for-sale. The directors determine the classification of its investments at initial recognition.

# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012 (continued)**

### **1 Accounting policies (continued)**

The Company recognises a financial asset or a financial liability on its balance sheet when it becomes party to the contractual provisions of the instrument

#### **Financial assets and financial liabilities held for trading**

The Company considers a financial asset or financial liability as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term, or forms part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking or it is a derivative

Financial assets and financial liabilities held for trading comprise both debt and equity securities and derivatives. These instruments are either held for trading purposes or used for hedging certain assets, liabilities, positions, cash flows or anticipated transactions. Included in financial assets held for trading are the reported receivables (unrealised gains) and in financial liabilities held for trading the reported payables (unrealised losses) related to derivatives. The instruments are initially recognised at fair value in the balance sheet with transaction costs being recorded in profit or loss and any gains or losses are taken directly to the profit and loss account. Subsequently, they are measured at fair value.

Since both the debt and equity securities and the derivatives are managed on a unified basis as part of the trading strategy, which includes hedging relationships between cash securities and derivatives, it is not meaningful to show the gains and losses on the cash instruments separately from the gains and losses on the derivatives, the net gain or loss is reported as trading profits.

#### **Financial assets and financial liabilities designated at fair value through profit or loss**

Financial assets and financial liabilities that the Company designates on initial recognition as being at fair value through profit or loss are recognised at fair value, with transaction costs being recognised in profit or loss and are subsequently measured at fair value. Gains and losses on financial assets and financial liabilities that are designated at fair value through profit or loss are recognised in profit or loss as they arise. A financial instrument may only be designated at inception as held at fair value through profit or loss and cannot subsequently be changed.

Financial assets or financial liabilities are designated at fair value through profit or loss only if such designation (a) eliminates or significantly reduces a measurement or recognition inconsistency, or (b) applies to a group of financial assets, financial liabilities or both that the Company manages and evaluates on a fair value basis, or (c) relates to an instrument that contains an embedded derivative unless the embedded derivative does not significantly modify the cash flows required by the contract or when a similar hybrid instrument is considered that separation of the embedded derivative is prohibited.

#### **Financial assets available-for-sale**

Non-derivative financial assets intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices, are included within the financial assets available-for-sale category. These are initially recognised at fair value plus directly related transaction costs and subsequently measured at fair value. Any changes in fair values of such assets subsequent to initial recognition are reported as movements in financial assets available-for-sale reserve, net of deferred tax, until the investment is sold, collected or otherwise disposed of, or the financial assets are considered impaired, at which time the cumulative gain or loss previously reported in the statement of total recognised gains and losses is included in the profit and loss account.

#### **Loans and advances to customers**

Loans and advances to customers are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market except those that are classified as held for trading or designated fair value through profit or loss.

Loans and advances to customers are initially recognised at fair value including directly related incremental transaction costs. They are subsequently measured at amortised cost, using the effective interest method less any impairment losses. They are derecognised when the rights to receive cash flows have expired or the Company has transferred substantially all the risks and rewards of ownership.



# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012 (continued)**

### **1 Accounting policies (continued)**

#### **Derecognition of financial assets and financial liabilities**

Financial assets are derecognised when the right to receive cash flows from the assets has expired or when the Company has transferred its contractual right to receive the cash flows of the financial assets, and either substantially all the risks and rewards of ownership have been transferred, or all the risks and rewards have neither been retained nor transferred but control is not retained

Financial liabilities are derecognised when they are extinguished, that is when the obligation is discharged, cancelled or expires

#### **1 12 Fair value**

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction

Fair values are determined by reference to observable market prices where available and reliable. Fair values of financial assets and financial liabilities are based on quoted market prices or dealer price quotations for financial instruments traded in active markets. For all other financial instruments where representative market prices for an instrument are not available or are unreliable because of poor liquidity, the fair value is derived from prices for its components using appropriate pricing or valuation techniques that are based on independently sourced market parameters. Valuation techniques include net present value techniques, the discounted cash flow method, comparison to similar instruments for which market observable prices exist and valuation models

#### **1 13 Recognition of deferred day one profit and loss**

The Company enters into transactions where fair value is determined using valuation models for which not all inputs are market observable prices or rates. Such a financial instrument is initially recognised at the transaction price, although the value obtained from the relevant valuation model may differ. The difference between the transaction price and the model value, commonly referred to as 'day one profit and loss', is not recognised immediately in profit and loss

The timing of recognition of deferred day one profit and loss is determined for each class of financial asset and liability. It is either amortised over the life of the transaction, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement. The financial instrument is subsequently measured at fair value, adjusted for the deferred day one profit and loss. Subsequent changes in fair value are recognised immediately in the profit and loss account without reversal of deferred day one profit and losses

#### **1 14 Impairment**

Intangible assets, Tangible Fixed assets and Investments in Group undertakings

Fixed assets are reviewed for impairment if there are events or changes in circumstances that indicate that the carrying values may not be recoverable

The impairment review, which is conducted in accordance with the provisions of FRS 11 'Impairment of Fixed Assets and Goodwill', comprises a comparison of the carrying amount of the fixed asset or goodwill with its recoverable amount, which is the higher of net realisable value and value in use. The carrying value of fixed assets and goodwill is written down by the amount of any impairment. This write down is recognised in the period in which it occurs

# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012 (continued)**

### **1 Accounting policies (continued)**

#### **Financial assets**

The Company assesses at each balance sheet date whether there is any objective evidence that a financial asset or group of financial assets is impaired. A financial asset or portfolio of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset and that that loss event has an adverse impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

When a decline in the fair value of an financial asset available-for-sale has been recognised through the statement of total recognised gains and losses and there is objective evidence that the asset is impaired, the cumulative loss that had been recognised through the statement of total recognised gains and losses is removed from reserves and recognised in the profit or loss account.

Specific provisions are raised against specific loans and advances to customers when the Group considers that the credit worthiness of the borrower has deteriorated such that the recovery of the whole or part of an outstanding advance is in serious doubt.

The amount of the cumulative loss that is removed from reserves and recognised in profit or loss is the difference between the acquisition cost and current fair value, less any impairment loss on that financial asset previously recognised in the profit or loss account.

Impairment losses recognised in profit or loss for an investment in an equity instrument classified as available-for-sale are not reversed through the profit or loss account.

#### **1.15 Securities purchased under agreement to resell and securities sold under agreement to repurchase**

Securities purchased under agreements to resell the securities to the counterparty, and securities sold under agreements to repurchase, are treated as collateralised lending and borrowing transactions respectively. The collateral can be in the form of cash or securities. If the collateral is given in cash the transaction is recorded on the balance sheet within securities purchased/sold under agreement to resell/repurchase. If the collateral is received or given in the form of securities the transaction is recorded off balance sheet.

The difference between sales and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest rate method.

#### **1.16 Securities borrowed and securities loaned transactions**

Securities borrowed and securities loaned are recorded at the amount of cash collateral advanced or received. Securities borrowed and securities loaned transactions require the borrower to deposit cash, letters of credit or other collateral with the lender. Fees received or paid in connection with securities borrowed and lent are treated as interest income or interest expense and accrued over the life of the transaction using the effective interest rate method.

#### **1.17 Offsetting financial assets and liabilities**

Financial assets and financial liabilities are offset and the net amount reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012 (continued)**

### **1 Accounting policies (continued)**

#### **1 18 Deferred taxation**

Deferred tax is recognised in respect of all timing differences that have originated but not reversed at the balance sheet date, where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date

A net deferred tax asset is recognised as recoverable and therefore recognised only when, on the basis of all available evidence, it can be regarded as more likely than not that there will be suitable taxable profits against which to recover carried forward tax losses and from which the future reversal of underlying timing differences can be deducted

Deferred tax is measured at the average tax rates that are expected to apply in the periods in which the timing differences are expected to reverse, based on tax rates and laws that have been enacted or substantively enacted by the balance sheet date. Deferred tax is measured on an undiscounted basis

#### **1 19 Provisions for liabilities and charges**

Provisions are recognised when the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made

#### **1.20 Pensions and other post-retirement benefits**

The Company operates defined contribution schemes for its employees. The Company also operates defined benefit and defined contribution schemes for employees in the European branches

##### **Defined contribution scheme**

Obligations for contributions to defined contribution pension plans are recognised as an expense and charged to the profit and loss account on an accrual basis

##### **Defined benefit scheme**

For defined benefit schemes, the service cost of providing retirement benefits to employees during the year is charged to the profit and loss account in accordance with FRS 17, 'Retirement benefits'. The pension costs are assessed based on the advice of qualified actuaries so as to recognise the full cost of provision of contracted pension benefits over the period of employees' service lives

The defined benefit schemes' liabilities are measured on an actuarial basis and scheme assets measured at their fair values separately for each plan. Any surplus or deficit of scheme assets over liabilities is recognised on the balance sheet as an asset (surplus) or liability (deficit). The current service cost and any past service costs together with the expected return on scheme assets less the unwinding of discount on the scheme liabilities is charged to the profit and loss account

#### **1.21 Share-based awards**

Share-based awards may be made to employees of the company under the Group's incentive awards schemes. In accordance with FRS 20, the fair value of any such shares, rights to shares or share options is measured when the conditional award is made. This value is recognised as the compensation expense to the Company over the period to which the performance criteria relate together with employer's social security expenses or other payroll taxes. All of the awards granted are equity settled. The Company estimates the level of forfeitures and applies this forfeiture rate at the grant date

Additionally, FRS 20 requires the consideration of the conditions that must be satisfied before an employee becomes entitled to equity instruments under the Group's incentive programs. The Group's Retirement Eligibility rules for restricted stock awarded as part of incentive programs under FRS 20 require the acceleration of the amortisation of the award such that the award is fully expensed at the time the retirement eligibility comes into force

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 2. Segmental analysis

In the opinion of the directors, the Company conducts only one class of business, the provision of international investment banking services. The Company operates six branches outside of the UK, but these do not generate material revenues. Therefore, any segmental analysis of the Company's revenues and assets is not considered necessary.

### 3. Interest receivable and similar income

	2012	2011
	\$'000	\$'000
Financial assets held for trading	1,725,787	2,371,966
Securities purchased under agreements to resell	496,098	782,576
Securities borrowed	46,815	59,928
Other	118,780	105,508
	2,387,480	3,319,978

Interest receivable and similar income includes the following amounts receivable from other Group undertakings:

	2012	2011
	\$'000	\$'000
Securities purchased under agreements to resell	135,750	189,897
Securities borrowed	46,705	41,252
Other	41,258	42,867
	223,713	274,016

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 4. Interest payable and similar charges

	2012	2011
	\$'000	\$'000
Financial liabilities held for trading	994,768	1,265,680
Securities sold under agreements to repurchase	281,079	764,467
Securities loaned	172,814	203,857
Other	331,794	561,179
	1,780,455	2,795,183

Interest payable and similar charges includes the following amounts payable to other Group undertakings

	2012	2011
	\$'000	\$'000
Securities sold under agreements to repurchase	140,611	516,389
Securities loaned	1,696	4,569
Other	274,502	444,097
	416,809	965,055

### 5 Directors' emoluments

	2012	2011
	\$'000	\$'000
Emoluments	1,547	2,136
Total contributions to a defined contribution plan	11	30
Compensation to non-executive directors	314	275
Number of directors who exercised share options	-	3
Number of directors with shares received or receivable under LTIPs	4	10
Number of directors to whom defined contribution pension rights accrued	4	9

In accordance with the Companies Act 2006, the directors' emoluments above represent the proportion paid or payable in respect of qualifying services only. Directors also received emoluments for non-qualifying services, which are not required to be disclosed.

### Highest paid director

The emoluments (excluding amounts paid or due to directors under long term incentive plans (LTIP) and the value of share options granted or exercised by directors) of the highest paid director were \$1,074,091 (2011: \$896,168).

The contribution to the defined contribution scheme for the highest paid director during the year was \$3,235 (2011: \$2,679). The highest paid director did not exercise share options during 2012 (2011: nil). Shares were received or are receivable by the highest paid director under long term incentive plans during 2012 and 2011.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 6 Profit on ordinary activities before taxation

	2012	2011
	\$'000	\$'000
Profit on ordinary activities before taxation is stated after charging		
Amortisation of intangible assets	103,681	62,902
Depreciation of tangible fixed assets	316	837
Auditors' remuneration for the audit of the Company's annual financial statements	2,603	2,310
Services relating to tax	-	86
Other services	-	438
Wages and salaries	655,734	428,900
Social security costs	99,153	46,755
Other pension costs	38,164	26,150
Share based awards	168,195	106,309
Intercompany fee	-	441,094

The average number of persons providing services to the Company during the year was 1,509 (2011: 1,602). From 1 June 2011 to 31 December 2011, the Company was a member of a Group undertaking, J P Morgan Services LLP ("LLP" or "the LLP"), which operated an outsourcing arrangement that had an impact on the way staff were employed to support the Company's businesses.

The average number of staff employed by the European branches during the year was 130 (2011: 121).

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 7. Tax on profit on ordinary activities

	2012	2011
	\$'000	\$'000
<b>(a) Analysis of tax charge for the year</b>		
<b>Current taxation</b>		
UK Corporation tax on profit for the year	299,620	184,078
Overseas taxation	207,432	164,432
Less Double tax relief	(184,457)	(164,432)
Adjustments in respect of previous years	(11,282)	(161,952)
<b>Current tax charge for the year</b>	<b>311,313</b>	<b>22,126</b>
Deferred tax charge for the year	38,284	120,207
Adjustments in respect of previous years	3,366	705
Effect of rate change on opening balance	1,512	13,459
<b>Total tax charge for the year</b>	<b>354,475</b>	<b>156,497</b>

### (b) Factors affecting the current tax charge for the year

The tax charge for the year differs from the standard rate of corporation tax in the UK (24%), reduced from 26% effective from 1 April 2012

The differences are explained below

	2012	2011
	\$'000	\$'000
Profit on ordinary activities before taxation	2,735,891	1,262,187
Profit on ordinary activities before taxation multiplied by standard rate of corporation tax in UK (24.5%)	670,217	334,393
Effects of		
Non-deductible expenses	36,733	21,213
Capital allowances in excess of depreciation	(1,061)	(1,439)
Emoluments deferral	31,528	11,956
Group relief claimed for nil consideration	(139,635)	(89,825)
Non-taxable dividend income	(220,500)	-
Adjustments in respect of previous years	(11,282)	(161,952)
Other adjustment	(849)	(919)
Other non-taxable income	(16,625)	-
Foreign taxation suffered	22,975	-
Brought forward losses utilised	(60,189)	(91,301)
<b>Current tax charge for the year</b>	<b>311,313</b>	<b>22,126</b>

### (c) Deferred taxation

Deferred taxation brought forward	75,599	208,352
Charge to the profit and loss account for the current year	(39,797)	(133,665)
Charge to the profit and loss account in respect of previous years	(3,366)	(705)
(Charge)/credit to the statement of total recognised gains and losses	259	1,617
<b>Deferred taxation carried forward</b>	<b>32,695</b>	<b>75,599</b>
Deferred taxation asset relates to		
Depreciation in excess of capital allowances	4,420	5,894
Deferral of emoluments	25,857	19,263
Trade losses	-	46,940
Other adjustment	2,418	3,502
	<b>32,695</b>	<b>75,599</b>

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 8. Loans and advances to banks

Loans and advances to banks includes bank balances held with Group undertakings. In the prior year, this balance was disclosed as 'Cash at bank and in hand'. Also included is \$10.9 billion (2011: \$12.2 billion) which relates to client money segregated in accordance with the Client Asset rules of the PRA. The corresponding liability is included in trade creditors. In the prior year this amount was disclosed in cash at bank and in hand.

### 9. Loans and advances to customers

	2012	2011
	\$'000	\$'000
Loans and advances to customers	1,099,819	160,177

#### Disclosure of loans and advances to customers maturity profile

	2012	2011
	\$'000	\$'000
Remaining maturity		
5 years or more	58,262	-
5 years or less but over 1 year	766,241	160,177
1 year or less but over 3 months	42,970	-
3 months or less	232,346	-
	1,099,819	160,177

There were no past due loans and advances to customers as at 31 December 2012 (2011: Nil)



# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 10. Securities purchased under agreements to resell

	2012	2011
	\$'000	\$'000
Securities purchased under agreements to resell	108,043,553	100,094,752

Included within securities purchased under agreements to resell, are the following balances with other Group undertakings

	2012	2011
	\$'000	\$'000
Securities purchased under agreements to resell	40,481,530	35,952,424

The fair value of securities purchased under agreements to resell and securities borrowed accepted as collateral that the Company is permitted to sell or re-pledge in the absence of default is \$160,392 million (2011 \$107,230 million) These transactions are conducted under terms that are customary to standard lending activities

### 11 Securities borrowed

	2012	2011
	\$'000	\$'000
Securities borrowed	19,020,210	23,092,244

Included within securities borrowed, are the following balances with other Group undertakings

	2012	2011
	\$'000	\$'000
Securities borrowed	6,932,518	4,965,483

The fair value of securities purchased under resale agreements and securities borrowed accepted as collateral that the Company is permitted to sell or re-pledge in the absence of default is \$160,392 million (2011 \$107,230 million) These transactions are conducted under terms that are customary to standard lending activities

### 12. Financial assets held for trading

	2012	2011
	\$'000	\$'000
At 1 January	136,856,987	145,217,089
Movements during the year	19,317,575	(8,360,102)
At 31 December	156,174,562	136,856,987

Included within financial assets held for trading, are the following balances with other Group undertakings

	2012	2011
	\$'000	\$'000
Financial assets held for trading	23,827,537	27,726,404

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 13. Financial assets designated at fair value through profit or loss

	2012	2011
	\$'000	\$'000
At 1 January	16,523	16,405
Movements during the year	(301)	118
At 31 December	16,222	16,523
Equity shares and other variable yield securities		
Unlisted	16,222	16,523
	16,222	16,523

### 14. Debtors

	2012	2011
	\$'000	\$'000
Trade debtors	24,822,581	15,084,231
Amounts owed by Group undertakings	8,564,744	8,302,531
Other debtors	4,891,671	6,561,199
	38,278,996	29,947,961

Trade debtors mainly consists of unsettled trades

Other debtors includes \$3.7 billion of cash collateral on derivatives

### 15. Other assets

	2012	2011
	\$'000	\$'000
Deferred taxation	32,695	75,599
Other taxation and social security	283,931	247,410
Prepayments and accrued income	534,674	548,643
	851,300	871,652

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 16. Investments in Group undertakings

	2012	2011
	\$'000	\$'000
<b>Investments in group undertakings at cost</b>		
At 1 January	3,625,233	302,250
Additions	-	5,280,383
Distribution of net assets of the subsidiary to the company	-	(1,957,400)
At 31 December	3,625,233	3,625,233

The above investments are shown at cost less any provision for impairment

In the opinion of the directors, the value of the Company's investment in each subsidiary undertaking is not less than the amount at which it is stated in the balance sheet

The only wholly owned (100% shares held) principal subsidiary of the Company is J P Morgan Europe Limited (JP MEL) which is incorporated in the United Kingdom, regulated by the PRA and is primarily involved in banking activity

The key holdings of the Company are as follows

Name	Country of incorporation	Principal activity	Proportion of ordinary shares held %
J P Morgan Chase Finance Limited	United Kingdom	Holding company	35 00
J P Morgan Europe Limited	United Kingdom	Banking	100 00
Claris Limited*	Channel Islands	Notes issuer	0 00
Gonzaga Finance SRL*	Italy	Notes issuer	0 00
Earls Eight Ltd*	Cayman Islands	Notes issuer	0 00
Cheyne Capital Guaranteed Credit*	Luxembourg	Notes issuer	0 00
Mizuho Trust 2010*	Japan	Notes issuer	0 00
Mizuho Trust TBI*	Japan	Notes issuer	0 00
Arosa Funding Limited Series 2006-7*	Channel Islands	Notes issuer	0 00
Morgan Stanley Aces SPC Series 2006-35A*	Cayman Islands	Notes issuer	0 00
Parcs Master Trust Jayhawks (Fixed Recovery) 2006-	United States	Notes issuer	0 00
Starts (Ireland) PLC Series 2006-21*	Ireland	Notes issuer	0 00
Starts Cayman Limited Series 2008-4*	Cayman Islands	Notes issuer	0 00
-			0 00

\* The above entities are special purpose vehicles which meet the definition (per section 1162 of the Companies Act 2006) of a subsidiary undertaking

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 17. Intangible assets

	<b>\$'000</b>
<b>Cost</b>	
At 1 January 2012	2,044,770
Additions	-
At 31 December 2012	2,044,770
<b>Accumulated Amortisation</b>	
At 1 January 2012	(123,628)
Charged during the year	(103,681)
At 31 December 2012	(227,309)
<b>Net book value</b>	
At 31 December 2011	1,921,142
At 31 December 2012	1,817,461

In May 2011, the Company recognised goodwill amounting to US\$1,957,400,000 in relation to the estimated levels of future profits to be generated by the businesses that were transferred to the Company from J P Morgan LES Limited as part of a transaction

A portion of the intangible assets relates to the purchase of the cash equities and equity derivatives businesses from Robert Fleming & Co Limited on 1 February 2001 for \$82.4 million. The full purchase consideration was in the form of cash and relates entirely to purchased goodwill. This represents the intrinsic value of the businesses transferred, based upon the estimated levels of future profits to be generated by the businesses.

The goodwill arising on these acquisitions is being amortised on a straight line basis over the period that the directors estimate that the value of the underlying businesses acquired are expected to exceed the value of the underlying assets. For the goodwill arising on the acquisition of business from J P Morgan LES Limited and Robert Fleming & Co Limited, this period is deemed to be 20 years and 14.5 years respectively. In the opinion of the directors, the value of the Company's goodwill is not less than the amount at which it is stated on the balance sheet.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 18. Tangible fixed assets

	Leasehold improvements, fixtures and fittings and office equipment
	\$'000
<b>Cost:</b>	
At 1 January 2012	9,954
Additions	501
Disposals	(574)
At 31 December 2012	9,881
<b>Accumulated depreciation:</b>	
At 1 January 2012	(8,221)
Charged during the year	(316)
Disposals	119
At 31 December 2012	(8,418)
<b>Net book value</b>	
At 31 December 2011	1,733
At 31 December 2012	1,463

### 19. Securities sold under agreements to repurchase

	2012	2011
	\$'000	\$'000
Securities sold under agreements to repurchase	75,394,524	85,000,575

Included within securities sold under agreements to repurchase are the following balances with other Group undertakings

	2012	2011
	\$'000	\$'000
Securities sold under agreements to repurchase	28,628,251	58,445,417

The fair value of securities sold under agreements to repurchase and securities loaned pledged to secure liabilities is \$142,880 million (2011 \$40,284 million). These transactions are conducted under terms that are customary to standard borrowing activities.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 20. Securities loaned

	2012	2011
	\$'000	\$'000
Securities loaned	20,448,502	19,565,299

Included within securities loaned are the following balances with other Group undertakings

	2012	2011
	\$'000	\$'000
Securities loaned	14,009,830	17,539,428

The fair value of securities sold under repurchase agreements and securities loaned pledged to secure liabilities is \$142,880 million (2011 \$40,284 million) These transactions are conducted under terms that are customary to standard borrowing activities

### 21. Financial liabilities held for trading

	2012	2011
	\$'000	\$'000
At 1 January	98,297,855	91,422,041
Movements during the year	3,497,979	6,875,814
At 31 December	101,795,834	98,297,855

Included within financial liabilities held for trading, are the following balances with other Group undertakings

	2012	2011
	\$'000	\$'000
Financial liabilities held for trading	53,166,142	47,990,959

### 22 Trade creditors and other liabilities

	2012	2011
	\$'000	\$'000
Trade creditors	50,466,724	39,097,782
Accruals and deferred income	728,396	466,713
Other liabilities	7,372,160	3,425,271
Total other liabilities	8,100,556	3,891,984
Total trade creditors and other liabilities	58,567,280	42,989,766

Trade creditors predominantly consists of unsettled trades and brokerage fees payable

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 23. Called-up share capital

	2012	2011
	\$'000	\$'000
<b>Issued and fully paid share capital</b>		
<b>At 1 January</b>		
835,242 ordinary shares (2011 571,603) of \$10,000 each	8,352,420	5,716,030
34,648 (2011 34,648) preferred ordinary shares of \$10,000 each	346,480	346,480
680,685 (2011 480,685) preference shares of \$10,000 each	6,806,850	4,806,850
<b>Movements during the year</b>		
Nil ordinary shares issued (2011 263,639) of \$10,000 each	-	2,636,390
Nil preference shares issued (2011 200,000) of \$10,000 each	-	2,000,000
Subdivision of 10 ordinary shares (2011 nil) of \$10,000 each	(100)	
50,000 ordinary shares issued (2011 nil) of £1 24 each	100	
	-	4,636,390
<b>At 31 December</b>		
835,232 ordinary shares (2011 835,242) of \$10,000 each	8,352,320	8,352,420
50,000 ordinary shares (2011 nil) of £1 24 each	100	-
34,648 (2011 34,648) preferred ordinary shares of \$10,000 each	346,480	346,480
680,685 (2011 680,685) preference shares of \$10,000 each	6,806,850	6,806,850
	15,505,750	15,505,750

On 28 May 2012, the Company sub-divided and reclassified 10 ordinary shares of \$10,000 each in the issued capital held by J P Morgan Chase International Holdings into 50,000 ordinary shares of \$2 each. The Company then redenominated these converted shares into 50,000 ordinary shares of £1 24 each. These steps were made in order to introduce the authorised minimum amount of £50,000 share capital denominated in sterling as required by sections 542(3) and 765 of the Companies Act 2006 prior to the re-registration of the Company as a public limited company.

	2012	2011
	\$'000	\$'000
<b>Preference shares in issue</b>		
5 year floating rate of \$10,000 each *	2,650,000	2,650,000
10 year fixed rate of \$10,000 each *	2,156,850	2,156,850
20 year fixed rate of \$10,000 each *	2,000,000	2,000,000
	6,806,850	6,806,850

\* Additional disclosure on the terms per tranche of preference shares is provided under Note 24 - Dividends

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 24. Dividends

Dividends of \$569,921,615 were paid on the preference shares (2011 Nil) and \$12,605,911 on the preferred ordinary shares of the Company (2011 Nil) in 2012. An interim dividend of \$317,472,474 (2011 Nil) was paid on the ordinary shares of the Company for 2012. No final dividend was paid or proposed for 2012 (2011 Nil).

The dividend rate on the preferred ordinary shares is 0.9% over 12 month US\$ LIBOR on the nominal amount, payable in priority to any dividend payable on ordinary shares, with no right to accumulation in the event of a deficiency of profits nor any further entitlement to participation in the profits of the Company. Subject to approval from the PRA, the Company may redeem at its option any preferred ordinary share at par, together with accrued dividend due, at any time after 26 March 2007. In the event of a winding-up the preferred ordinary shareholders shall be repaid both capital and any accrued dividend due in priority to any payment to the ordinary shareholders. The preferred ordinary shares carry no voting rights at a general meeting of the Company. The ordinary shares carrying 100% of the voting rights.

The dividend rate on the 5 year floating rate preference shares is 0.9% over 12 month US\$ LIBOR on the nominal amount, payable in priority to any dividend payable on ordinary shares, but *pari passu* to any payment to the holders of the preferred ordinary shares or any other preference shares, with no right to accumulation in the event of a deficiency of profits nor any further entitlement to participation in the profits of the Company. Subject to approval from the PRA, the Company may redeem at its option any 5 year floating rate preference share at par, together with accrued dividend due, at any time after 9 June 2009. In the event of a winding-up the preference shareholders shall be repaid both capital and any accrued dividend due in priority to any payment to the ordinary shareholders but *pari passu* to any payment to the holders of preferred ordinary shares or other preference shares. The 5 year floating rate preference shares carry no voting rights at general meetings.

The dividend rate on the 10 year fixed rate preference shares is a fixed rate of 2.75% and 2.85%, per series, above the Ten-year U.S. Treasury Rate as at the date of issue, payable in priority to any dividend payable on the ordinary shares, but *pari passu* to any payment to the holders of the preferred ordinary shares or any other preference shares, with no right to accumulation in the event of a deficiency of profits nor any further entitlement to participation in the profits of the Company. Subject to approval from the PRA, the Company may redeem any series of the 10 year fixed rate preference shares at par at any time after the 10th anniversary of the date of issue of that series provided that the Company may only redeem exactly twenty per cent of the total number of preference shares issued in that series at par. In the event of a winding-up, the 10 year fixed rate preference shareholder shall be repaid both capital and any accrued dividend due in priority to any payment to the ordinary shareholder but *pari passu* to any payment to the holders of the preferred ordinary shares and any other preference shares. The preference shares carry no voting rights at general meetings.

The dividend rate on the 20 year fixed rate preference shares is a fixed rate of 8%, payable in priority to any payment of dividend or other distribution to the holders of any junior obligations, but *pari passu* to any payment of dividend or other distribution to the holders of any parity obligations, with no right to accumulation in the event of a deficiency of profits nor any further entitlement to participation in the profits of the Company. Subject to approval from the PRA, the Company may redeem at its option any 20 year fixed rate preference share at par, together with accrued dividend due, at any time after 20 years and one month of the date of issue of that series. In the event of a winding-up, the 20 year fixed rate preference shareholder shall be repaid both capital and any accrued dividend due in priority to any payment to the holders of ordinary shares and any other securities issued by the company, but *pari passu* to any payment to the holders of any other series of preference shares issued by the company. The preference shares carry no voting rights at general meetings.

### 25. Reconciliation of movement in reserves

	Capital contribution reserve	Pension reserve	Other reserves	Share premium account	Profit and loss account
	\$'000	\$'000	\$'000	\$'000	\$'000
At 1 January 2012	1,583,800	(3,817)	51,103	4,646,581	4,601,714
Profit for the financial year	-	-	-	-	2,381,416
Dividends paid	-	-	-	-	(900,000)
Movement in other reserves	-	-	16,868	-	-
Movement in pension reserve	-	(1,113)	-	-	-
Tax effect on movement in pension reserve	-	259	-	-	-
At 31 December 2012	1,583,800	(4,671)	67,971	4,646,581	6,083,130

The movement in other reserves is due to share based payment awards granted to employees by the Group.



# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 26 Reconciliation of movements in shareholder's funds

	2012	2011
	\$'000	\$'000
Opening shareholder's funds	26,385,131	15,952,688
Increase in share capital	-	4,636,390
Increase in share premium	-	4,643,993
Movement in other reserves	16,868	51,103
Profit for the financial year	2,381,416	1,105,690
Dividends paid	(900,000)	-
Movement in pension reserve	(1,113)	(6,350)
Tax effect on movement in pension reserve	259	1,617
Closing shareholder's funds	27,882,561	26,385,131

### 27. Commitments

	2012	2011
	\$'000	\$'000
Lending commitments	1,663,246	-

Included within lending commitments are commitments to other group undertakings of \$nil (2011 \$nil)

# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012 (continued)**

### **28. Registered charges**

The following charges have been registered with the Registrar of Companies and were outstanding at 31 December 2012

Amounts due, or which may become due, under the Company's facility agreement with National Westminster Bank plc are secured by a charge over the benefits arising from the Company's European Settlements Office membership agreement with the Governor and Company of the Bank of England

Amounts due or to become due from the Company to the Emerging Markets Clearing Corporation are secured by a charge over all assets and property placed by the Company in the possession of the Emerging Markets Clearing Corporation. This includes all securities and cash on deposit with the Emerging Markets Clearing Corporation

Amounts due or to become due from the Company to Deutsche Bank under the terms of Master Novation Agreement, creating or evidencing the charge, are secured by a charge over all rights, title and interest to and in all deposited instruments

Amounts due or to become due from the Company to Barclays Bank Plc under the terms of the Security Deed, creating or evidencing the charge, are secured by a charge over all rights in respect of the Setter Swap Agreement

Amounts due or to become due from the Company to BNY Corporate Trustee Services & EBS Mortgage Finance under the terms of the Security Deed are secured by a fixed charge over the charged property and all its right, title and interest in the charged account (5304199780)

Amounts due or to become due from the Company to The Bank Of New York Mellon under the terms of the Debenture Agreement are secured by a floating charge on all securities, deposits and any other assets in respect of a designated account

Amounts due or to become due from the Company to Nasdaq OMX Stockholm AB under the terms of the Security Deed are secured by a fixed charge over all rights, title and interest in and to all cash collateral and all money, now or in the future, standing to the credit of each cash collateral account

Amounts due or to become due from the Company to J P Morgan Structured Products B V under the terms of the Credit Support Deed are secured by a charge over all posted collateral

Amounts due or to become due from the Company to J P Morgan Structured Products B V under the terms of the Credit Support Deed are secured by a first fixed legal mortgage over all posted collateral other than posted collateral in the form of cash

Amounts due or to become due from the Company to JPMorgan Chase Bank, N A (The Security Trustee) under the terms of the Security Agreement are secured by collateral securities, related rights and collateral cash

Amounts due or to become due from the Company to JPMorgan Chase Bank, N A under the terms of the Pledge Agreement are secured by a charge over the pledged property in relation to any Korean Security

Amounts due or to become due from the Company to JPMorgan Chase Bank, N A (The Collateral Agent) under the terms of the Pledge Agreement are secured by a charge over posted collateral

Amounts due or to become due from the Company to Nasdaq OMX Stockholm AB under the terms of the GBP Collateral Security Deed are secured by a fixed charge over all rights, title and interest in and to all cash collateral and all money now or in the future standing to the credit of each cash collateral account

Amounts due or to become due from the Company to J P Morgan Limited under the terms of the Charge and Security Trust Deed are secured by way of a first fixed charge over all right, title and interest from time to time in the financial assets

Amounts due or to become due from the Company to J P Morgan Limited are secured by a charge over accounts with full title guarantee over all rights, title and interest in the accounts

Amounts due or to become due from the Company to JPMorgan Chase Bank N A , as security trustee under the terms of the supplemental deed are secured by way of a first fixed charge over all present and future claims or rights to or in respect of all the securities from time to time recorded in and represented by the additional non-English securities collateral accounts

Amounts due or to become due from the Company to JPMorgan Chase Bank, N A as security trustee under the terms of the Supplemental Deed are secured by way of a fixed charge over all present and future claims or rights to, or in respect of all the securities from time to time, represented by the additional non-English securities collateral accounts

Amount due or to become due from the Company to Morgan Guaranty Trust Company of New York under the terms of the Collateral Agreement are secured by all collateral including in particular cash and securities clearance accounts opened in connection with the Euroclear system by the Brussels office of Morgan Guaranty on its books in the name of the Company

Amount due or to become due from the Company to Morgan Guaranty Trust Company of New York under the terms of the Collateral Agreement Governing Secured Borrowings by Groups of Participants in the Euroclear System are secured by all collateral including in particular, cash and securities clearance accounts opened in connection with the Euroclear system by the Brussels office of Morgan Guaranty on its books in the name of the Company

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 29. Assets and liabilities in foreign currencies

	2012	2011
	\$'000	\$'000
<b>Assets</b>		
United States (US) dollars	151,411,657	121,546,758
Euro	112,599,978	135,880,249
Great British pounds	53,840,941	39,303,778
Currencies other than above	26,579,404	19,518,084
<b>Total assets</b>	<b>344,431,980</b>	<b>316,248,869</b>
<b>Liabilities</b>		
United States (US) dollars	123,639,341	94,994,827
Euro	112,641,197	135,887,503
Great British pounds	53,862,385	39,426,948
Currencies other than above	26,406,496	19,554,460
<b>Total liabilities</b>	<b>316,549,419</b>	<b>289,863,738</b>

Due to off-balance sheet items, the above should not be considered to demonstrate the entity's exposure to foreign exchange risk

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 30 Assets and liabilities measured at fair value

	Level 1 Quoted market prices in active markets \$'000	Level 2 Internal models with significant observable market parameters \$'000	Level 3 Internal models with significant unobservable market parameters \$'000	Total carrying value \$'000
At 31 December 2012				
Financial assets				
Debt and equity instruments	52,021,571	38,236,882	3,161,337	93,419,790
Derivative receivables	-	56,357,909	6,413,085	62,770,994
<b>Total financial assets</b>	<b>52,021,571</b>	<b>94,594,791</b>	<b>9,574,422</b>	<b>156,190,784</b>
Financial liabilities				
Debt and equity instruments	12,364,870	8,666,833	139,454	21,171,157
Derivative payables	-	59,645,494	5,302,183	64,947,677
Other financial liabilities	-	12,745,006	2,931,994	15,677,000
<b>Total financial liabilities</b>	<b>12,364,870</b>	<b>81,057,333</b>	<b>8,373,631</b>	<b>101,795,834</b>

In determining the fair value of a derivative portfolio, Credit valuation adjustments (CVA) are necessary when the model derived fair value is not indicative of the credit quality of the counterparty. Similarly, Debit valuation adjustments (DVA) are necessary to reflect the credit quality of the company in the valuation of liabilities measured at fair value. The Company is not generally exposed to either counterparty or its own credit risk on its derivative portfolio as J P Morgan Chase Bank, a group undertaking, provides counterparty credit default insurance to the Company on its derivatives portfolio in return for an initial fee paid for each new transaction at its inception. Accordingly, the Company does not recognise Credit or Debit valuation adjustments.

	Level 1 Quoted market prices in active markets \$'000	Level 2 Internal models with significant observable market parameters \$'000	Level 3 Internal models with significant unobservable market parameters \$'000	Total carrying value \$'000
At 31 December 2011				
Financial assets				
Debt and equity instruments	40,158,533	30,786,722	3,053,379	73,998,634
Derivative receivables	-	58,571,890	4,302,986	62,874,876
<b>Total financial assets</b>	<b>40,158,533</b>	<b>89,358,612</b>	<b>7,356,365</b>	<b>136,873,510</b>
Financial liabilities				
Debt and equity instruments	10,942,574	10,010,859	54,225	21,007,658
Derivative payables*	-	58,569,407	6,110,665	64,680,072
Other financial liabilities*	-	12,047,835	562,290	12,610,125
<b>Total financial liabilities</b>	<b>10,942,574</b>	<b>80,628,101</b>	<b>6,727,180</b>	<b>98,297,855</b>

\* An amount of \$12,610,125,000 has been reclassified from derivatives payable to 'other financial liabilities' in respect of the balances as of 31 December 2011 as this reflects the substance of the financial instruments more appropriately. The corresponding amount for 31 December 2012 amounted to \$15,677,000,000.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 30. Assets and liabilities measured at fair value (continued)

#### Movement in assets and liabilities in Level 3 during year ended 31 December 2012

	Debt and equity instruments	Derivative receivables	Total financial assets
	\$'000	\$'000	\$'000
At 1 January 2012	3,053,379	4,302,986	7,356,365
Total gains/(loss) recognised in profit or loss	200,439	(852,059)	(651,620)
Purchases	6,679,334	6,810,006	13,489,340
Sales	(6,650,690)	(4,068,240)	(10,718,930)
Issuances	(42,649)	-	(42,649)
Settlements	(47,794)	(85,085)	(132,879)
Transfers in to Level 3	133,266	404,434	537,700
Transfers out of Level 3	(163,948)	(98,957)	(262,905)
<b>At 31 December 2012</b>	<b>3,161,337</b>	<b>6,413,085</b>	<b>9,574,422</b>

	Debt and equity instruments	Derivative payables	Other financial liabilities	Total financial liabilities
	\$'000	\$'000	\$'000	\$'000
At 1 January 2012	54,225	6,110,665	562,290	6,727,180
Total (gains)/loss recognised in profit or loss	(2,151)	(421,174)	22,212	(401,113)
Purchases	(2,928,956)	1,584,540	-	(1,344,416)
Sales	3,056,312	193,374	-	3,249,686
Issuances	-	-	2,343,421	2,343,421
Settlements	(35,292)	(1,892,548)	(31,496)	(1,959,336)
Transfers in to Level 3	1,832	(73,664)	39,179	(32,653)
Transfers out of Level 3	(6,516)	(199,010)	(3,612)	(209,138)
<b>At 31 December 2012</b>	<b>139,454</b>	<b>5,302,183</b>	<b>2,931,994</b>	<b>8,373,631</b>

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 30 Assets and liabilities measured at fair value (continued)

#### Movement in assets and liabilities in Level 3 during year ended 31 December 2011

	Debt and equity instruments	Derivative receivables	Total financial assets
	\$'000	\$'000	\$'000
At 1 January 2011	3,487,164	7,274,814	10,761,978
Total gains recognised in profit or loss	(65,945)	(439,414)	(505,359)
Purchases	7,732,188	745,906	8,478,094
Sales	(7,675,971)	(11,894)	(7,687,865)
Issuances	17,945	-	17,945
Settlements	(624,776)	(3,011,875)	(3,636,651)
Transfers in to Level 3	503,479	84,264	587,743
Transfers out of Level 3	(320,705)	(338,815)	(659,520)
<b>At 31 December 2011</b>	<b>3,053,379</b>	<b>4,302,986</b>	<b>7,356,365</b>

	Debt and equity instruments	Derivative payables	Other financial liabilities	Total financial liabilities
	\$'000	\$'000	\$'000	\$'000
At 1 January 2011	-	7,883,096	-	7,883,096
Total gains recognised in profit or loss	(9,292)	283,611	-	274,319
Purchases	(385,455)	687,768	-	302,313
Sales	529,022	(923)	-	528,099
Issuances	-	-	562,290	562,290
Settlements	(84,260)	(2,891,622)	-	(2,975,882)
Transfers in to Level 3	4,210	818,633	-	822,843
Transfers out of Level 3	-	(669,898)	-	(669,898)
<b>At 31 December 2011</b>	<b>54,225</b>	<b>6,110,665</b>	<b>562,290</b>	<b>6,727,180</b>

In relation to sensitivity of level 3 disclosures, there would be no significant impact to the profit and loss from the use of alternative inputs due to economic hedging in place and other risk mitigants

# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012 (continued)**

### **31. Pensions**

The Company operates pension schemes for employees in the UK as well as the European branches

The Company also operates defined benefit and defined contribution schemes for its employers in the overseas branches in Switzerland, Germany, France, Italy and Spain

Based on full actuarial valuations carried out during the year, the net liability in respect of these schemes as at 31 December 2012 amounted to \$7,787,000 (2011 \$7,105,000). The charge for the year through profit and loss was \$2,657,000 (2011 \$1,787,000), and total expense charged through statement of total recognised gains and losses was \$1,113,000 (2011 \$6,351,000)

#### **UK pension schemes**

The Group maintains a defined benefit plan that is closed to additional benefit accruals known as the JPMC UK Retirement Plan. Whilst the Company is not a participating employer in this plan, it does have certain obligations under a Withdrawal Agreement, dated 24 May 2011, that was entered into in relation to JPM Services LLP ("LLP"), a group undertaking which had previously been a participating employer in the plan. Under the terms of this agreement, the Company became responsible for LLP's portion of the pension obligations calculated in accordance with paragraph 5(2) of Schedule 1A to the Occupational Pension Schemes (Employer Debt) Regulations 2005 (as amended) with effect from 1 June 2011. The Company was not required to make any payments immediately or in relation to the ongoing funding of the plan. However, payments may become due from the Company on the occurrence of the earliest of the following events:

- The commencement of the winding up of the plan
- The insolvency of the plan's last remaining participating employer
- The insolvency of the Company
- Any other date agreed between the Company and the Trustee of the Plan

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 32. Share based payments

The ultimate parent of the Company, JPMorgan Chase & Co (the Firm) has granted long-term stock-based awards to certain key employees under the 2005 Long-Term Incentive Plan (the "2005 Plan"). The 2005 Plan became effective on 17 May 2005, and was amended in May 2011. Under the terms of the amended 2005 plan, as of 31 December 2012, 283 million shares of common stock are available for issuance through May 2015. The amended 2005 Plan is the only active plan under which the Firm is currently granting stock-based incentive awards. The 2005 Plan, plus prior Firm plans and plans assumed as the result of acquisitions, are referred to collectively as the "LTI Plans" and such plans constitute the Firm's stock-based incentive plans.

The Firm separately recognises compensation expense for each tranche of each award as if it were a separate award with its own vesting date. For each tranche granted, compensation expense is recognised in line with how awards vest from the grant date until the vesting date of the respective tranche, provided that the employees will not become full-career eligible during the vesting period. For awards with full-career eligibility provisions and awards granted with no future substantive service requirement, the Firm accrues the estimated value of awards expected to be awarded to employees as of the grant date without giving consideration to the impact of post-employment restrictions. For each tranche granted to employees who will become full-career eligible during the vesting period, compensation expense is recognised in line with how awards vest from the grant date until the earlier of the employee's full-career eligibility date or the vesting date of the respective tranche.

#### Restricted stock units

Restricted stock units ("RSUs") are awarded at no cost to the recipient upon their grant. RSUs are generally granted annually and generally vest at a rate of 50% after two years and 50% after three years and convert into shares of common stock at the vesting date. In addition, RSUs typically include full-career eligibility provisions, which allow employees to continue to vest upon voluntary termination, subject to post-employment and other restrictions based on age or service-related requirements. All of these awards are subject to forfeiture until vested and contain clawback provisions that may result in cancellation prior to vesting under certain specified circumstances. RSUs entitle the recipient to receive cash payments equivalent to any dividends paid on the underlying common stock during the period the RSUs are outstanding.

Compensation expense for RSUs is measured based upon the number of shares granted multiplied by the stock price at the grant date, and for employee stock options and SARs (stock appreciation rights), is measured at the grant date using the Black-Scholes valuation model. Compensation expense for these awards is recognised as described above.

The following table summarises grants of restricted stock and RSUs to employees of the Company for each of the years ended 31 December 2012 and 31 December 2011.

	2012	2012	2011	2011
	Shares	Weighted	Shares	Weighted
	'000	average	'000	average
		fair value \$		fair value \$
Restricted stock units outstanding at 1 January	11,373	38.61	-	-
Granted	3,902	35.68	426	41.64
Exercised	(5,609)	35.74	(430)	42.22
Cancelled	(255)	38.99	(10)	28.17
Transferred	99	40.62	11,387	38.61
Outstanding 31 December	9,510	40.62	11,373	38.61



# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 32 Share based payments (continued)

#### Key employee stock options and SARs

Under the LTI Plans, stock options and SARs have generally been granted with an exercise price equal to the fair value of JPMorgan Chase's common stock on the grant date. The Firm typically awards SARs to certain key employees once per year, the Firm also periodically grants employee stock options and SARs to individual employees. The 2012, 2011 and 2010 grants of SARs to key employees vest ratably over five years (i.e., 20% per year) and awards contain clawback provisions similar to RSUs. The 2012, 2011 and 2010 grants of SARs contain full-career eligibility provisions. SARs generally expire 10 years after the grant date. The following table summarises activity in options and SARs granted to employees of the Company for each of the years ended 31 December 2012 and 31 December 2011.

	2012	2012	2011	2011
	Number of	Weighted	Number of	Weighted
	options/ SARs	average exercise price \$	options/ SARs	average exercise price \$
	'000		'000	
Outstanding, 1 January	2,084	38.74	-	-
Granted	93	35.61	35	44.29
Exercised	(55)	38.27	-	45.58
Cancelled	(172)	37.41	(83)	58.96
Transferred	(52)	40.51	2,132	38.74
Outstanding, 31 December	1,898	40.51	2,084	38.74
Exercisable, 31 December	1,100	42.41	1,030	42.19

The weighted-average share price during the year ended 31 December 2012 was \$39.22 (2011: \$39.36).

The weighted-average grant-date fair value of options granted during the year ended 31 December 2012 was \$8.89 (2011: \$13.04).

The following table summarises additional information about options and SARs outstanding as at 31 December 2012 and 31 December 2011.

	31 December 2012			31 December 2011		
	Outstanding	Weighted	Weighted	Outstanding	Weighted	Weighted
	'000	average	average	'000	average	average
		exercise	remaining		exercise	remaining
		price \$	contractual		price \$	contractual
			life (in years)			life (in years)
Range of exercise prices						
\$min - \$20.00	325	19.49	6.06	380	19.49	7.06
\$20.01 - \$35.00	134	31.48	2.12	144	30.94	2.98
\$35.01 - \$50.00	1,432	43.94	6.11	1,553	43.76	6.43
\$50.01 and above	7	482.14	2.19	8	122.23	1.46
Total	1,898	40.51	5.80	2,085	38.74	6.29

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 32 Share based payments (continued)

#### Broad-based employee stock options

No broad-based employee stock options were granted in 2011 or in 2012. In prior years, awards were granted by the Firm under the Value Sharing Plan, a nonshareholder-approved plan. For each grant, the exercise price was equal to the Group's common stock price on the grant date. The options become exercisable over various periods and generally expire 10 years after the grant date.

The following table presents a summary of the Company's broad-based employee stock option activity for each of the years ended 31 December 2012 and 31 December 2011.

	2012	2012	2011	2011
	Number of	Weighted	Number of	Weighted
	options	average	options	average
	'000	exercise	'000	exercise
		price \$		price \$
Range of exercise prices				
Outstanding, 1 January	49	34.49	-	-
Exercised	(5)	42.10	-	45.04
Cancelled	(30)	36.86	(1)	51.22
Transferred	3	33.46	50	34.49
Outstanding, 31 December	17	33.46	49	34.49
Exercisable, 31 December	17	33.46	49	34.49

The weighted-average share price during the year ended 31 December 2012 was \$39.22 (2011: \$39.36).

The following table summarises additional information about options outstanding at 31 December 2012 and 31 December 2011.

	31 December 2012			31 December 2011		
	Outstanding	Weighted	Weighted	Outstanding	Weighted	Weighted
	'000	average	average	'000	average	average
		exercise	remaining		exercise	remaining
		price \$	contractual		price \$	contractual
			life (in years)			life (in years)
Range of exercise prices						
\$20.01 - \$35.00	6	21.92	0.12	10	21.90	1.12
\$35.01 - \$50.00	11	39.96	1.12	39	37.72	0.62
Total	17	33.46	0.76	49	34.49	0.72

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 32 Share based payments (continued)

#### Compensation expense related to stock-based incentives

The total expense for the year relating to share based payments was \$168 million (2011 \$476 million), all of which relates to equity settled share based payments

The following table presents the assumptions used to value key employee stock options and SARs granted during the period under a Black-Scholes valuation model

	2012	2011
<b>Weighted-average annualised valuation assumptions</b>		
Weighted-average share price	\$39.22	\$39.36
Exercise price	\$35.53	\$32.27
Risk-free interest rate (US Treasury)	1.19%	2.58%
Expected dividend yield	3.15%	2.2%
Expected common stock price volatility	35%	34%
Expected life (in years)	6.60	6.50

The expected volatility assumption is derived from the implied volatility of the Group's publicly traded stock options. The expected life assumption is an estimate of the length of time that an employee might hold an option or SAR before it is exercised or cancelled, and the assumption is based on the Group's historical experience.

# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012 (continued)**

### **33. Financial risk management**

Risk management is an inherent part of the Group's (of which the Company is a part) business activities and the Company has adopted the same risk management policies and procedures as the Group as a whole. The Group and Company's risk management framework and governance structure are intended to provide comprehensive controls and ongoing management of the major risks. The Company employs a holistic approach to risk management to ensure the broad spectrum of risk types are considered in managing its business activities. The risk management framework is intended to create a culture of risk awareness and personal responsibility throughout the entity where collaboration, discussion, escalation and sharing of information is encouraged. The Company exercises oversight through the Board of Directors and delegation from the Board to various sub-committees which are organised in line with the Group risk management policy.

An overview of the key aspects of risk management and use of financial instruments is provided below. A more detailed description of the policies and processes adopted by the Group may be found within the Group annual report.

The Company is primarily in the business of underwriting, sales and trading of securities, swaps and derivative marketing, investment banking advisory and brokerage and clearing services for exchange traded futures and options contracts.

Positions held as a result of the above activities give rise primarily to operational, credit and market risks. The Group has a defined process for allocating desk limits and monitoring against them. Desk limits are aggregated into portfolio or business limits and these are policed on a daily basis. Traders may use financial instruments and derivative products to reduce or hedge their exposures and to maintain effective utilisation of limits.

The limits themselves are stress tested and reviewed to ensure they provide a satisfactory confidence level and that they aggregate up to appropriate limits for the businesses as a whole.

Derivative instruments may be used for reducing market risk exposures, managing or hedging risk including futures, forward rate agreements, interest rate swaps, cross currency swaps, default swaps, total return swaps, traded options and over the counter options. All of these are used to varying degrees to manage credit risk and market risk. Additionally, on balance sheet financial instruments are used as natural hedges wherever possible.

#### **Credit risk**

Credit risk refers to the risk of loss arising from a borrower, counterparty or obligor failing to meet its contractual obligations.

#### *Governance*

Credit risk is managed by the Group on a global as well as at a Company level. The Group has developed policies and practices that the Company is subject to, that are designed to preserve the independence and integrity of the approval and decision making of extending credit. These policies are intended to ensure that credit risks are assessed accurately, approved properly, monitored regularly and managed actively at both the transaction and portfolio levels. In addition, the Company has its own credit policy which contains standards pertaining to governance, management of concentrations, credit risk limits, new business initiative approvals and credit risk reporting which is distributed to the Board of the Company.

The Company has a designated Chief Risk Officer (CRO) who is also a Board member of the Company. Credit Executives within this Line of Business approve extensions of credit for the Company and ultimately report to the Head of Wholesale Credit Risk. Each Line of Business within the Group has its own independent credit risk management function, reporting to the Group Chief Risk Officer. The Company has its own Credit Risk management function, reporting to the Group Chief Risk Officer. The Company is exposed to credit risk through lending and capital markets activities.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 33. Financial risk management (continued)

#### *Methodology*

A range of methodologies are adopted for estimating the likelihood of counterparty (or obligor) default including, calculating the potential amount of credit exposure or loss should the obligor or the counterparty default, the probability of default, and the loss severity given a default event

The Company reduces its credit risk exposure through the effect of risk mitigants such as netting agreements with counterparties that permit the Company to offset receivables and payables with such counterparties and obtaining collateral from counterparties

The Company utilises counterparty credit risk stress testing scenarios that help to identify exposure concentrations, idiosyncratic events and other factors to protect the Company in the event of adverse economic or market events

The Credit Risk Management function works in partnership with the business segments in identifying and aggregating exposures. Methodologies for measuring credit risk vary depending on several factors, including type of asset. Based on these factors and related market-based inputs, the Company estimates replacement cost for derivatives (net mark-to-market ("MTM")), statistical estimates of losses for loans, and unexpected losses for its portfolios as follows

- For derivatives, the net MTM is an indicator of replacement cost, were an obligor to default, and reflects netting and collateral arrangements that may be in place
- For loans, Loss Given Default (LGD) is an indicator of potential loss as a result of obligor or counterparty default. However, probable losses are not the sole indicators of risk
- Unexpected losses, reflected in the allocation of economic credit risk capital, representing the potential volatility of actual losses relative to the probable level of incurred losses

Risk measurement for the portfolio is assessed primarily on a risk-rated basis

#### *Risk rated exposure*

Risk ratings are assigned to differentiate risk within the portfolio and are reviewed on an ongoing basis by Credit Risk Management and revised, if needed, to reflect the counterparties' current financial positions, risk profiles and the related collateral. For each credit facility, a Loss Given Default (LGD) is calculated and is an estimate of losses given a default event and takes into consideration collateral and structural support. Calculations and assumptions are based on management information systems and methodologies which are under continual review

#### *Risk monitoring and control*

The Company has adopted and applied the policies and practices developed by the Group. The policy framework establishes credit approval authorities, risk-rating methodologies, portfolio review parameters and guidelines for management of distressed exposures. In addition certain models, assumptions and inputs used in evaluating and monitoring credit risk are independently validated by support functions that are independent from the businesses

Credit risk is monitored regularly at an individual counterparty basis with credit limits established that are reviewed and revised, typically on an annual basis. Management of the Company's exposure is accomplished through a number of means including

- Loan syndications, participations and loan sales
- Use of master netting agreements
- Collateral and other risk-reduction techniques

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 33. Financial risk management (continued)

#### *Risk reporting*

To enable monitoring of credit risk, aggregate credit exposure, concentration levels and risk profile changes are reported to senior credit risk management and to the Board of the Company

The amounts in the table below show the maximum credit exposure of the Company

	2012	2011
	\$'000	\$'000
Balance Sheet		
Cash and balances at central banks	35,156	28,175
Loans and advances to banks	15,468,005	19,632,290
Loans and advances to customers	1,099,819	160,177
Securities purchased under agreements to resell	108,043,553	100,094,752
Securities borrowed	19,020,210	23,092,244
Financial assets held for trading	156,174,562	136,856,987
Financial assets designated at fair value	16,222	16,523

Financial assets held for trading, Securities purchased under resale agreements and Securities borrowed include certain external sub investment grade assets. All other financial assets are investment grade or held with other Group undertakings

#### **Liquidity risk**

Liquidity risk is the potential inability to meet cash flow and collateral obligations as they become due

The Group's liquidity risk management is intended to ensure that the Group has the appropriate amount, composition and tenor of funding and liquidity in support of its assets. The primary objective of effective liquidity management is to ensure that the Group's core businesses are able to operate in support of client needs and meet contractual and contingent obligations through normal economic cycles as well as during market stress and maintain debt ratings that enable the Group to optimize its funding mix and liquidity sources while minimising costs.

The liquidity policy for the Company is reviewed and approved in line with the Group liquidity risk governance framework. Specific risk committees responsible for liquidity risk governance for the Company include the Group Asset Liability Committee (ALCO) at the Group level and a regional ALCO. The regional ALCO reports on liquidity risk matters to the Company's Risk Committee and the Company's Board and is chaired by the European Treasurer.

The directors consider the Company's liquidity position to be strong as of December 31, 2012, and believes that the Company's unsecured and secured funding capacity is sufficient to meet its on and off-balance sheet obligations.

The Company is locally subject to the PRA's liquidity regulations. The key elements of the regulations are that the Company has adequate liquidity and self-sufficiency of liquidity resources, and that it has systems and controls in place to monitor this. The Company's funding strategy is intended to ensure that it will have sufficient liquidity and diversity of funding sources necessary to enable it to meet actual and contingent liabilities during both normal and stress periods. The Company reports its liquidity position against 'Individual Liquidity Guidance' provided by the PRA for regulatory purposes. The Company has established a daily monitoring process to monitor liquidity adequacy and ensure compliance with regulatory requirements.

The Company will also be subject to the Liquidity Coverage Ratio ("LCR") and Net Stable Funding Ratio ("NSFR") requirements once the Basel III regulations are locally adopted. The Company is monitoring the LCR, based on its current understanding of the requirements on a regular basis.

A regular internal assessment of the liquidity risk management framework is performed which informs the Board of the liquidity risks resulting from business activities in addition to the current and future funding needs of the Company.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 33. Financial risk management (continued)

#### Funding

The Company has very low reliance on short term unsecured funding markets

A significant portion of the total liabilities of the Company relate to securities sold under agreements to repurchase and securities loaned, both of which are incurred to support its client-driven market making activities. Securities loaned or sold under agreements to repurchase generally mature between one day and three months and are secured predominantly by high-quality securities collateral. This includes government-issued debt and agency debt.

The Company has entered into revolving committed liquidity facilities with other group undertakings to manage liquidity risk.

#### Liquidity Asset Buffer

Under the PRA liquidity requirements the Company holds a liquidity reserve of high-quality, marketable securities available to raise liquidity, if required.

#### Stress testing

Liquidity stress tests are intended to ensure sufficient liquidity for the Group and the Company under a variety of adverse conditions.

#### Contingency funding plan

The Company also maintains a legal entity liquidity policy and contingency funding plan ("CFP"), which is reviewed and approved by ALCO as well as reviewed and approved by the Company's Board. This provides a documented framework for managing both temporary and longer-term unexpected adverse liquidity situations. It sets out a list of indicators and metrics that are reviewed on a daily basis to identify the emergence of increased risks or vulnerabilities in the Company's liquidity position. The CFP identifies alternative contingent liquidity resources that can be accessed under adverse liquidity circumstances.

The following table provides details on the contractual maturity of all financial liabilities.

	Less than 1 year 2012 \$'000	More than 1 year 2012 \$'000	Total 2012 \$'000	Less than 1 year 2011 \$'000	More than 1 year 2011 \$'000	Total 2011 \$'000
Securities sold under agreements to repurchase	74,936,527	457,997	75,394,524	85,000,575	-	85,000,575
Securities loaned	20,448,502	-	20,448,502	19,565,299	-	19,565,299
Financial liabilities held for trading	101,795,834	-	101,795,834	98,297,855	-	98,297,855
Trade creditors	50,466,724	-	50,466,724	39,097,782	-	39,097,782
Amounts due to group undertakings	60,343,279	-	60,343,279	44,010,243	-	44,010,243
	307,990,866	457,997	308,448,863	285,971,754	-	285,971,754

The above financial liabilities are presented based on the earliest contractual maturity.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 33 Financial risk management (continued)

#### Market risk

Market risk is the exposure to an adverse change in the market value of portfolios and financial instruments caused by a change in market prices. The primary categories of market risk factors are

- Interest Rates - Interest rate risk primarily results from exposure to changes in the level, slope and curvature of the yield curve, the volatility of interest rates, and mortgage prepayment rates,
- Foreign Exchange Rates - Foreign exchange rate risk results from exposure to changes in prices and volatility of currency rates,
- Equity Prices - Equity price risk arises from exposure to changes in prices and volatility of individual equities, equity baskets and equity indices,
- Credit Spreads - Credit spreads are the difference between yields on corporate debt subject to default risk and government bonds free of such risk, and
- Commodity Prices - Commodity price risks result from exposures to changes in prices and volatility of commodities, such as natural gas, crude oil, petroleum products, precious and base metals and electricity

#### *Market risk management*

The Company's Board is ultimately responsible for managing market risk. The Company has a designated Chief Risk Officer who has responsibilities in relation to market risk management. The Market Risk management function is an independent risk management function that works in close partnership with the lines of business to identify and monitor market risks throughout the Group and to define market risk policies and procedures. The market risk function reports to the Group's Chief Risk Officer.

The Market Risk management function seeks to control risk, facilitate efficient risk/return decisions, reduce volatility in operating performance and provide transparency into the Group and the Company's market risk profile for senior management and the Board of Directors. The Market Risk management risk is responsible for the following functions

- Establishing a market risk policy framework,
- Independent measurement, monitoring and control of line of business market risk,
- Definition, approval and monitoring of limits, and
- Performance of stress testing and qualitative risk assessments

#### *Risk identification and classification*

Each line of business is responsible for the management of the market risks within its units. The Market Risk management function is responsible for overseeing each line of business ensures that all material market risks are appropriately identified, measured, monitored and managed in accordance with the risk policy framework set out by the Market Risk management function.

#### *Risk measurement*

Because no single measure can reflect all aspects of market risk, the Company uses various metrics, both statistical and non-statistical, including

- Value-at-Risk (VAR)
- Economic-value stress testing
- Non-statistical risk measures



# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 33 Financial risk management (continued)

#### *Value-at-risk*

The Company utilises Value-at risk ("VaR"), a statistical risk measure, to estimate the potential loss from adverse market moves in a normal market environment. The Company uses the Group's VaR model framework, which utilises historical simulation based on data for the previous twelve months. The framework's approach assumes that historical changes in market values are representative of the distribution of potential outcomes in the immediate future. VaR is calculated assuming a one-day holding period and an expected tail-loss methodology, which approximates a 95% confidence level. Underlying the overall VaR model framework are individual VaR models. The VaR model results across all portfolios are aggregated at the Company level.

Because VaR is based on historical data, it is an imperfect measure of market risk exposure and potential losses and VaR measures are inherently limited in their ability to measure certain risks and to predict losses, particularly those associated with market illiquidity and sudden or severe shifts in market conditions. Therefore, the Company uses economic stress testing and other techniques to capture and manage market risk arising under stressed scenarios.

#### *Economic value stress testing*

While VaR reflects the risk of loss due to adverse changes in markets using recent historical market behaviour as an indicator of losses, stress testing captures the Company's exposure to unlikely but plausible events in abnormal markets using multiple scenarios that assume significant changes in credit spreads, equity prices, interest rates, currency rates or commodity prices. Scenarios are updated dynamically and may be redefined on an ongoing basis to reflect current market conditions. Along with VaR, stress testing is important in measuring and controlling risk, it enhances understanding of the Company's risk profile and loss potential, as stress losses are monitored against limits. Stress testing is also employed in cross-business risk management. Stress-test results, trends and explanations based on current market risk positions are reported to the Company's senior management and to the lines of business to allow them to better understand event risk-sensitive positions and manage risks with more transparency.

#### *Non-statistical measures*

Non-statistical risk measures include sensitivities to variables used to value positions, such as credit spread sensitivities, interest rate basis point values and market values. These measures provide granular information on the Company's market risk exposure. They are aggregated by line-of-business and by risk type.

### **Risk monitoring and control**

#### *Limits*

Market risk is controlled primarily through a series of limits. Limits reflect the Company's risk appetite in the context of the market environment and business strategy. The Market risk management function regularly reviews and updates risk limits, as a minimum on a semi-annual basis. The Company's Board and the Chief Risk Officer are responsible for reviewing and approving certain risk limits on an ongoing basis. Any one-off limit exceptions require approval by the Company's Chief Executive Officer (CEO) on behalf of the Company's Board. In setting limits, the Company takes into consideration factors such as senior management risk appetite, market volatility, product liquidity, accommodation of client business and management experience.

#### *Risk reporting*

Non-statistical risk measures, VaR trends and limit excesses are reported daily to the lines of businesses and to senior management. Market risk stress-test results are also performed weekly and reported weekly to the lines of business and to senior management. Additional scenarios are run on a quarterly basis. In addition to the above, monthly market risk updates are provided to the monthly EMEA Investment Banking Risk Committee meetings and the Company's quarterly Board meetings.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 33. Financial risk management (continued)

#### Currency risk

The Company's primary business activity does not include currency trading, however, its core business lines will trade in multiple currencies. It must therefore convert its profits back to functional currency and must be able to eliminate exposures to movements in non-functional currencies. It does this in the normal course of events through matching non-functional assets and liabilities with others in the same non-functional currency. They use futures, forward rate agreements, cross currency swaps, traded options and over the counter options to manage the risk.

Foreign exchange risk represents the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company manages its exposure to Sterling and Euro against US dollar (the functional currency of the Company) to within acceptable risk management limits on a daily basis. The following table shows the effect of a reasonably possible change in exchange rates on the financial profit of the Company.

	2012	2011
	\$'000	\$'000
5% increase in GBP/USD exchange rate	(14)	(252)
5% decrease in GBP/USD exchange rate	15	278
5% increase in EUR/USD exchange rate	(773)	(1,254)
5% decrease in EUR/USD exchange rate	855	1,386

#### Interest rate risk

Interest rate risk represents the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company has a cash flow and fair value interest rate risk. The following table shows the effect of a reasonably possible change in interest rates on the financial profit of the Company.

	2012	2011
	\$'000	\$'000
1 basis point increase in local interest rates	200	200
1 basis point decrease in local interest rates	(200)	(200)

#### Price risk

Price risk represents the risk that the fair value or future cash flows of a financial instrument will fluctuate because of movements in market price for those instruments. Financial assets and liabilities held for trading include derivatives, equities and hedge funds that are subject to price risk movements from changes in their credit risk profile or movements in indices and other market indicators.

Loans and advances to customers are subject to price risk from changes in the credit risk profiles of the loans. The following table shows the effect on the pre-tax profits of changes in credit spreads, major market indices, hedge fund research indices and other equity price movements.

	2012	2011
	\$'000	\$'000
10% widening of the credit spread	(49,465)	(189,000)
10% shortening of the credit spread	49,865	189,000
10% increase in major market indices	17,440	8,000
10% decrease in major market indices	(10,090)	(1,000)
10% increase across hedge fund research indices	(12,608)	(7,000)
10% decrease across hedge fund research indices	12,608	7,000

# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012 (continued)**

### **33 Financial risk management (continued)**

#### **Operational risk**

Operational risk is the risk of loss resulting from inadequate or failed processes or systems, human factors or external events

Operational risk is inherent in each of the Group and the Company's businesses and support activities. Operational risk can manifest itself in various ways including error, fraudulent acts, business interruptions, inappropriate behaviour of employees, or vendors that do not perform in accordance with their arrangements. These events could result in financial losses and other damage to the Group including reputational harm.

To monitor and control operational risk, the Group maintains an overall framework including strong oversight and governance, comprehensive policies, consistent practices and enterprise risk management tools intended to provide a sound and well-controlled operational environment. The framework clarifies

- Ownership of the risk by the businesses and functional areas
- Monitoring and validation by business Control Officers
- Oversight by independent risk management
- Governance through business risk & control committees
- Independent review by Internal Audit

The objective is to keep operational risk at appropriate levels, in light of the Company's financial strength, the characteristics of its business, the markets in which it operates, and the competitive and regulatory environment to which it is subject.

#### **Fair value of financial assets and financial liabilities**

For all financial assets and financial liabilities, carrying value is a reasonable approximation of fair value.

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 34 Capital management

The Company sees its strong capital position as essential to its strategy and competitive position with a focus on long-term stability, positioning itself to build and invest in market-leading businesses even in a highly stressed environment. Accordingly, its capital management framework is designed to ensure that the Company is strongly capitalised at all times in relation to

- minimum regulatory requirements (Pillar 1 capital plus Pillar 2 / Individual Capital Guidance),
- the risks faced by the Company, through regular comparisons of regulatory and internal capital requirements, and
- The Company's risk appetite, for example, through the application of an internal capital buffer

The framework used to manage capital is based around a regular cycle of point-in-time capital calculations and reporting, supplemented by forward-looking projections and stress-testing, with corrective action taken as and when required to maintain an appropriate level of capitalisation. Each part of the process is subject to rigorous control including daily capital adequacy calculations and internal reporting, monthly and ad hoc capital projections, and capital usage limits by business area.

Risk management is an inherent part of the Group's (of which the Company is a part) business activities and the Company has adopted similar risk management policies and procedures to the Group as a whole, in addition to ensuring the adherence to local regulatory requirements and risk appetite. Through the quarterly Internal Capital Adequacy Assessment Process (ICAAP), the Company ensures that it is adequately capitalised in relation to its risk profile and appetite, not only as at the ICAAP date, but through the economic cycle and under a range of severe but plausible stress scenarios.

The composition of capital of the Company as of 31 December 2012 is as follows

	31 December 2012 \$'000	31 December 2011 \$'000
Total Tier 1 capital (Share capital and reserves - net of deductions)	19,878,053	19,418,268
Tier 2 (Preference shares)	367,383	367,383
Tier 3 (Interim trading book profits - net of deductions)	552,008	
<b>Total capital resources</b>	<b>20,797,444</b>	<b>19,785,651</b>

As of 31 December 2012 and 2011, the Company was adequately capitalised

# J.P. MORGAN SECURITIES PLC

## Notes to the financial statements for the year ended 31 December 2012 (continued)

### 35. Transfer of financial assets

In the course of its normal business activities, the Company makes transfers of financial assets. Depending on the nature of the transaction, this may result in derecognition of the assets in their entirety, partial derecognition or no derecognition of the assets subject to the transfer. A summary of the main transactions, and the assets and liabilities and the financial risks arising from these transactions, is set out below.

#### Transfers of financial assets that do not result in derecognition

Assets are transferred under repurchase and securities lending agreements with other banks and financial institutions. The substance of these transactions is secured borrowings and therefore the assets are not derecognised from the balance sheet. The recipient is generally able to use, sell or pledge the transferred assets for the duration of the transaction. The Company remains exposed to interest and credit risk on these instruments. The counterparty's recourse is generally not limited to the transferred assets. The fair value of the collateral and the carrying amounts of the liabilities is disclosed in notes 19 and 20 of these financial statements.

The Company also entered into certain other transactions, whereby the assets were transferred but the transfer did not meet the derecognition requirements and therefore the assets continue to be recognised on the balance sheet together with the related liability. The following is a summary of the fair value of the assets and carrying amount of related liabilities.

	Fair value of the assets		Carrying amount of the related liability	
	2012	2011	2012	2011
	\$'m	\$'m	\$'m	\$'m
Financial assets held for trading	9,466	6,142	8,900	5,830

#### Continuing involvement in financial assets that have been derecognised

In some cases, the Company transfers financial assets that it derecognises in its entirety even though it may have continuing involvement in them. This typically happens when the Company has sold a financial asset to a special purpose vehicle (SPV) with limited other assets and enters into a derivative with the SPV to provide investors with a specified exposure. (Examples include credit linked note vehicles and asset swap vehicles that are established on behalf of investors). The total notional and the market value of all derivatives executed by the Company with such SPVs (including those with such SPVs to which the Company did not transfer any financial assets) amounted to \$6.284 billion and \$53 million as of 31 December 2012.

### 36. Related parties

In accordance with the exemption afforded by FRS 8, 'Related Party Disclosures', certain details of transactions with parent and fellow subsidiary companies that are also wholly-owned within the Group, are not disclosed as they are included in the consolidated financial statements of the Group, which are publicly available. There were no other material disclosable related party transactions during the year.

# **J.P. MORGAN SECURITIES PLC**

## **Notes to the financial statements for the year ended 31 December 2012 (continued)**

### **37. Parent undertaking**

The Company's immediate parent undertaking is J P Morgan Chase International Holdings, incorporated in Great Britain

The Company's ultimate parent undertaking and controlling party is JPMorgan Chase & Co , which is incorporated in the state of Delaware in the United States of America JPMorgan Chase & Co is also the parent undertaking of the largest group in which the results of the Company are consolidated

The parent undertaking of the smallest group in which the Company's results are consolidated is J P Morgan Capital Holdings Limited, incorporated in Great Britain

The largest and smallest parent groups' consolidated financial statements can be obtained from the Company's registered office

25 Bank Street  
Canary Wharf  
London  
E14 5JP  
England

### **38. Post balance sheet events**

On 8 April 2013, the Board approved interim dividends in aggregate of \$372,776,521 on the preference shares, \$7,065,700 on the preferred ordinary shares and \$470,157,779 on the ordinary shares of the Company