

Audited Financial Statements
STATE REGULATORY REGISTRY LLC
December 31, 2018

State Regulatory Registry LLC

Contents

<i>Independent Auditor's Report</i>	1 - 2
<i>Financial Statements</i>	
Statements of financial condition	3
Statements of operations and owner's equity	4
Statements of cash flows	5
Notes to the financial statements	6 - 12



Independent Auditor’s Report

To the Board of Managers
State Regulatory Registry LLC

We have audited the accompanying financial statements of State Regulatory Registry LLC (SRR), a limited liability company whose sole member is the Conference of State Bank Supervisors, Inc., which comprise the statements of financial condition as of December 31, 2018 and 2017, and the related statements of operations and owner’s 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 control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor’s 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 audits to obtain reasonable assurance about whether the financial statements are free of 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 control relevant to SRR’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 SRR’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 State Regulatory Registry LLC as of December 31, 2018 and 2017, 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.

• • • • •
2021 L STREET, NW

• • • • •
SUITE 400

• • • • •
WASHINGTON, DC

20036

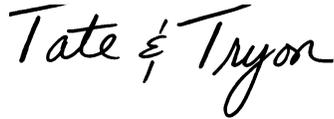
TELEPHONE
202/293-2200

• • • • •
FACSIMILE
202/293-2208

To the Board of Directors
Page 2 of 2
April 22, 2019

Adoption of Accounting Standards Update 2016-14

As described in Note A to the consolidated financial statements, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities* (ASU 2016-14). As required by the FASB, SRR adopted the provisions of ASU 2016-14 during the year ended December 31, 2018. In addition to changes in terminology used to describe categories of net assets throughout the financial statements, new disclosures were added regarding functional expenses and liquidity and the availability of resources. There was no change in SRR's previously reported change in net assets as a result of the adoption of the ASU. Our opinion is not modified with respect to this matter.



Washington, DC
April 22, 2019

State Regulatory Registry LLC

Statements of Financial Condition

December 31,	2018	2017
Assets		
Cash and cash equivalents	\$ 75,182,380	\$ 56,376,308
Accounts receivable	856,265	606,576
Investments	57,787,313	58,327,132
Prepaid expenses and other	168,977	114,192
Due from related parties, net	-	240,152
NMLS development costs, net	16,600,221	22,043,364
Capitalized test development costs, net	-	11,818
Total assets	\$ 150,595,156	\$ 137,719,542
Liabilities and Owner's Equity		
Liabilities		
Accounts payable and accrued expenses	\$ 5,574,482	\$ 5,879,001
Deferred revenue	1,197,421	1,048,684
Due to related party, net	295,324	-
Total liabilities	7,067,227	6,927,685
Owner's equity		
Retained earnings - undesignated	16,600,224	22,055,182
Retained earnings - designated for reserves and development	126,927,705	108,736,675
Total owner's equity	143,527,929	130,791,857
Total liabilities and owner's equity	\$ 150,595,156	\$ 137,719,542

State Regulatory Registry LLC

Statements of Operations and Owner's Equity

Year ended December 31, 2018

(With comparative totals for the year ended December 31, 2017)

	2018		2018	2017
	Operations (Undesignated)	Designated for reserves and development		
Revenue				
NMLS processing fees	\$ 42,184,348	\$ 8,645,692	\$ 50,830,040	\$ 50,734,506
NMLS professional services	17,298,542	3,545,338	20,843,880	22,364,710
Registration fees	248,751		248,751	258,196
Other income	3,086,000		3,086,000	-
Net investment income	162,071		162,071	3,465,548
Total revenue	62,979,712	12,191,030	75,170,742	76,822,960
Expenses				
Program expenses				
NMLS system operations	11,967,375		11,967,375	13,561,479
NMLS professional services	10,986,091		10,986,091	10,769,669
NMLS - call center	4,629,532		4,629,532	3,805,441
Professional services - legal, audit & other	8,306,974		8,306,974	7,442,332
Staff, board & member travel/meetings	1,395,095		1,395,095	1,316,997
Grants to Education Foundation	720,000		720,000	600,000
Total program expenses	38,005,067	-	38,005,067	37,495,918
Staffing & administrative expenses				
Salaries and benefits	18,639,981		18,639,981	16,324,773
Technology & general office	3,789,955		3,789,955	3,932,236
Rent and occupancy	1,999,667		1,999,667	1,772,382
Total staffing & administrative expenses	24,429,603	-	24,429,603	22,029,391
Total expenses	62,434,670	-	62,434,670	59,525,309
Change in net assets	545,042	12,191,030	12,736,072	17,297,651
Owner's equity, beginning of year	22,055,182	108,736,675	130,791,857	113,494,206
Designation of net assets to reserve	(6,000,000)	6,000,000	-	-
Owner's equity, end of year	\$ 16,600,224	\$ 126,927,705	\$ 143,527,929	\$ 130,791,857

State Regulatory Registry LLC

Statements of Cash Flows

Year Ended December 31,	2018	2017
Cash flows from operating activities		
Net income	\$ 12,736,072	\$ 17,297,651
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Depreciation and amortization	3,507,744	4,404,683
Loss on disposition of assets	1,947,217	-
Loss (gain) on investments, net	2,116,428	(2,182,744)
Changes in assets and liabilities:		
Accounts receivable	(249,689)	(112,998)
Prepaid expenses	(54,785)	221,535
Accounts payable and accrued expenses	(304,519)	1,378,542
Due to (due from) related parties	535,476	(129,133)
Deferred revenue	148,737	42,940
Total adjustments	7,646,609	3,622,825
Net cash provided by operating activities	20,382,681	20,920,476
Cash flows from investing activities		
Purchases of NMLS systems and development	-	(12,726,118)
Purchases of investments	(1,602,390)	(1,127,881)
Proceeds from sales of investments	25,781	-
Net cash used in investing activities	(1,576,609)	(13,853,999)
Net increase in cash and cash equivalents	18,806,072	7,066,477
Cash and cash equivalents, beginning of year	56,376,308	49,309,831
Cash and cash equivalents, end of year	\$ 75,182,380	\$ 56,376,308

State Regulatory Registry LLC

Notes to the Financial Statements

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization: The State Regulatory Registry LLC (SRR) is a nonprofit entity that operates Nationwide Multistate Licensing System and Registry (NMLS) on behalf of state financial services regulatory agencies. SRR is governed by an eight-member Board of Managers comprised of state banking and financial regulators and a representative of the American Association of Residential Mortgage Regulators (AARMR). The SRR Board of Managers is responsible for all development, operations, and policy matters concerning NMLS.

SRR is a single-member limited liability company owned entirely by the Conference of State Bank Supervisors, Inc. (the Conference) and is therefore, consolidated with the Conference and its affiliates. The Conference was founded in 1902 as a nonprofit organization. The primary purpose of the Conference is to assure the ability of each state banking authority to provide safe, sound, and well-regulated financial institutions to meet the unique financial needs of local economies and their citizens. Its members are public entities who charter, regulate, and supervise state-chartered banks of the United States. State bankers are also members.

NMLS is a web-based system that allows state-licensed non-depository companies, branches, and individuals in the mortgage, consumer lending, money services businesses, and debt collection industries to apply for, amend, update, or renew a license online for all participating state agencies using a single set of uniform applications. Mortgage loan originators employed by insured depository institutions are also registered through NMLS. NMLS brings greater uniformity and transparency to these non-depository financial services industries while maintaining and strengthening the ability of state regulators to monitor these industries and protect their citizens. NMLS began operation on January 2, 2008. All individual mortgage loan originators are represented in the system.

Income taxes: As a single-member limited liability company, SRR is treated as a disregarded entity for income tax purposes. Thus, SRR's financial activity is reported in conjunction with the Federal income tax filings of the Conference.

Basis of accounting: SRR prepares its financial statements on the accrual basis of accounting. As such, revenue is recognized when earned and expenses when the underlying obligations are incurred.

Use of estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from estimates.

New accounting principle: The Financial Accounting Standards Board (FASB) issued *Accounting Standards Update 2016-14, Presentation of Financial Statements of Not-for-Profit Entities* (ASU 2016-14). SRR adopted the provisions of ASU 2016-14 during the year ended December 31, 2018. In addition to changes in terminology used to describe categories of net assets throughout the financial statements, new disclosures were added regarding functional expenses and liquidity and the availability of resources. There was no change in SRR's previously reported change in net assets as a result of the adoption of the ASU. As permitted by the ASU, SRR's footnote J regarding functional expenses is not reported on a comparative basis during the initial year of the ASU's adoption.

Cash and cash equivalents: For financial statement purposes, SRR considers all highly liquid investments with an original maturity of three months or less that are not held in investment accounts to be cash equivalents.

State Regulatory Registry LLC

Notes to the Financial Statements

A. ORGANIZATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

Accounts receivable: Accounts receivable consist primarily of NMLS processing fees for system transactions pending final processing by the bank, education course and credit banking fees, and registration fees for user training courses. Accounts receivable are presented at the net amount due to SRR (i.e., gross amount less allowance, if any). SRR's management periodically reviews the status of all accounts receivable balances for collectability. Each receivable balance is assessed based on management's knowledge of the customer, SRR's relationship with the customer, and the age of the receivable balance. SRR has established an allowance for doubtful accounts to estimate the portion of receivables that will not be collected. The allowance was less than \$1,000 as of both December 31, 2018 and 2017. This allowance is regularly reviewed by management.

Deferred revenue: Deferred revenue consists of NMLS processing fees paid in advance to SRR by participating third parties.

Owner's equity: SRR has designated a portion of its owner's equity as a reserve for the continued future maintenance and upgrading of NMLS.

Allocation of functional expenses: Expenses have been summarized on a functional basis in Note J. Accordingly, costs primarily associated with personnel, professional fees, information technology, supplies, and other shared services have been allocated among the program and supporting services benefited on the basis of the labor costs utilized by each area.

Reclassifications: As a result of the adoption of ASU 2016-14, certain costs were modified to conform to definitions within the ASU. Thus, investment expenses of \$25,161 were reclassified from expenses to be netted with investment income as part of the line item "net investment income" as shown within revenues on the statements of operations and owner's equity.

Subsequent events: Subsequent events have been evaluated through April 22, 2019 which is the date the financial statements were available to be issued.

B. CREDIT AND MARKET RISK

Cash: SRR maintains demand deposits and overnight treasury fund sweep accounts with commercial banks. At times, certain balances held within these accounts may not be fully guaranteed or insured by the U.S. federal government. SRR has not experienced any such losses in the past, and does not believe it is exposed to any significant financial risk on these cash balances.

Investments: SRR invests primarily in mutual funds and exchange-traded funds (ETFs). Such investments are exposed to market and credit risks. Thus, SRR's investments may be subject to significant fluctuations in fair value. As a result, the investment balances reported in these financial statements may not be reflective of the portfolio's value during subsequent periods.

State Regulatory Registry LLC

Notes to the Financial Statements

C. INVESTMENTS AND FAIR VALUE MEASUREMENTS

SRR has implemented the accounting standard regarding fair value measurements. The standard defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. The standard uses the following prioritized input levels to measure fair value. The input levels used for valuing investments are not necessarily an indication of risk.

Level 1 – Observable inputs that reflect quoted prices for identical assets or liabilities in active markets such as stock quotes;

Level 2 – Includes inputs other than level 1 inputs that are directly or indirectly observable in the marketplace such as yield curves or other market data;

Level 3 – Unobservable inputs which reflect the reporting entity's assessment of the assumptions that market participants would use in pricing the asset or liability including assumptions about risk such as bid/ask spreads and liquidity discounts.

The following is a summary of the input levels used to determine fair values, measured on a recurring basis, of the investment assets at December 31, 2018 and 2017:

2018	Total	Level 1	Level 2	Level 3
Equity mutual funds & ETFs	\$ 9,285,761	\$ 9,285,761	\$ -	\$ -
Fixed income mutual funds & ETFs	48,491,791	48,491,791		
Assets carried at fair value	57,777,552	\$ 57,777,552	\$ -	\$ -
Money market funds & cash*	9,761			
Total investments	\$ 57,787,313			
2017	Total	Level 1	Level 2	Level 3
Equity mutual funds & ETFs	\$ 12,087,854	\$ 12,087,854	\$ -	\$ -
Fixed income mutual funds & ETFs	46,157,100	46,157,100		
Assets carried at fair value	58,244,954	\$ 58,244,954	\$ -	\$ -
Money market funds & cash*	82,178			
Total investments	\$ 58,327,132			

*Money market funds and cash included in the investment portfolio are not subject to the provisions of fair value measurements as they are recorded at cost.

Investments consist of the following at December 31,:

	2018	2017
Fixed income mutual funds	\$ 27,248,240	\$ 26,148,178
Bond market ETFs	21,243,551	20,008,922
Equity mutual funds	7,984,139	10,555,028
Equity ETFs	1,301,622	1,532,826
Money market funds and cash	9,761	82,178
Total investments	\$ 57,787,313	\$ 58,327,132

State Regulatory Registry LLC

Notes to the Financial Statements

C. INVESTMENTS AND FAIR VALUE MEASUREMENTS - CONTINUED

Investment income consists of the following for the years ended December 31,:

	2018	2017
Dividends and interest	\$ 2,304,280	\$ 1,307,965
Net (loss) gain on investments	(2,116,428)	2,182,744
Investment fees	<u>(25,781)</u>	<u>(25,161)</u>
Net investment income	<u>\$ 162,071</u>	<u>\$ 3,465,548</u>

D. RELATED PARTY TRANSACTIONS

Due to/from related party – CSBS Education Foundation: At December 31, 2018, CSBS Education Foundation (the Foundation) owed SRR \$19,912 for expenses paid by SRR on the Foundation's behalf. At December 31, 2017, SRR owed CSBS Education Foundation (the Foundation) \$37,480 for expenses paid by the Foundation on SRR's behalf.

Due to/from related party – CSBS: Since 2007, the Boards of the Conference and SRR have orally agreed to allow certain expenses to be paid by the Conference as an administrative convenience to SRR. In addition, SRR may incur certain costs on behalf of the Conference. The Conference reimburses SRR for these costs. The total amount due to the Conference, net of amounts owed by SRR for accrued liabilities, was \$315,236 at December 31, 2018. The total amount due from the Conference, net of amounts owed by SRR for accrued liabilities, was \$277,632 at December 31, 2017.

Grant to affiliate: For the years ended December 31, 2018 and 2017, SRR made unconditional grants to the Foundation of \$720,000 and \$600,000, respectively.

Expense allocations: The Conference pays the payroll costs of the employees allocated to SRR and certain other costs. Benefit costs, such as health insurance premiums and retirement plan costs, are allocated on the basis of each department's or entity's percentage of total salaries. As a result of SRR's share of this allocation, the Conference allocated \$2,426,185 and \$2,302,066 of its benefit costs to SRR for the years ended December 31, 2018 and 2017, respectively. Administrative and overhead costs, such as rent for SRR's portion of office space, are allocated on the basis of the percentage of office space each department's or entity's employees occupy at the Conference's DC offices.

The Conference performs services related to non-depository activities on behalf of SRR. Costs allocated to SRR for these services were \$1,500,000 and \$900,000 for the years ended December 31, 2018 and 2017, respectively. Total costs allocated by the Conference to SRR were as follows for the years ended December 31,:

	2018	2017
Salaries and benefits	\$ 7,337,954	\$ 6,260,570
Rent and occupancy	1,999,667	1,772,383
Overhead and administrative services	<u>5,666,817</u>	<u>7,412,152</u>
Total allocated costs	<u>\$ 15,004,438</u>	<u>\$ 15,445,105</u>

State Regulatory Registry LLC

Notes to the Financial Statements

E. NMLS DEVELOPMENT COSTS

Acquisitions of property and equipment greater than \$5,000 are recorded at cost. The capitalized development costs of NMLS began amortizing when the system went live on January 2, 2008, and they were being amortized over the system's estimated useful life of seven years. The capitalized development costs of each subsequent update release version begins amortizing when the release becomes operational, and will be amortized over the estimated useful lives of each release, which are also determined to be seven years.

The capitalized purchase costs of the Cogent Background Check Automation System began amortizing when the system became operational in January 2010, and was amortized over a five year term. During the years ended December 31, 2018 and 2017, SRR recognized \$3,495,927 and \$4,357,409, respectively, of amortization expense related to capitalized software costs.

Net property and equipment consisted of the following at December 31,:

	2018	2017
NMLS development	\$ 57,509,165	\$ 59,456,381
Cogent Background Check Automation System	<u>505,838</u>	<u>505,838</u>
	58,015,003	59,962,219
Less accumulated amortization	<u>(41,414,782)</u>	<u>(37,918,855)</u>
Total property and equipment, net	<u>\$ 16,600,221</u>	<u>\$ 22,043,364</u>

F. CAPITALIZED TEST DEVELOPMENT COSTS

In order to address provisions of the Secure and Fair Enforcement of Mortgage Licensing Act of 2008, SRR developed a national test component as well as state-specific test components which all state-licensed mortgage loan originators registering on NMLS are required to take. SRR is amortizing these test development costs over an estimated useful life of five years. During the years ended December 31, 2018 and 2017, SRR recognized \$11,818 and \$47,274, respectively, of amortization expense.

Net capitalized test development costs consisted of the following at December 31,:

	2018	2017
National test component	\$ 633,595	\$ 633,595
State-specific test components	<u>376,047</u>	<u>376,047</u>
	1,009,642	1,009,642
Less accumulated amortization	<u>(1,009,642)</u>	<u>(997,824)</u>
Total capitalized test development costs, net	<u>\$ -</u>	<u>\$ 11,818</u>

State Regulatory Registry LLC

Notes to the Financial Statements

G. COMMITMENTS AND CONTINGENCIES

Vendor relationship: The development of NMLS and its update releases is performed by the Financial Industry Regulatory Authority (FINRA). FINRA is also contracted to provide development support for NMLS' education and testing components. Given the size of the FINRA services contract, a disruption in the capabilities provided by FINRA could have a detrimental impact on SRR.

NMLS 2.0 development: In March 2017, the Boards of SRR and CSBS approved a contract for the development of NMLS 2.0, a redesign of the NMLS that will incorporate the latest technology and streamline the license approval process. The contract was subsequently terminated during 2018 when the Boards and management of SRR and CSBS decided to take the project in a different direction. The process to choose a new vendor is underway and a new vendor is expected to be selected in late 2019. Budgeted expenditures range between \$42 million and \$50 million and the project is expected to be completed over several years.

H. RESERVES

In May 2014, SRR established a formal reserve policy. The primary purposes of the reserves are to ensure that SRR is financially prepared to meet the needs for planned system enhancements as well as uninsurable risks. Reserves are defined as net assets without donor restrictions less investments in items such as NMLS development costs and capitalized test development costs. Thus, the reserve balance at December 31, 2018 and 2017 was \$126,927,705 and \$108,736,675, respectively.

I. LIQUIDITY

SRR strives to maintain liquid financial assets sufficient to cover general expenditures anticipated within one year. Financial assets in excess of daily cash requirements are invested in overnight treasury sweep accounts with commercial banks, mutual funds and exchange-traded funds (ETFs).

The following table reflects SRR's financial assets that are available to meet general expenditures within one year of the statement of financial position date. Amounts not available are primarily board-designated funds as determined under SRR's Reserve Policy and Liquidity Policy. Continuing development and enhancement of the NMLS licensing database is the largest anticipated future need. In the event the need arises to utilize the board-restricted funds for liquidity purposes, the reserves could be drawn upon through board resolution.

	2018	2017
Cash and cash equivalents	\$ 75,182,380	\$ 56,376,308
Investments	57,787,313	58,327,132
Accounts receivable	<u>856,265</u>	<u>606,576</u>
Total financial assets	133,825,958	115,310,016
Board-designated funds for future development	<u>(34,171,226)</u>	<u>(34,981,709)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u>\$ 99,654,732</u>	<u>\$ 80,328,307</u>

State Regulatory Registry LLC

Notes to the Financial Statements

J. FUNCTIONAL PRESENTATION OF EXPENSES

Schedule of functional expense at December 31, 2018 with comparative functional totals at December 31, 2017:

	Program Services NMLS	Management and General	Total
Expenses			
NMLS system operations	\$ 11,967,375	\$ -	\$ 11,967,375
NMLS professional services	10,986,091	-	10,986,091
NMLS - call center	4,629,532	-	4,629,532
Professional services - legal, audit & other	6,805,298	1,501,676	8,306,974
Staff, board & member travel/meetings	1,111,615	283,480	1,395,095
Grants to Education Foundation	720,000	-	720,000
Salaries and benefits	13,092,870	5,547,111	18,639,981
Technology and general office	1,238,924	2,551,031	3,789,955
Rent and occupancy	1,757,283	242,384	1,999,667
Total 2018 expenses by nature and function	\$ 52,308,988	\$ 10,125,682	\$ 62,434,670
Total 2017 expenses by function	\$ 48,388,971	\$ 11,136,338	\$ 59,525,309