

Fixed Income Clearing Corporation

Financial Statements as of September 30, 2019 and
December 31, 2018 and for the three and nine months ended
September 30, 2019 and 2018

FIXED INCOME CLEARING CORPORATION

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FIXED INCOME CLEARING CORPORATION
STATEMENTS OF FINANCIAL CONDITION (UNAUDITED)

(In thousands, except share data)	As of September 30, 2019	As of December 31, 2018
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 296,382	\$ 265,724
Accounts receivable	12,176	9,802
Clearing Fund	27,678,870	26,522,224
Other Participants' assets	1,370	1,618
Other current assets	4,425	7,661
Total current assets	<u>27,993,223</u>	<u>26,807,029</u>
NON-CURRENT ASSETS:		
Premises and equipment - net of accumulated depreciation of \$320 and \$304 as of September 30, 2019 and December 31, 2018, respectively	664	680
Intangible assets - net of accumulated amortization of \$33,944 and \$77,740 as of September 30, 2019 and December 31, 2018, respectively	40,697	27,117
Total non-current assets	<u>41,361</u>	<u>27,797</u>
TOTAL ASSETS	<u><u>\$ 28,034,584</u></u>	<u><u>\$ 26,834,826</u></u>
LIABILITIES AND SHAREHOLDER'S EQUITY		
CURRENT LIABILITIES:		
Accounts payable and accrued expenses	\$ 12,239	\$ 10,328
Clearing Fund	27,678,870	26,522,224
Payable to Participants	1,370	1,618
Other current liabilities	1,297	—
Total current liabilities	<u>27,693,776</u>	<u>26,534,170</u>
OTHER NON-CURRENT LIABILITIES:		
Other non-current liabilities	14,331	12,358
Total liabilities	<u>27,708,107</u>	<u>26,546,528</u>
COMMITMENTS AND CONTINGENCIES (Note 2)		
SHAREHOLDER'S EQUITY		
Common stock, \$0.50 par value - 105,000 shares authorized; 20,400 shares issued and outstanding	10	10
Paid-in capital	86,617	86,617
Retained earnings	239,850	201,671
Total shareholder's equity	<u>326,477</u>	<u>288,298</u>
TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	<u><u>\$ 28,034,584</u></u>	<u><u>\$ 26,834,826</u></u>

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

FIXED INCOME CLEARING CORPORATION**STATEMENTS OF INCOME (UNAUDITED)**

(In thousands)	For the three months ended September 30,		For the nine months ended September 30,	
	2019	2018	2019	2018
REVENUES				
Clearing services	\$ 76,530	\$ 62,359	\$ 224,027	\$ 194,482
Other services	(227)	97	105	269
	<u>76,303</u>	<u>62,456</u>	<u>224,132</u>	<u>194,751</u>
EXPENSES				
Employee compensation and related benefits	24,865	20,098	70,494	62,084
Information technology	4,322	4,116	12,758	12,140
Professional and other services	25,873	23,247	74,022	71,708
Occupancy	1,275	1,247	3,719	3,620
Depreciation and amortization	1,713	1,776	5,094	5,583
General and administrative	3,254	2,904	9,648	9,228
Total expenses	<u>61,302</u>	<u>53,388</u>	<u>175,735</u>	<u>164,363</u>
Total operating income	<u>15,001</u>	<u>9,068</u>	<u>48,397</u>	<u>30,388</u>
NON-OPERATING INCOME (EXPENSE)				
Interest income	37,885	38,959	122,589	117,367
Refunds to Participants	(36,430)	(37,737)	(118,016)	(114,353)
Interest expense	(1,245)	(1,130)	(3,718)	(3,439)
Other non-operating income	815	990	3,681	2,900
Total non-operating income	<u>1,025</u>	<u>1,082</u>	<u>4,536</u>	<u>2,475</u>
Income before taxes	16,026	10,150	52,933	32,863
Provision (benefit) for income taxes	4,415	(1,071)	14,754	5,652
Net income	<u>\$ 11,611</u>	<u>\$ 11,221</u>	<u>\$ 38,179</u>	<u>\$ 27,211</u>

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

FIXED INCOME CLEARING CORPORATION

STATEMENTS OF CHANGES IN SHAREHOLDER'S EQUITY (UNAUDITED)

<u>(In thousands)</u>	<u>Common Stock</u>	<u>Paid-In Capital</u>	<u>Retained Earnings</u>	<u>Total Shareholder's Equity</u>
BALANCE - January 1, 2019	\$ 10	\$ 86,617	\$ 201,671	\$ 288,298
Net income	—	—	12,586	12,586
BALANCE - March 31, 2019	10	86,617	214,257	300,884
Net income	—	—	13,982	13,982
BALANCE - June 30, 2019	10	86,617	228,239	314,866
Net income	—	—	11,611	11,611
BALANCE - September 30, 2019	<u>\$ 10</u>	<u>\$ 86,617</u>	<u>\$ 239,850</u>	<u>\$ 326,477</u>

<u>(In thousands)</u>	<u>Common Stock</u>	<u>Paid-In Capital</u>	<u>Retained Earnings</u>	<u>Total Shareholder's Equity</u>
BALANCE - January 1, 2018	\$ 10	\$ 86,617	\$ 166,982	\$ 253,609
Net income	—	—	8,290	8,290
BALANCE - March 31, 2018	10	86,617	175,272	261,899
Net income	—	—	7,700	7,700
BALANCE - June 30, 2018	10	86,617	182,972	269,599
Net income	—	—	11,221	11,221
BALANCE - September 30, 2018	<u>\$ 10</u>	<u>\$ 86,617</u>	<u>\$ 194,193</u>	<u>\$ 280,820</u>

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

FIXED INCOME CLEARING CORPORATION

STATEMENTS OF CASH FLOWS (UNAUDITED)

(In thousands)	For the nine months ended September 30,	
	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 38,179	\$ 27,211
Adjustments to reconcile net income to net cash provided by/(used in) operating activities:		
Depreciation and amortization	5,094	5,583
Loss on Impairment of Intangible assets	97	—
Discount on investments in marketable securities	—	(46)
Deferred income taxes	1,635	3,020
Net change in:		
Accounts receivable	(2,374)	1,975
Other assets	3,236	3,132
Other Participants' assets	382	—
Accounts payable and accrued expenses	1,911	3,111
Other liabilities	1,635	(7,476)
Clearing Fund liabilities, net	2,454,224	(2,705,841)
Payable to Participants	(248)	137
Net cash provided by/(used in) operating activities	<u>2,503,771</u>	<u>(2,669,194)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Maturities of investments in marketable securities	—	75,000
Purchases of investments in marketable securities	—	(50,000)
Capitalized software development costs	(18,755)	(12,162)
Net cash provided by/(used in) investing activities	<u>(18,755)</u>	<u>12,838</u>
Net increase/(decrease) in Cash and cash equivalents, Clearing Fund cash deposits, Cash in Other Participants' assets	2,485,016	(2,656,356)
Cash and cash equivalents, Clearing Fund cash deposits, Cash in Other Participants' assets - Beginning of period	<u>7,114,232</u>	<u>9,053,091</u>
Cash and cash equivalents, Clearing Fund cash deposits, Cash in Other Participants' assets - End of period	<u>\$ 9,599,248</u>	<u>\$ 6,396,735</u>
SUPPLEMENTAL DISCLOSURE:		
Income taxes paid - net of refunds	<u>\$ 10,011</u>	<u>\$ 6,016</u>

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

FIXED INCOME CLEARING CORPORATION

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

AS OF SEPTEMBER 30, 2019 AND DECEMBER 31, 2018 AND FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018

1. BUSINESS AND OWNERSHIP

Fixed Income Clearing Corporation (FICC or the Company), a clearing agency registered with the U.S. Securities and Exchange Commission (SEC), provides central counterparty (CCP) services to firms that participate in the U.S. government and mortgage-backed securities markets (collectively referred to as Participants). Services provided by FICC consist principally of automated real-time trade comparison, netting, settlement, trade confirmation, risk management and electronic pool notification. FICC has two Divisions, the Government Securities Division (GSD) and the Mortgage-Backed-Securities Division (MBSD).

FICC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (DTCC). Other subsidiaries of DTCC include The Depository Trust Company (DTC), National Securities Clearing Corporation (NSCC), DTCC ITP LLC, DTCC Deriv/SERV LLC and DTCC Solutions LLC.

FICC 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 enhanced standards for operation and governance, as established by the SEC's Standards for Covered Clearing Agencies (CCAS).

2. BASIS OF PRESENTATION AND USE OF ESTIMATES

Basis of presentation. The accompanying unaudited Financial Statements (interim 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 exclude some of the disclosures required in audited financial statements and should be read in conjunction with FICC's Audited Financial Statements for the years ended December 31, 2018 and 2017, which are located on the Company's website at <http://www.dtcc.com/legal/financial-statements>. See Note 2 in FICC's Audited Financial Statements for the years ended December 31, 2018 and 2017, for additional information on the Company's Summary of Significant Accounting Policies.

The 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.

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 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, expense allocations 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.

Commitments and Contingencies. 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 Statements of Financial Condition, Income or Cash Flows.

FIXED INCOME CLEARING CORPORATION

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

AS OF SEPTEMBER 30, 2019 AND DECEMBER 31, 2018 AND FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018

2. BASIS OF PRESENTATION AND USE OF ESTIMATES (CONTINUED)

Revenue recognition. 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, which represent fees generated from offering referential based data and business processing solutions to financial institutions globally, is recognized when services are provided based on contractual terms.

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

Clearing services. The Company delivers clearing services across the fixed income markets. Clearing services include mortgage backed securities clearing and government securities clearing.

Other services. The Company offers referential and activity-based, announcement, security reference, and liquidity data through the DTCC Data Services product. These offerings are delivered in fixed or configurable formats, sourced from the Company's transaction, reference, position and asset servicing data.

Expense allocations. Substantially all expenses are recorded at DTCC and are allocated to its subsidiaries, including FICC, based upon their estimated use of such goods or services as determined by various allocation factors including direct expenses, level of support provided and utilization of technology resources. Accordingly, the expenses in the accompanying Statements of Income represent allocated costs including Employee compensation and related benefits, Information technology, Professional and other services, Occupancy, Depreciation and amortization and General and administrative.

Impacts to previously reported results. The Company reclassified prior period amounts related to allocated depreciation and amortization to conform to the current year presentation. This reclassification had no impact on previously reported total assets, total liabilities, revenues, net income, and cash flows.

The impact of the change in presentation for allocated depreciation and amortization on the Company's previously reported results for the three and nine months ended September 30, 2018 follows (in thousands):

	For the three months ended September 30, 2018			For the nine months ended September 30, 2018		
	As Previously Reported	Reclassification Presentation Adjustment	As Restated	As Previously Reported	Reclassification Presentation Adjustment	As Restated
Information technology	\$ 5,775	\$ (1,659)	\$ 4,116	\$ 17,271	\$ (5,131)	\$ 12,140
Occupancy	1,591	(344)	1,247	4,661	(1,041)	3,620
General and administrative	901	2,003	2,904	3,056	6,172	9,228

FIXED INCOME CLEARING CORPORATION

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

AS OF SEPTEMBER 30, 2019 AND DECEMBER 31, 2018 AND FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018

2. BASIS OF PRESENTATION AND USE OF ESTIMATES (CONTINUED)

Restricted cash. The Company has reported the cash and cash equivalents related to Clearing Fund cash deposits, Other Participants' assets within the beginning and ending balances of Cash and cash equivalents, Clearing Fund cash deposits, Other Participants' assets on the accompanying Statements of Cash Flows.

A reconciliation of Cash and cash equivalents, Clearing Fund cash deposits, Cash in Other Participants' assets, reported within the accompanying Statements of Financial Condition that sum to the total of the same such amounts shown on the accompanying Statements of Cash Flows follows (in thousands):

	September 30, 2019	December 31, 2018	September 30, 2018
Cash and cash equivalents	\$ 296,382	\$ 265,724	\$ 261,270
Clearing Fund cash deposits	9,301,496	6,847,272	6,135,027
Cash in Other Participants' assets	1,370	1,236	438
Total Cash and cash equivalents, Clearing Fund cash deposits, Cash in Other Participants' assets shown on the Statement of Cash Flows	\$ 9,599,248	\$ 7,114,232	\$ 6,396,735

As a result of this accounting change, net cash provided by operating activities of approximately \$2,504 million is primarily driven by the change in Clearing Fund liabilities and Payable to Participants.

3. ACCOUNTING AND REPORTING DEVELOPMENT

See Note 3 in FICC's Audited Financial Statements for the years ended December 31, 2018 and 2017, for additional information on the Company's Accounting and Reporting Developments.

Standard	Description	Impact on the financial statements or other significant matters
<i>Financial Accounting Standards Board Standard Issued, but not yet Adopted</i>		
ASU 2019-05 Financial Instruments - Credit Losses: Targeted Transition Relief <i>Issued May 2019</i>	<ul style="list-style-type: none">Provides entities with an option upon adoption of ASU 2016-13 <i>Customer's Financial Instruments - Credit Losses</i> to irrevocably elect the fair value option on an instrument-by-instrument basis for certain financial instruments that are both within the scope of the current expected credit loss and eligible for the fair value option.	<ul style="list-style-type: none">Effective January 1, 2020.The Company does not intend to elect the fair value option on any instrument within the scope and therefore no impact is expected.

FIXED INCOME CLEARING CORPORATION**NOTES TO FINANCIAL STATEMENTS (UNAUDITED)**

AS OF SEPTEMBER 30, 2019 AND DECEMBER 31, 2018 AND FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018

4. CLEARING FUND

Details for the Clearing Fund deposits as of September 30, 2019 and December 31, 2018 follow (in thousands):

	2019			2018		
	GS Division	MBS Division	Total	GS Division	MBS Division	Total
Required deposits	\$ 15,675,833	\$ 4,040,573	\$ 19,716,406	\$ 13,576,152	\$ 4,477,522	\$ 18,053,674
Excess deposits	6,192,312	1,770,152	7,962,464	7,029,000	1,439,550	8,468,550
Total	<u>\$ 21,868,145</u>	<u>\$ 5,810,725</u>	<u>\$ 27,678,870</u>	<u>\$ 20,605,152</u>	<u>\$ 5,917,072</u>	<u>\$ 26,522,224</u>

Details for the Clearing Fund deposits as of September 30, 2019 and December 31, 2018 follow (in thousands):

	2019			2018		
	GS Division	MBS Division	Total	GS Division	MBS Division	Total
Securities on deposit - at fair value	\$ 14,721,506	\$ 3,655,868	\$ 18,377,374	\$ 15,253,927	\$ 4,421,025	\$ 19,674,952
Cash deposits	7,146,639	2,154,857	9,301,496	5,351,225	1,496,047	6,847,272
Total	<u>\$ 21,868,145</u>	<u>\$ 5,810,725</u>	<u>\$ 27,678,870</u>	<u>\$ 20,605,152</u>	<u>\$ 5,917,072</u>	<u>\$ 26,522,224</u>

Details for the Clearing Fund cash deposits as of September 30, 2019 and December 31, 2018 follow (in thousands):

	2019	2018
Bank deposits	\$ 7,200,496	\$ 5,466,272
Money market fund investments	1,601,000	931,000
Reverse repurchase agreements	500,000	450,000
Total	<u>\$ 9,301,496</u>	<u>\$ 6,847,272</u>

Clearing Fund cash deposits. Cash deposits of the Clearing Fund, may be applied to satisfy obligations of the depositing Participant, other Participants, or the Company as provided in FICC's rules.

5. OTHER PARTICIPANTS' ASSETS AND PAYABLE TO PARTICIPANTS

Details for Other Participants' assets and Payable to Participants as of September 30, 2019 and December 31, 2018 follow (in thousands):

	2019	2018
Assets:		
Other Participants' assets:		
Cash	\$ 1,370	\$ 1,236
Other	—	382
Total Other Participants' assets	<u>\$ 1,370</u>	<u>\$ 1,618</u>
Liabilities:		
Payable to Participants	<u>\$ 1,370</u>	<u>\$ 1,618</u>

FIXED INCOME CLEARING CORPORATION

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

AS OF SEPTEMBER 30, 2019 AND DECEMBER 31, 2018 AND FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018

6. PENSION AND POSTRETIREMENT BENEFITS

Eligible DTCC employees participate in DTCC's trustee 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 FICC were \$1,621,000 and \$307,000 for the three months ended September 30, 2019 and 2018, respectively, and \$4,013,000 and \$1,231,000 for the nine months ended September 30, 2019 and 2018, respectively. These costs are included in Employee compensation and related benefits, Interest expense, and Other non-operating income in the accompanying Statements of Income based on the nature of the pension expense component.

7. CAPITAL REQUIREMENTS

The capital requirements for FICC is equal to the sum of the general business risk capital requirement and corporate contribution, as described below. The Company must meet the capital requirements by holding liquid net assets funded by equity, as described in rule 17Ad-22(e)(15) of the CCAS and the Clearing Agency Policy on Capital Requirements.

General Business Risk Capital Requirement. The general business risk capital requirement is determined according to Rule 17Ad-22(e)(15) of the CCAS and the Clearing Agency Policy on Capital Requirements. The capital requirement is held to cover potential general business losses so that the Company can continue operations and provide services as a going concern if those losses materialize. It is determined based on the Company's general business risk profile and estimated time to execute a recovery or orderly wind-down of critical operations and, at a minimum, is equal to six months of operating expenses.

Corporate Contribution. The Company maintains an amount referred to as the corporate contribution, to be applied to losses of the Company as provided in the clearing agency rules. The amount of the corporate contribution is generally equal to 50% of the Company's general business risk capital requirement.

Details for general business risk capital requirement, corporate contribution and liquid net assets funded by equity for the Company as of September 30, 2019 and December 31, 2018 follow (in thousands):

	2019	2018
General business risk capital requirement	\$ 113,727	\$ 107,845
Corporate contribution	56,863	53,922
Total requirement	170,590	161,767
Liquid net assets funded by equity	296,382	265,724
Excess	\$ 125,792	\$ 103,957

FIXED INCOME CLEARING CORPORATION

NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

AS OF SEPTEMBER 30, 2019 AND DECEMBER 31, 2018 AND FOR THE THREE AND NINE MONTHS ENDED SEPTEMBER 30, 2019 AND 2018

8. CREDIT RATINGS

Credit Ratings. The Company is rated by Moody's Investors Service, Inc. (Moody's) and S&P Global Inc. (S&P). Details for issuer credit ratings and ratings outlooks for the Company as of September 30, 2019 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.

9. GUARANTEES

FICC, through GSD and MBSD, provides CCP services, including clearing, settlement and risk management services. Acting as a CCP, FICC guarantees the settlement of trades, with respect to each division, in the event one or more of its Participants defaults. A Participant default is defined in each division's rules. In its guarantor role, FICC has equal claims to and from Participants on opposite sides of netted transactions. To cover its guarantee risk, FICC uses risk-based margining to collect cash and securities collateral through its Clearing Fund. FICC maintains separate Clearing Funds for each of GSD and MBSD.

Details for each division's open positions for which a trade guaranty applied as of September 30, 2019 and December 31, 2018 follow (in billions):

Division	2019	2018
GSD	\$ 1,099	\$ 1,160
MBSD	469	333

There were no defaults by Participants to these obligations.

See Note 15 in FICC's Audited Financial Statements for the years ended December 31, 2018 and 2017 for additional information.

10. SUBSEQUENT EVENTS

In October 2019, the Board of Directors authorized revenue rebates to FICC's customers for approximately \$26 million. Customers will receive a rebate based on a pro rata share of qualifying revenues. Estimated 2019 profitability was used as the basis for the calculation of the rebates, which will be paid in December 2019.

The Company evaluated events and transactions occurring after September 30, 2019 through October 30, 2019, for potential recognition or disclosure in these accompanying Financial Statements. No additional events or transactions occurred during such period that would require recognition or disclosure in these accompanying Financial Statements.