2005 Annual Report

# get the glow.

Primary Financial

a history of bright futures

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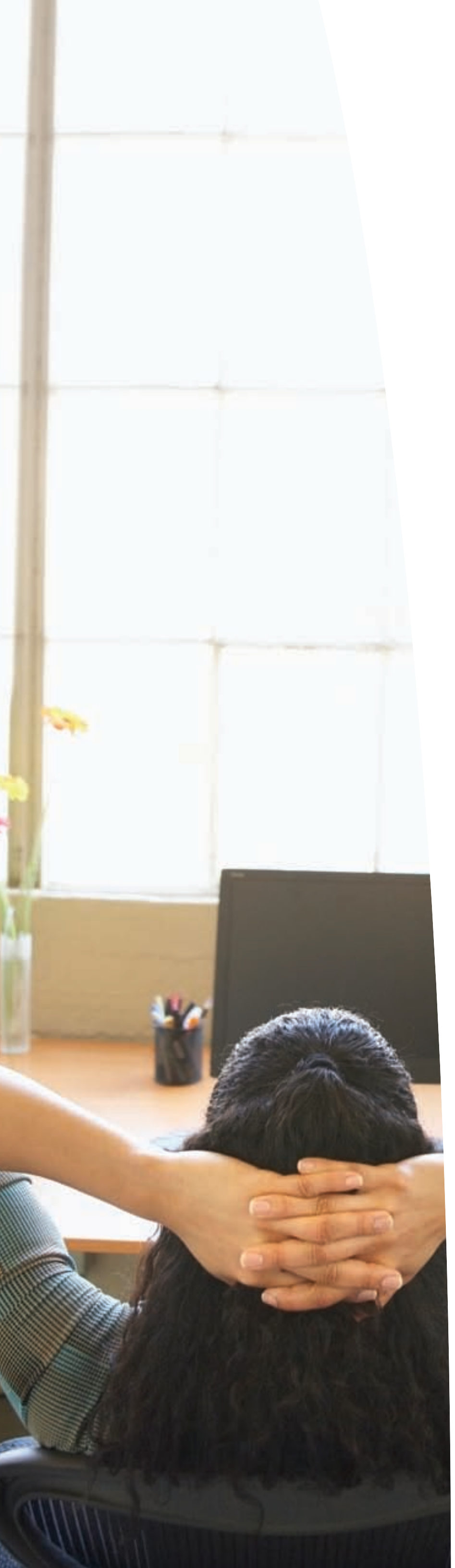




# Spreading the Glow

Mark Solomon (left) and Gregory S. Moore (right)

With tightened liquidity, a flattened yield curve, and a rising rate environment in 2005, credit unions faced unique challenges when it came to managing their investment portfolios.

But those challenges couldn't dim the glow of the nearly 2,900 credit unions who turned to Primary Financial's SimpliCD program and their corporate credit union for convenient ways to generate liquidity and invest substantial funds in federally insured CDs.

Last year, Primary Financial continued to demonstrate our operational and financial soundness. Not only did we manage more than $4.4 billion in sales and maturities volume in 2005, our balance sheet continued to strengthen from positive cash flow and the absence of debt. Additionally, Primary Financial had net income of $873,000 in 2005, an increase of $278,000 from 2004.

We'd like to thank our board of directors and owners for their guidance and support. Our success is truly a reflection of their dedication and commitment. We'd also like to recognize our management and staff who work hard to give our owners and customers the SimpliCD glow.

Here's to a proud history and a bright future.

Gregory S. Moore, Chairman
President and CEO, Georgia Central Credit Union

Mark Solomon, President and CEO
Primary Financial

## Board of Directors

From left to right: Jeff Navin, Vice President/CIO, Constitution Corporate FCU (Director); Bob Burrell, Executive Vice President, Chief Investment Officer, Western Corporate FCU (Treasurer); Greg Moore, President and CEO, Georgia Central CU (Chairman); Kathy Garner, President/CEO, Northwest Corporate FCU (Vice Chairman); Lee Butke, President/CEO, Corporate One FCU (Director); Lew Lambert, President - Minnesota Operations, Mid-States Corporate FCU (Secretary)

# Get the glow.

Primary Financial is a credit union service organization owned jointly by 29 corporate credit unions and U.S. Central Credit Union. This ownership structure, with the corporate owners also serving as resellers, gives Primary Financial potential relationships with nearly 9,000 credit unions across America.

Primary Financial is the creator, owner and operator of SimpliCD, a turnkey certificate of deposit program that enables financial institutions to invest substantial funds in federally insured CDs or to generate liquidity by issuing certificates to a nationwide market of potential investors.

## We do the work. You get the glory.

The value of the SimpliCD program continues to be convenience and ease of use. When credit unions need to earn competitive rates on federally insured jumbo certificates, one phone call to their corporate gives them easy access to great rates, with the convenience of free performance reviews, single transaction settlement, and concise daily and monthly statements.

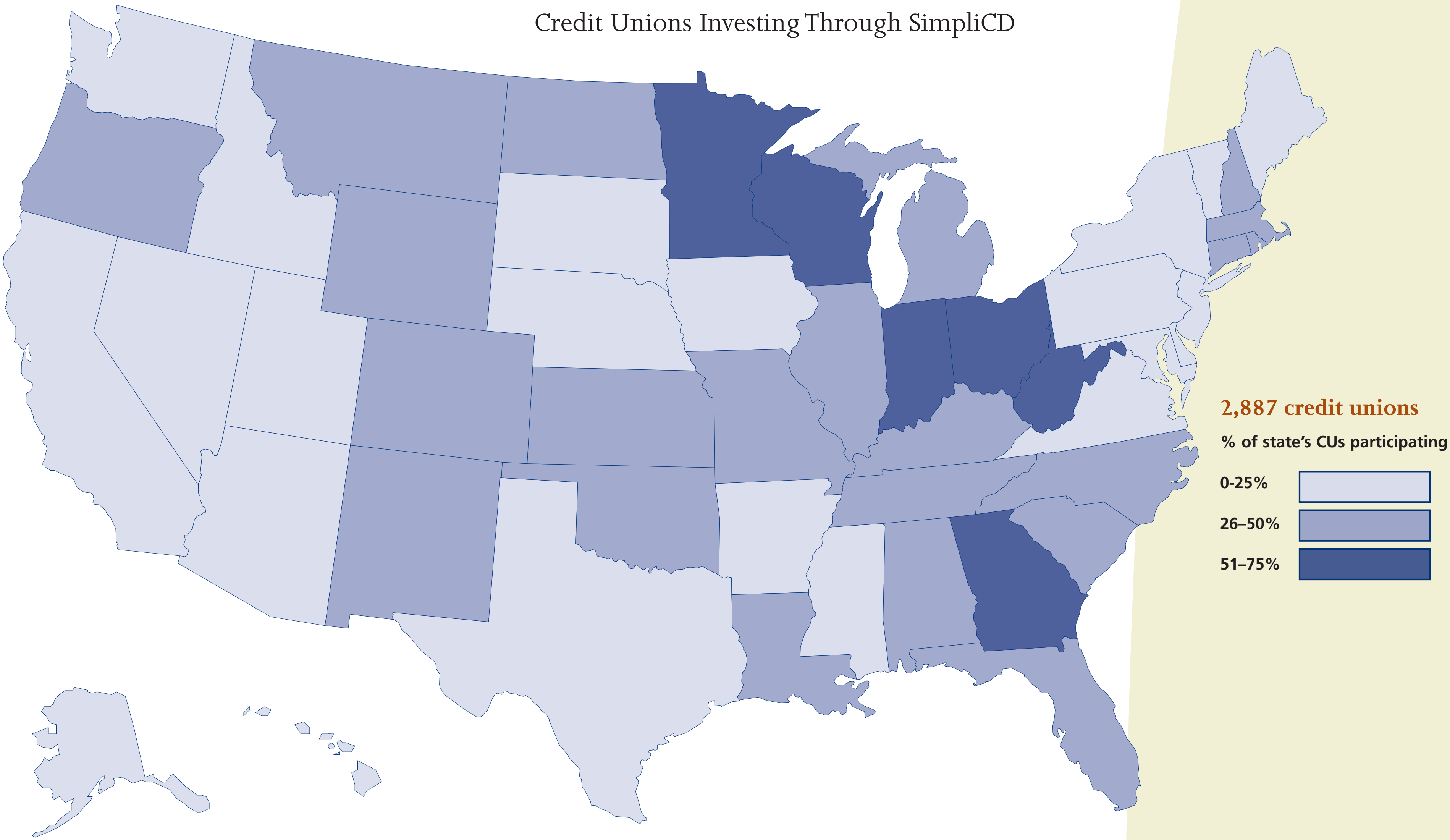
Likewise, when financial institutions need liquidity, one phone call is all it takes to market their deposit offerings nationwide and generate funds quickly. By plugging into our powerful network of corporates, credit unions, and other financial institutions, issuers can raise liquidity without having to spend the time and money to market their deposits nationally, analyze the market, or manage multiple CDs and deposit relationships.

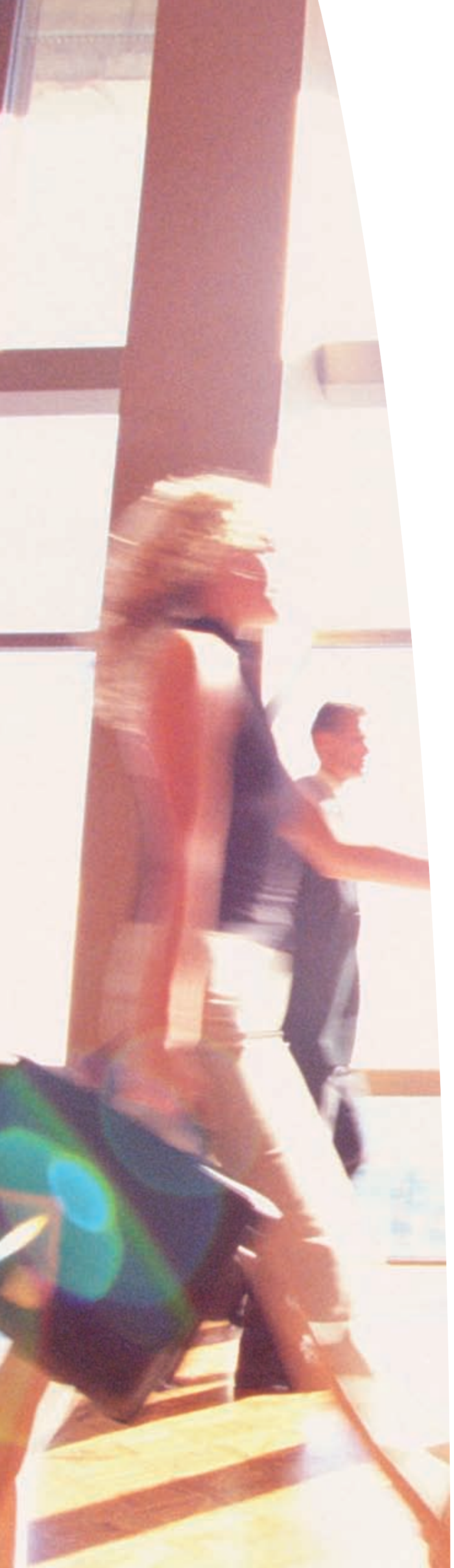
Last year, Primary Financial facilitated the payment of more than $86 million in interest to credit unions.

SimpliCD takes the time and hassle out of generating large amounts of liquidity and investing substantial funds in federally insured CDs. In short, SimpliCD does the work so credit unions can bask in the glow of success.

## National Market Share

Credit Unions Investing Through SimpliCD





## Shining examples of success

In 2005, Primary Financial continued its commitment to provide corporates and their member credit unions with a turnkey brokered CD solution unlike any other in the credit union movement. However, our efforts are only half of the story.

Our ownership structure and co-broker distribution network is unique in the credit union movement. Since its inception, SimpliCD has been distributed through corporate credit unions, because they have gained the trust of their members and have developed a unique understanding of their members' asset/liability management needs. Even with the convenience, ease of use, great rates, and great service of SimpliCD, it's the efforts of our corporate co-brokers that truly make SimpliCD successful. They are the key link in the powerful network that connects SimpliCD to credit unions.

Last year, tightened credit union liquidity and rising interest rates caused Primary Financial's assets under management to decline to $2.35 billion. However, efforts by our corporate co-brokers to market SimpliCD to their members continued to drive growth in the program's scope.

In 2005, SimpliCD grew its market share to 32 percent of America's credit unions, up from 28 percent in 2004. Nearly 2,900 credit unions across America now participate in SimpliCD. Additionally, our co-brokers helped us increase the number of credit unions with agreements to issue certificates through SimpliCD to 214, up 152 percent over 2004. These efforts help to position Primary Financial for continued growth in the future.

## The power of the network

Investors and issuers aren't the only ones basking in the glow of SimpliCD. The corporate credit unions that own Primary Financial continue to find SimpliCD to be a valuable enhancement to their investment offerings. Much of our success can be attributed to this unique, cooperative ownership structure and the powerful distribution network that allows us to reach nearly every credit union in America. Best of all, because we're owned by corporate credit unions, who are in turn owned by credit unions, the earnings generated by Primary Financial stay in the network.

In 2006, Primary Financial will continue to work with our corporate co-brokers to help them strengthen their relationships with their members. We also expect to add more issuers to SimpliCD in 2006, giving investors access to competitive rates from a wider selection of institutions.

## On the horizon

In 2006, Primary Financial remains committed to providing financial institutions across America with a convenient and easy way to manage their investment and liquidity needs.

Easy to use solutions, great rates from issuers nationwide, superior service, and a powerful network of corporate credit union partners continue to make SimpliCD the premier brokered CD program in the credit union movement.

The future is bright – and SimpliCD is spreading the glow.

SimpliCD

**$2.35 billion** in assets under management

**2,887** investors nationwide

**32%** of America's credit unions participate in SimpliCD

As of 12/31/05

# Independent Auditors' Report

The Board of Directors
Primary Financial Company LLC

We have audited the accompanying balance sheets of Primary Financial Company LLC, (the Company), as of December 31, 2005 and 2004, and the related statements of income, changes in members' equity and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Primary Financial Company LLC as of December 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

Columbus, Ohio
March 13, 2006

# Balance Sheets

| | December 31, 2005 | December 31, 2004 |
|---|---|---|
| Assets | | |
| Cash | $ 4,750,989 | $ 4,008,377 |
| Gross spreads receivable | 4,067,363 | 6,434,632 |
| Advances to customers | 99,000 | 301,000 |
| Goodwill and intangible assets | 3,682,281 | 3,628,055 |
| Other assets | 212,213 | 248,644 |
| TOTAL ASSETS | $ 12,811,846 | $ 14,620,708 |
| Liabilities and Members' Equity | | |
| Liabilities: | | |
| Deferred spreads | $ 1,786,664 | $ 2,439,315 |
| Co-broker spreads payable | 2,280,915 | 3,408,686 |
| Amounts due to customers | 1,336,036 | 1,305,054 |
| Note payable | | 1,096,484 |
| Accounts payable and accrued expenses | 427,618 | 263,343 |
| TOTAL LIABILITIES | 5,831,233 | 8,512,882 |
| Members' Equity | 6,980,613 | 6,107,826 |
| TOTAL LIABILITIES AND MEMBERS' EQUITY | $ 12,811,846 | $ 14,620,708 |

See accompanying notes to financial statements.

# Statements of Income

| | Year ended December 31, 2005 | 2004 |
|---|---|---|
| Revenue | | |
| Spread income: | | |
| Gross spread income | $ 6,215,394 | $ 4,922,266 |
| Co-broker spread | (3,099,013) | (2,374,067) |
| NET SPREAD INCOME | 3,116,381 | 2,548,199 |
| Interest and other income | 171,564 | 487,343 |
| TOTAL REVENUE | 3,287,945 | 3,035,542 |
| Expenses | | |
| Salaries and benefits | 1,002,802 | 752,389 |
| Professional and other outside services | 603,830 | 766,921 |
| Settlement processing | 298,786 | 392,606 |
| Office operations and occupancy | 223,180 | 207,639 |
| Other | 286,560 | 321,300 |
| TOTAL EXPENSES | 2,415,158 | 2,440,855 |
| NET INCOME | $ 872,787 | $ 594,687 |

See accompanying notes to financial statements.

# Statements of Changes in Members' Equity

| | Members' Equity |
|---|---|
| Balance at January 1, 2004 | $ 5,513,139 |
| Net income | 594,687 |
| Balance at December 31, 2004 | 6,107,826 |
| Net income | 872,787 |
| Balance at December 31, 2005 | $ 6,980,613 |

See accompanying notes to financial statements.

# Statements of Cash Flows

| | Year ended December 31, 2005 | 2004 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $ 872,787 | $ 594,687 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 39,305 | (261,958) |
| Net change in: | | |
| Gross spreads receivable | 2,478,620 | 992,292 |
| Certificates held for resale | | 100,000 |
| Advances to customers | 202,000 | (101,000) |
| Other assets | 42,995 | (75,332) |
| Deferred spreads | (652,651) | 1,421,174 |
| Co-broker spreads payable | (1,135,309) | 20,108 |
| Amounts due to customers | 30,982 | 137,339 |
| Accounts payable and accrued expenses | 153,165 | 100,203 |
| NET CASH PROVIDED BY OPERATING ACTIVITIES | 2,031,894 | 2,927,513 |
| Cash flows from investing activities: | | |
| Payment of royalties to Corporate One | (134,952) | (112,573) |
| Purchase of property and equipment | (54,241) | (26,833) |
| NET CASH USED IN INVESTING ACTIVITIES | (189,193) | (139,406) |
| Cash flows from financing activities: | | |
| Payments on note to Corporate One | (1,100,089) | (2,200,177) |
| NET CASH USED IN FINANCING ACTIVITIES | (1,100,089) | (2,200,177) |
| NET INCREASE IN CASH | 742,612 | 587,930 |
| CASH AT BEGINNING OF PERIOD | 4,008,377 | 3,420,447 |
| CASH AT END OF PERIOD | $ 4,750,989 | $ 4,008,377 |

See accompanying notes to financial statements.

# Notes to Financial Statements

## (1) Summary of Significant Accounting Policies

### (a) Organization, Operations and Cash Flow Information

Primary Financial Company LLC (the Company) is a multiple-member limited liability company and is a corporate credit union service organization (CUSO) of its members – 29 corporate credit unions and U.S. Central. The Company was established in accordance with the regulations of the National Credit Union Administration (NCUA) and the Ohio Revised Code. As an LLC, the Company is not subject to federal or state income tax.

The Company is registered with the State of Ohio as a licensed securities dealer. The Company brokers non-negotiable certificates of deposit through a turnkey program, called SimpliCD, which enables its customers to invest in federally insured certificates of deposit. As part of this service, the Company places certificates and collects principal and interest on behalf of its customers. The Company earns a spread over the term of the certificates for performing the services of the SimpliCD program.

The Company sells SimpliCD via its co-broker network. The co-brokers, most of which are the corporate credit unions that are also the owners, earn a portion of the spread for certificates of deposit they sell.

The Company's office located at 3260 Middle Road, Columbus, Indiana, 47203, has been designated an Office of Supervisory Jurisdiction (OSJ) of CU Investment Solutions Inc. (ISI), a member of the National Association of Securities Dealers (NASD). As an OSJ, the Company is subject to the jurisdiction of the Securities and Exchange Commission under the Securities and Exchange Act of 1934.

The accounting and reporting policies of the Company conform to accounting principles generally accepted in the United States of America (GAAP). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

**(b) Cash**

Cash represents demand deposits with Corporate One Federal Credit Union (Corporate One) and other financial institutions. At December 31, 2005, nearly $4.44 million was held in interest-earning demand deposit accounts at Corporate One.

**(c) Gross Spreads Receivable and Deferred Spreads**

Gross spreads receivable represents the total amount of spread the Company expects to receive from the placement of certificates of deposit over the term of the certificates. This receivable is recorded upon placement of the certificates, along with the corresponding deferred spreads and co-broker spreads payable. The deferred spreads are recognized as revenue over the term of the certificates.

**(d) Advances to Customers**

The Company generally receives the proceeds of its customers' maturing certificates of deposit from the certificate issuer and remits the proceeds to the customer on the maturity date. Occasionally, there is a slight delay in the receipt of principal from the issuer. In those instances, as a service to its customers, the Company advances the principal to its customers.

### (e) Goodwill and Identifiable Intangible Assets

The goodwill and identifiable intangible assets relate to the 2003 purchase of the Company from Corporate One. Goodwill is not amortizable but is subject to an annual impairment test. There were no impairment losses in 2005 or 2004. Identifiable intangible assets totaling $459,200 consist of acquired co-broker relationships. Identifiable intangible assets are amortized straight line over their estimated useful lives of five years. Accumulated amortization of the identifiable intangible asset was $214,300 and $122,400 at December 31, 2005 and 2004, respectively. Amortization expense for the identifiable intangible asset over the next three years is estimated to be as follows:

| | |
|---|---|
| 2006 | $ 91,800 |
| 2007 | 91,800 |
| 2008 | 61,300 |

### (f) Co-broker Spreads Payable

Co-broker spreads payable represents the amount of spread the Company expects the co-brokers will earn over the life of the certificates sold by the co-brokers.

### (g) Amounts Due to Customers

Amounts due to customers represents interest that the Company has received on behalf of its customers, but has not yet remitted to its customers.

## (2) Related Party Transactions

In conjunction with the purchase of the Company from Corporate One in 2003, the Company agreed to pay Corporate One, for 12 years, amounts above the spread it pays to corporate co-brokers for placements of certificates of deposit. The Company, for five years, also agreed to pay Corporate One a portion of the spread on all certificates placed by certain co-brokers that were placing certificates at the time of the purchase. These additional payments are considered compensatory and are expensed as incurred. Such expense was $542,800 and $426,800 in 2005 and 2004, respectively, and is included in co-broker spread in the accompanying statements of income. For 12 years, the Company also agreed to pay Corporate One a royalty on all other co-broker placements through the Company, including all placements by new co-brokers. These royalties are considered additional purchase consideration and have been recorded as additional goodwill. The total of such royalties was $146,000 and $113,000 in 2005 and 2004, respectively.

The Company entered into a management contract with Corporate One on September 1, 2003. For a period of two years beginning September 1, 2003 Corporate One agreed to provide the Company executive management services, including executive oversight, event planning and marketing services. For a period of three years beginning September 1, 2003, with the option to renew annually, Corporate One agreed to provide the Company certain support services including accounting, payroll and benefits administration, technical support and certain treasury functions. Expense related to this agreement was $475,000 in 2005 and $524,000 in 2004.

## (3) Commitments and Contingencies

The Company and Corporate One have an agreement whereby Corporate One has extended a $3 million line of credit to the Company to be used to facilitate the settlement of customer transactions. The credit line is secured by the assets of the Company. The interest rate on the credit line is equal to the rate Corporate One charges other borrowers under similar lending agreements. At December 31, 2005 and 2004, no advances were outstanding on the credit line.

The Company leases an office facility under an operating lease that expires in July 2006. The minimum annual rental related to this agreement is $17,369 in 2006. The Company has the option to extend this lease until 2009 at a rate not to exceed $32,849 annually. It is likely the Company will extend such lease.

## (4) Net Capital Requirement

The Company, as a licensed securities dealer with the State of Ohio, is required to maintain net capital, as defined, of at least $25,000. The Company was in compliance with this requirement at December 31, 2005 and 2004.

## (5) Retirement Plans

All of the Company's employees participate with Corporate One employees in two defined contribution plans in which the Company contributed a total of 11.5 percent of the participant's eligible compensation to the participant's accounts in the plans. One of the plans is a contributory plan, to which employees can contribute a portion of their compensation on a pre-tax basis. Retirement expense was approximately $88,000 in 2005 and $65,000 in 2004.

Primary**Financial**

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