
Primary Financial Company LLC
2001 Annual Report

# Primary Financial Company LLC 2001 Annual Report



**On the cover:** Sheila R. Ponder (on right), Senior Vice President and Chief Financial Officer, Telhio Credit Union, Columbus, Ohio; Tammy Cantrell, Senior Vice President and Chief Investment Officer, Corporate One Federal Credit Union.

**2001** was an exceptional year for Primary Financial Company LLC (Primary Financial). With the United States facing unprecedented challenges and the economy in decline, Primary Financial continued to strengthen relationships, expand its scope, and improve its ability to deliver great investment products and superior service. I'm pleased to provide you with this year's annual report, which documents the specific accomplishments that comprise Primary Financial's best year ever.

*Investing in federally insured CDs through the SimpliCD program just makes sense for my credit union. By purchasing SimpliCD through Primary Financial, I know I'll receive competitive rates and excellent service. With single-transaction settlement and consolidated reporting, SimpliCD makes investing easy.*

*Sheila R. Ponder*
*Senior Vice President, Chief Financial Officer*
*Telhio Credit Union*

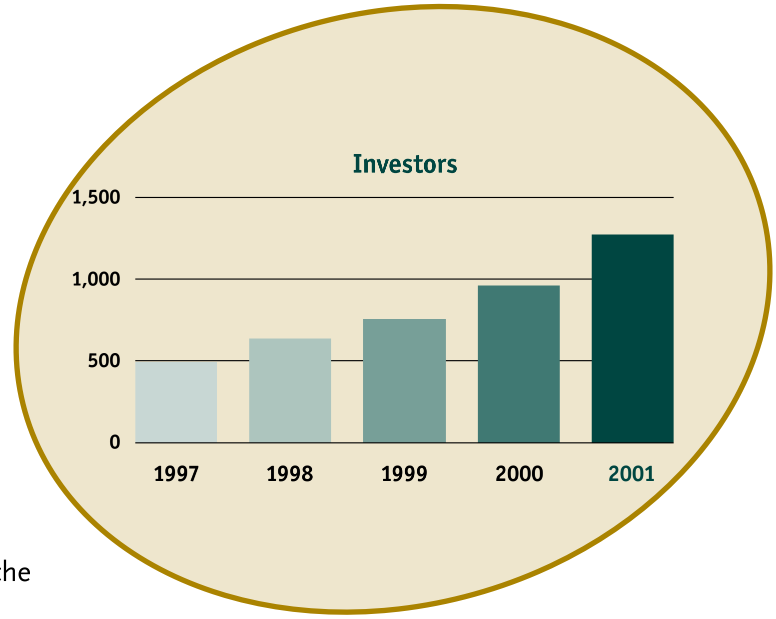
## Who We Are

Primary Financial is a wholly owned credit union service organization (CUSO) of Corporate One Federal Credit Union, and we're proud of the valuable role we play in serving the investment needs of the credit union movement. SimpliCD, our managed jumbo certificate program, has captured more than 8 percent of the market share of credit union deposits held at commercial banks, S&Ls, and other savings banks*. Our securities program, which we began in 2000, is also doing well, showing significant increases in trading volume. This remarkable success is thanks to our dedicated volunteer Board of Directors, a committed staff, and a growing network of SimpliCD co-agents that are spreading the message that Primary Financial provides its customers maximum yield with minimum effort.

*Peer to Peer©, Callahan and Associates, Credit Union data as of 12/31/01.

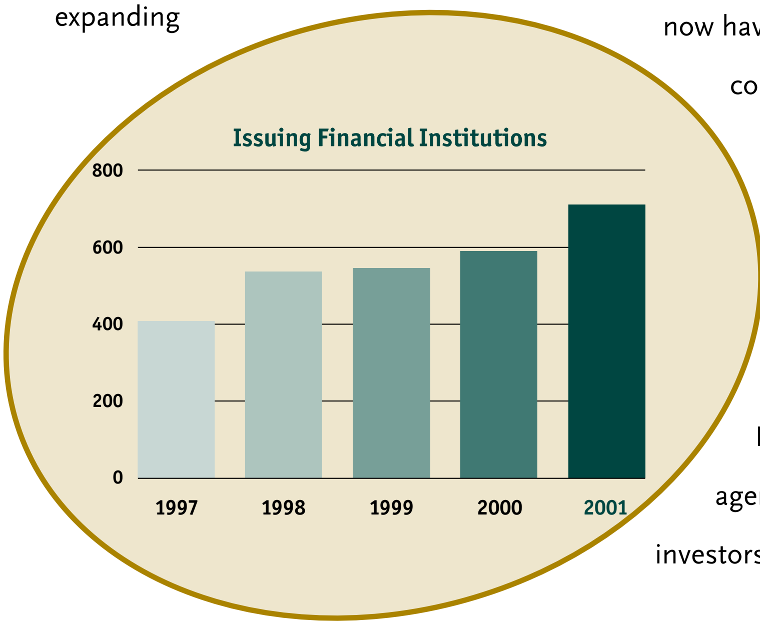
## SimpliCD

In 2001, placements for SimpliCD experienced triple digit growth, increasing 130 percent to $2.5 billion from $1.1 billion in 2000. Some of this growth can be attributed to last year's dramatic increase in liquidity. A record-setting influx of funds into the credit union network and multiple rate cuts by the Federal Reserve combined to enhance the market for brokered CDs.



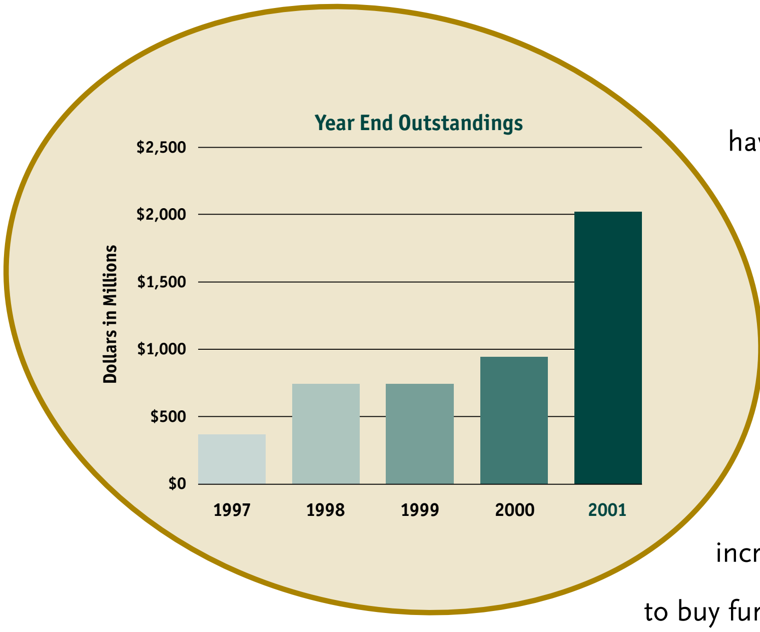

## Our Co-agents

Other growth can be attributed to our expanding distribution channel of co-agent partners. Placements from existing co-agent partners increased substantially last year, aided by three new corporate credit union co-agents that were added to our list of partners. We now have 24 co-agents, including 15 corporate credit unions, which serve clients in 35 states and the District of Columbia.




## Investors and Issuers

In addition to our growing list of co-agent partners, we continue to add new investors and issuers to the SimpliCD




program. Our number of investors increased to 1,272 in 2001 from 965 in 2000. We've also seen an increase in the number of issuing institutions as more credit unions and banks find Primary Financial offers a simple and reliable method to raise funds. In 2001, the number of issuers increased to 707 from 589 in 2000.

## Securities

In 2000, Primary Financial began offering securities by becoming an Office of Supervisory Jurisdiction (OSJ) through an arrangement with Westminster Financial Securities, Inc. As a result, credit unions now have access to treasuries, agencies and collateralized mortgage obligations (CMOs) through a trusted member of the credit union network. Last year, as the yield curve began to show signs of steepness, trading volume increased as more credit unions began to buy further out on the curve to take advantage of higher rates. This trend back to an historical shape, combined with an increasing recognition of our program, helped boost securities trading volume through Primary Financial by more than 700 percent. With economists projecting the yield curve to continue to steepen, we expect volume in this program to increase as more credit unions find us to be a convenient source for securities trading.

## Revenue

With all the growth in our SimpliCD program, it's no surprise that revenue at Primary Financial grew as well. Revenue in 2001 grew 84 percent from 2000, due to increased placements. This increase in revenue is impressive, but so is the amount of revenue earned by our co-agent partners. In 2001, co-agents earned approximately $1.3 million for placements. Clearly, one of the benefits of Primary Financial is our ability to harness the cooperative spirit of corporate credit unions to help both the natural-person credit union, and our co-agent partners. This win-win situation is what has driven our amazing success.

**Primary Financial Board of Directors – From left to right: (back) Mark D. Solomon; John J. Shirilla; Jerome R. Valco; (seated) Lee C. Butke, Chairman of the Board; Tammy E. Cantrell.**

## Looking Ahead

2001 was a record-setting year for Primary Financial, and we have no reason to expect less in 2002. As the markets begin to recover from last year's turmoil, we expect our SimpliCD placements and securities trading volume to increase as even more credit unions look to us as an innovative, convenient and reliable source for investing their excess funds. Primary Financial is a value-driven organization, with a focus on helping credit unions succeed.

**Primary Financial – Maximum Return with Minimum Effort**

Lee C. Butke

# 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, 2001 and 2000, and the related statements of income, changes in member's 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 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Primary Financial Company LLC as of December 31, 2001 and 2000 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 1, 2002

# Balance Sheets

| | December 31, | |
|---|---|---|
| **Assets** | **2001** | **2000** |
| Cash | $ 4,414,828 | $ 2,565,839 |
| Certificates held for resale | | 100,000 |
| Gross spreads receivable | 3,841,228 | 1,767,233 |
| Advances to customers | 848,000 | 799,000 |
| Other assets | 226,639 | 239,462 |
| TOTAL ASSETS | $ 9,330,695 | $ 5,471,534 |
| **Liabilities and Member's Equity** | | |
| Liabilities: | | |
| Deferred spreads | $ 2,857,604 | $ 1,262,033 |
| Co-broker and sales spreads payable | 1,082,634 | 520,331 |
| Amounts due to customers | 1,150,591 | 790,788 |
| Accounts payable and accrued expenses | 588,854 | 612,036 |
| TOTAL LIABILITIES | 5,679,683 | 3,185,188 |
| Member's Equity | 3,651,012 | 2,286,346 |
| TOTAL LIABILITIES AND MEMBER'S EQUITY | $ 9,330,695 | $ 5,471,534 |

See accompanying notes to financial statements.

# Statements of Income

| | Year ended December 31, | |
|---|---|---|
| | **2001** | **2000** |
| Revenue: | | |
| Spread income | $ 3,157,255 | $ 1,691,852 |
| Other | 53,650 | 56,280 |
| TOTAL REVENUE | 3,210,905 | 1,748,132 |
| Expenses: | | |
| Salaries and benefits | 1,145,702 | 803,016 |
| Office operations and occupancy | 268,251 | 207,558 |
| Settlement processing | 205,878 | 118,723 |
| Professional and other outside services | 122,411 | 86,542 |
| Other | 103,997 | 179,552 |
| TOTAL EXPENSES | 1,846,239 | 1,395,391 |
| NET INCOME | $ 1,364,666 | $ 352,741 |

See accompanying notes to financial statements.

# Statements of Changes in Member's Equity

| | Member's Equity |
|---|---|
| Balance at January 1, 2000 | $ 1,933,605 |
| Net income | 352,741 |
| Balance at December 31, 2000 | 2,286,346 |
| Net income | 1,364,666 |
| Balance at December 31, 2001 | $ 3,651,012 |

See accompanying notes to financial statements.

# Statements of Cash Flows

| | Year ended December 31, | |
|---|---|---|
| | **2001** | **2000** |
| Cash flows from operating activities: | | |
| Net income | $ 1,364,666 | $ 352,741 |
| Adjustments to reconcile net income to net cash provided by (used in) operating activities: | | |
| Depreciation and amortization | 34,247 | 56,007 |
| Net change in: | | |
| Gross spreads receivable | (2,073,995) | (383,147) |
| Certificates held for resale | 100,000 | |
| Other assets | (1,066) | (10,260) |
| Advances to customers | (49,000) | (799,000) |
| Amounts due to customers | 359,803 | (73,425) |
| Deferred spreads | 1,595,571 | 181,067 |
| Co-broker and sales spreads payable | 562,303 | 250,575 |
| Accounts payable and accrued expenses | (23,182) | 145,413 |
| NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES | 1,869,347 | (280,029) |
| Cash flows from investing activities: | | |
| Purchase of property and equipment | (20,358) | (4,418) |
| NET CASH USED IN INVESTING ACTIVITIES | (20,358) | (4,418) |
| Net increase (decrease) in cash | 1,848,989 | (284,447) |
| CASH AT BEGINNING OF YEAR | 2,565,839 | 2,850,286 |
| CASH AT END OF YEAR | $ 4,414,828 | $ 2,565,839 |

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 single member limited liability company (LLC) and is a credit union service organization (CUSO) of the sole member, Corporate One Federal Credit Union (Corporate One). The Company was established in accordance with the provisions of the National Credit Union Administration (NCUA) regulations and the Ohio Revised Code. As an LLC, the Company is not subject to federal income tax.

The Company is registered with the State of Ohio as a licensed securities dealer. The Company is engaged primarily in the sale of non-negotiable certificates of deposit with credit unions and other depository institutions for which it earns a spread over the term of the certificate.

The Company sells its product via its own direct sales staff, Corporate One's sales staff, as well as other co-brokers, mainly other corporate credit unions. The co-brokers earn a portion of the spread for certificates of deposit sold by the co-brokers.

The Company is also an Office of Supervisory Jurisdiction (OSJ) of Westminster Financial Securities, Inc. (Westminster), a National Association of Securities Dealers (NASD) registered broker/dealer. As an OSJ, the Company is subject to the jurisdiction of the Securities and Exchange Commission under the Securities and Exchange Act of 1934. This agreement allows the Company to offer its customers access to the government, agency and collateralized mortgage obligation markets. In connection with such securities sales activities, Westminster reimburses the company for certain administrative, marketing, record keeping, compliance and other costs. This expense reimbursement agreement is in lieu of the company receiving revenue in connection with these activities. The dollar amount of such reimbursement is limited to a percentage of the revenue generated for Westminster from the sale of securities by the Company and amounted to approximately $77,000 and $5,000 in 2001 and 2000, respectively.

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 and other financial institutions. At December 31, 2001, approximately $3.9 million was held in non-interest earning demand deposit accounts at Corporate One.

***(c) Certificates Held for Resale***

Certificates held for resale represent the Company's inventory of certificates of deposit. The certificates are held at cost which,approximates fair market value.

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

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

***(e) Advances to Customers***

Principal from certificates of deposit that have matured is generally received on the day of maturity and remitted to the customer. 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.

***(f) Amounts Due to Customers***

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

***(g) Co-broker Payable***

Co-broker 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. The net settlement of co-broker spread was approximately $1,259,000 and $616,000 for the years ended December 31, 2001 and December 31, 2000, respectively.

***(h) Reclassification***

Certain 2000 amounts have been reclassified to conform with 2001 presentation. These reclassifications had no effect on total revenues, total expenses, or net income.

**(2) RELATED PARTY TRANSACTIONS**

Corporate One provides various support to the Company including settlement, accounting, personnel administration, data processing, and office space, all of which are reimbursed by the Company. Reimbursement for these services was $378,000 and $325,000 in 2001 and 2000, respectively. There is no assurance that such transactions would have occurred under the same terms and conditions with an unrelated party.

## (3) COMMITMENTS AND CONTINGENCIES

The Company has entered into an agreement with Corporate One whereby Corporate One has extended a $1 million line of credit to the Company to be used to facilitate the settlement of customer transactions. The line is secured by the assets of the Company and the interest rate on the line is equal to the fed funds rate plus 40 basis points. This is the same rate Corporate One charges to other borrowers under similar lending agreements. At December 31, 2001 no advances were outstanding on this line.

The Company leases certain office facilities under operating agreements requiring the following minimum annual rentals:

| | |
|---|---|
| 2002 | $ 34,338 |
| 2003 | 35,539 |
| 2004 | 20,651 |
| Total | $ 90,528 |

## (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, 2001 and 2000.

## (5) PENSION PLAN

The Company's employees participate in two defined contribution plans which cover substantially all of its employees and the employees of Corporate One. One of the plans is a contributory plan, to which employees can contribute up to 10% of their compensation on a pre-tax basis. In 2001 and 2000, for each eligible participant, the Company contributed a total of 11.5% of the participant's eligible compensation to the participant's accounts in the plans. Retirement plan expense was approximately $86,000 in 2001 and $59,000 in 2000.

Primary Financial Company LLC

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