Financial Statements

# Primary Financial Company LLC

December 31, 2017 and 2016

## C O N T E N T S

230 West Street
Suite 700
Columbus, OH 43215
tel 614.221.1120
fax 614.227.6999
www.gbq.com

GBQ Partners

To the Board of Directors of
Primary Financial Company LLC

## Independent Auditor's Report

We have audited the accompanying financial statements of Primary Financial Company LLC, which comprise the balance sheets as of December 31, 2017 and 2016 and the related statements of income, changes in members' equity and cash flows for the years then ended, and the related notes to the financial statements.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audits. 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 from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *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, 2017 and 2016, and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

GBQ Partners LLC

Columbus, Ohio
February 26, 2018

## Balance Sheets

| Assets | | December 31, 2017 | | December 31, 2016 |
|---|---|---|---|---|
| Cash and cash equivalents | $ | 23,431,898 | $ | 21,847,631 |
| Gross spreads receivable | | 18,545,296 | | 19,686,718 |
| Net Fixed Assets | | 1,607,631 | | 1,614,874 |
| Goodwill | | 5,430,543 | | 5,430,543 |
| Deferred issuer incentive expense | | 2,542,324 | | 2,492,052 |
| Other Assets | | 94,672 | | 363,542 |
| TOTAL ASSETS | $ | 51,652,364 | $ | 51,435,360 |
| **Liabilities and Members' Equity** | | | | |
| Liabilities: | | | | |
| Deferred spreads | $ | 9,316,360 | $ | 10,066,606 |
| Co-broker spreads payable | | 16,138,847 | | 16,788,153 |
| Amounts due to customers | | 2,904,215 | | 2,793,884 |
| Accounts payable and accrued expenses | | 2,612,031 | | 2,188,262 |
| Distributions payable | | 1,125,000 | | - |
| TOTAL LIABILITIES | | 32,096,453 | | 31,836,905 |
| Members' Equity | | 19,555,911 | | 19,598,455 |
| TOTAL LIABILITIES AND MEMBERS' EQUITY | $ | 51,652,364 | $ | 51,435,360 |

The accompanying notes are an integral part of the financial statements.

## Statements of Income

| | Year Ended December 31, | |
|---|---|---|
| | 2017 | 2016 |
| **Revenue** | | |
| Spread income: | | |
| Gross spread income | $ 15,779,978 | $ 15,557,026 |
| Co-broker spread & incentives | (10,669,201) | (10,557,996) |
| NET SPREAD INCOME | 5,110,777 | 4,999,030 |
| Interest and other income | 200,603 | 110,917 |
| TOTAL REVENUE | 5,311,380 | 5,109,947 |
| **Expenses** | | |
| Salaries and benefits | 2,739,907 | 2,927,455 |
| Office operations and occupancy | 593,141 | 556,048 |
| Settlement processing | 162,501 | 175,761 |
| Professional and other outside services | 291,352 | 215,660 |
| Advertising and promotion | 287,768 | 405,585 |
| Other | 154,255 | 120,384 |
| TOTAL EXPENSES | 4,228,924 | 4,400,893 |
| NET INCOME | $ 1,082,456 | $ 709,054 |

The accompanying notes are an integral part of the financial statements.

## Statements of Changes in Members' Equity

| | | | Members' Equity |
|---|---|---|---|
| Balance at December 31, 2015 | (75 Units Outstanding) | $ | 18,889,401 |
| Net Income | | | 709,054 |
| Balance at December 31, 2016 | (75 Units Outstanding) | $ | 19,598,455 |
| Net Income | | | 1,082,456 |
| Distributions declared to members ($15,000 per unit) | | | (1,125,000) |
| Balance at December 31, 2017 | (75 Units Outstanding) | $ | 19,555,911 |

The accompanying notes are an integral part of the financial statements.

## Statements of Cash Flows

| | Year Ended December 31, 2017 | Year Ended December 31, 2016 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $ 1,082,456 | $ 709,054 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 271,380 | 256,702 |
| Net change in: | | |
| Gross spreads receivable | 1,141,422 | (4,673,552) |
| Deferred spreads | (750,246) | 1,872,139 |
| Co-broker spreads payable | (649,306) | 1,198,235 |
| Amounts due to customers | 110,331 | (37,911) |
| Deferred issuer incentive expense | (50,272) | (822,319) |
| Other, net | 692,639 | 764,725 |
| NET CASH AND CASH EQUIVALENTS PROVIDED BY (USED IN) OPERATING ACTIVITIES | 1,848,404 | (732,927) |
| Cash flows from investing activities | | |
| Purchase of property and equipment | (264,137) | (86,786) |
| NET CASH AND CASH EQUIVALENTS USED IN INVESTING ACTIVITIES | (264,137) | (86,786) |
| Cash flows from financing activities | | |
| Distribution to members | - | (2,250,000) |
| NET CASH AND CASH EQUIVALENTS PROVIDED BY (USED IN) FINANCING ACTIVITIES | - | (2,250,000) |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | 1,584,267 | (3,069,713) |
| CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR | 21,847,631 | 24,917,344 |
| CASH AND CASH EQUIVALENTS AT END OF YEAR | $ 23,431,898 | $ 21,847,631 |

The accompanying notes are an integral part of the financial statements.

# Notes to Financial Statements

## (1) ORGANIZATION

Primary Financial Company LLC (the Company) is a multiple-member limited liability company and is a corporate credit union service organization (CUSO), owned by its 10 corporate credit union members. The Company was established in accordance with the regulations of the National Credit Union Administration (NCUA) and the Ohio Revised Code. Because of its structure, 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 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. Certain co-brokers also earn an incentive for referring institutions that issue certificates through the SimpliCD program. These incentives are recognized over the respective term of the certificate as a part of the Co-Broker spread and incentives as an adjustment to the spread.

The Company's office located at 700 Washington Street, Suite 202, Columbus, Indiana, 47201, has been designated an Office of Supervisory Jurisdiction (OSJ) of CU Investment Solutions LLC (ISI), a member of the Financial Industry Regulatory Authority (FINRA) and SIPC. ISI's home office is located at 8500 W 110th St, Suite 650, Overland Park, KS 66210.

## (2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### *(a) Use of Estimates*

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 and Cash Equivalents***

Cash and cash equivalents include demand deposits with Corporate One Federal Credit Union (Corporate One) and other financial institutions and short-term certificates of deposit, which may at times exceed federally insured limits. During 2017 and 2016, insurance coverage was $250,000 per depositor at each financial institution. The balance of cash and cash equivalents in excess of federally insured limits was approximately $22.4 million and $19.5 million, respectively. At December 31, 2017 and 2016, demand deposits held in interest bearing accounts at Corporate One totaled approximately $22.6 million and $19.8 million, respectively.

**(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, less the amount of spread received. This receivable is recorded upon placement of the certificates, along with the corresponding deferred spreads and co-broker spreads payable and the receivable is reduced as the spreads are received. The deferred spreads are recognized as revenue over the term of the certificates. Outstanding certificates of deposit placed by the Company on behalf of customers totaled $7,477,864,731 and $7,750,813,000 at December 31, 2017 and 2016, respectively.

**(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 on the maturity date. There were no advances as of December 31, 2017 or December 31, 2016.

**(e) *Goodwill***

Goodwill relates to the 2003 purchase of the Company from Corporate One. Management has elected not to amortize Goodwill, but instead performs an annual impairment test. The annual impairment test involves comparing the fair value of the Company to its carrying amount. If the fair value exceeds the carrying amount, goodwill is considered not to be impaired. The fair value of the Company is an estimate, as no ready market exists for the ownership interests of the Company. Such estimate of fair value is calculated based upon the present value of estimated future cash flows. There were no impairment losses in 2017 or 2016.

**f) *Fixed Assets***

Fixed assets are stated at cost less accumulated depreciation. Depreciation is computed using the straight-line method over the estimated useful life of the related asset. Equipment under construction is capitalized, however depreciation does not begin until the asset is placed in service. Maintenance and repairs are expensed as incurred. When assets are retired or otherwise disposed of, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is recognized as income. The lives of assets range from three to ten years. Fixed assets at December 31 are summarized as follows:

| | 2017 | 2016 |
|---|---|---|
| Under Construction | $ 37,641 | $ 1,250 |
| Computer Equipment | 3,119,720 | 3,119,720 |
| Furniture, Fixtures, Other | 462,299 | 234,553 |
| Total Cost | $ 3,619,660 | $ 3,355,523 |
| Less: Accumulated depreciation | ( 2,012,029) | ( 1,740,649) |
| Net Fixed Assets | $ 1,607,631 | $ 1,614,874 |

**(g) *Other Assets***

Included in other assets are accounts receivable, prepaid accounts, and deferred charges.

**(h) *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.

**(i) *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.

**(j) *Loss Contingencies***

Loss contingencies, including claims and legal actions arising in the ordinary course of business, are recorded as liabilities when the likelihood of loss is probable and an amount or range of loss can be reasonably estimated. Management does not believe there currently are such matters that will have a material effect on the financial statements.

### *(k) Subsequent Event*

Management has performed an analysis of activities and transactions subsequent to December 31, 2017 to determine the need for any adjustments to and/or disclosures within the audited financial statements for the year ended December 31, 2017. Management has performed such analysis through the date of the Independent Auditor's Report, the date which the financial statements were available to be issued.

## (3) RELATED PARTY TRANSACTIONS

The Company maintains deposit accounts and conducts cash management activities through one of its owners, Corporate One. Expenses related to the cash management activities totaled $58,868 and $71,645 for 2017 and 2016, respectively. The Company also maintains a line of credit with Corporate One. There were no expenses related to the line of credit in 2017 or 2016.

## (4) COMMITMENTS AND CONTINGENCIES

The Company and Corporate One have an agreement whereby Corporate One has extended an $8 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, 2017 and 2016, no advances were outstanding on the credit line.

The Company leases various office facilities under operating leases with remaining terms from one to ten years. The minimum annual rentals related to these agreements are as follows:

| | | |
|---|---|---|
| 2018 | $ | 102,526 |
| 2019 | $ | 65,151 |
| 2020 | $ | 65,151 |
| 2021 | $ | 65,151 |
| 2022 and beyond | $ | 359,537 |

## (5) 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, 2017 and 2016.

## (6) Retirement Plans

The Company's employees participate in a defined contribution plan in which the Company contributed a total of 11.5 percent of the participant's eligible compensation to the participant's account in the plan. Employees can also contribute a portion of their compensation on a pre- or post-tax basis. Retirement expense was $157,447 in 2017 and $171,234 in 2016.

The Company has non-qualified deferred compensation agreements with certain employees. Under such agreements the Company pays the premiums on life insurance policies that are owned by the employees. Under the terms of the agreements, though the employees own the policies, they are not fully vested in the cash value of such policies until 2021 to 2025, and the unvested cash value is pledged to the Company under a collateral assignment. Expense associated with these agreements was $225,416 in 2017 and $210,555 in 2016.

In addition, the Company has a long-term retention agreement with an executive officer. The performance and vesting provisions of the long-term retention agreement were met on December 31, 2017, and the amount due was paid to the executive on January 26, 2018. The Company accrued the expected cost of the agreement over the service period. Expense related to this agreement was $483,878 and $350,216 in 2017 and 2016, respectively.

## (7) Distribution

In December 2017, the Company declared a distribution of $1,125,000 ($15,000 per membership unit), payable during the first quarter of 2018 to members of record as of December 31, 2017. The distribution was paid on February 20, 2018. In December 2015, the Company declared a distribution of $2,250,000 ($30,000 per membership unit), payable during the first quarter of 2016 to members of record as of December 31, 2015. The distribution was paid on January 29, 2016. No distribution was declared in 2016.