# National Securities Clearing Corporation

Condensed Financial Statements
as of March 31, 2018 and December 31, 2017 and for the
three months ended March 31, 2018 and 2017

# NATIONAL SECURITIES CLEARING CORPORATION

## TABLE OF CONTENTS

# NATIONAL SECURITIES CLEARING CORPORATION

**CONDENSED STATEMENTS OF FINANCIAL CONDITION (UNAUDITED)**

| **(In thousands, except share data)** | **As of March 31, 2018** | **As of December 31, 2017** |
|---|---|---|
| **ASSETS:** | | |
| CURRENT ASSETS: | | |
| Cash and cash equivalents | $ 3,697,599 | $ 3,623,482 |
| Participants' segregated cash | 32,267 | 20,120 |
| Accounts receivable | 27,828 | 28,689 |
| Clearing Fund | 8,715,955 | 3,991,770 |
| Other Participants' assets | 1,322 | 1,196 |
| Other current assets | 6,746 | 18,004 |
| Total current assets | 12,481,717 | 7,683,261 |
| NON-CURRENT ASSETS: | | |
| Premises and equipment - net of accumulated depreciation of $4,378 and $4,352 as of March 31, 2018 and December 31, 2017, respectively | 3,340 | 3,366 |
| Intangible assets - net of accumulated amortization of $99,618 and $96,035 as of March 31, 2018 and December 31, 2017, respectively | 26,968 | 27,606 |
| Total non-current assets | 30,308 | 30,972 |
| TOTAL ASSETS | $ 12,512,025 | $ 7,714,233 |
| **LIABILITIES AND SHAREHOLDER'S EQUITY:** | | |
| CURRENT LIABILITIES: | | |
| Commercial paper - net of unamortized discount of $5,644 and $3,371 as of March 31, 2018 and December 31, 2017, respectively | $ 3,242,850 | $ 3,222,571 |
| Accounts payable and accrued expenses | 6,793 | 1,868 |
| Clearing Fund | 8,715,955 | 3,991,770 |
| Payable to Participants | 33,589 | 21,316 |
| Other current liabilities | 7,232 | — |
| Total current liabilities | 12,006,419 | 7,237,525 |
| OTHER NON-CURRENT LIABILITIES: | | |
| Other non-current liabilities | 19,335 | 18,459 |
| Total liabilities | 12,025,754 | 7,255,984 |
| COMMITMENTS AND CONTINGENCIES (Note 9) | | |
| SHAREHOLDER'S EQUITY: | | |
| Common stock, $0.50 par value - 30,000 shares authorized; 20,000 shares issued and outstanding | 10 | 10 |
| Paid-in capital | 69,442 | 69,442 |
| Retained earnings | 416,819 | 388,797 |
| Total shareholder's equity | 486,271 | 458,249 |
| TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY | $ 12,512,025 | $ 7,714,233 |

The Notes to Condensed Financial Statements are an integral part of these statements.

# NATIONAL SECURITIES CLEARING CORPORATION

**CONDENSED STATEMENTS OF INCOME (UNAUDITED)**

| **(In thousands)** | **For the three months ended March 31, 2018** | **2017** |
|---|---|---|
| REVENUES: | | |
| Clearing services | $ 87,409 | $ 70,558 |
| Wealth management services | 28,375 | 27,208 |
| Other services | 989 | 785 |
| Total revenues | 116,773 | 98,551 |
| EXPENSES: | | |
| Employee compensation and related benefits | 33,773 | 28,742 |
| Information technology | 10,801 | 9,062 |
| Professional and other services | 25,612 | 24,600 |
| Occupancy | 2,575 | 1,940 |
| Depreciation and amortization | 3,609 | 5,729 |
| General and administrative | 1,921 | 1,526 |
| Total expenses | 78,291 | 71,599 |
| Total operating income | 38,482 | 26,952 |
| NON-OPERATING INCOME (EXPENSE): | | |
| Interest income | 40,595 | 15,950 |
| Refunds to Participants | (26,832) | (10,083) |
| Interest expense | (14,484) | (7,295) |
| Other non-operating income | 1,656 | 1,589 |
| Total non-operating income | 935 | 161 |
| Income before taxes | 39,417 | 27,113 |
| Provision for income taxes | 11,395 | 11,136 |
| Net income | $ 28,022 | $ 15,977 |

The Notes to Condensed Financial Statements are an integral part of these statements.

# NATIONAL SECURITIES CLEARING CORPORATION

**CONDENSED STATEMENTS OF CHANGES IN SHAREHOLDER'S EQUITY (UNAUDITED)**

| **(In thousands)** | **Common Stock** | **Paid-In Capital** | **Retained Earnings** | **Total Shareholder's Equity** |
|---|---|---|---|---|
| BALANCE - January 1, 2017 | $ 10 | $ 69,442 | $ 328,505 | $ 397,957 |
| Net income | — | — | 60,292 | 60,292 |
| BALANCE - December 31, 2017 | 10 | 69,442 | 388,797 | 458,249 |
| Net income | — | — | 28,022 | 28,022 |
| BALANCE - March 31, 2018 | $ 10 | $ 69,442 | $ 416,819 | $ 486,271 |

The Notes to Condensed Financial Statements are an integral part of these statements.

# NATIONAL SECURITIES CLEARING CORPORATION

**CONDENSED STATEMENTS OF CASH FLOWS (UNAUDITED)**

| **(In thousands)** | **For the three months ended March 31, 2018** | **2017** |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | $ 28,022 | $ 15,977 |
| Adjustments to reconcile net income to net cash provided by/(used in) operating activities: | | |
| Depreciation and amortization | 3,609 | 5,729 |
| Deferred income taxes | 366 | 526 |
| Net change in: | | |
| Accounts receivable | 861 | (531) |
| Other assets | 11,258 | 7,750 |
| Other Participants' assets | (126) | (188) |
| Accounts payable and accrued expenses | 4,925 | 3,389 |
| Other liabilities | 7,742 | 8,535 |
| Payable to Participants | 12,273 | 13,888 |
| Net cash provided by/(used in) operating activities | 68,930 | 55,075 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Sale/(Purchase) of securities under Reverse repurchase agreements | — | 100,000 |
| Change in Participants' segregated cash | (12,147) | (13,700) |
| Purchases of Intangible assets | (2,945) | (4,005) |
| Net cash provided by/(used in) investing activities | (15,092) | 82,295 |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Change in Commercial paper, net | 20,279 | (11,160) |
| Net cash provided by/(used in) financing activities | 20,279 | (11,160) |
| Net increase/(decrease) in Cash and cash equivalents | 74,117 | 126,210 |
| Cash and cash equivalents - Beginning of period | 3,623,482 | 2,767,668 |
| Cash and cash equivalents - End of period | $ 3,697,599 | $ 2,893,878 |
| SUPPLEMENTAL DISCLOSURE: | | |
| Cash interest paid | $ 12,059 | $ 5,820 |

The Notes to Condensed Financial Statements are an integral part of these statements.

## 1. BUSINESS AND OWNERSHIP

National Securities Clearing Corporation (NSCC or the Company) is organized as a business corporation under New York law, and is a clearing agency registered with the U.S. Securities and Exchange Commission (SEC). NSCC provides clearing, settlement, risk management, and central counterparty (CCP) services to its members (collectively referred to as Participants) for broker-to-broker trades involving equities, corporate and municipal debt, exchange-traded funds, and unit investment trusts.

NSCC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (DTCC). Other subsidiaries of DTCC include The Depository Trust Company (DTC), Fixed Income Clearing Corporation (FICC), DTCC ITP LLC (formerly known as Omgeo LLC), DTCC Deriv/SERV LLC, Business Entity Data, B.V. and DTCC Solutions LLC.

NSCC is designated as a Systemically Important Financial Market Utility (SIFMU) by the U.S. Financial Stability Oversight Council pursuant to Title VIII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, which subjects the Company to the SEC's standards for covered clearing agencies.

## 2. BASIS OF PRESENTATION AND USE OF ESTIMATES

**Basis of presentation.** The accompanying Condensed Financial Statements are prepared in accordance with generally accepted accounting principles in the United States of America (U.S. GAAP). The accompanying interim financial statements have not been audited. These interim financial statements do not include all of the information and notes required by U.S. GAAP for complete financial statements and should be read in conjunction with NSCC's Audited Financial Statements for the years ended December 31, 2017 and 2016, which are located on the Company's website at *http://www.dtcc.com/legal/financial-statements*. See Note 2 in NSCC's Audited Financial Statements for the years ended December 31, 2017 and 2016, for additional information on the Company's Summary of Significant Accounting Policies.

The Condensed Financial Statements reflect all adjustments of a normal recurring nature that are, in the opinion of management, necessary for the fair presentation of the results for the interim period. The results of operations for interim periods are not necessarily indicative of results for the entire year.

The Company reclassified prior period amounts related to Refunds to Participants and certain components of net periodic pension cost to conform to the current year presentation. See below Revenue recognition and Note 3 for additional information.

**Use of estimates.** The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the amounts reported in the Condensed Financial Statements. Management makes estimates regarding, among other things, the collectability of receivables, the outcome of litigation, the realization of deferred taxes, unrecognized tax benefits, fair value measurements and other matters that affect the reported amounts. Estimates are based on judgment and available information; therefore, actual results could differ materially from those estimates.

**Revenue recognition.** The core principle of the new revenue recognition standard is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. To achieve that principle, the entity applies the following steps: identify the contract(s) with the customer, identify the performance obligations in the contract(s), determine the transaction price, allocate the transaction price to the performance obligations in the contract and recognize revenue when (or as) the entity satisfies a performance obligation. See Note 3 for additional information.

The Company enters into contracts that can include various services, in which each service, an explicit promise, is generally distinct and accounted for as separate performance obligations. Certain promised services are substantially the same and have the same pattern of transfer to the customer and therefore are considered as a series of services.

In accordance with the new revenue recognition standard, the Company recognizes revenue from contracts with customers as performance obligations are satisfied when promised services are transferred to the customer. The majority of the promised services and related performance obligations are recognized at the point in time when the control of the promised service is transferred to the customer. The amount of revenue recognized reflects the consideration the Company expects to be entitled to for transferring the promised services to the customer. For certain contracts with customers, the consideration in which the Company expects to be entitled to in exchange for transferring promised service to a customer consists of variable consideration. The variable consideration primarily relates to volume based discounts for certain services however, the volume targets or thresholds typically reset on a monthly basis therefore, the variable consideration does not have an impact on the Company's Condensed Financial Statements.

The Company derives its revenue from transaction fees and other services. Revenue from transaction fees is recognized at a point in time on the transaction date, as the customer obtains the control and benefit of the service at that point. Other services represents fees generated from providing various support services and is recognized when services are provided based on contractual terms. The Company typically bills its customers 30 days in arrears.

***Revenue streams***

Details for each revenue stream presented in the Company's Condensed Statements of Income follow:

*Clearing services.* The Company delivers clearing services across the U.S. equities markets. Clearing services include continuous net settlement and mortgage backed securities clearing.

*Wealth management services*. Drives centralized, automated processing and information services. Provides seamless, end-to-end communications with broker/dealers and other distribution partners are enabled for funds, asset managers and insurance companies and their service providers. Wealth management services include mutual fund, alternative investment, and insurance and retirement services.

*Other services.* DTCC DataPro™ offers referential and activity-based data, delivered in fixed or configurable formats, sourced from the Company's transaction, reference and position. Other services include data on market and benchmark analytics and security reference.

***Accounts receivable and contract balances***

The period in which the Company recognizes revenue may differ from the timing of payments received from customers. The Company records a receivable when revenue is recognized prior to payment and there is an unconditional right to payment. See Accounts receivable on the Condensed Statements of Financial Condition for the Company's receivables related to revenues from contracts with customers. Alternatively, when payment precedes the provision of the related services, the Company records deferred revenue until the performance obligations are satisfied. Deferred revenue represents the Company's contract liabilities related to billings or payments received in advance for other services, where the performance obligation has not yet been satisfied.

***Impacts to previously reported results***

On January 1, 2018, the Company adopted the new revenue recognition standard under the full retrospective method of adoption. See Note 3 for additional information.

Details of the revenue recognition impact to the Company's previously reported results for the three months ended March 31, 2017 follow (in thousands):

| | As Previously Reported | New Revenue Standard Adjustment | As Restated |
|---|---|---|---|
| Interest income | $ 5,867 | $ 10,083 | $ 15,950 |
| Refunds to Participants | — | (10,083) | (10,083) |

## 3. ACCOUNTING AND REPORTING DEVELOPMENTS

See Note 3 in NSCC's Audited Financial Statements for the years ended December 31, 2017 and 2016, for additional information on the Company's Accounting and Reporting Developments.

| Standard | Description | Impact on the financial statements or other significant matters |
|---|---|---|
| *Recently Adopted Accounting Standards* | | |
| Revenue Recognition - Revenue from Contracts with Customers<br><br>*Issued May 2014* | • Requires revenue from contracts with customers to be recognized upon transfer of control of a good or service in the amount of consideration expected to be received.<br><br>• Changes the accounting for certain contract costs, including whether they may be offset against revenue in the accompanying Condensed Statements of Income, and requires additional disclosures about revenue and contract costs.<br><br>• May be adopted using a full retrospective approach or a modified, cumulative effect approach wherein the guidance is applied only to existing contracts as of the day of initial application, and to new contracts transacted after that date. | • Adopted January 1, 2018.<br><br>• The Company adopted the revenue recognition standard under the full retrospective transition method of adoption.<br><br>• The Company's implementation efforts included the identification of revenue within the scope of the standard and the evaluation of revenue contracts using the practical expedient portfolio approach.<br><br>• The adoption of the standard did not have a material impact to the recognition and timing of its revenues, but required the Company to change the presentation of Interest Income and Refunds to Participants from a net basis to a gross basis in the accompanying Condensed Statements of Income. |
| Compensation - Retirement Benefits<br><br>Issued March 2017 | • Requires the service cost component of net periodic pension and postretirement benefit cost to be reported separately in the Company's Condensed Statements of Income<br><br>• Requires retrospective application and presentation in the Condensed Statements of Income.<br><br>• Requires the service cost component in the same line item as other employee compensation costs and presentation of the other components in a different line item from the service cost component. | • Adopted January 1, 2018.<br><br>• The adoption of the standard and required reclassification did not have a material impact or a change to the Company's Condensed Statements of Income. The adoption required the Company to reclassify certain components of net periodic pension cost from Total operating income to Total non-operating income (expense). The service cost component is presented in Employee compensation and related benefits, the interest cost component is presented in Interest expense, and all other components of net periodic pension cost are presented in Other non-operating income (expense) in the accompanying Condensed Statements of Income. |

## 4. PARTICIPANTS' SEGREGATED CASH, OTHER PARTICIPANTS' ASSETS AND PAYABLE TO PARTICIPANTS

Details for Participants' segregated cash, Other Participants' assets and Payable to Participants as of March 31, 2018 and December 31, 2017 follow (in thousands):

| | 2018 | 2017 |
|---|---|---|
| Assets: | | |
| Participants' segregated cash | $ 32,267 | $ 20,120 |
| Other Participants' assets | 1,322 | 1,196 |
| Total | $ 33,589 | $ 21,316 |
| Liabilities: | | |
| Payable to Participants | $ 33,589 | $ 21,316 |

Participants' segregated cash represents cash received from Participants to facilitate their compliance with SEC customer protection rules. Unclaimed balances are remitted to the appropriate authority when required by abandoned property laws.

## 5. CLEARING FUND

Details for the Clearing Fund deposits as of March 31, 2018 and December 31, 2017 follow (in thousands):

| | 2018 | 2017 |
|---|---|---|
| Required deposits | $ 8,119,996 | $ 3,360,160 |
| Excess deposits | 595,959 | 631,610 |
| Total | $ 8,715,955 | $ 3,991,770 |

Details for the Clearing Fund deposits as of March 31, 2018 and December 31, 2017 follow (in thousands):

| | 2018 | 2017 |
|---|---|---|
| Cash deposits | $ 8,321,580 | $ 3,725,574 |
| Securities on deposit - at fair value | 394,375 | 266,196 |
| Total | $ 8,715,955 | $ 3,991,770 |

Details for the Clearing Fund Cash deposits as of March 31, 2018 and December 31, 2017 follow (in thousands):

| | 2018 | 2017 |
|---|---|---|
| Bank deposits | $ 6,745,580 | $ 2,820,574 |
| Money market fund investments | 1,341,000 | 595,000 |
| Reverse repurchase agreements | 235,000 | 310,000 |
| Total | $ 8,321,580 | $ 3,725,574 |

**Clearing Fund Cash deposits**. Participant Cash deposits of the Clearing Fund may be applied to satisfy obligations of the depositing Participants, as provided in NSCC's rules.

**Refunds to Participants.** Interest income earned from the investment of Clearing Fund deposits is refunded to Participants and totaled $26,832,000 and $10,083,000 for the three months ended March 31, 2018 and 2017, respectively. The amounts refunded are included in Refunds to Participants in the accompanying Condensed Statements of Income. See Revenue recognition section of Note 2 and Note 3 for additional information.

## 6. COMMERCIAL PAPER

Details for Commercial paper as of March 31, 2018 and December 31, 2017 follow (in thousands):

| | 2018 | 2017 |
|---|---|---|
| Commercial paper - net of unamortized discount of \$5,644 and \$3,371 as of March 31, 2018 and December 31, 2017, respectively | \$ 3,242,850 | \$ 3,222,571 |
| Weighted-average interest rate | 1.88% | 1.43% |

Interest expense on Commercial paper included in the accompanying Condensed Statements of Income was \$12,483,000 and \$5,486,000 for the three months ended March 31, 2018 and 2017, respectively.

Details for the cash flows associated with the issuance and maturities of Commercial paper for the three months ended March 31, 2018 and 2017 follow (in thousands):

| | 2018 | 2017 |
|---|---|---|
| Maturities less than 90 days: | | |
| Proceeds from/(Repayments of) Commercial paper less than 90 days, net | \$ (71,034) | \$ 68,999 |
| Maturities greater than 90 days: | | |
| Proceeds from Commercial paper | 551,005 | 574,246 |
| Repayments of Commercial paper | (459,692) | (654,405) |
| Proceeds from/(Repayments of) Commercial paper greater than 90 days, net | 91,313 | (80,159) |
| Change in Commercial paper, net | \$ 20,279 | \$ (11,160) |

## 7. DEBT

**Line of credit.** The Company maintains a line of credit to support settlement. Details for the terms of the outstanding line of credit as of March 31, 2018 and December 31, 2017 follow:

| | 2018 | 2017 |
|---|---|---|
| **Committed Amount** | \$12.2 billion | \$12.2 billion |
| **Number of Participants/Lenders** | 32/41 | 32/41 |

There were no borrowings under the line of credit as of March 31, 2018 and December 31, 2017.

Details for debt covenants related to the line of credit as of March 31, 2018 and December 31, 2017 follow:

| | 2018 | 2017 |
|---|---|---|
| **Minimum Net Worth** | \$125 million | \$125 million |
| **Minimum Clearing Fund deposits** | \$1 billion | \$1 billion |

As of March 31, 2018 and December 31, 2017, the Company was in compliance with its debt covenants.

**Credit Ratings.** The Company is rated by Moody's Investors Service, Inc. (Moody's) and S&P Global Inc. (S&P). Details for senior debt ratings and ratings outlooks for the Company as of March 31, 2018 follow:

| Moody's (1) | | | S&P | | |
|---|---|---|---|---|---|
| **Long-term** | **Short-term** | **Outlook** | **Long-term** | **Short-term** | **Outlook** |
| Aaa | P-1 | Stable | AA+ | A-1+ | Stable |

(1) Moody’s categorizes the long-term issuer ratings of the Company as a clearing counterparty rating (CCR) under the agency's Clearing Houses Rating Methodology.

## 8. PENSION AND POSTRETIREMENT BENEFITS

Eligible DTCC employees participate in DTCC's trusteed non-contributory defined benefit pension plan, supplemental executive retirement plan and benefit restoration plan, which provide for certain benefits upon retirement. Eligible DTCC employees also participate in DTCC's life insurance program, which provides for the payment of death benefits to beneficiaries of eligible retired employees, and DTCC's health care program, which provides benefits to eligible retired employees.

**Cost allocation.** DTCC allocates the cost of these plans to its subsidiaries based primarily upon the estimated proportion of each subsidiary's salary cost relative to DTCC's total salary cost. The benefit plan costs allocated to NSCC were $749,000 and $663,000 for the three months ended March 31, 2018 and 2017, respectively. These costs are included in Employee compensation and related benefits, Interest expense, and Other non-operating income in the accompanying Condensed Statements of Income.

## 9. COMMITMENTS AND CONTINGENCIES

**Litigation.** The Company is involved in legal proceedings and litigation arising in the ordinary course of business. In the opinion of management, the outcome of such proceedings and litigation is not expected to have a material effect on the accompanying Condensed Statements of Financial Condition, Income or Cash Flows.

## 10. GUARANTEES

NSCC provides CCP services, including clearing, settlement and risk management services. Acting as a CCP, NSCC guarantees the settlement of trades in the event one or more of its Participants defaults. A Participant default is defined in NSCC's rules. In its guarantor role, NSCC has equal claims to and from Participants on opposite sides of netted transactions. To cover its guarantee risk, NSCC uses risk-based margining to collect cash and securities collateral through its Clearing Fund. NSCC's trade guaranty attaches at the point of validation for locked-in submissions, or at the point of comparison and validation for bilateral submissions.

Details for certain NSCC's open positions for which a trade guarantee applied as of March 31, 2018 and December 31, 2017 follow (in billions):

| | 2018 | 2017 |
|---|---|---|
| NSCC | $ 191 | $ 135 |

There were no defaults by Participants to these obligations.

See Note 15 in NSCC's Audited Financial Statements for the years ended December 31, 2017 and 2016 for additional information.

## 11. SUBSEQUENT EVENTS

The Company evaluated events and transactions occurring after March 31, 2018 through April 27, 2018, for potential recognition or disclosure in these accompanying Condensed Financial Statements. No events or transactions occurred during such period that would require recognition or disclosure in these accompanying Condensed Financial Statements.