

CU*NORTHWEST, INC.

FINANCIAL STATEMENTS

September 30, 2018 and 2017

CU*NORTHWEST, INC.
Liberty Lake, WA

FINANCIAL STATEMENTS
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INDEPENDENT AUDITOR'S REPORT

Board of Directors and Stockholders
CU*Northwest, Inc.
Liberty Lake, WA

Report on the Financial Statements

We have audited the accompanying financial statements of CU*Northwest, Inc., which comprise the balance sheets as of September 30, 2018 and 2017 and the related statements of income, stockholders' 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 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 control 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.

(Continued)

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of CU*Northwest, Inc. as of September 30, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Crowe LLP

Crowe LLP

Grand Rapids, Michigan
November 13, 2018

CU*NORTHWEST, INC.
BALANCE SHEETS
September 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 676,922	\$ 1,152,662
Certificates of deposit	200,000	-
Accounts receivable	287,439	252,750
Accounts receivable - related party (Note 7)	11,985	19,438
Income taxes receivable (Note 3)	3,857	26,401
Prepaid expenses and other assets	<u>38,134</u>	<u>46,355</u>
Total current assets	1,218,337	1,497,606
Property and equipment		
Equipment	211,967	237,838
Furniture and fixtures	91,365	91,365
Software	<u>9,847</u>	<u>9,847</u>
	313,179	339,050
Less accumulated depreciation	<u>(274,920)</u>	<u>(272,483)</u>
	38,259	66,567
Other assets		
Investment	36,780	26,175
Note receivable (Note 4)	20,000	20,000
Goodwill	120,000	120,000
Other receivable (Note 8)	<u>347,291</u>	<u>-</u>
	<u>524,071</u>	<u>166,175</u>
	<u>\$ 1,780,667</u>	<u>\$ 1,730,348</u>
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable - trade	\$ 9,203	\$ 13,196
Accounts payable - related party (Note 7)	94,378	77,300
Current portion of capital lease obligation (Note 6)	1,929	201
Patronage dividend payable	125,000	125,000
Other liabilities	<u>84,223</u>	<u>220,668</u>
Total current liabilities	314,733	436,365
Long-term liabilities		
Capital lease obligation (Note 6)	6,303	-
Deferred compensation (Note 8)	13,358	-
Deferred rent	29,034	30,229
Deferred income taxes (Note 3)	<u>28,900</u>	<u>27,200</u>
	77,595	57,429
Stockholders' equity		
Common stock; Class A, no par value; 150 shares authorized; shares issued and outstanding: 21 and 20 at September 30, 2018 and 2017, respectively.	-	-
Common stock; Class B, no par value; 1 share authorized; 1 share issued and outstanding at September 30, 2018 and 2017	-	-
Additional paid-in capital	1,139,823	1,026,706
Retained earnings	<u>248,516</u>	<u>209,848</u>
	<u>1,388,339</u>	<u>1,236,554</u>
	<u>\$ 1,780,667</u>	<u>\$ 1,730,348</u>

See accompanying notes to financial statements.

CU*NORTHWEST, INC.
STATEMENTS OF INCOME
Years ended September 30, 2018 and 2017

	2018		2017	
	Amount	%	Amount	%
Revenues	\$ 4,116,684	100.00 %	\$ 3,805,409	100.00 %
Cost of goods sold	<u>1,504,263</u>	<u>36.54</u>	<u>1,306,528</u>	<u>34.33</u>
Gross margin	2,612,421	63.46	2,498,881	65.67
Operating expenses	<u>2,429,949</u>	<u>59.03</u>	<u>2,320,993</u>	<u>60.99</u>
Income before other income (expense), patronage dividends and income taxes	182,472	4.43	177,888	4.68
Other income (expense)				
Interest income	3,062	0.07	6,150	0.16
Interest expense	(140)	-	(63)	-
Income on investment	<u>10,605</u>	<u>0.26</u>	<u>10,985</u>	<u>0.29</u>
	<u>13,527</u>	<u>0.33</u>	<u>17,072</u>	<u>0.45</u>
Income before patronage dividends and income taxes	195,999	4.76	194,960	5.13
Patronage dividends	<u>125,000</u>	<u>3.04</u>	<u>125,000</u>	<u>3.28</u>
Income before provision for income taxes	70,999	1.72	69,960	1.85
Provision for income taxes (Note 3)	<u>32,331</u>	<u>0.79</u>	<u>18,322</u>	<u>0.48</u>
Net income	<u>\$ 38,668</u>	<u>0.93 %</u>	<u>\$ 51,638</u>	<u>1.37 %</u>

See accompanying notes to financial statements.

CU*NORTHWEST, INC.
STATEMENTS OF STOCKHOLDERS' EQUITY
Years ended September 30, 2018 and 2017

	Additional Paid-In Capital	Retained Earnings	Total
Balance, October 1, 2016	\$ 954,706	\$ 158,210	\$ 1,112,916
Issuance of common stock	72,000	-	72,000
Net income	<u>-</u>	<u>51,638</u>	<u>51,638</u>
Balance, September 30, 2017	1,026,706	209,848	1,236,554
Redemption of common stock	(58,883)	-	(58,883)
Issuance of common stock	172,000	-	172,000
Net income	<u>-</u>	<u>38,668</u>	<u>38,668</u>
Balance, September 30, 2018	<u>\$ 1,139,823</u>	<u>\$ 248,516</u>	<u>\$ 1,388,339</u>

See accompanying notes to financial statements.

CU*NORTHWEST, INC.
STATEMENTS OF CASH FLOWS
Years ended September 30, 2018 and 2017

	<u>2018</u>	<u>2017</u>
Cash flows from (used in) operating activities		
Net income	\$ 38,668	\$ 51,638
Adjustments to reconcile net income to net cash from operating activities		
Depreciation and amortization	32,913	41,756
Gain on investment	(10,605)	(10,985)
Loss on disposal of assets	5,476	-
Deferred income taxes	1,700	8,200
Change in assets and liabilities		
Accounts receivable	(34,689)	114,379
Accounts receivable - related party	7,453	(10,237)
Income taxes	22,544	(87,517)
Prepaid expenses and other assets	8,221	(2,198)
Accounts payable	(3,993)	(1,071)
Accounts payable - related party	17,078	6,800
Other liabilities	<u>(124,282)</u>	<u>(50,500)</u>
Net cash from (used in) operating activities	<u>(39,516)</u>	<u>60,265</u>
 Cash flows used in investing activities		
Purchases of equipment and software	-	(14,627)
Certificates of deposit	(200,000)	-
Other receivable	<u>(347,291)</u>	<u>-</u>
Net cash used in investing activities	<u>(547,291)</u>	<u>(14,627)</u>
 Cash flows from financing activities		
Payments on capital lease obligations	(2,050)	(2,354)
Proceeds from issuance of common stock	172,000	72,000
Payments on redemption of common stock	<u>(58,883)</u>	<u>-</u>
Net cash from financing activities	<u>111,067</u>	<u>69,646</u>
 Net change in cash and cash equivalents	 (475,740)	 115,284
Cash and cash equivalents at beginning of year	<u>1,152,662</u>	<u>1,037,378</u>
 Cash and cash equivalents at end of year	 <u>\$ 676,922</u>	 <u>\$ 1,152,662</u>
 Supplemental disclosure of cash flow information		
Cash paid during the year for		
Interest	\$ 140	\$ 63
Income taxes	10,000	108,086
 Capital lease obligation entered into during the year	 \$ 10,081	 \$ -

See accompanying notes to financial statements.

CU*NORTHWEST, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2018 and 2017

NOTE 1 - NATURE OF BUSINESS

Nature of Business: CU*Northwest, Inc. ("the Company") provides automated processing services for credit unions throughout the Northwest United States. The Company also markets a software product and provides support to customers. Revenue is recognized based on the number of members for each of its credit union customers as services are performed. Additionally, the Company receives revenue from sales of certain software and computer hardware products as they are sold. The Company is organized as a credit union service organization (CUSO) and a co-operative.

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

Statement of Cash Flows: For the purpose of the statement of cash flows, cash includes cash equivalents which are demand deposit accounts, savings accounts, money market accounts and instruments purchased with a maturity of three months or less. The Company frequently has deposits in excess of \$250,000 at various financial institutions, some of which are also shareholders.

Certificates of Deposit: Certificates of deposit consist of bank time deposits with original maturity dates greater than 90 days and with remaining maturity dates of less than 365 days. These certificates of deposit have a fixed rate of interest which is paid upon maturity. They may not be redeemed before the maturity date without a penalty and are not transferable.

Accounts Receivable: The Company sells to customers using credit terms customary in their industry. Interest is not normally charged on receivables. Management establishes a reserve for losses on their accounts based on historic loss experience and current economic conditions. Losses are charged off to the reserve when management deems further collection efforts will not produce additional recoveries. These financial statements contain no allowance for losses since management expects that all accounts receivable are fully collectible at September 30, 2018 and 2017.

Advertising Costs: The Company expenses advertising costs as incurred. Advertising costs for the years ended September 30, 2018 and 2017 were \$168,566 and \$65,878, respectively.

Property and Equipment: Property and equipment are stated at cost less accumulated depreciation. Depreciation is provided by use of straight-line and accelerated methods over the estimated useful lives of the assets which generally range from three to seven years. When properties are retired or otherwise disposed of, the appropriate accounts are relieved of cost and accumulated depreciation, and any resulting gain or loss is recognized. The Company reviews property and equipment for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If it is determined that an impairment loss has occurred based on expected future undiscounted cash flows from operations, a current charge to income is recognized, and the carrying amount of the long-lived asset is adjusted.

Goodwill: Goodwill resulted from a business acquisition in prior years and represents the excess of the purchase price over the fair value of the acquired tangible assets and liabilities and identifiable intangible assets. Goodwill is assessed at least annually for impairment, and any such impairment will be recognized in the period identified. Management has determined that goodwill was not impaired at September 30, 2018 and 2017.

Escalating Base Rent: The Company recognizes rent expense on a straight-line basis over the term of related lease for leases that include escalating minimum base rents and records a deferred rent liability for the difference between straight-line expense and rent payments. The liability for deferred rent is recorded as a long-term liability.

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CU*NORTHWEST, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2018 and 2017

NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Patronage Dividends: Patronage dividends reflect discretionary distributions to shareholders, as approved by the Board of Directors. These distributions are limited to a portion of the net earnings of the Company from business done with their shareholders, and are allocated to individual shareholders based upon the volume of business done with the Company.

Income Taxes: The Company records income tax expense based on the amount of taxes due on their tax returns plus deferred taxes computed based on the expected future tax consequences of temporary differences between the carrying amounts and tax bases of assets and liabilities, using enacted tax rates. A valuation allowance, if needed, reduces deferred tax assets to the amount expected to be realized.

Uncertain tax positions are recognized and measured under provisions of FASB ASC 740. These provisions require the Company to recognize a tax benefit only if it is "more likely than not" that the tax position would be sustained in a tax examination, with a tax examination being presumed to occur. The amount recognized is the largest amount of tax benefit that is greater than 50% likely of being realized on examination. For tax positions not meeting the more likely than not test, no tax benefit is recorded.

The Company recognizes interest and penalties related to unrecognized tax benefits in interest and income tax expense, respectively. There were no amounts expensed or accrued as of and for the years ended September 30, 2018 and 2017, for tax related interest and penalties.

The Company is no longer subject to examination for federal tax years before 2014 and for state income taxes before 2013. The Company does not expect that total amount of unrecognized tax benefits to significantly increase or decrease in the next 12 months.

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 the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Subsequent Events: Management has performed an analysis of the activities and transactions subsequent to September 30, 2018 to determine the need for any adjustments to and/or disclosures within these financial statements for the year ended September 30, 2018. Management has performed their analysis through November 13, 2018, the date the financial statements were available for issuance and has determined that there are no subsequent events to disclose.

NOTE 3 - INCOME TAXES

The provision (benefit) for income taxes consists of the following:

	<u>2018</u>	<u>2017</u>
Current federal and state income tax expense	\$ 30,631	\$ 10,122
Deferred federal and state income tax (benefit) expense	(5,500)	8,200
Expense of Tax Reform	<u>7,200</u>	<u>-</u>
	<u>\$ 32,331</u>	<u>\$ 18,322</u>

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CU*NORTHWEST, INC.
NOTES TO FINANCIAL STATEMENTS
September 30, 2018 and 2017

NOTE 3 - INCOME TAXES (Continued)

On December 22, 2017, the Tax Cuts and Jobs Act (the "Act") was signed into law. The Act increases the Company's federal tax rate from 15% to 21% effective January 1, 2018. As a result, the Company is required to re-measure the deferred tax assets and liabilities using the enacted rate at which the Company expects them to be recovered or settled. The effect of this re-measurement is recorded to provision (benefit) for income taxes in the year the tax law is enacted. For the year ended September 30, 2018, the re-measurement of the net deferred tax liability resulted in an additional income tax expense of approximately \$7,200.

Deferred tax assets and liabilities are as follows:

	<u>2018</u>	<u>2017</u>
Deferred tax assets	\$ 7,600	\$ 1,100
Deferred tax liabilities	<u>(36,500)</u>	<u>(28,300)</u>
	<u>\$ (28,900)</u>	<u>\$ (27,200)</u>

Income tax expense differs from expense at statutory rates due to the effect of graduated tax rates and nondeductible expenses. Significant temporary differences between financial statements and tax returns include accumulated depreciation, accumulated amortization and accrued expenses.

NOTE 4 - NOTE RECEIVABLE

Note receivable from a company; dated December 18, 2013, including interest at 2% due quarterly. Originally maturing on December 31, 2015, the note receivable was extended during 2016 and matures on December 31, 2019.

NOTE 5 - INVESTMENT

On July 1, 2012, the Company purchased one Class B Unit of Site Four, LLC for \$25,000 representing a 20% ownership interest. This investment is accounted for under the equity method. The Company recorded income of \$10,605 and \$10,985 related to this investment in the years ended September 30, 2018 and 2017, respectively.

NOTE 6 - LEASE COMMITMENTS

The Company is obligated under a capital lease agreement for a copier. Lease payments are generally due monthly and expire at various dates through September 2022. The copier recorded under a capital lease amounts to the following:

	<u>2018</u>
Equipment	\$ 10,081
Accumulated depreciation	<u>2,015</u>
	<u>\$ 8,066</u>

(Continued)

CU*NORTHWEST, INC.
NOTES TO FINANCIAL STATEMENTS
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NOTE 6 - LEASE COMMITMENTS (Continued)

The Company also leases its facility and certain equipment under noncancelable operating lease agreements expiring on various dates. Rent expense was \$120,794 and \$121,367 for the years September 30, 2018 and 2017, respectively.

Future minimum payments due under operating and capital leases with initial or remaining noncancelable lease terms in excess of one year are as follows:

	Operating <u>Leases</u>	Capital <u>Leases</u>
2019	\$ 119,805	\$ 2,241
2020	124,623	2,241
2021	127,993	2,241
2022	<u>10,689</u>	<u>2,241</u>
Total minimum lease payments	<u>\$ 383,110</u>	8,964
Less amounts representing interest		<u>(732)</u>
		8,232
Current portion of capital lease obligation		<u>1,929</u>
Long term portion of capital lease obligation		<u>\$ 6,303</u>

NOTE 7 - RELATED PARTY TRANSACTIONS

Operational support services are provided to the Company by a stockholder and renewed on an annual basis. Services under this agreement include accounting management, human resources, and shared services which the Company incurred expenses of approximately \$87,460 and \$88,210 for the years ended September 30, 2018 and 2017, respectively. The Company provides services to this stockholder in the normal course of business. Sales were approximately \$503,680 and \$556,246 during the years ended September 30, 2018 and 2017, respectively. At September 30, 2018 and 2017, amounts due from this stockholder included in accounts receivable - related party were \$11,985 and \$19,438, respectively. The Company also had accounts payable due to this stockholder of \$94,378 and \$77,300 at September 30, 2018 and 2017, respectively.

The Company provides services to all of its shareholders. Revenues from transactions with shareholders constituted 74% and 75% of total revenues during fiscal 2018 and 2017, respectively. At September 30, 2018 and 2017, 82% and 69%, respectively, of the Company's accounts receivable were from its shareholders. Cash and cash equivalents held at shareholder credit unions totaled approximately \$876,921 and \$1,152,662 at September 30, 2018 and 2017, respectively.

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NOTE 8 - DEFERRED COMPENSATION PLAN

In May 2018, the Company entered into an employee retention agreement (the "agreement") with the Chief Executive Officer ("CEO"). The Company agreed to purchase a loan for a property owned by the CEO in an amount of \$347,291, recorded as an other receivable at September 30, 2018. The CEO will vest in reductions in the obligation owed through continued service, becoming 25% vested on February 28, 2021, 70% vested on February 28, 2026, and becoming fully vested on February 28, 2029. In the event that the CEO does not remain employed by the Company for cause, the Company will be entitled to payment for the unvested obligation. The obligation under the agreement was \$13,358, included in deferred compensation liability at September 30, 2018. The expense attributable to the agreement due to vesting, included in operating expenses, was \$13,358 during the year ended September 30, 2018.