2018 FINRA Annual Financial Report

Contents

Robert W. Cook | President and Chief Executive Officer

A MESSAGE FROM THE PRESIDENT AND CEO

For 80 years, FINRA has served a unique and vital role in the U.S. financial regulatory structure as a not-for-profit, self-regulatory organization (SRO) whose operations are funded by industry fees—not taxpayer dollars. Performing this role effectively requires that FINRA prudently manage its finances to ensure we can appropriately fund our mission of protecting investors and promoting market integrity in a manner that supports vibrant capital markets.

Our Financial Guiding Principles (the Principles) outline how we seek to do just that: fund our mission, manage expenses responsibly, maintain reasonable member firm fees, use fine monies to promote compliance and improve markets, and sustain appropriate financial reserves. We first published the Principles in January 2018 to underscore our commitment to financial transparency, and they were reaffirmed by the FINRA Board of Governors in December. These Principles build on a long-standing practice—dating back to at least 1960—of publishing an Annual Financial Report. With the publication of this year's report, we once again outline our financial operations for the prior year in accordance with U.S. generally accepted accounting principles (GAAP).

Financial Operations and Use of Fine Monies in 2018

As described in the 2018 Annual Financial Report, FINRA's operating revenues increased 3.5 percent to $857.4 million in 2018, while expenses for 2018 decreased slightly as we continued to closely manage our spending. Overall, we reported a net loss of $68.7 million for the year, driven primarily by an operating loss of $29.2 million, coupled with investment losses and other expenses of $39.5 million. By way of context, over the last five years we have reported cumulative net income of $120.1 million, as well as an average annual decrease in expenses of 0.4 percent. FINRA continues to maintain a strong balance sheet to support its operations, with approximately $1.5 billion in equity (net assets) as of December 31, 2018. The key drivers of last year's financial performance are discussed more fully in the Annual Financial Report.

Our Financial Guiding Principles provide that FINRA only use fine monies it collects for specific purposes—such as capital initiatives that enable improved oversight of and compliance by member firms—and only with the approval of the FINRA Board of Governors or the Finance, Operations and Technology Committee. FINRA released its public Report on Use of 2018 Fine Monies in April, which details the Board-approved initiatives that were supported by 2018 fine monies.

2019 Budget

To further promote the financial transparency called for in the Financial Guiding Principles, FINRA also recently began releasing a forward-looking annual budget summary. FINRA's 2019 Annual Budget Summary was published earlier this year, together with comparable financial data, and outlines how FINRA plans to deploy its resources to meet its varied and complex regulatory responsibilities in 2019 in accordance with the Principles.

As described more fully in the budget summary, we project our expenses will again exceed our operating revenues in 2019. However, FINRA will not increase member fees in 2019, marking the sixth consecutive year without a fee increase. Instead, we are again budgeting for a potential drawdown, if necessary, on our financial reserves to fund our regulatory operations. While drawing down our reserves may result in net losses, this measure is part of a longer-term plan to reduce reserves before increasing member firm fees. It will become necessary to increase member fees once reserves have been reduced to the level targeted by FINRA's Board pursuant to the Financial Guiding Principles.

By managing our expenses responsibly, monitoring and planning for reasonable member fee levels, and sustaining appropriate reserves, FINRA continues to plan for the long-term financial sustainability of the organization and its ability to meet the regulatory challenges ahead.

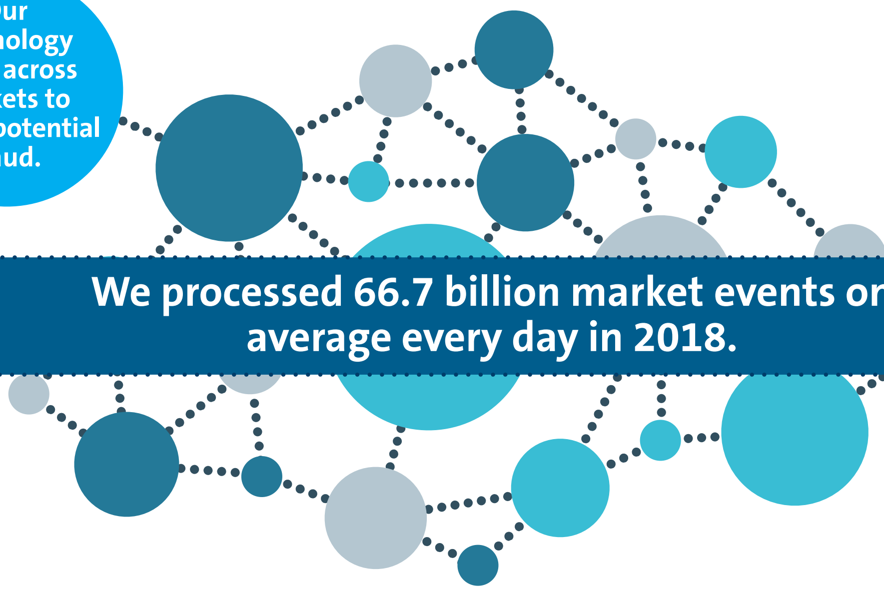
Robert W. Cook

Robert W. Cook
President and Chief Executive Officer

FINRA plays an essential role in the oversight of U.S. broker-dealers.

We promote market integrity in a manner that supports the important role our capital markets play in the U.S. financial systems.

Our technology looks across markets to detect potential fraud.



We processed 66.7 billion market events on average every day in 2018.

We protect investors from bad actors.

- More than 6,300 exams and reviews conducted in 2018
- $61.0 million in fines
- $25.5 million in restitution to harmed investors
- 16 firms expelled
- 472 brokers suspended
- 386 brokers barred

Coordinating closely with the SEC and other federal and state regulators is an important part of our regulatory work.

919 FRAUD AND INSIDER TRADING CASES

referred to the SEC and other federal or state law enforcement agencies for prosecution

We work to keep investors informed.

FINRA Investor Education Foundation
Committed **$115 million+ for financial capability** and fraud prevention initiatives since inception

Securities Helpline for Seniors
Facilitated the **return of $6.6 million** in voluntary reimbursements to senior investors from April 2015 through April 2019

Management Report on Operations

Who We Are

The Financial Industry Regulatory Authority, Inc.® (FINRA®) is a not-for-profit self-regulatory organization (SRO) authorized by federal law to help protect investors and ensure the fair and honest operation of securities markets. Under the oversight of the U.S. Securities and Exchange Commission (SEC), we regulate the activities of U.S. broker-dealers and perform market regulation pursuant to our own statutory responsibility and under contract for certain exchanges.

Our Mission

Our core mission is to provide investor protection and promote market integrity through comprehensive and effective regulation of the broker-dealer industry.

Our Regulatory Model

To carry out its mission, FINRA uses a multi-pronged approach that includes regulation, rulemaking, transparency and education:

Member Supervision—monitors and examines for member firm compliance with applicable statutes and rules.

Market Regulation—conducts automated surveillance, examinations and investigations of trading activity in U.S. equities, options and fixed income markets.

Enforcement—investigates possible misconduct and brings disciplinary actions for violations of industry rules and regulations.

Fraud Detection—centralizes FINRA's review of allegations of serious fraud and significant investor harm, analyzes trading activity across U.S. markets for evidence of insider trading, and analyzes tips and complaints of possible fraud or other misconduct that are submitted to FINRA's Whistleblower hotline or mailbox.

Rulemaking and Guidance—assists in adopting and interpreting rules applicable to securities firms and brokers, and evaluates the potential impacts of FINRA's rulemaking on all market participants. FINRA solicits comment on its proposed rules from its member firms, investors and other interested parties, and, with limited exceptions, all FINRA rules must be approved by the SEC.

Registration and Disclosure—operates FINRA's utilities to register and test securities industry personnel and provides those same services under contract for the benefit of investment advisers and mortgage brokers.

Market Transparency—operates facilities that disseminate real-time and historical market information for over-the-counter (OTC) trading in the equity and fixed income markets, and maintains the databases FINRA uses to oversee OTC securities.

Dispute Resolution—operates a dispute resolution forum for investors, brokerage firms and their registered employees, and administers arbitrations and mediations.

Advertising Regulation—oversees compliance with rules intended to ensure that member firm communications to the public are fair, balanced and not misleading.

Corporate Financing—oversees compliance with rules intended to prevent fraudulent private placements by member firms and ensure underwriting compensation is fair.

Investor Education—provides investors with financial tools and resources; and through the FINRA Investor Education Foundation® (the Foundation), FINRA supports important research and financial education initiatives.

FINRA's Board of Governors (Board) and its committees meet multiple times throughout the year to review the operations, risks and challenges associated with the furtherance of FINRA's mission. These committees include the Audit Committee; Regulatory Policy Committee; Regulatory Operations Oversight Committee; Finance, Operations and Technology Committee (Finance Committee); Management Compensation Committee; and Executive Committee.

Further description of FINRA's statutory responsibilities, as well as its responsibilities under contract for certain exchanges, can be found in Note 1, "Organization and Nature of Operations," to the consolidated financial statements.

This Management Report should be read in connection with the consolidated financial statements and accompanying notes included elsewhere in this Annual Financial Report. The 2018 consolidated financial statements reflect the activities of FINRA and its consolidated subsidiaries, collectively referred to as "we," "our," "us," "FINRA" or the "Company" throughout this Management Report. As of and for the years ended December 31, 2018 and 2017, FINRA's primary consolidated subsidiaries are FINRA Regulation, Inc. and the Foundation.

Our consolidated financial statements are prepared in conformity with U.S. generally accepted accounting principles (U.S. GAAP). Under U.S. GAAP, we are required to adopt accounting principles and make estimates and judgments to develop amounts reported in the consolidated financial statements and accompanying notes.

We describe our significant accounting policies in Note 2, "Summary of Significant Accounting Policies," Note 5, "Fair Value Measurement," and Note 7, "Employee Benefit Liabilities," to the consolidated financial statements.

RESULTS OF OPERATIONS

Summary of Operations

The following table provides a summary of our financial results on a U.S. GAAP basis for the two years ended December 31, 2018.

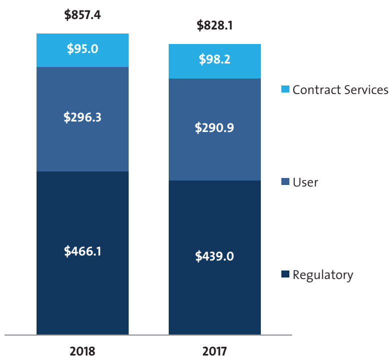
	Years Ended December 31,	
	2018	2017
	(in millions)	
Operating revenues	$ 857.4	$ 828.1
Fines	61.0	64.9
Net activity assessment revenues	0.1	—
Net revenues	918.5	893.0
Expenses	(975.3)	(992.3)
Interest and dividend income	27.6	26.0
Operating loss	(29.2)	(73.3)
Net realized and unrealized investment (losses) gains	(51.1)	32.6
Equity (losses) earnings from other investments	12.0	83.9
Other expense	(0.4)	(1.6)
Net (loss) income	$ (68.7)	$ 41.6

We reported a net loss of $68.7 million in 2018 versus net income of $41.6 million in 2017, a decrease of $110.3 million year over year. Our net loss of $68.7 million was driven by an operating loss of $29.2 million coupled with investment losses and other expenses of $39.5 million. An increase in operating revenues, combined with a decline in expenses, led to a decrease in our year-over-year operating loss. Our investment portfolio (the Portfolio) experienced losses for the year, which were modest relative to broader equity market declines. A more detailed look at our operating results follows.

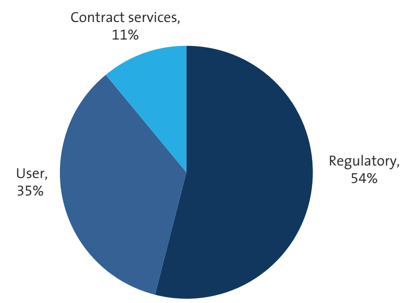
Management Report on Operations (continued)

OPERATING REVENUES

Operating Revenues
($ in millions)



Operating Revenues By Type – 2018



COMMENTARY: 2018 – 2017

Regulatory revenues, such as the Gross Income Assessment (GIA), Personnel Assessment (PA), Branch Office Assessment and Trading Activity Fees (TAF), consistently represent approximately half of FINRA's operating revenues on an annual basis. User revenues (dispute resolution, transparency services, registrations, qualification examinations, FINRA-sponsored educational programs and conferences, and reviews of advertisements, corporate filings and disclosures) consistently represent approximately one-third of FINRA's operating revenues on an annual basis.

FINRA's operating revenues for 2018 increased $29.3 million or 3.5 percent. The following table identifies the changes in operating revenues year over year.

Operating Revenues
(in millions)

2018 – 2017	
2017	**$828.1**
Regulatory revenues	27.1
User revenues	5.4
Contract services revenues	(3.2)
2018	**$857.4**

Regulatory revenues. Higher TAF and GIA led to an increase in regulatory revenues. Volume increases drove the increase in TAF, while an increase in industry revenues drove the increase in GIA.

User revenues. The increase in user revenues resulted from increases in qualification examination, transparency services and dispute resolution revenues, which were partially offset by decreases in advertising, disclosure review and corporate financing revenues.

Qualification examination revenues increased due to an increase in legacy examination registrations prior to the restructuring of our representative-level qualification exam program effective October 1, 2018. The increase in transparency services revenue was driven by higher fixed income trading volumes partially offset by lower OTC compare/accept fees. An increase in arbitration cases drove the increase in dispute resolution revenues.

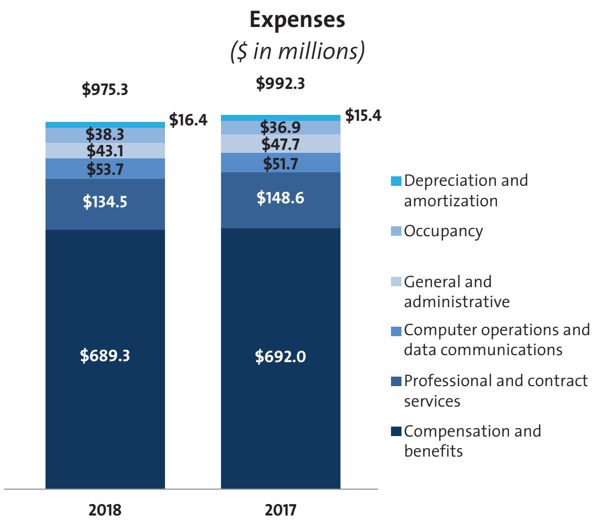
Lower volumes in advertising and late disclosure review filings, combined with a decline in the average size (proposed maximum aggregate offering price) of initial and secondary public offerings year over year resulted in decreases to our advertising, disclosure review and corporate financing revenues.

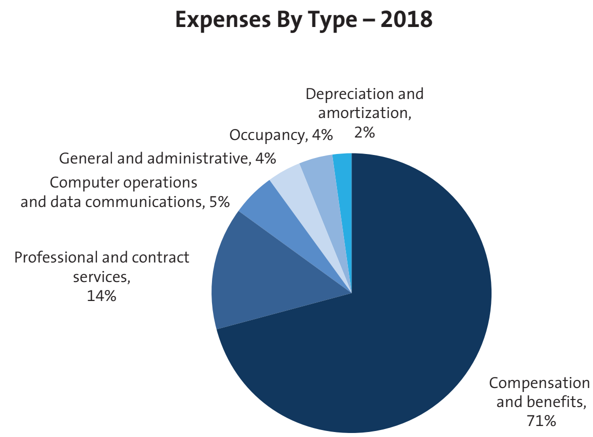
Contract services revenues. Lower service levels related to the mortgage licensing system FINRA developed and deployed to the State Regulatory Registry LLC (SRR) primarily drove the decline in contract services revenues.

Descriptions of the nature of and accounting for FINRA's revenues are described in Note 2, "Summary of Significant Accounting Policies," to the consolidated financial statements.

Management Report on Operations (continued)

EXPENSES





COMMENTARY: 2018 – 2017

FINRA is largely a service organization. Our expenses are driven by employee-related costs, as we seek to attract, develop and retain a diverse group of talented staff, particularly in the highly specialized areas of regulation and technology, to enable FINRA to carry out its regulatory mandate in today's ever-changing markets. Employee compensation and benefits are FINRA's largest expense, consistently representing more than two-thirds of total expenses on an annual basis. Information regarding FINRA's compensation philosophy can be found in the accompanying Management Compensation Committee Report of this 2018 Annual Financial Report. FINRA had approximately 3,400 employees as of December 31, 2018, and 3,500 employees as of December 31, 2017.

Expenses for 2018 decreased $17 million or 1.7 percent, as we continued to closely manage operating expenses. The following table identifies the changes in expenses year over year.

Expenses
(in millions)

2018 – 2017	
2017	**$992.3**
Professional and contract services	(14.1)
General and administrative	(4.6)
All other	1.7
2018	**$975.3**

Professional and contract services. An increase in the capitalization of costs associated with software development in 2018 versus 2017 accounts for the decrease in professional and contract services expenses.

General and administrative. In 2018, there were continued managed reductions of general and administrative expenses.

INVESTMENT RETURNS

Traditionally, FINRA has relied on the investment returns from its balance sheet to fund operating expenditures in excess of its annual revenues in any given year. FINRA's Portfolio, which we also refer to as our financial reserves, lost 2.3 percent in 2018 compared to an 8.8 percent return in 2017. Although the Portfolio lost 2.3 percent, this loss is modest relative to several common market indices and standard portfolios of equities and bonds.

Additional information regarding the Portfolio, strategy and returns can be found in the accompanying Investment Committee Report of this 2018 Annual Financial Report. Descriptions of the nature of and accounting for FINRA's investments are described in Note 2, "Summary of Significant Accounting Policies," and Note 4, "Investments," to the consolidated financial statements.

RESTITUTION AND FINES

FINRA is dedicated to investor protection and market integrity through effective and efficient regulation of broker-dealers. One of FINRA's tools for achieving this objective is vigorous, fair and effective enforcement of our member firms' compliance with securities laws and regulations.

When a member firm or registered representative engages in misconduct, restitution for harmed customers is our highest priority, although there are many cases in which it is not practical. Restitution may be ordered when an investor has suffered a quantifiable loss due to misconduct. The calculation of restitution is based on the actual amount of the harm sustained by the investor, as demonstrated by evidence. We ordered restitution to harmed investors of $25.5 million during 2018. Restitution is assessed separately from fines and has no impact on how or when we use fine money. Restitution is payable to the harmed party and has no effect on our financial position.

When a member firm or registered representative engages in misconduct, we also assess whether a sanction should be imposed in order to discourage similar conduct by the firm, registered representative or others. When we impose fines, the amounts are based on the facts and circumstances of the misconduct and the principles set forth in the *FINRA Sanction Guidelines*. The National Adjudicatory Council (NAC), which is composed of industry and non-industry members, continues to maintain the *FINRA Sanction Guidelines* for use by the various bodies adjudicating FINRA disciplinary decisions, including Hearing Panels and the NAC itself, in determining appropriate remedial sanctions. FINRA publishes the *FINRA Sanction Guidelines* so that member firms, associated persons and their counsel may become more familiar with the types of disciplinary sanctions that may be applicable to various violations.

Fines are not based on revenue considerations, and we do not establish any minimum amount of fines that must be issued for purposes of our annual budget. These monies are not considered in determining employee compensation and benefits. The total amount of fines decreased by $3.9 million in 2018 to $61 million.

FINRA's use of fine monies is governed by FINRA's Financial Guiding Principles (Principles), which we published in January 2018 to provide more transparency about how we manage our financial resources to ensure we fulfill our regulatory responsibilities and further our mission. FINRA's Board reaffirmed the Principles in December 2018. As the Principles describe, FINRA accounts for fine monies separately, and any use of such monies is approved, separately from other expenditures, by the Board or its Finance Committee. The Board or its Finance Committee may authorize the use of fine monies only for one of four enumerated purposes: (1) capital/initiatives or non-recurring strategic expenditures that promote more effective and efficient regulatory oversight by FINRA (including leveraging technology and data in a secure manner) or that enable improved compliance by member firms; (2) activities to educate investors, promote compliance by member firms through education, compliance resources or similar projects, or ensure our employees are highly trained in the markets, products and businesses we regulate; (3) capital initiatives required by new legal, regulatory or audit requirements; or (4) replenishing reserves in years where such reserves drop below levels reasonably appropriate to preserve FINRA's long-term ability to fund its regulatory obligations.

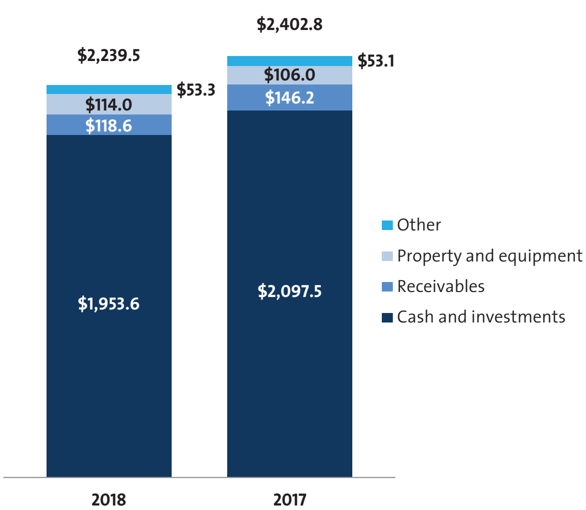
In accordance with the Principles, in April 2019, FINRA issued a separate detailed report covering all projects for which fine monies were used in 2018.

BALANCE SHEET

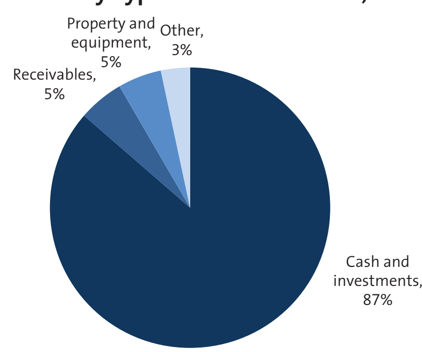
Our focus is to ensure a balance sheet that positions FINRA to fulfill our regulatory obligations and mission in today's continually evolving markets. To that end, our balance sheet remains strong, with net assets of approximately $1.5 billion as of December 31, 2018 and approximately $1.6 billion as of December 31, 2017. FINRA's working capital (excluding fines and our consolidated limited partnership) was $784 million as of December 31, 2018, and $721.7 million as of December 31, 2017. Our working capital and cash ratios (excluding fines and our consolidated limited partnership) were 2.53 and 2.28 as of December 31, 2018, compared to 2.28 and 1.89 as of December 31, 2017. The increases in FINRA's working capital and the working capital and cash ratios were driven by the purchase of trading (short-term) investments with proceeds from the redemption of other (long-term) investments.

Assets

Assets By Type as of December 31
($ in millions)



Assets By Type as of December 31, 2018



Management Report on Operations (continued)

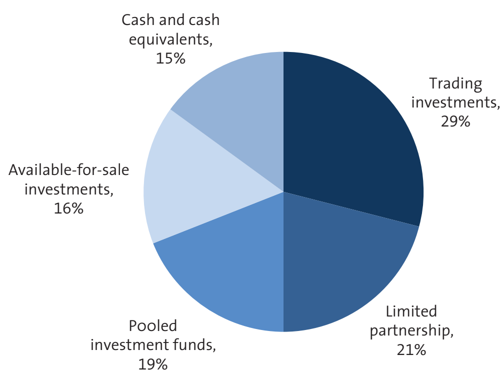
Assets (continued)

COMMENTARY: 2018 – 2017

Cash and investments (cash, cash equivalents and trading, available-for-sale and other investments, including investments receivable), are the largest portion of FINRA's total assets, consistently representing close to 90 percent of total assets annually. Our primary market risk relates to the Portfolio. The value of our investments are impacted by fluctuations in the economic climate, as well as changes in individual security prices associated with a diverse array of investment strategies.

Cash and investments as of December 31, 2018, are presented in the following chart.

Cash and Investments By Type as of December 31, 2018



Descriptions of the nature of and accounting for FINRA's investments are described in Note 2, "Summary of Significant Accounting Policies," and Note 4, "Investments," to the consolidated financial statements.

Total assets decreased $163.3 million or 6.8 percent. The following table identifies the changes in assets year over year.

Assets
(in millions)

2018 – 2017	
2017	**$2,402.8**
Property and equipment	8.0
Receivables	(27.6)
Cash and investments	(143.9)
All other	0.2
2018	**$2,239.5**

Property and equipment. The increase in property and equipment is primarily due to the capitalization of internal use software partially offset by depreciation and amortization, which represents the normal reduction in our property, equipment and intangible asset base year over year.

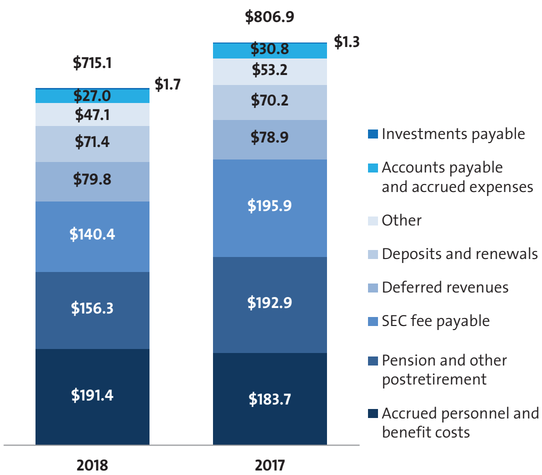
Receivables. Decreases in SEC fees and fines receivable drove the decrease in receivables. An approximate 44 percent SEC fee rate decrease from December 31, 2017 to December 31, 2018 led to the decrease in SEC fees receivable. Fines collections in excess of fines billed led to the decrease in fines receivable. There was a lower amount of fines billed both for the year and in the month of December in 2018 versus 2017.

Cash and investments. Cash and investments decreased due to the following: (1) funding operations, as operating expenditures in 2018 exceeded operating revenues; (2) investment losses of 2.3 percent in 2018; (3) a lower cash balance in 2018 compared to 2017 due to the approximate 44 percent decrease in SEC fee rates mentioned above; and (4) the funding of our pension plan.

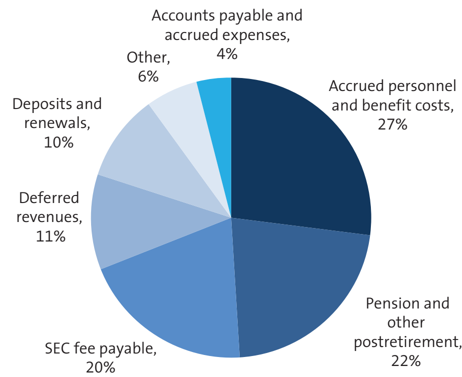
Liabilities

Liabilities By Type as of December 31

($ in millions)



Liabilities By Type as of December 31, 2018



COMMENTARY: 2018 – 2017

Total liabilities decreased $91.8 million or 11.4 percent. The following table identifies the individually material changes in liabilities year over year.

Liabilities

(in millions)

2018 – 2017	
2017	**$806.9**
Accrued personnel and benefit costs	7.7
Other liabilities	(6.1)
Pension and other postretirement	(36.6)
SEC fee payable	(55.5)
All other	(1.3)
2018	**$715.1**

Accrued personnel and benefit costs. A year-over-year increase in accrued employee incentive compensation was the primary driver for the increase in accrued personnel and benefit costs.

Other liabilities. The amortization of tenant rent and work allowances, primarily related to our leased office space in New York, was the primary driver of the decrease in other liabilities.

Pension and other postretirement. Contributions and changes in actuarial assumptions, offset by normal costs and asset performance, led to a $36.6 million decrease in our pension and postretirement liabilities, of which the pension plan accounted for $33.1 million. The pension plan decrease was driven by $77 million of actuarial gains and a $25 million pension plan contribution, offset by normal costs of $39 million and unfavorable asset performance of $29.9 million. The actuarial gains were primarily driven by an increase in the discount rate from 3.65 percent at December 31, 2017, to 4.3 percent at December 31, 2018. Service and interest costs represent benefits attributed to the current year.

Pension and other postretirement benefit costs represent a significant liability to FINRA in terms of both the assumptions used to estimate the liability and its portion of FINRA's total liabilities. These costs have historically represented approximately one-quarter of total liabilities on an annual basis. Further disclosures regarding the assumptions used in determining our pension and other postretirement liabilities can be found in Note 2, "Summary of Significant Accounting Policies."

SEC fee payable. The rate decrease from $23.10 to $13 per million dollars in transactions drove the decrease in our SEC fee payable. We remit these SEC fees to the U.S. Treasury semiannually, in March and September.

LIQUIDITY AND CAPITAL RESOURCES

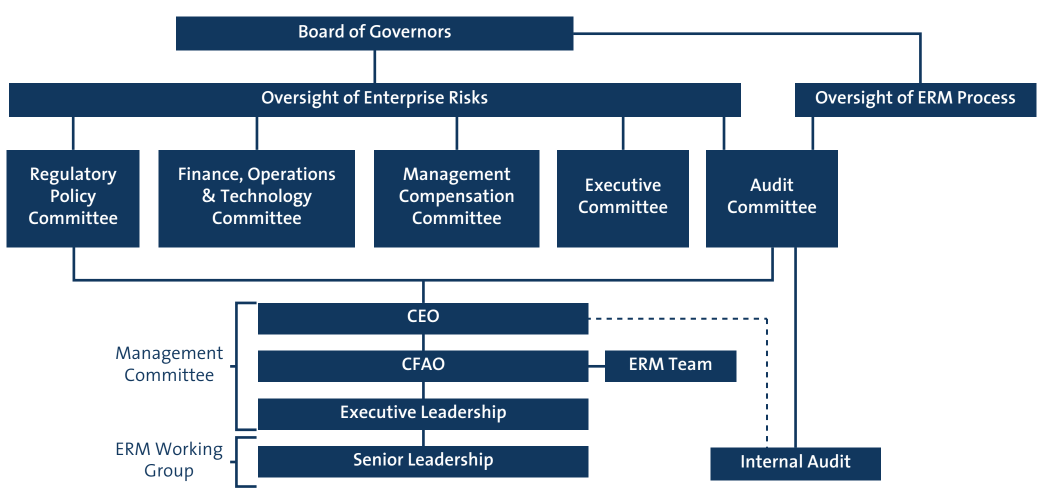
Liquidity is the ongoing ability to fund asset growth and business operations and meet contractual obligations through unrestricted access to funding at reasonable market rates. Liquidity management involves forecasting funding requirements and maintaining sufficient working capital to meet business needs and accommodate fluctuations in asset and liability levels due to changes in business operations or unanticipated events. We primarily rely on operating cash flows to fund current and future operations.

We maintain a seasonal unsecured line of credit agreement with the option to borrow up to $150 million at the LIBOR Daily Floating Rate plus 0.45 percent (2.83 percent at December 31, 2018). This line of credit was available to us from February 1, 2019 to May 31, 2019. The line of credit provides us with a mechanism to fund operations prior to the annual billing of the GIA and PA in April, and the subsequent receipt of those funds, without having to make redemptions from the Portfolio. As of December 31, 2018, and December 31, 2017, no amounts were outstanding under this line of credit.

The Portfolio is governed by a policy based on the degree of risk deemed appropriate for FINRA assets by the Board as applied to its investment objectives. FINRA's Investment Committee, whose members have extensive background and experience in the investment community, provides overall guidance and advice in determining the appropriate policy and allocation for the Portfolio. As of December 31, 2018, our investments remained liquid, with 77 percent available in 60 days or less. Additional information regarding the Portfolio can be found in the accompanying Investment Committee Report of this 2018 Annual Financial Report.

ENTERPRISE RISK MANAGEMENT

FINRA's Enterprise Risk Management (ERM) program is designed to provide a consolidated, organization-wide view of the risks that FINRA faces in the execution of its mission, strategic goals and key business objectives. The program covers a broad spectrum of risks in various risk categories, such as strategic, operational, legal and compliance, and financial, and provides transparency for senior management and the Board regarding FINRA's enterprise-level risks and how they are being managed. The chart below shows the governance structure FINRA has in place to oversee and manage enterprise risk.



The Board oversees the ERM program, with oversight of the ERM process delegated to the Audit Committee and the primary oversight for each enterprise risk assigned to a specific Board committee, with support by other committees and working groups as the need arises.

Where Board committees are assigned primary risk oversight responsibility, those committees meet to review and discuss the assigned enterprise risk with the designated risk owners, including factors impacting the risk, risk response, and risk tolerances and metrics.

Executive support and oversight of ERM is effected through the Management Committee, composed of the Chief Executive Officer (CEO), Chief Financial and Administrative Officer (CFAO) and other senior executives across the organization. Additionally, an ERM Working Group brings together senior managers across FINRA to provide fresh perspectives and support. FINRA's Internal Audit Department serves the ERM program in an advisory capacity.

CYBER AND INFORMATION SECURITY

FINRA operates a comprehensive security program designed to mitigate cyber and physical information security threats and ensure compliance with applicable data privacy regulations and laws. We base our program upon industry best practices, and are guided by federal and international standards, and data privacy laws and regulations. Cybersecurity and information security breach risks are integrated into FINRA's ERM program.

Specifically, FINRA's information-security practices and operational controls include leading practices such as a formal security assessment program used to evaluate vendor, partner and third-party security practices, and real-time logging, monitoring and alerting of security events.

FINRA's adoption of cloud technology provides numerous benefits, such as access to best-of-breed security solutions made available by the cloud provider's scale of operations. Another benefit is our ability to use micro-segmentation, or putting each server into a security zone of one, which dramatically reduces attack surface area. Cloud technology also enables us to focus on the automation and tools necessary to raise the compliance bar and simplify controls.

FINRA information technology systems are subject to numerous mandatory and voluntary inspections including, but not limited to, the following:

- regular vulnerability scans;
- application code analysis and security testing using automated scans, dynamic testing and manual attack techniques to identify application-level vulnerabilities;
- periodic independent, third-party penetration tests and application security assessments;
- annual inspections conducted by the SEC;
- an annual Service Organization Control (SOC) 2 Type II Assessment; and
- annual assessments by our Internal Audit department.

Investment Committee Report

Year Ended December 31, 2018

FINRA's investment portfolio*, also referred to as our financial reserves, originally derived from the sale of Nasdaq that culminated in 2006, is overseen by the Investment Committee, a standing committee of FINRA, and managed to preserve principal and support our regulatory operations. FINRA has a set of Financial Guiding Principles that establish a goal of maintaining investment balances equal to at least one year of expenditures. Distributions from the portfolio are subject to prior approval by the Board of Governors (Board), and may be used to defer member firm fee increases or make up cash flow losses, among other uses.

FINRA's investment portfolio lost 2.3 percent in 2018, including returns from its cash operating fund. The investment climate was characterized by a volatile fourth quarter that led to broad-based losses across global equity markets, as measured by the S&P 500 (-4.4 percent) and the MSCI All Country World Index (-8.9 percent). Bonds finished the year with roughly flat results. The chart below shows investment results for FINRA and for several common market indices and conventional portfolios of equities and bonds. As of December 31, 2018, FINRA's investment portfolio, including cash, totaled approximately $1.7 billion. Portfolio liquidity remains strong, with $1.3 billion, or 77 percent, available in 60 days or less as of December 31, 2018.

		Annualized Returns		
	2018	3-Year	5-Year	Inception (1)
FINRA	–2.3%	3.3%	3.2%	3.3%
U.S. Consumer Price Index	1.9%	2.0%	1.5%	2.1%
100% Equities	–8.9%	7.2%	4.8%	6.7%
100% Bonds	0.0%	2.1%	2.5%	3.9%
40% Equities /60% Bonds	–3.6%	4.2%	3.6%	5.3%
60% Equities /40% Bonds	–5.4%	5.2%	4.0%	5.9%

Standard Deviation	2018	3-Year	5-Year
FINRA	3.5%	3.0%	3.3%
100% Equities	13.5%	10.6%	10.9%
100% Bonds	3.1%	2.9%	2.8%
40% Equities /60% Bonds	5.2%	4.5%	4.6%
60% Equities /40% Bonds	7.8%	6.4%	6.5%

Sharpe Ratio (2)	3-Year	5-Year
FINRA	0.8	0.8
100% Equities	0.6	0.4
100% Bonds	0.4	0.7
40% Equities /60% Bonds	0.7	0.7
60% Equities /40% Bonds	0.7	0.5

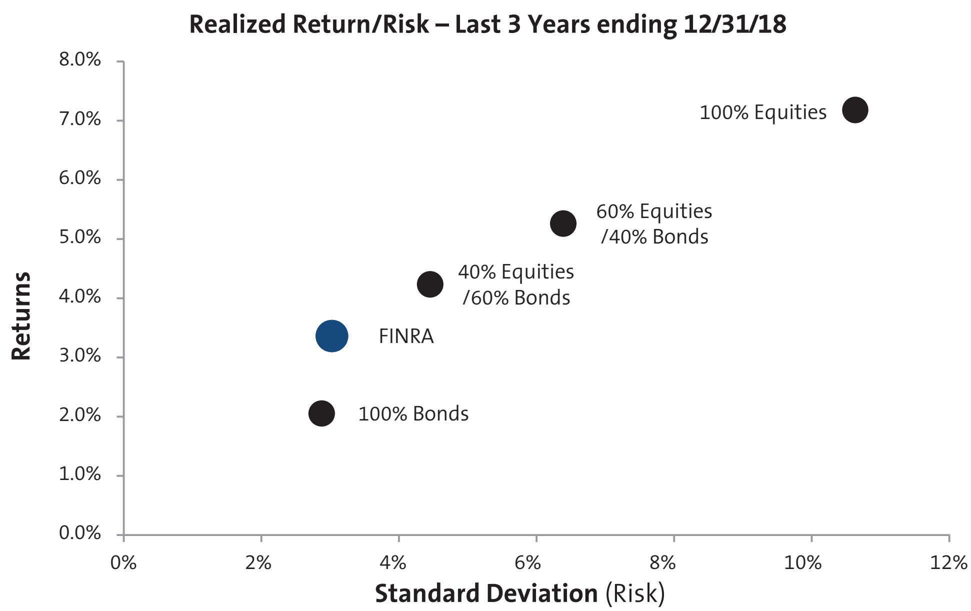
Benchmark Definitions: Equities = MSCI ACWI, Bonds = Bloomberg Barclays U.S. Aggregate Bond Index.

(1) Since inception as of 1/1/04.

(2) The Sharpe ratio is the return earned in excess of the risk-free rate (3-Month U.S. Treasury Bill) on a portfolio, relative to the portfolio's total risk, as measured by the standard deviation of its returns over the measurement period.

* For the purposes of this Investment Committee report, FINRA's investment portfolio includes the FINRA Investor Education Foundation's investments and investments net of their related receivables and payables on the consolidated balance sheet. The values reported exclude Section 31 fees received but not yet remitted to the U.S. Securities and Exchange Commission.

Investment Committee Report (continued)



As shown above, FINRA's investment portfolio outperformed a passive portfolio of high quality bonds by approximately 130 basis points (or 1.3 percent) over the rolling 3-year period, while exhibiting a volatility level of just 10 basis points (or 0.10 percent) higher. While the portfolio did not keep up with higher-returning equity markets, the inherent risk borne by the portfolio has been significantly lower, in line with the portfolio's investment objectives.

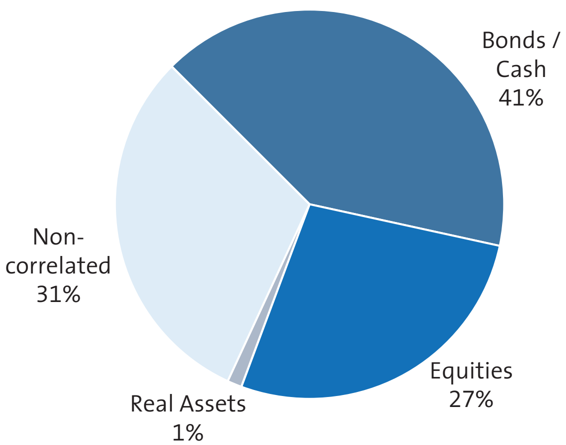
The FINRA Board is responsible for FINRA's investments and approved the charter that guides the FINRA Investment Committee. The Investment Committee, which is composed of members of the Board and other outside investment professionals, advises the Board and provides guidance in determining the appropriate policy, guidelines and allocation for FINRA's investments. The FINRA Investment Office is responsible for management of the investments within the framework of the investment policy. FINRA engages investment consultants to support the Investment Office as needed. The Investment Committee met five times during 2018.

FINRA invests its financial reserves with the objective of creating a lower-risk portfolio than a traditional 60 percent stock/ 40 percent bond allocation as measured by standard deviation. In addition, due to the high correlation of FINRA's operating revenues with traditional equity and bond markets, it is important to diversify the portfolio's investments away from these market segments. In 2018, the Investment Committee continued to direct the gradual implementation of revisions to FINRA's investment policy that were approved by the Board in December 2016. The revised policy consists of a core portfolio of stocks and bonds and a satellite portfolio of strategies with lower correlations to the capital markets for risk-managed diversification. The policy increases portfolio liquidity and reduces overall fees, while remaining consistent with FINRA's low risk tolerance. With this policy, FINRA continues to maintain a broadly diversified investment portfolio, representing a wide range of assets and asset classes, in order to attain acceptable levels of risk as determined by the Board. The Investment Committee reviews the policy annually and may recommend changes subject to approval by the Board.

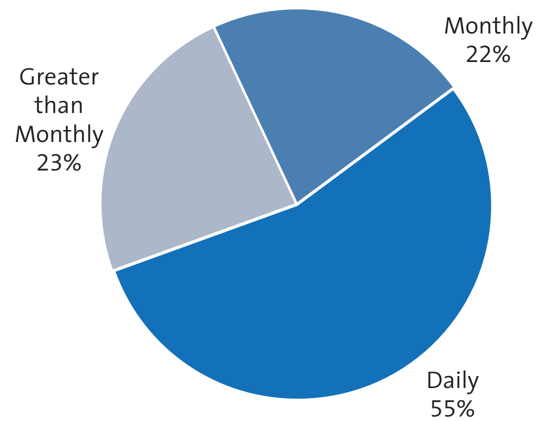
Investment Committee Report (continued)

The charts below show portfolio exposures and general liquidity as of December 31, 2018. Primary exposures are 41 percent bonds/cash, 27 percent equities, and 31 percent in non-correlated assets. Over half of the portfolio can be available on a daily basis.

Exposures as of December 31, 2018



Liquidity as of December 31, 2018



FINRA has an Investments Conflicts of Interest policy that establishes the standards governing the separation of investment activities and decisions from FINRA's regulatory operations. FINRA's investment strategy limits the direct ownership of investment assets to debt securities, mutual and other commingled funds, Treasury futures, limited partnership interests and shares in pooled investment funds. Within our fixed income portfolio, all securities in the banking and brokerage sectors are held in a blind trust, in order to prohibit any knowledge of or participation in the making of such investments by any FINRA regulatory personnel, and to avoid any appearance of a conflict of interest with FINRA's responsibilities. Our limited partnership interest and our investments in public and private funds are each maintained as a pooled vehicle in which FINRA has neither management discretion nor direct ownership of the underlying investments.

Third-party providers make all implementation decisions within the portfolio. With respect to internal activities, the oversight and management of the portfolio is performed by the Investment Committee and limited to essential staff only—defined as the Chief Executive Officer, Chief Financial and Administrative Officer, Investment Office, Corporate General Counsel, Corporate Secretary, Internal Audit and FINRA subject-matter experts assisting the internal auditors and the independent auditor in the performance of audit responsibilities with respect to the FINRA investment portfolio. With those exceptions, no individual in the regulatory arm of the organization has access to information regarding the securities within our investment portfolio.

Members of the Investment Committee:

Luis M. Viceira, Chair
John B. Ehnes
Richard J. Flannery
William H. Heyman
Charles I. Plosser
Richard C. Romano
George (Gus) Sauter
John W. Thiel

June 25, 2019

Audit Committee Report

Year Ended December 31, 2018

The Audit Committee of the Board of Governors (Board) assists the Board in fulfilling its responsibility for Board oversight of the quality and integrity of the accounting, auditing and financial reporting practices of FINRA in accordance with the Charter adopted by the Board.

Each member of the Audit Committee is an independent director as defined by the U.S. Securities and Exchange Commission's (SEC) Rule 10A-3 under the Securities Exchange Act of 1934, Listing Standards Relating to Audit Committees. In addition, the Audit Committee and Board have determined that Leslie F. Seidman and Eileen K. Murray are audit committee financial experts, as defined by the SEC.

During 2018, the Audit Committee met seven times.

The Charter and the By-Laws of FINRA make the Chief Audit Executive directly responsible to the Audit Committee. In all material respects, the Charter complies with standards applicable to publicly-owned companies. (The Charter for the FINRA Audit Committee is available at: *www.finra.org/about/audit-committee-charter*.)

Additionally, the Charter gives the Audit Committee responsibility for monitoring the independence of the independent auditor, recommending the appointment of the independent auditor for approval by the Board, ensuring sufficient scope of independent auditor activities to perform an adequate financial statement audit and ensuring the independent auditor is fairly and appropriately compensated for its effort. The Charter makes clear that the independent auditor is accountable to the Audit Committee and the Board, as representatives of the members and the public. In addition, the Audit Committee discusses significant areas of the audit engagement with the independent auditor, with and without management present, as needed.

In discharging its oversight responsibility, the Audit Committee reviewed the assessments of audit risk and the audit plans of both the independent and internal auditors. The Audit Committee also discussed with management, the internal auditors, and the independent auditor the quality and adequacy of FINRA's internal controls and the internal audit organization, responsibilities, budget and staffing.

In conducting its formal annual assessment of the independent auditor, Audit Committee considerations include, but are not limited to, the following factors: (i) the most recent results from surveys conducted by management regarding the performance of the independent auditor, incorporating audit quality, the experience of the engagement team, reasonableness of audit cost, Public Company Accounting Oversight Board (PCAOB) inspection results of the independent auditor and the ongoing strength of the independent audit firm's reputation; (ii) the length of time the firm has served as FINRA's independent auditor; and (iii) the timeliness of the independent auditor in escalating issues and reporting results to and answering questions proposed by the Audit Committee.

The lead audit partner, having primary responsibility for the audit, rotates off the engagement every five years, and the Audit Committee is involved in the selection of the lead audit partner. The current lead audit partner was appointed in July 2016.

Ernst & Young LLP (EY) has served as FINRA's auditor since 1986.

Audit Committee Report (continued)

The Audit Committee obtained a written statement from EY, describing all relationships with FINRA. The Audit Committee discussed those relationships and was satisfied that none of the relationships were incompatible with the auditor's independence. The Audit Committee has reviewed and approved all services, including non-audit services, performed by EY for FINRA and the associated fees before initiation of each engagement. We have summarized such services and fees in the following table:

	FINRA	
	2018	2017 (1)
Audit services (2)	$1,096,000	$1,189,000
Audit-related services (3)	291,700	277,700
Tax services (4)	130,770	116,530
All other services (5)	—	12,168
Total	$1,518,470	$1,595,398

(1) FINRA has updated the 2017 fees from the prior year's report to reflect final amounts paid for the 2017 approved services.

(2) For 2018, audit services represent the consolidated financial statement audit. For 2017, audit services represent the consolidated financial statement audit and the audit of internal control over financial reporting.

(3) Audit and attest services provided to FINRA and subsidiaries.

(4) Tax services represent fees related to tax return preparation and review services in connection with the 2018 and 2017 Form 990s and related Form 990-Ts, as well as other tax compliance, advice and planning.

(5) All other services represent EY's advisory services related to certain compliance matters.

The Audit Committee discussed and reviewed with the independent auditor all communications required by applicable professional standards. Further, the Audit Committee has reviewed and discussed with management and EY, with and without management present, the consolidated audited financial statements as of December 31, 2018, and EY's report on the consolidated financial statements. Based on those discussions, the Audit Committee recommended to the Board that FINRA's audited consolidated financial statements be included in the Annual Report for the year ended December 31, 2018.

Members of the Audit Committee:

Leslie F. Seidman, Chair
Andrew S. Duff
John B. Ehnes
Eileen K. Murray

June 25, 2019

Management Compensation Committee Report

Year Ended December 31, 2018

FINRA Compensation Philosophy

FINRA's compensation philosophy is a pay-for-performance model that seeks to achieve pay levels in line with the competitive market while meeting the objectives of attracting, developing and retaining high-performing individuals who are capable of achieving our mission, and to provide rewards commensurate with individual contributions and FINRA's overall performance. This philosophy applies to employees at all levels within the organization.

Benchmarking

FINRA strives to be competitive with the external market when establishing starting pay rates, annual incentives and salary structures. A number of external sources are leveraged to compile market data to establish these structures. FINRA uses specific position survey data to evaluate skill sets and benchmarks the compensation paid to internal talent to determine whether compensation is comparable to the price that those skills would command on the open market. Ultimately, in assessing how to price staff positions, FINRA places an emphasis foremost on the demands and competitiveness of each job to ensure that FINRA is paying equitably for skills, expertise and performance level within the overall context of remaining comparable to the market.

Defining the relevant employment market for competitive compensation benchmarking purposes is a significant challenge for FINRA due to the scarcity of natural comparisons, the uniqueness of functions performed, the need for specialized expertise in financial services and securities law and a constantly changing environment under heightened scrutiny.

As part of its compensation philosophy, FINRA has determined that its competitive compensation positioning for all employees should be considered against a broad section of financial services and capital market companies, as this is the most likely sector from which FINRA will recruit talent, and that would recruit talent away from the Company. FINRA also benchmarks against general industry positions and law departments for jobs that are not unique to the financial services industry. FINRA recognizes that it does not provide fully competitive opportunities, particularly in the equity/long-term incentive area, when compared to certain global investment and securities firms. As a result, benchmarking for key executives will follow the same philosophy but with ranges geared to offset the lack of long-term incentives.

Executive Compensation

The Management Compensation Committee (the Committee), which is composed solely of public members of the Board of Governors (Board), is responsible for approving salary levels and incentive compensation ranges for top-level executives. The Committee determines the incentive compensation awards based on actual performance. In determining salary and incentive compensation, management and the Committee consider operational, strategic and financial factors in addition to individual performance. The salary and incentive compensation recommendations for the CEO are reviewed and approved by the Board annually. The Committee met five times during 2018.

Management Compensation Committee Report (continued)

The Committee has the sole right and responsibility to hire and terminate a compensation consultant. In 2018, as in past years, the Committee engaged Mercer, Inc. (Mercer), an independent third-party compensation consultant, to prepare a compensation study, which included objective analysis of current compensation levels and benchmarking using information from a comparable segment of the market for key executives. To ensure the independence of Mercer:

- throughout the year, Mercer reported directly and exclusively to the Committee;
- no Mercer employee was hired by FINRA;
- Mercer provided no significant services, other than compensation consulting services, to FINRA;
- any interaction between Mercer and FINRA executive management was limited to discussions on behalf of the Committee and information that was presented to the Committee for approval; and
- fees paid to Mercer for compensation consulting services were reasonable and in line with industry standards.

In determining a benchmarking strategy for key executives, financial services organizations (broker-dealers, investment banks, Federal Reserve banks, commercial banks, insurance companies, exchanges and regulators) were determined to be the most relevant group for comparison purposes. The Committee and Mercer engaged in substantial research and consideration of the functions and operations of several potential comparisons as well as general competitive conditions. Ultimately, the Committee approved a benchmarking process for key executives that focused on the following sources:

- A public comparison group comprising a blend of financial services organizations engaged in brokerage or other related banking activities.
- Public exchanges and regulators.
- Financial services industry survey data.

The Committee will routinely review the aforementioned sources in determining annual salary and incentive compensation.

Management Compensation Committee Report (continued)

Summary Compensation Table

The following table presents actual 2018 and 2017 compensation data in the year paid (all amounts are in dollars). The 2019 salary information represents the base annual salary at which the named executives, as of June 25, 2019, are compensated. It does not represent 2019 year-to-date earnings. The 2019 incentive compensation amounts represent the actual payment in March 2019 based on 2018 performance. Other amounts, including deferred compensation and other benefits, are not presented for 2019, as these accumulate over the course of the year and final amounts are not determined until year-end. The top 10 executives are determined based on total 2019 salary and incentive compensation as described above.

Name and principal position		Salary (1)	Incentive compensation (2)	Other compensation and deferrals (3)	Other benefits (4)	Total
Robert W. Cook	2019	1,000,000	1,500,000 (5)	*	*	2,500,000 (5)
President and Chief Executive Officer	2018	1,000,000	1,350,000 (6)	520,268	10,104	2,880,372 (6)
	2017	1,000,000	0 (7)	440,984	10,539	1,451,523
Todd T. Diganci	2019	600,000	685,000	*	*	1,285,000
EVP – Chief Financial and	2018	600,000	625,500	142,195	25,683	1,393,378
Administrative Officer	2017	600,000	695,000	145,105	37,250	1,477,355
Steven J. Randich	2019	500,000	580,000	*	*	1,080,000
EVP and Chief Information Officer	2018	500,000	527,000	269,287	35,101	1,331,388
	2017	500,000	580,000	239,633	33,415	1,353,048
Robert L. D. Colby	2019	500,000	500,000	*	*	1,000,000
EVP and Chief Legal Officer	2018	500,000	441,000	139,275	42,414	1,122,689
	2017	500,000	490,000	173,840	29,297	1,193,137
Bari Havlik	2019	490,000	475,000	*	*	965,000
EVP, Member Supervision	2018 (8)	301,443	—	35,750	210,486	547,679
	2017	—	—	—	—	—
Thomas R. Gira	2019	465,000	470,000	*	*	935,000
EVP, Market Regulation and	2018	450,000	418,500	16,500	38,680	923,680
Transparency Services	2017	450,000	465,000	76,230	28,027	1,019,257
Susan Schroeder	2019	430,000	450,000	*	*	880,000
EVP, Enforcement	2018 (9)	416,154	400,000	118,788	30,396	965,338
	2017 (9)	353,390	240,000	214,731	30,176	838,297
Cameron K. Funkhouser	2019	375,000	418,000	*	*	793,000
EVP, Office of Fraud Detection and	2018	375,000	384,500	16,500	43,837	819,837
Market Intelligence	2017	375,000	418,000	90,799	30,664	914,463
Marcia E. Asquith	2019	380,000	400,000	*	*	780,000
EVP, Board and External Relations	2018 (9)	364,231	370,000	131,187	34,630	900,048
and Corporate Secretary	2017 (9)	332,308	355,000	128,673	24,909	840,890
Michael G. Rufino	2019	370,000	390,000	*	*	760,000
EVP, Head of Member Supervision –	2018	365,000	380,000	94,633	19,006	858,639
Sales Practice	2017	365,000	413,000	134,050	41,406	953,456

* 2019 deferred compensation and other benefits cannot be fully determined until the end of the calendar year, and are therefore not included in the above table.

1 Salary is paid bi-weekly, one week in arrears. 2019 salary information represents the executives' current base annual rate of pay as of June 25, 2019.

2 Incentive compensation is paid after the close of the calendar year based on the prior year's performance. Payments are reflected in the table above in the year paid, consistent with FINRA's reporting in its Form 990 tax returns. Thus, the amount presented in 2019 was paid in March 2019, based on 2018 performance.

3 Other compensation and deferrals include earnings and accruals in supplemental executive retirement plans, which are not available to all employees. Mr. Diganci, Mr. Gira and Mr. Funkhouser participate in FINRA's supplemental defined benefit retirement plan, which is now closed to new participants. The remaining listed executives are participants in the supplemental defined contribution retirement plan. Other compensation and deferrals also include payments and accruals for multi-year retention arrangements as well as employer-funded 401(k) matching contributions and the accrual of benefits in FINRA's employee retirement plans. The 401(k) and retirement plans are generally available to all employees.

4 Other benefits include taxable and non-taxable benefits such as employer-paid health, life and disability insurance, which are generally available to all employees. They also include parking, travel subsidies, tax gross-ups and other miscellaneous fringe benefits.

5 In 2019, Mr. Cook contributed $150,000 of his 2018 incentive compensation (less estimated taxes payable by him) to the FINRA Investor Education Foundation. After consideration of this contribution, Mr. Cook's total salary and incentive compensation for 2019 is effectively $2,350,000.

6 In 2018, Mr. Cook contributed $675,000 of his 2017 incentive compensation (less estimated taxes payable by him) to the FINRA Investor Education Foundation. After consideration of this contribution, Mr. Cook's total compensation for 2018 was effectively $2,205,372.

7 Mr. Cook was eligible for but declined to accept incentive compensation for 2016.

8 The 2018 compensation for Ms. Havlik represents a partial year of employment.

9 The year-over-year increase in compensation for these individuals is driven by their promotion to Executive Vice President during 2017.

Components of Compensation

Direct Compensation

- Base salaries consist of job-grade structures to provide for appropriate flexibility in hiring and retention. Actual salaries are based on job content, performance and relevant experience levels, and may fall above or below competitive levels.
- Incentive compensation is an additional "at-risk" compensation that is performance-based and determined in relation to individual achievements and FINRA's overall performance. The size of the actual award varies based on goal achievement, performance, grade level and degree of responsibility within the organization. If awarded, it is paid as a lump sum in the following year.

Indirect Compensation

- Supplemental retirement benefits are provided for top executives and are either defined benefit or defined contribution based on employment start date. These plans are non-qualified and are based on salary, officer level and, depending on officer level, a portion of incentive compensation.
- Employee and family health, life and other insurance, pension and 401(k) deferral and matching programs, health club subsidies and other benefits are generally available to all employees. Additionally, certain executives receive miscellaneous taxable fringe benefits that may include parking, travel subsidies and similar minor items.

Members of the Management Compensation Committee:

Rochelle B. Lazarus, Chair
William H. Heyman
Eileen K. Murray
Hillary Sale
Luis M. Viceira

June 25, 2019

Management Report on Internal Control Over Financial Reporting

FINRA management is responsible for the preparation and integrity of the consolidated financial statements appearing in our annual report. The consolidated financial statements were prepared in conformity with U.S. generally accepted accounting principles (U.S. GAAP) and include amounts based on management's estimates and judgments. FINRA management is also responsible for establishing and maintaining adequate internal control over financial reporting and for the assessment of the effectiveness of internal control over financial reporting. Internal control over financial reporting is a process designed by management to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with U.S. GAAP.

FINRA maintains a system of internal control that is designed to provide reasonable assurance as to the fair and reliable preparation and presentation of the consolidated financial statements, as well as to safeguard assets from unauthorized use or disposition that could have a material effect on the consolidated financial statements. FINRA's internal control over financial reporting includes written policies and procedures that 1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of FINRA's assets; 2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of consolidated financial statements in accordance with U.S. GAAP, and that receipts and expenditures of FINRA are being made only in accordance with authorizations of FINRA's management and governors; and 3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of FINRA's assets that could have a material effect on the consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements due to error or fraud, including the possibility of the circumvention or overriding of controls. Projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision of the President and Chief Executive Officer and the Chief Financial and Administrative Officer, FINRA's management assessed the effectiveness of FINRA's internal control over financial reporting as of December 31, 2018. This evaluation included, among other things, reviews of the documentation of controls, evaluations of the design effectiveness of controls and reviews of evidence supporting the operating effectiveness of controls. Based on this assessment, we conclude that FINRA maintained effective internal control over financial reporting as of December 31, 2018.

June 25, 2019

Robert W. Cook
President and Chief Executive Officer

Todd T. Diganci
Executive Vice President – Chief Financial and
Administrative Officer

Report of Independent Registered Public Accounting Firm

To the Board of Governors of
Financial Industry Regulatory Authority, Inc.

Opinion on the Financial Statements

We have audited the accompanying consolidated balance sheets of the Financial Industry Regulatory Authority, Inc. (FINRA or the Company) as of December 31, 2018 and 2017, the related consolidated statements of operations, comprehensive income, changes in equity and cash flows for the years then ended, and the related notes (collectively referred to as the "consolidated financial statements"). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of FINRA at December 31, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Basis for Opinion

These financial statements are the responsibility of FINRA's management. Our responsibility is to express an opinion on FINRA's financial statements based on our audits. We are required to be independent with respect to FINRA in accordance with the relevant ethical requirements relating to our audits.

We conducted our audits in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States) and 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 of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits we are required to obtain an understanding of internal control over financial reporting but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that our audits provide a reasonable basis for our opinion.

Ernst & Young LLP

We have served as FINRA's auditor since 1986.

Tysons, Virginia
June 25, 2019

FINRA Consolidated Balance Sheets

(In millions)

	December 31,	
	2018	2017
Assets		
Current assets:		
Cash and cash equivalents	$ 298.7	$ 311.7
Cash held at Consolidated Entity	9.9	—
Investments:		
Trading, at fair value	563.1	431.6
Available-for-sale, at fair value	312.5	323.1
Receivables, net	118.6	146.2
Investments receivable	0.2	78.1
Other current assets	23.3	22.7
Total current assets	1,326.3	1,313.4
Property and equipment:		
Land, buildings and improvements	127.2	127.6
Data-processing equipment and software	130.1	113.8
Furniture, equipment and leasehold improvements	69.4	70.5
	326.7	311.9
Less accumulated depreciation and amortization	(212.7)	(205.9)
Total property and equipment, net	114.0	106.0
Other investments:		
Investments of Consolidated Entity, at fair value	395.6	—
Pooled investment funds, at fair value	373.3	309.8
All other	0.3	0.4
Limited partnership	—	642.8
Other assets	30.0	30.4
Total assets	$2,239.5	$2,402.8

See accompanying notes.

FINRA Consolidated Balance Sheets (continued)

(In millions)

	December 31, 2018	December 31, 2017
Liabilities and equity		
Current liabilities:		
Accounts payable and accrued expenses	$ 27.0	$ 30.8
Accrued personnel and benefit costs	200.3	192.9
Deferred revenue	66.0	65.9
Deposits and renewals	71.4	70.2
Investments payable	1.7	1.3
Other current liabilities	8.1	7.7
SEC fee payable	140.4	195.9
Total current liabilities	514.9	564.7
Accrued pension and other postretirement benefit costs	147.4	183.7
Deferred revenue	13.8	13.0
Long-term debt	14.0	15.2
Other liabilities	25.0	30.3
Total liabilities	715.1	806.9
Equity	1,606.6	1,675.3
Accumulated other comprehensive loss		
Unrealized (loss) gain on available-for-sale investments	(0.6)	32.0
Net unrecognized employee benefit plan amounts	(81.6)	(111.4)
Total accumulated other comprehensive loss	(82.2)	(79.4)
Total equity	1,524.4	1,595.9
Total liabilities and equity	$2,239.5	$2,402.8

See accompanying notes.

FINRA Consolidated Statements of Operations

(In millions)

	Years Ended December 31,	
	2018	2017
Revenues		
Operating revenues		
Regulatory revenues	$ 466.1	$ 439.0
User revenues	296.3	290.9
Contract services revenues	95.0	98.2
Total operating revenues	857.4	828.1
Fines	61.0	64.9
Activity assessment revenues	531.4	547.9
Total revenues	1,449.8	1,440.9
Activity assessment cost of revenues	(531.3)	(547.9)
Net revenues	918.5	893.0
Expenses		
Compensation and benefits	689.3	692.0
Professional and contract services	134.5	148.6
Computer operations and data communications	53.7	51.7
Occupancy	38.3	36.9
Depreciation and amortization	16.4	15.4
General and administrative	43.1	47.7
Total expenses	975.3	992.3
Interest and dividend income	27.6	26.0
Operating loss	(29.2)	(73.3)
Other (expense) income		
Net realized and unrealized investment (losses) gains	(51.1)	32.6
Equity method earnings from other investments	12.0	83.9
Other expense	(0.4)	(1.6)
Net (loss) income	$ (68.7)	$ 41.6

See accompanying notes.

FINRA Consolidated Statements of Comprehensive (Loss) Income

(In millions)

	Years Ended December 31,	
	2018	2017
Net (loss) income	$(68.7)	$ 41.6
Change in unrealized gain or loss on available-for-sale investments	(32.6)	31.3
Employee benefit plan adjustments	29.8	(28.7)
Comprehensive (loss) income	$(71.5)	$ 44.2

See accompanying notes.

FINRA Consolidated Statements of Changes in Equity

(In millions)

	Equity	Accumulated Other Comprehensive Income (Loss): Unrealized Gain (Loss) on Available-for-Sale Investments	Accumulated Other Comprehensive Income (Loss): Net Unrecognized Employee Benefit Plan Amounts	Total
Balance, January 1, 2017	$1,633.7	$ 0.7	$ (82.7)	$1,551.7
Comprehensive income	41.6	31.3	(28.7)	44.2
Balance, December 31, 2017	1,675.3	32.0	(111.4)	1,595.9
Comprehensive loss	(68.7)	(32.6)	29.8	(71.5)
Balance, December 31, 2018	$1,606.6	$ (0.6)	$ (81.6)	$1,524.4

See accompanying notes.

FINRA Consolidated Statements of Cash Flows

(In millions)

	Years Ended December 31,	
	2018	2017
Reconciliation of net (loss) income to cash provided by (used in) operating activities		
Net (loss) income	$(68.7)	$ 41.6
Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities:		
Depreciation and amortization	16.4	15.4
Net realized and unrealized investment losses (gains)	51.1	(32.6)
Equity method investments	54.6	(60.3)
Bad debt expense	3.5	2.7
Loss on disposal of property and equipment	0.4	2.1
Net change in operating assets and liabilities:		
Receivables, net	24.1	(21.3)
Other current assets	(0.6)	(2.8)
Other assets	1.2	(5.1)
Accounts payable and accrued expenses	(2.1)	(0.6)
Accrued personnel and benefit costs	7.4	2.3
Deferred revenue	0.9	(1.0)
Deposits and renewals	1.2	(7.6)
SEC fee payable	(55.5)	22.2
Other current liabilities	0.4	—
Accrued pension and other postretirement benefit costs	(6.5)	7.5
Other liabilities	(5.3)	(1.2)
Net cash provided by (used in) operating activities	$ 22.5	$(38.7)

See accompanying notes.

FINRA Consolidated Statements of Cash Flows (continued)

(In millions)

	Years Ended December 31,	
	2018	2017
Cash flow from investing activities		
Net (purchases) proceeds from sales of trading securities	$(144.8)	$ 268.6
Proceeds from redemptions of available-for-sale investments	20.2	105.6
Purchases of available-for-sale investments	(29.9)	(104.7)
Equity method investments	167.3	55.8
Purchases of other investments	(100.0)	(297.8)
Net purchases of property and equipment	(25.2)	(7.3)
Other	(2.2)	(1.3)
Cash flow from investing activities of the Consolidated Entity		
Purchases of other investments	(16.7)	—
Proceeds of redemptions of other investments	84.6	—
Cash contribution at fund transfer date	22.3	—
Net cash (used in) provided by investing activities	(24.4)	18.9
Cash flow from financing activities		
Principal payment on long-term debt	(1.2)	(0.9)
Net cash used in financing activities	(1.2)	(0.9)
Decrease in cash and cash equivalents	(3.1)	(20.7)
Cash and cash equivalents at beginning of year	311.7	332.4
Cash and cash equivalents at end of year	$ 308.6	$ 311.7

See accompanying notes.

FINRA 2018 Notes to Consolidated Financial Statements

1. ORGANIZATION AND NATURE OF OPERATIONS

References to the terms “we,” “our,” “us,” “FINRA” or the “Company” used throughout these Notes to Consolidated Financial Statements refer to the Financial Industry Regulatory Authority, Inc. (FINRA), a Delaware corporation, and its wholly owned subsidiaries. FINRA wholly owns the following significant subsidiaries: FINRA Regulation, Inc. (FINRA REG) and the FINRA Investor Education Foundation (the Foundation). The Foundation is a tax-exempt membership corporation incorporated in the State of Delaware, with FINRA as the sole member.

We are a self-regulatory organization (SRO) for brokerage firms doing business with the public in the United States. We regulate the activities of U.S. broker-dealers and perform market regulation pursuant to our own statutory responsibility and under contract for certain exchanges. Our statutory regulatory functions include examinations of securities firms, continuous surveillance of markets, reviews of fraud allegations and disciplinary actions against firms and registered representatives. FINRA’s examination process is risk-based, meaning our approach for identifying firms for examination is based upon risk, scale and scope of firm operations. We conduct examinations to determine whether firms are in compliance with federal securities law and FINRA rules, as well as in response to investor complaints, terminations of brokerage employees for cause, arbitrations and referrals from other regulators. FINRA operates unique equity and options cross-market surveillance programs. Employing advanced technology, these programs collect and integrate trading data across exchanges and alternative trading systems to detect potential market manipulation and other rule violations. We provide a heightened and expedited review of allegations of serious fraud and consolidate recognized expertise in expedited fraud detection and investigation to prevent further harm to investors. We bring disciplinary actions against firms and their employees that may result in sanctions including censures, fines, suspensions and, in egregious cases, expulsions or bars from the industry. In appropriate cases, we require firms and individuals to provide restitution to harmed investors and often impose other conditions on a firm’s business to prevent repeated wrongdoing.

We perform market regulation services under contract for the New York Stock Exchange LLC (NYSE), NYSE Arca, Inc. (NYSE Arca), NYSE American, LLC (NYSE American), NYSE Chicago, Inc. (NYSE Chicago), NYSE National, Inc. (NYSE National), The Nasdaq Stock Market LLC (Nasdaq), Nasdaq BX, Inc. (Boston), Nasdaq PHLX LLC (Philadelphia), Nasdaq ISE, LLC, Nasdaq GEMX, LLC, Nasdaq MRX, LLC, Cboe Global Markets, Inc. (the Cboe, C2, BZX, BYX, EDGA and EDGX exchanges, collectively referred to as Cboe), The Investors Exchange (IEX), the Boston Options Exchange, LLC (BOX), the Miami International Securities Exchange, LLC (MIAX Options), MIAX EMERALD LLC (MIAX EMERALD), and MIAX PEARL LLC (MIAX PEARL). We also regulate the over-the-counter (OTC) securities markets for listed and unlisted equities and the OTC markets for corporate bonds, Treasury Securities, asset-backed instruments, certain government agency instruments, municipal securities and other fixed income instruments.

We provide arbitration and mediation services to assist in the resolution of monetary and business disputes between and among investors, broker-dealers and individual brokers. We also provide dispute resolution services for several exchanges through contractual agreements, thereby offering consistent procedures and the uniformity of a single forum for the resolution of securities-industry related disputes.

We provide technology-driven registration, testing and continuing education, and other regulatory services, as well as operational and support services to firms, other SROs, the U.S. Securities and Exchange Commission (SEC), the North American Securities Administrators Association, state regulators, the investing public, the Conference of State Bank Supervisors and its wholly owned subsidiary, the State Regulatory Registry LLC (SRR). We continue to enhance BrokerCheck®, a free tool that helps investors research the professional backgrounds of current and former FINRA-registered brokerage firms and brokers, as well as investment adviser firms and representatives.

We are committed to ensuring that investors and market participants have access to market information, so they can more effectively assess securities prices and valuations, through the management and operation of FINRA’s OTC market transparency facilities. These facilities include the Trade Reporting and Compliance Engine® (TRACE®) for fixed income

1. ORGANIZATION AND NATURE OF OPERATIONS (CONTINUED)

securities, the OTC Reporting Facility™ (ORF™) and OTC Bulletin Board® (OTCBB®) for equity securities not listed on an exchange and the Trade Reporting Facilities® (TRFs®), operated in partnership with NYSE and Nasdaq, for OTC trading in equity securities that are listed on an exchange. In this capacity, we provide the public and professionals with timely trade information for equity and debt securities and quotes for certain equity securities.

The Foundation empowers underserved Americans with the knowledge, skills and tools to make sound financial decisions throughout life. The Foundation accomplishes this mission through educational programs and research that help consumers achieve their financial goals and that protect them in a complex and dynamic world.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The accompanying consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP) and include the accounts of the Company, its wholly owned subsidiaries and the Consolidated Entity.

During 2018, we transferred all of our interest in a Limited Partnership (the Limited Partnership) to the Consolidated Entity, a variable interest entity (VIE) for which the Company is the primary beneficiary. The Limited Partnership was accounted for under the equity method. We account for the Consolidated Entity as an investment company that follows the industry specialized basis of accounting established by U.S. GAAP.

All intercompany balances and transactions have been eliminated in consolidation.

RECLASSIFICATIONS

FINRA has reclassified certain amounts from the prior year to conform to the 2018 presentation. Specifically, amounts previously classified as transparency services, dispute resolution or other revenues are now classified as user revenues in the consolidated statements of operations and accompanying notes to the financial statements.

USE OF ESTIMATES

The preparation of these consolidated financial statements requires management to make estimates and assumptions, including estimates of fair value of investments, valuation of investments and assumptions related to our benefit plans, and the estimated service periods related to our recognition of certain revenue, that affect the amounts reported in the consolidated financial statements and accompanying notes. Actual results could materially differ from those estimates.

CONSOLIDATION

FINRA consolidates any VIE in which it is deemed to be the primary beneficiary and reflects the assets, liabilities, revenues, expenses and cash flows of the consolidated VIE on the consolidated financial statements. An entity is determined to be the primary beneficiary if it holds a controlling financial interest. A controlling financial interest is defined as (a) the power to direct the activities of a VIE that most significantly impact the entity's economic performance; and (b) the obligation to absorb losses of the entity or the right to receive benefits from the entity that could potentially be significant to the VIE. The consolidation guidance requires an analysis to determine (a) whether an entity in which the Company holds a variable interest is a VIE; and (b) whether the Company's involvement, through holding interests directly or indirectly in the entity or contractually through other variable interests such as management and performance-based fees, would give it a controlling financial interest. Performance of that analysis requires the exercise of judgment.

The Company determines whether it is the primary beneficiary of a VIE at the time it becomes involved with a VIE and reconsiders that conclusion at each reporting date. In evaluating whether the Company is the primary beneficiary, FINRA

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

evaluates its economic interests in the entity held either directly by the Company or indirectly through related parties. The consolidation analysis can generally be performed qualitatively; however, if it is not readily apparent that the Company is not the primary beneficiary, a quantitative analysis may also be performed.

Investments and redemptions (either by the Company, affiliates of the Company or third parties) or amendments to the governing documents of a VIE could affect an entity's status as a VIE or the determination of the primary beneficiary. At each reporting date, the Company assesses whether it is the primary beneficiary and will consolidate or deconsolidate accordingly.

CASH AND CASH EQUIVALENTS

Cash and cash equivalents include demand cash, cash held in banks and all non-restricted, highly liquid investments with maturities of 90 days or less when acquired.

Additionally, cash held at the Consolidated Entity may include overnight investments and money market funds held with financial institutions. As of December 31, 2018, the Consolidated Entity held no cash and cash equivalents in foreign currencies. Cash held at the Consolidated Entity represents cash that may only be used to settle obligations of the Consolidated Entity. Although not legally restricted, this cash is not available to fund the general liquidity needs of FINRA.

INVESTMENTS

Debt and Marketable Equity Securities

At the time of purchase, we classify individual debt and marketable equity securities as trading, available-for-sale or held-to-maturity based on the type of security and our intent and ability to sell or to hold the securities. We have designated our investments in debt and marketable equity securities as either trading or available-for-sale. Trading securities are carried at fair value, with changes in fair value recorded as a component of net realized and unrealized investment (losses) gains in the consolidated statements of operations. We present cash flows from purchases and sales of trading securities as investing activities based on the nature and purpose for which the securities were acquired. We record available-for-sale securities at fair value and recognize temporary changes in fair value as unrealized (losses) gains as a separate component of other comprehensive (loss) income.

Fair value is determined based on quoted market prices, when available, or on estimates provided by external pricing sources or dealers who make markets in such securities. Realized gains and losses on sales of securities are included in earnings using the average cost method. Investment receivables or payables relate to security trades and other investment redemptions or purchases executed on or prior to the balance sheet date, but not yet settled, as we follow trade-date accounting.

Other Investments

Investments held in the Consolidated Entity include pooled investment vehicles without a readily determinable fair value. These investments are generally valued at the most recent net asset value per unit or capital account information from the general partners of such vehicles. Investment transactions are accounted for on a trade-date basis. For the purposes of determining net realized gains and losses, the Consolidated Entity uses a specific identification methodology.

FINRA elected the fair value option for its investments in pooled investment funds to better reflect the value of these investments. Such election is irrevocable and applied on a financial instrument by financial instrument basis at initial recognition. These pooled investment funds calculate net asset value per share (or its equivalent) as the investment account value in the absence of readily ascertainable market values to determine fair value. Interest and dividends are recorded when reported to us.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

During the time FINRA invested in a limited partnership, it was accounted for under the equity method. The application of the equity method to the limited partnership, including our related equity earnings (losses), retained the investment company accounting applied by such a fund.

Other-Than-Temporary Impairment

FINRA periodically monitors and evaluates the realizability of its available-for-sale and equity method investments. When assessing realizability, including other-than-temporary declines in value, we consider such factors as intent to hold, the extent of the decline in value, the duration of unrealized losses, the potential for recovery in the near term and the probability that we will sell an equity method investment at an amount different from the net asset value of our ownership interest. We also review the financial statements of our equity method investments for potential indicators of impairment. If events and circumstances indicate that a decline in the value of these assets has occurred and is deemed other-than-temporary, the carrying value of the investment is reduced to its fair value and the impairment is charged to earnings.

RECEIVABLES, NET

The Company's receivables are primarily concentrated with FINRA-registered firms, associated persons and exchanges. The consolidated financial statements present receivables net of an allowance for uncollectible accounts. As of December 31, 2018 and 2017, an allowance for uncollectible accounts of $9.9 million and $11 million, respectively, was presented in the accompanying consolidated balance sheets within receivables, net. We calculate the allowance based on the age, source of the underlying receivable and past collection experience. We maintain the allowance at a level that management believes to be sufficient to absorb estimated losses inherent in our accounts receivable portfolio. The allowance as of December 31, 2018 and 2017, primarily related to fines and arbitration activities. The allowance is increased by the provision for bad debts, which is charged against operating results and decreased by the amount of charge-offs, net of recoveries. We base the amount charged against operating results on several factors, including a periodic assessment of the collectibility of each account. In circumstances where a specific firm's inability to meet its financial obligations is known (*e.g.*, bankruptcy filings), we record a specific provision for bad debts to reduce the receivable to the amount we reasonably believe will be collected.

PROPERTY AND EQUIPMENT

FINRA records property and equipment at cost less accumulated depreciation. We expense repairs and maintenance costs as incurred. We calculate depreciation and amortization as follows:

Asset category	Depreciation/amortization method	Estimated useful lives
Buildings and improvements	Straight-line	10 to 40 years
Data-processing equipment and software	Straight-line	2 to 5 years
Furniture and equipment	Straight-line	5 to 10 years
Leasehold improvements	Straight-line	Shorter of term of lease or useful life of improvement

Depreciation and amortization expense for property and equipment totaled $11.4 million and $11.8 million for 2018 and 2017, respectively.

SOFTWARE COSTS

FINRA capitalizes internal use software development costs incurred during the application development stage. Software costs incurred prior to or subsequent to the application development stage are charged to expense as incurred. We

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

capitalize significant purchased application software and operational software programs that are an integral part of hardware, and amortize them using the straight-line method over their estimated useful life, generally three to five years. We expense all other purchased software as incurred.

Unamortized capitalized software development costs of $18 million as of December 31, 2018, were included in the consolidated balance sheets within total property and equipment, net. There were $5.7 million and $5.5 million of net additions to capitalized software related to 2018 and 2017. Amortization of capitalized internal use software costs totaled $2.6 million and $1.0 million related to 2018 and 2017 and was included in depreciation and amortization in the consolidated statements of operations.

IMPAIRMENT OF LONG-LIVED ASSETS

We review our long-lived assets for impairment whenever facts and circumstances indicate that long-lived assets or other assets may be impaired. If indicators are present, we perform an evaluation of recoverability that compares the estimated future, undiscounted cash flows associated with the asset to the asset's carrying amount. If the evaluation fails the recoverability test, we would then prepare a discounted cash flow analysis to estimate fair value and the amount of any impairment. In 2018 and 2017, there were no indicators of long-lived asset impairment, and no impairment charges were recognized.

DEFERRED REVENUE

Deferred revenue represents cash received for which we have not yet provided the related services. Included in deferred revenue is the unearned portion of mediation fees, arbitration fees, registration fees and firm application fees. We recognize revenue from the upfront initial components of these fees on a straight-line basis over estimated service periods.

The following chart reflects our estimated service periods and the basis for those estimated service periods for each deferred fee:

Fee type	Service period	Estimation basis
Mediation fees	4 months	Average duration of a mediation case
Arbitration fees	14 months	Average duration of an arbitration case
Registration fees	4 years	Average time individuals spend at a single firm
Firm application fees	13 years	Average lifespan for all member firms

The estimated service period for firm application fees, based on historical experience, is 13 years as of December 31, 2018, and 12 years as of December 31, 2017. The change in estimated service period represents a change in accounting estimate that did not have a material effect on FINRA's consolidated statements of operations.

DEPOSIT AND RENEWAL LIABILITIES

FINRA's deposit and renewal liabilities primarily represent deposits into our Central Registration Depository (CRD®) system. FINRA-registered firms use these deposits to pay for services, including registration fees charged by states and other SROs.

REVENUE RECOGNITION AND COST OF REVENUE

Revenues are generally measured by an exchange of values and recognized when: (1) there is persuasive evidence of an arrangement; (2) services have been rendered and payment has been contractually earned; (3) the fee is fixed or determinable; and (4) collectability is reasonably assured.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The following table provides a summary of revenues by type for the years ended December 31, 2018 and 2017.

	Years ended December 31,	
	2018	2017
	(in millions)	
Regulatory revenues	$ 466.1	$ 439.0
User revenues		
Registration, qualification exams, conferences and other filing fees	182.1	180.4
Transparency services	73.5	72.2
Dispute resolution	39.1	36.6
Other	1.6	1.7
Total user revenues	296.3	290.9
Contract services revenues	95.0	98.2
Total operating revenues	857.4	828.1
Fines	61.0	64.9
Activity assessment	531.4	547.9
Total revenues	1,449.8	1,440.9
Activity assessment cost of revenues	(531.3)	(547.9)
Net revenue	$ 918.5	$ 893.0

Our recognition policy by type of fee is described in the paragraphs below.

Regulatory Revenues

Regulatory revenues include assessments for the supervision and regulation of firms through examination, policy making, rulemaking and enforcement activities. Regulatory revenues are recorded net of any firm rebates. The primary regulatory revenues are the Trading Activity Fee (TAF), Gross Income Assessment (GIA), Personnel Assessment (PA) and Branch Office Assessment (BOA). The TAF is calculated on the sell side of all transactions by firms in all covered securities regardless of where the trade is executed and is assessed directly on the firm responsible for clearing the transaction. Firms self-report the TAF to us, and we recognize the income in the month the transactions occur. As the TAF is a self-reported revenue stream for us, subsequent adjustments may occur. We recognize these adjustments as revenue adjustments in the period they become known to us. The GIA, PA and BOA represent annual fees charged to firms and representatives. We recognize these fees ratably over the applicable annual period.

User Revenues

User revenues represent amounts charged for initial and annual registrations; qualification examinations; FINRA-sponsored educational programs and conferences; reviews of corporate filings (corporate financing fees), advertisements and disclosures; and transparency and dispute resolution services.

FINRA charges registration fees for all registered representatives and investment advisers. First-year registration and application fees consist of two deliverables that we account for as separate units of accounting: upfront registration delivered at inception and an ongoing service obligation for the remainder of that calendar year. We allocate arrangement consideration to upfront registrations based on our estimates of selling price. We estimate the selling prices of upfront registrations based on our internal cost structure, pricing practices and objectives, and historical prices. We allocate arrangement consideration to the remaining service obligation based on vendor-specific objective evidence of the pricing for these services. Upfront registration revenue is recognized over the estimated service period for individual representatives (four years) and firms (13 years as of December 31, 2018 and 12 years as of December 31, 2017), while the

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

remaining service obligation revenue is recognized ratably over the related remaining annual period. While the pricing model currently in use captures all critical variables, unforeseen changes due to external market forces may result in the revision to some of our inputs. These modifications may result in the allocation of consideration in future periods that differs from the allocation presently in use. Absent a significant change in the pricing inputs, future changes in the pricing model are not expected to materially impact our allocation of arrangement consideration.

Qualification fees consist of examination and continuing education fees. We recognize qualification fees as we administer examinations or continuing education programs. FINRA-sponsored meeting and conference fees include fees paid by financial services industry participants for participating in our educational programs. We recognize these fees when the program or conference takes place. Advertising fees are charged for our review of firms' communications to ensure that they are fair, balanced and not misleading. We recognize advertising fees as revenue when our review is complete. Corporate financing fees are charged for our review of proposed public offerings. We recognize corporate financing fees when our review is completed. FINRA requires the timely disclosure of regulatory actions, liens and judgments, among other things, and charges a fee to review the disclosures to determine whether an applicant is subject to a statutory disqualification or whether the applicant may present a regulatory risk for the firm and customers. FINRA recognizes these disclosure review fees when our review is complete.

Transparency services revenues represent amounts charged for the use of TRACE, our fixed income market real-time price reporting and dissemination service, as well as the ORF service for the reporting of trades and comparison in certain OTC equity securities. TRACE fees include market data fees, as well as fees charged on secondary market transactions in eligible fixed income securities reported to us. The OTCBB is a regulated quotation service in which fees are charged for a variety of services related to the display of real-time quotes in OTC equity securities that are eligible for quotation on the OTCBB. In addition, fees are earned for the sale of market data from the OTCBB and the ORF. We recognize transparency services revenues as the transactions occur or when the market data is sold.

FINRA earns fees during the arbitration and mediation processes. Certain arbitration fees, such as initial, counterclaim, cross-claim and other filing fees, and surcharge fees, relate to the entire period covered by an arbitration case, and are recognized as revenue over the average duration of an arbitration case (14 months). Mediation filing fees are recognized over the average duration of a mediation case (four months). All other arbitration- and mediation-related fees, such as pre-hearing and hearing processing fees, adjournment fees, hearing session fees and mediation session fees, which are event-driven, are recognized as the service is provided.

Contract Services Revenues

Contract services revenues represent amounts charged for regulatory services provided primarily to the NYSE markets, the Nasdaq markets, the Cboe markets and other exchanges, as well as the TRFs, for services including surveillance reviews, investigations, examinations and the disciplinary process. Contract services revenues also include fees for the mortgage licensing system FINRA developed and deployed to SRR. We recognize contract services revenues as the services are provided according to the terms and timeframes associated with each individual contract.

Fines

Fines represent sanctions for rule violations. FINRA recognizes fine revenue upon issuance of a written consent or disciplinary decision. We do not view fines as part of our operating revenues. FINRA limits the use of fine monies to capital expenditures and regulatory and other projects reported to and approved by our Finance, Operations and Technology Committee or Board of Governors (Board).

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Activity Assessment Revenues and Cost of Revenues

FINRA, as an SRO, pays certain fees and assessments to the SEC pursuant to Section 31 of the Securities Exchange Act of 1934. These fees are designed to recover costs incurred by the government for the supervision and regulation of securities markets and securities professionals, and are calculated based on the aggregate dollar amount of sales of covered securities transacted by or through any firm other than on a national securities exchange. Such covered transactions are reported to us through the TRFs and ORF. We remit these SEC fees to the U.S. Treasury semiannually, in March and September.

We recover the cost of the Section 31 fees and assessments through an activity assessment, charged to the firm responsible for clearing the transaction, based on the aggregate dollar amount of sales of covered securities transacted by or through any firm other than on a national securities exchange. The assessments billed to securities firms are recognized when the transactions are reported. As of December 31, 2018 and 2017, we had $36.0 million and $50.3 million, respectively, of SEC fee receivables presented in the accompanying consolidated balance sheets within receivables, net. FINRA, as the primary obligor to the SEC, reports the activity assessment on a gross basis within revenues. Amounts due to the SEC are reported as a cost of revenue. We report amounts pending remittance to the SEC in SEC fee payable in the accompanying consolidated balance sheets.

Activity assessment revenues and cost of revenues are driven by third-party providers and securities firms reporting activity in a complete, accurate and timely manner. As a result, subsequent adjustments may occur. We recognize any resulting activity assessment adjustments in the period they become known to us.

Interest and Dividend Income

FINRA recognizes interest income from cash, trading investments and available-for-sale investments as it is earned. Dividend income is recognized on the ex-dividend date. Interest and dividend income from the Consolidated Entity is accounted for in the same manner.

CLOUD COMPUTING COSTS

We account for our cloud computing arrangement as a service contract and expense applicable costs as incurred. As our hosting arrangement does not give us the contractual right to the software at any time during the hosting period without penalty, we are not deemed to have a software license. Cloud computing costs totaled $19.9 million and $18.8 million for the years ended December 31, 2018 and 2017, respectively, and were included in computer operations and data communications in the consolidated statements of operations.

PENSION AND OTHER POSTRETIREMENT LIABILITIES

FINRA provides two non-contributory defined benefit pension plans for the benefit of eligible employees. The non-contributory defined benefit plans consist of a qualified Employees Retirement Plan (ERP) and a non-qualified Supplemental Executive Retirement Plan (SERP). Both plans are now closed to new participants. We also offer access to retiree medical coverage for eligible retirees and their dependents. Eligible retirees pay the full premium cost to be enrolled in the Company's retiree medical coverage. Additionally, we provide a Retiree Medical Savings Plan to help our retirees offset health care premiums during retirement. Under the Retiree Medical Savings Plan, employer-funded defined contribution Retiree Medical Accounts are created for eligible employees and fixed annual credits are applied to those accounts for each year of FINRA service beginning at age 40.

In calculating the expense and liability related to all of the abovementioned plans, we use several statistical and other factors, which attempt to anticipate future events. Key factors include assumptions about the expected rates of return on plan assets and the discount rate as determined by FINRA, within certain guidelines, as well as assumptions regarding

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

future salary increases, mortality, turnover, retirement ages and the medical expense trend rate. We consider market conditions, including changes in investment returns and interest rates, in making these assumptions. The discount rate used in the calculations is developed using a composite yield curve analysis based on a portfolio of high-quality, non-callable, marketable bonds. We determine the long-term rate of return based on analysis of historical and projected returns as prepared by our actuary and external investment consultant. FINRA's Pension/401(k) Plan Committee (the Pension Committee) reviews and advises FINRA management on both the expected long-term rate of return and the discount rate assumptions. Amortization of net gain or loss included in accumulated other comprehensive income (loss) reflects a corridor based on 10 percent of the greater of the projected benefit obligation or the market-related value of plan assets as of the beginning of the plan year, and is included as a component of net periodic pension cost.

The actuarial assumptions that we use in determining pension and other postretirement liabilities and expenses may differ materially from actual results due to changing market and economic conditions, as well as early withdrawals by terminating plan participants. While we believe that the assumptions used are appropriate, differences in actual experience or changes in assumptions related to the ERP may materially affect our financial position. A 25 basis-point increase (decrease) in the discount rate assumption as of December 31, 2018, would cause the ERP projected benefit obligation to decrease (increase) by approximately $18.5 million.

INCOME TAXES

FINRA and FINRA REG are tax-exempt organizations under Internal Revenue Code (IRC) Section 501(c)(6). The Foundation is a tax-exempt organization under IRC Section 501(c)(4). However, unrelated business income activities are taxed at normal corporate rates to the extent that they result in taxable net income. We determine deferred tax assets and liabilities based on differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities (*i.e.*, temporary differences). We measure these assets and liabilities at the enacted rates that we expect will be in effect when we will realize these differences. We also determine deferred tax assets based on the amount of net operating loss carryforwards. If necessary, we establish a valuation allowance to reduce deferred tax assets to the amount that is more likely than not to be realized.

The Consolidated Entity has elected to be taxed as a Partnership for U.S. federal tax purposes. FINRA is responsible for reporting income or loss from the Consolidated Entity, to the extent required by the federal and state income tax laws, for income tax purposes.

CONCENTRATION OF CREDIT RISK

Financial instruments that potentially subject us to concentrations of credit risk consist of cash and cash equivalents, trading investments, other investments and accounts receivable. We do not require collateral on these financial instruments.

We maintain cash and cash equivalents in excess of federally insured limits, principally with financial institutions located in the U.S. Risk on accounts receivable is reduced by the number of entities comprising our member firm base and through ongoing evaluation of collectability of amounts owed to us. We use outside investment managers to manage our investment portfolio and a custody agent, a publicly traded company headquartered in New York, to hold our trading securities.

We maintain a broadly diversified investment portfolio, representing a wide range of assets and asset classes, in order to attain acceptable levels of risk and return. FINRA's investment portfolio consists of investments in predominantly investment grade debt securities, mutual and commingled funds containing equity securities and other investments. The Foundation's investment portfolio consists of commingled funds and a pooled investment fund.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The Company attempts to minimize credit risk by monitoring the creditworthiness of the financial institutions with which it transacts business.

As of December 31, 2018, substantially all of the Consolidated Entity's cash, investments in securities and amounts due from brokers are positions with and amounts due from its clearing brokers. Risks with respect to the Consolidated Entity include market risk as a result of changes in the market or fair value of a particular financial instrument, and credit risk from the potential loss should the counterparties fail to perform pursuant to the terms of their obligations. The Consolidated Entity minimizes these risks by carrying out investment transactions through established and reputable institutions.

RECENT ACCOUNTING PRONOUNCEMENTS

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014–09, *Revenue from Contracts with Customers (Topic 606).* The ASU provides that a company recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the company expects to be entitled in exchange for those goods or services. Accordingly, companies will need to use more judgment and make more estimates, which may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. In August 2015, the FASB issued ASU 2015–14, *Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date*, which deferred the effective date of the new standard by one year. In 2016 and 2017, the FASB continued to issue various technical improvements through various ASUs, including principal versus agent considerations, identifying performance obligations and licensing. FINRA adopted this ASU on January 1, 2019. As a result of adopting the ASU, on January 1, 2019, we expect to recognize a cumulative increase to equity of approximately $20 million, which represents the release of previously deferred initial fees that no longer qualify for deferral under the ASU.

In January 2016, the FASB issued ASU 2016–01, *Financial Instruments—Overall (Subtopic 825–10): Recognition and Measurement of Financial Assets and Financial Liabilities.* The ASU eliminates the available-for-sale classification of equity investments and requires entities to measure equity investments that do not result in consolidation and are not accounted for under the equity method at fair value and recognize any changes in fair value in net income. The ASU should be applied by means of a cumulative-effect adjustment to the balance sheet as of the beginning of the fiscal year of adoption. FINRA adopted this ASU on January 1, 2019, and accordingly, all of our equity investments previously classified as available-for-sale investments will be measured at fair value with changes in fair value recognized in net income for 2019. The adoption of this ASU is not expected to have a material impact on our consolidated financial statements.

In August 2016, the FASB issued ASU 2016–15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*, which clarifies how entities should classify certain cash receipts, such as distributions received from equity method investees, and cash payments on the statement of cash flows. The ASU must be applied retrospectively to all periods presented but may be applied prospectively from the earliest date practicable if retrospective application would be impracticable. FINRA adopted this ASU on January 1, 2019, and it is not expected to have a material impact on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016–02, *Leases*. The ASU requires lessees to put most leases on their balance sheets but recognize expenses on their statements of operations in a manner similar to today's accounting. The ASU also eliminates today's real estate-specific provisions for all entities. For lessors, the ASU modifies the classification criteria and the accounting for sales-type and direct financing leases. The ASU is effective for FINRA on January 1, 2020. Early adoption is permitted; however, we do not intend to early adopt the ASU. We are currently completing a diagnostic assessment of the ASU based on our current inventory of leases. We are planning to elect the additional transition option, which allows

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

entities to not apply the new leases standard in the comparative period they present in their financial statements in the year of adoption. We are currently assessing the impact that the ASU will have on our consolidated financial statements.

In July 2016, the FASB issued the final guidance on credit losses, ASU 2016–13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, which will significantly change how entities will measure credit losses for most financial assets and certain other instruments that are not measured at fair value through net income. Entities will be required to use a new forward-looking "expected loss" model and record an allowance that, when deducted from the amortized cost basis of the financial asset, presents the net amount expected to be collected on the financial asset. This approach will apply to most financial assets measured at amortized cost and certain other instruments, including trade and other receivables, loans, held-to-maturity debt securities, net investments in leases and off-balance-sheet credit exposures. The ASU will also require significantly more disclosures to be made in an entity's financial statements. In November 2018, the FASB issued ASU 2018–19, *Codification Improvements to Topic 326, Financial Instruments—Credit Losses*, which aligned the implementation date for nonpublic entities' annual financial statements with the implementation date for their interim financial statements and thereby deferring the initial effective date by one year. As a result of ASU 2018–19, FINRA plans to adopt the new credit loss guidance on January 1, 2022. Early adoption is permitted; however, we do not intend to early adopt the ASU. We are currently assessing the potential impact that the ASU will have on our consolidated financial statements.

The following accounting pronouncements were also recently issued:

- ASU No. 2018–14, *Compensation—Retirement Benefits—Defined Benefit Plans—General (Subtopic 715–20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans*; effective for FINRA in 2021;
- ASU No. 2018–13, *Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement*; effective for FINRA in 2020;
- ASU No. 2016–16, *Income Taxes (Topic 710): Intra-Entity Transfers of Assets Other Than Inventory*; effective for FINRA in 2019;
- ASU No. 2017–06, *Plan Accounting: Defined Benefit Pension Plans (Topic 960), Defined Contribution Pension Plans (Topic 962), Health and Welfare Benefit Plans (Topic 965): Employee Benefit Plan Master Trust Reporting (a consensus of the Emerging Issues Task Force)*, effective for FINRA in 2019; and
- ASU No. 2017–07, *Compensation—Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost*, effective for FINRA in 2019.

We have assessed these pronouncements and determined that they do not have any material impact on our consolidated results of operations or financial position, and they will be adopted as of their future effective date.

The following accounting pronouncements have been adopted by FINRA with no material effect on our consolidated financial statements:

- ASU No. 2015–02, *Consolidations (Topic 810): Amendments to the Consolidation Analysis,* effective for FINRA in 2017;
- ASU No. 2015–07, *Fair Value Measurement (Topic 820): Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)—a consensus of the FASB Emerging Issues Task Force*; effective in 2017, but early adopted in 2015; and
- ASU No. 2015–17, *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*; effective in 2018, but early adopted in 2015.

3. DEFERRED REVENUE

The following is a summary of amounts that we included in current and non-current deferred revenue as of December 31, 2018, and the years over which we expect to recognize those amounts:

	Registration	Arbitration	Annual	Total
		(in millions)		
Year ending December 31,				
2019	$ 7.0	$4.9	$54.1	$66.0
2020	5.1	—	—	5.1
2021	3.4	—	—	3.4
2022	1.6	—	—	1.6
2023 and thereafter	3.7	—	—	3.7
	$20.8	$4.9	$54.1	$79.8

The following is a summary of activity in our current and non-current deferred revenue for the periods ended December 31, 2018 and 2017, for all revenue arrangements. Annual revenue below primarily includes the GIA, PA, BOA and registered representative renewal fees. The additions reflect the fees charged during the period, while the amortization reflects the revenues recognized during the period based on the significant accounting policies described in Note 2:

	Registration	Arbitration	Annual	Total
		(in millions)		
Balance as of January 1, 2018	$20.1	$ 4.5	$ 54.3	$ 78.9
Additions	9.4	9.0	314.8	333.2
Amortization	(8.7)	(8.6)	(315.0)	(332.3)
Balance as of December 31, 2018	$20.8	$ 4.9	$ 54.1	$ 79.8

	Registration	Arbitration	Annual	Total
		(in millions)		
Balance as of January 1, 2017	$19.9	$ 4.9	$ 55.1	$ 79.9
Additions	8.9	8.2	306.8	323.9
Amortization	(8.7)	(8.6)	(307.6)	(324.9)
Balance as of December 31, 2017	$20.1	$ 4.5	$ 54.3	$ 78.9

4. INVESTMENTS

FINRA owns a diverse investment portfolio consisting of 1) U.S. government (and state and local) securities; 2) agency mortgage-backed securities; 3) corporate and asset-backed securities; 4) mutual and commingled funds; 5) other investments (including pooled investment funds); and 6) other financial instruments. We have classified our marketable investments as trading or available-for-sale based on their nature, and our intent and ability to sell or to hold the securities.

4. INVESTMENTS (CONTINUED)

Our investment policy strives to preserve principal, in real terms, while seeking to earn a long-term rate of return commensurate with the degree of risk deemed appropriate by the Board. We execute our investment strategy through a separately managed account and direct investments. FINRA's investment portfolio consisted of the following as of:

	December 31, 2018	December 31, 2017
	(in millions)	
Trading investments	$ 563.1	$ 431.6
Available-for-sale investments: FINRA	266.1	271.6
Available-for-sale investments: Foundation	46.4	51.5
Other investments:		
Investments of Consolidated Entity	395.6	—
Pooled investment funds: FINRA	345.5	282.1
Pooled investment fund: Foundation	27.8	27.7
Limited partnership: FINRA	—	642.8
Other	0.3	0.4
Total other investments	769.2	953.0
Total	$1,644.8	$1,707.7

TRADING INVESTMENTS

During 2018, our active trading portfolio was managed by an investment manager, who had the authority to buy and sell investments within FINRA-determined, pre-established parameters. Our unrealized loss for the period on trading securities held at December 31, 2018, was $15.3 million. Our unrealized gain for the period on trading securities held at December 31, 2017, was $4.2 million.

AVAILABLE-FOR-SALE INVESTMENTS

FINRA's available-for-sale investments consisted of the following:

	Amortized Cost	Gross Unrealized Gain	Gross Unrealized Loss	Fair Value
		(in millions)		
As of December 31, 2018:				
FINRA:				
Mutual funds	$165.1	$ 4.7	$ —	$169.8
Commingled funds	100.3	—	(4.0)	96.3
Total FINRA	$265.4	$ 4.7	$(4.0)	$266.1
Foundation:				
Commingled funds	$ 47.7	$ —	$(1.3)	$ 46.4
As of December 31, 2017:				
FINRA:				
Mutual funds	$166.0	$20.2	$ —	$186.2
Commingled funds	75.1	10.3	—	85.4
Total FINRA	$241.1	$30.5	$ —	$271.6
Foundation:				
Commingled funds	$ 50.0	$ 1.5	$ —	$ 51.5

4. INVESTMENTS (CONTINUED)

For 2018 and 2017, gross investment gains recognized from our investments in mutual and commingled funds, including amounts reclassified from unrealized gains and losses in accumulated other comprehensive income (loss), were as follows:

	2018	2017
	(in millions)	
Gross investment gains recognized	$1.9	$9.1
Amounts reclassified from accumulated other comprehensive income (loss)	1.9	1.2

For 2018 and 2017, there were no gross investment losses recognized from our investments in mutual and commingled funds.

Other-Than-Temporary Declines in Fair Value

In 2018 and 2017, we did not record any impairment charges related to our mutual and commingled funds. As of December 31, 2018 and 2017, we did not identify any events or circumstances that would indicate the value of our mutual and commingled funds should be impaired. Should there be any impairment charges related to other-than-temporary declines in the fair value of available-for-sale investments, they would be reflected in net realized and unrealized investment (losses) gains in the consolidated statements of operations.

Temporary Declines in Fair Value

As of December 31, 2018, FINRA had two commingled investments that have been in a continuous unrealized loss position for less than 12 months with a fair value of $96.3 million, reflecting unrealized losses of $4 million. As of December 31, 2017, FINRA had no available-for-sale investments with aggregate unrealized losses. As of December 31, 2018, the Foundation had two commingled investments that have been in a continuous unrealized loss position for less than 12 months with a fair value of $46.4 million, reflecting unrealized losses of $1.3 million. As of December 31, 2017, the Foundation had no available-for-sale investments with aggregate unrealized losses.

OTHER INVESTMENTS

In 2018, our other investments consist of investments of the Consolidated Entity and pooled investment funds for which the fair value option has been elected. In 2017, our other investments consisted of an investment in one limited partnership accounted for under the equity method and pooled investment funds for which the fair value option has been elected.

4. INVESTMENTS (CONTINUED)

Consolidated Entity, Investments of the Consolidated Entity and Limited Partnership

On July 1, 2018, FINRA transferred all of its interest from the Limited Partnership to the Consolidated Entity. FINRA's pro-rata share of the Limited Partnership's cash and underlying investments were transferred in-kind at fair value to the Consolidated Entity, which represented our equity interest on July 1, 2018. No gain or loss was recognized. The objective of the Consolidated Entity is to maximize risk-adjusted returns over the long-term horizon through potential investment in a wide array of investments and strategies. As of December 31, 2018, FINRA holds a 100 percent equity interest in the Consolidated Entity, and the general partner of the Consolidated Entity is fully independent of FINRA management and its Board. The following table summarizes 2018 and 2017 activity related to the Limited Partnership and the Consolidated Entity.

	Limited Partnership	Consolidated Entity
	(in millions)	
Balance, January 1, 2017	$ 692.6	$ —
Equity earnings	81.9	—
Redemptions	(131.7)	—
Balance, December 31, 2017	642.8	—
Equity earnings	12.0	—
Redemptions	(156.0)	—
Transfer of interest on July 1, 2018	(498.8)	498.8
Investment losses	—	(16.0)
Redemptions	—	(156.0)
Balance, December 31, 2018	$ —	$ 326.8

As of December 31, 2018, the carrying value of the net assets and liabilities of the Consolidated Entity were $326.8 million, which represented its maximum risk of loss as of that date. The assets of the Consolidated Entity primarily consisted of cash and investments, while the liabilities primarily represented accrued expenses of the Consolidated Entity. The assets of the Consolidated Entity may be used only to settle obligations of the Consolidated Entity. In addition, there is no recourse to the Company for the Consolidated Entity's liabilities.

4. INVESTMENTS (CONTINUED)

Investments held by the Consolidated Entity, summarized below, primarily consist of limited partnerships managed by the investment manager of the Consolidated Entity, as well as hedge funds, private equity funds or similar investment vehicles managed by external managers directly or through subsidiary funds that are controlled by the investment manager of the Consolidated Entity. These investments are included in other investments in the accompanying consolidated balance sheets. The Consolidated Entity's net assets consist primarily of its investments accounted for at fair value; the majority of the Consolidated Entity's fair value measurements are based on the estimates made by the general partner of the Consolidated Entity. The investment strategy of these limited partnerships is multi-strategy.

	Fair value as of December 31, 2018	Fair value as a percentage of investments of Consolidated Entity as of December 31, 2018
	(in millions)	
Investments of Consolidated Entity		
North America		
HighVista Master Fund Limited Partnership	$137.2	34.7%
HVS Clarendon I Limited Partnership	81.3	20.5%
Other	177.1	44.8%
Total investments (1) (cost $410.4 million)	$395.6	100.0%

(1) Total investments included the amount liquidated on January 1, 2019 in order to satisfy the $78 million redemption request effective December 31, 2018. The redemption transaction that was recorded by FINRA and the Consolidated Entity as a redemption receivable and payable, respectively, has been eliminated upon consolidation.

As of December 31, 2018, no underlying investment held by these limited partnerships had a fair value that exceeded 5% of FINRA's total consolidated equity.

Realized and unrealized gains and losses on the Consolidated Entity's investments were included in net realized and unrealized investment (losses) gains in the consolidated statement of operations. Unrealized gains or losses result from changes in the fair value of these investments. Upon disposition of an investment, unrealized gains or losses are reversed and an offsetting realized gain or loss is recognized in the current period. As of December 31, 2018, the net change in unrealized depreciation on the Consolidated Entity's investments held was $14.8 million, and net realized gains from the disposition of investments were $1.2 million.

As of December 31, 2017, the Limited Partnership investment represented a variable interest in an investment limited partnership, whose general partner was fully independent of FINRA management and its Board. The purpose of the Limited Partnership was to maximize risk-adjusted returns over the long term by investing in a highly diversified asset allocation strategy. The nature of the Limited Partnership included investments in equity, fixed income, real assets and alternative investments. As of December 31, 2017, the maximum exposure to loss related to the Limited Partnership was limited to $642.8 million, the carrying amount of the investment, due to the legal structure and design of this partnership. We did not have outstanding capital commitments, guarantees or any other liquidity arrangements with this partnership. Our ownership interest in this partnership was 69.7 percent at December 31, 2017.

The Limited Partnership investment was included in other investments in the consolidated balance sheets as of December 31, 2017. The gains, including those earned prior to the aforementioned transfer in 2018, were included in equity method earnings from other investments in the consolidated statements of operations.

We did not recognize any impairment charges on our equity method investments for the years ended December 31, 2018 and 2017.

4. INVESTMENTS (CONTINUED)

Pooled Investment Funds

FINRA and the Foundation invest in pooled investment funds for which the fair value option was elected. The following table summarizes the activity related to the pooled investment funds for both FINRA and the Foundation as of December 31, 2018 and 2017.

	Pooled investment funds: FINRA	Pooled investment funds: Foundation	Total
		(in millions)	
Balance, January 1, 2017	$ —	$ —	$ —
Purchases	270.0	27.9	297.9
Net gains (losses) from changes in fair value	12.1	(0.2)	11.9
Balance, December 31, 2017	282.1	27.7	$309.8
Purchases	100.0	—	100.0
Net (losses) gains from changes in fair value	(36.6)	0.1	(36.5)
Balance, December 31, 2018	$345.5	$27.8	$373.3

The aggregate carrying amounts of these investments were included in other investments in the consolidated balance sheets. Net gains (losses) from changes in fair value on these investments were included in net realized and unrealized (losses) gains in the consolidated statements of operations. No interest and dividends were recorded.

5. FAIR VALUE MEASUREMENT

The Company considers cash and cash equivalents, trading and available-for-sale investments, receivables, investments receivable and investments payable to be its financial instruments. The carrying amounts reported in the consolidated balance sheets for these financial instruments equal or closely approximate fair value.

U.S. GAAP defines fair value as the price that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants as of the measurement date (*i.e.*, an exit price).

U.S. GAAP prioritizes the level of market price observability used in measuring assets and liabilities at fair value. There are a number of factors that impact market price observability, including the type of assets and liabilities, and the specific characteristics of the assets and liabilities. Assets and liabilities with prices that are readily available, actively quoted or for which fair value can be measured from actively quoted prices generally will have a higher degree of market price observability and less degree of judgment used in measuring fair value.

Assets and liabilities measured at fair value are classified into one of the following categories:

- Level 1 Quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity has the ability to access as of the measurement date.
- Level 2 Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly, through corroboration with observable data.
- Level 3 Unobservable inputs, such as internally developed pricing models for the asset or liability due to little or no market activity for the asset or liability.

In certain cases, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, an asset or liability's level within the fair value hierarchy is based on the lowest level input that is significant to the fair value measurement. The assessment of significance of a particular input to the fair value measurement in its entirety requires judgment and factors specific to the asset or liability.

5. FAIR VALUE MEASUREMENT (CONTINUED)

The following table presents information about our assets that are measured at fair value on a recurring basis as of December 31, 2018, and indicates the fair value hierarchy of the valuation techniques used to determine fair value:

Description	Total carrying amount in consolidated balance sheet December 31, 2018	Fair Value Measurement at December 31, 2018 Measured Using: Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)
		(in millions)	
Assets:			
Trading securities			
Fixed income			
Agency mortgage-backed securities			
FHLMC	$ 51.9	$ —	$ 51.9
FNMA	20.8	—	20.8
GNMA	8.1	—	8.1
Corporate debt securities			
Banking	99.9	—	99.9
Industrial	51.9	—	51.9
Consumer non-cyclical	46.5	—	46.5
Other financial institutions	34.6	—	34.6
Utility	34.5	—	34.5
Communication	21.3	—	21.3
Other	6.5	—	6.5
Asset-backed securities	53.2	—	53.2
Collateralized mortgage obligations	49.4	—	49.4
Government securities	46.3	—	46.3
Mutual funds	38.2	38.2	—
Available-for-sale securities			
Mutual funds			
U.S. equity	165.4	165.4	—
Other	4.4	4.4	—
Commingled funds			
International equity	81.7	—	81.7
U.S. equity	30.8	—	30.8
U.S. fixed income	30.2	—	30.2
Total assets in the fair value hierarchy	875.6	208.0	667.6
Pooled investment funds, measured at net asset value (a)	373.3	—	—
Investments of Consolidated Entity (a)	395.6	—	—
Total assets measured at fair value	$1,644.5	$208.0	$667.6

5. FAIR VALUE MEASUREMENT (CONTINUED)

The following table presents information about our assets that are measured at fair value on a recurring basis as of December 31, 2017, and indicates the fair value hierarchy of the valuation techniques used to determine fair value:

		Fair Value Measurement at December 31, 2017 Measured Using	
Description	Total carrying amount in consolidated balance sheet December 31, 2017	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)
		(in millions)	
Assets:			
Trading securities			
Fixed income			
Agency mortgage-backed securities			
FNMA	$ 24.9	$ —	$ 24.9
GNMA	9.9	—	9.9
FHLMC	8.9	—	8.9
Corporate debt securities			
Banking	76.2	—	76.2
Consumer non-cyclical	37.7	—	37.7
Industrial	34.5	—	34.5
Other financial institutions	33.4	—	33.4
Utility	32.1	—	32.1
Consumer cyclical	19.1	—	19.1
Communication	18.9	—	18.9
Other	1.9	—	1.9
Asset-backed securities	55.8	—	55.8
Government securities	39.8	—	39.8
Mutual funds	38.5	38.5	—
Available-for-sale securities			
Mutual funds			
U.S. equity	180.1	180.1	—
Other	6.1	6.1	—
Commingled funds			
International equity	79.4	—	79.4
U.S. fixed income	31.3	—	31.3
U.S. equity	26.2	—	26.2
Total assets in the fair value hierarchy	754.7	224.7	530.0
Pooled investment funds, measured at net asset value (a)	309.8	—	—
Total assets measured at fair value	$1,064.5	$224.7	$530.0

(a) In accordance with ASC Subtopic 820–10, a certain investment that is measured at fair value using the net asset value per share practical expedient has not been classified in the fair value hierarchy. The fair value amount presented in this table is intended to permit reconciliation of the fair value hierarchy to the fair value of plan assets presented in the consolidated balance sheets.

5. FAIR VALUE MEASUREMENT (CONTINUED)

The Company invests in pooled investment funds for which the fair value option has been elected. These investments are offshore feeder funds in a “master-feeder” structure, and substantially all of their capital is invested in their respective master funds. The master funds’ investment objectives generally include producing risk-adjusted returns while maintaining low correlation to traditional markets by taking long and short positions in major equities, fixed income, currencies and commodities markets offering a high level of liquidity. These investments generally have a redemption notice period between three to 30 days, and shares may be redeemed on a semimonthly or a monthly basis. We do not have any outstanding capital commitments related to these investments.

Additionally, the investments held in the Consolidated Entity consist of limited partnerships managed by the investment manager of the Consolidated Entity as well as hedge funds, private equity funds or similar investment vehicles. These investments generally employ a multi-strategy investment strategy. The fair value of the investments of the Consolidated Entity is measured at net asset value on the balance sheet date. The investment manager of the Consolidated Entity has a valuation committee consisting of its key officers and select members of the investment operations team for the investment manager. The valuation committee reviews and approves valuations for all investments for which the third-party administrator is unable to obtain a price independently. The Consolidated Entity had unfunded commitments through its investment in limited partnerships of $46.8 million as of December 31, 2018. Capital calls will be funded with available cash held by the Consolidated Entity or by liquidating investments of the Consolidated Entity, as needed. The underlying investments held by these limited partnerships may be subject to various levels of liquidity restrictions.

As of December 31, 2018 and 2017, we had no investments categorized in Level 3 of the fair value hierarchy.

Changes in the fair value of trading securities and other investments measured at net asset value are recorded as a component of net realized and unrealized investment (losses) gains in the consolidated statements of operations. Temporary changes in the fair value of available-for-sale securities are recognized as unrealized gains as a separate component of other comprehensive income (loss).

For the years ended December 31, 2018 and 2017, there were no transfers between Level 1, Level 2 or Level 3 of the fair value hierarchy.

The following is a description of the valuation methodologies used for financial assets measured at fair value on a recurring basis and the general classification of these instruments pursuant to the fair value hierarchy.

Fixed Income

All of our fixed income securities classified as trading securities are priced using the services of third-party pricing vendors. These vendors utilize evaluated and industry-accepted pricing models that vary by asset class and incorporate market inputs such as available trade, bid and other market information to determine the fair value of the securities. Accordingly, the valuation of these securities is categorized in Level 2 of the fair value hierarchy.

We independently validate the fair value measurement of our trading securities to determine that the assigned fair values are appropriate. To validate pricing information received, our policy is to employ a variety of procedures throughout the year, including comparing information received to other pricing sources and performing independent price checks.

Mutual Funds

All of the mutual funds classified as trading securities, which consist of funds invested in domestic bonds, as well as domestic and international equities, relate to our defined contribution SERP for senior officers and deferred compensation plan for officers under the provisions of Section 457(b) of the IRC.

5. FAIR VALUE MEASUREMENT (CONTINUED)

The Company also invests in mutual funds that are classified as available-for-sale investments based on our intent and ability to sell or to hold these investments. One mutual fund investment, related to our closed defined benefit SERP obligation, consists of a life-cycle fund focused on asset allocation through investments in other mutual funds, primarily in bonds with the remainder in equities. Additionally, we have a domestic mutual fund that invests in high-quality companies that have both the ability and the commitment to grow their dividends over time.

These investments are valued at the publicly quoted net asset value per share which is computed as of the close of business on the balance sheet date. Accordingly, the valuation of these securities is categorized in Level 1 of the fair value hierarchy.

Commingled Funds

All of our commingled funds are classified as available-for-sale investments based on our intent and ability to sell or to hold these investments. Our commingled funds employ a variety of strategies, including domestic and international equities and domestic fixed income securities.

These investments are valued at the quoted net asset value per unit, computed as of the close of business on the balance sheet date. Units of these investments are valued daily and a unit-holder's ability to transact in the funds' units occurs daily; however, units are not traded on an active exchange. As the fair value per unit is readily determinable, the valuation of these securities is categorized in Level 2 of the fair value hierarchy.

6. INCOME TAXES

FINRA and FINRA REG are tax-exempt organizations under IRC Section 501(c)(6). The Foundation is a tax-exempt organization under IRC Section 501(c)(4).

Unrelated Business Income

Unrelated business income activities are taxed at normal corporate rates to the extent that they have taxable net income. Our unrelated business activities consist primarily of mortgage licensing services provided under our contract with SRR, certain external client exams and other consulting services.

NASD Holding, Inc. (NAHO), a wholly owned taxable subsidiary of FINRA prior to its liquidation in 2005, had net operating losses (NOLs) to which FINRA, as the parent organization, succeeded. The related deferred tax asset resulting from the transfer of the NAHO NOLs to FINRA was measured at $20.5 million based on federal tax rates then in effect, and FINRA recorded a valuation allowance equal to that amount. Aside from the NAHO NOLs, FINRA's deferred tax asset is primarily composed of losses related to other contractual work performed in the past. The deferred tax asset, which remains entirely reserved, is remeasured each period at rates expected to be in effect in the future period that the asset is used. As of December 31, 2018 and 2017, FINRA had federal unrelated business loss carryforwards of $49.4 million and $51.3 million, respectively, which are scheduled to expire beginning in 2022 through 2028.

6. INCOME TAXES (CONTINUED)

The following table summarizes the 2018 and 2017 activity related to the federal deferred tax asset and valuation allowance:

	Deferred tax asset—NOLs	Other deferred tax asset	Valuation allowance	Net deferred tax assets
Deferred tax asset, January 1, 2017	$ 18.4	$ 0.6	$ (19.0)	$—
2017 federal provision	(1.0)	—	1.0	—
2017 deferred tax asset before the Tax Cuts and Jobs Act recognition	17.4	0.6	(18.0)	—
Adjustment for future effective rate reduction from 34 percent to 21 percent	(6.6)	—	6.6	—
Adjustment for alternative minimum tax elimination	—	(0.6)	0.6	—
Deferred tax asset, December 31, 2017	10.8	—	(10.8)	—
2018 federal provision	(0.2)	—	0.2	—
Other	(0.2)	—	0.2	—
Deferred tax asset, December 31, 2018	$ 10.4	$ —	$ (10.4)	$—

There were no other significant deferred tax assets related to unrelated business income. The 2018 and 2017 income tax provision of $0.4 million and $1.6 million, respectively, primarily represented the net change in deferred tax assets related to unrelated business loss carryforwards during the year in addition to state income tax and other minor adjustments. The income tax provision was included in other expense in the consolidated statements of operations.

We did not have any significant unrelated business income taxes payable in 2018 or 2017.

Uncertain Tax Positions

U.S. GAAP provides a two-step approach for evaluating tax positions. Recognition (step 1) occurs when an entity concludes that a tax position, based solely on its technical merits, is more likely than not to be sustained upon examination. Measurement (step 2) occurs when the tax benefit is measured as the largest amount of benefit, determined on a cumulative probability basis, that is more likely than not to be realized upon ultimate settlement. From 2015 through 2018, the years management considers to be open for examination by taxing authorities, management did not identify the existence of any uncertain tax positions related to current operations. Additionally, FINRA has not recognized any material uncertain tax positions related to the succession to the NAHO NOLs.

7. EMPLOYEE BENEFIT LIABILITIES

BENEFIT PLANS

The following table summarizes the benefit plans offered by FINRA.

Plan	Eligible employees
Defined benefit ERP	As of January 1, 2019, fewer than 700 current employees not previously transitioned out of the plan (closed to new participants)
Defined benefit SERP	Fewer than 10 current senior executives not previously phased out of the plan in 2011 (closed to new participants)
Retiree medical plan	Eligible active employees, retirees and their dependents
Postretirement life insurance benefit plan	Fewer than 150 retirees who opted into the plan (closed to new participants)
Voluntary contributory savings plan	All active employees
Defined contribution component of the savings plan	Active employees not participating in the defined benefit ERP
Deferred compensation plan for officers	Active officer-level employees (vice president and above)
Supplemental defined contribution plan for senior officers	Active senior executives not participating in the defined benefit SERP

A brief description of the plans follows.

Defined Benefit ERP and SERP

We provide two non-contributory defined benefit pension plans to eligible employees, including a qualified ERP and a non-qualified SERP. The benefits are based primarily on years of service and employees' average compensation during the highest 60 consecutive months of employment. Both plans are now closed to new participants. The benefits of those participants who previously transitioned out of the ERP were frozen at the time of transition, and will be made available to them upon retirement.

Retiree Medical Plan

The Company maintains the Retiree Medical Plan to provide health benefits to eligible retired employees and their eligible dependents. Eligible retirees pay the full premium cost to be enrolled in the Company's retiree medical coverage. Under the Retiree Medical Plan, the Company offers a Retiree Medical Savings Plan that provides eligible retirees with credits that can be used to help pay for health care premiums during retirement. Included in the Retiree Medical Plan are Retiree Medical Accounts created for eligible employees and retirees with fixed annual credits applied to those accounts for each year of FINRA service beginning at age 40, and accrual of credits for a portion of the active employee's unused vacation and personal leave. The credits can be accessed only in retirement and may be used only toward paying a portion of monthly premiums under FINRA-sponsored retiree health plans.

Postretirement Life Insurance Benefit Plan

The Company provides a non-contributory specified life insurance benefit to eligible retired employees. The postretirement life insurance benefit plan is closed with respect to new participants.

7. EMPLOYEE BENEFIT LIABILITIES (CONTINUED)

Voluntary Contributory Savings Plan

FINRA maintains a voluntary contributory savings plan for eligible employees. Employees are immediately eligible to make elective contributions to the plan up to specified plan limits. Employees are also eligible to receive from FINRA a corresponding dollar-for-dollar matching contribution on any elective contribution made by the participant to the savings plan up to a maximum of 6 percent of base compensation.

The savings plan expense for both 2018 and 2017 was $24 million, which was included within compensation and benefits expense in the consolidated statements of operations.

Defined Contribution Component of the Savings Plan

FINRA offers a defined contribution component of the savings plan to all eligible employees not currently participating in the ERP.

The Company's contributions for this component are based on a participant's age plus years of service, and vesting is on a graduated scale over six years. The investment options are the same as the current options in the savings plan. Expenses related to the defined contribution component of the savings plan for 2018 and 2017 were $23.5 million and $22.9 million, respectively, which were included within compensation and benefits expense in the consolidated statements of operations.

Deferred Compensation Plan for Officers

FINRA maintains a deferred compensation plan for officers under the provisions of Section 457(b) of the IRC. Eligible employees may contribute to the plan and, at its discretion, FINRA may make additional contributions to the plan. FINRA placed the assets of this plan into an irrevocable rabbi trust that the Company consolidates. As of December 31, 2018, $20.4 million of investments and $20.4 million of amounts due to plan participants were included in trading investments and accrued personnel and benefit costs in the consolidated balance sheet, representing participant contributions to this plan and accrued earnings. As of December 31, 2017, $20.5 million of investments and $20.5 million of amounts due to plan participants were included in trading investments and accrued personnel and benefit costs in the consolidated balance sheet, representing participant contributions to this plan and accrued earnings. As of December 31, 2018 and 2017, FINRA made no additional contributions to this plan.

Supplemental Defined Contribution Plan for Senior Officers

FINRA maintains a supplemental defined contribution plan for the Company's senior officers and makes annual contributions based on salary and a portion of incentive compensation. Contributions and earnings vest upon the earlier of 1) the end of each third year of participation following such contribution; 2) attainment of age 62; 3) death; or 4) a disabled participant's termination of employment. FINRA placed the assets of this plan into an irrevocable rabbi trust that the Company consolidates. As of December 31, 2018, $17.8 million of investments and $17.8 million of amounts due to plan participants were included in trading investments and accrued personnel and benefit costs in the consolidated balance sheet, representing FINRA's contributions to this plan and accrued earnings. As of December 31, 2017, $18 million of investments and $18 million of amounts due to plan participants were included in trading investments and accrued personnel and benefit costs in the consolidated balance sheet, representing FINRA's contributions to this plan and accrued earnings.

7. EMPLOYEE BENEFIT LIABILITIES (CONTINUED)

PLAN DISCLOSURES

The following tables disclose information related to our "Pension Plans," which include the ERP and SERP described above, and "Other Plans," which include the retiree medical and postretirement life insurance benefit plans described above. The reconciliation of the projected benefit obligation, the change in the fair value of plan assets for the periods ended December 31, 2018 and 2017, and the accumulated benefit obligation at December 31, 2018 and 2017, were as follows:

	Pension Plans		Other Plans	
	2018	2017	2018	2017
	(in millions)			
Change in benefit obligation				
Benefit obligation at beginning of period	$636.4	$ 549.3	$ 78.1	$ 67.6
Service cost	17.4	16.2	3.8	3.6
Interest cost	22.5	23.0	2.8	2.8
Actuarial (gains) losses	(78.8)	66.6	(5.6)	6.0
Benefits paid	(25.8)	(18.7)	(2.0)	(1.9)
Benefit obligation at end of period	$571.7	$ 636.4	$ 77.1	$ 78.1
Change in plan assets				
Fair value of plan assets at beginning of period	$521.6	$ 462.5	$ —	$ —
Actual return on plan assets	(29.9)	65.8	—	—
Company contributions	26.6	12.0	2.0	1.9
Benefits paid	(25.8)	(18.7)	(2.0)	(1.9)
Fair value of plan assets at end of period	$492.5	$ 521.6	$ —	$ —
Underfunded status of the plan	$ (79.2)	$(114.8)	$(77.1)	$(78.1)
Accumulated benefit obligation	$517.2	$ 576.9		

Our total accrued pension and other postretirement liability in the consolidated balance sheets comprised the following:

	Pension Plans		Other Plans	
	2018	2017	2018	2017
	(in millions)			
Current	$ 6.4	$ 7.5	$ 2.5	$ 1.7
Noncurrent	72.8	107.3	74.6	76.4
Net amount at December 31	$79.2	$114.8	$77.1	$78.1

The current portion of pension and other liabilities represented the net present actuarial value of benefits to be paid over the next 12 months in excess of plan assets, and was included in accrued personnel and benefit costs in the consolidated balance sheet. There are no plan assets for the SERP, retiree medical and postretirement life insurance benefit plans.

The Company does not expect any plan assets to be returned to it during the year ending December 31, 2019.

7. EMPLOYEE BENEFIT LIABILITIES (CONTINUED)

The components of net periodic benefit cost included in the consolidated statements of operations were as follows:

	Pension Plans		Other Plans	
	2018	2017	2018	2017
	(in millions)			
Service cost	$ 17.4	$ 16.2	$3.8	$3.6
Interest cost	22.5	23.0	2.8	2.8
Expected return on plan assets	(29.2)	(25.8)	—	—
Recognized net actuarial losses	2.8	2.2	0.1	—
Prior service cost recognized	0.1	0.1	1.4	1.4
Settlement expense	0.1	0.2	—	—
Total	$ 13.7	$ 15.9	$8.1	$7.8

The assumed health care cost trend rate to be used for the next year to measure the expected cost of other plan liabilities is 7.2 percent, with a gradual decline to 6.5 percent by the year 2023. This estimated trend rate is subject to change. The assumed health care cost trend rate can have a significant effect on the amounts reported. However, a 1-percentage-point change in the assumed health care cost trend rate would not have a material impact on the benefit obligation or service and interest components of net periodic benefit cost.

The net amounts included in accumulated other comprehensive (loss) income were as follows:

	Pension Plans		Other Plans	
	2018	2017	2018	2017
	(in millions)			
Unrecognized net actuarial loss	$(74.1)	$(96.7)	$(4.1)	$ (9.8)
Unrecognized prior service cost	—	(0.1)	(3.4)	(4.8)
Net amount at December 31	$(74.1)	$(96.8)	$(7.5)	$(14.6)

The following amounts were included in other comprehensive loss during 2018:

	Incurred but Not Yet Recognized in Net Periodic Benefit Cost	Reclassification Adjustment for Prior Period Amounts Recognized
	(in millions)	
Actuarial gains (losses)		
Pension plans	$19.8	$2.8
Other plans	5.6	0.1
	25.4	2.9
Prior service cost		
Pension plans	—	0.1
Other plans	—	1.4
	—	1.5
	$25.4	$4.4

7. EMPLOYEE BENEFIT LIABILITIES (CONTINUED)

The estimated amounts to be amortized from accumulated other comprehensive (loss) income into net periodic benefit cost during 2019 based on December 31, 2018, plan measurements were as follows:

	Pension Plans	Other Plans
	(in millions)	
Unrecognized prior service costs	$ —	$1.4
Unrecognized actuarial losses	1.7	—

The weighted-average assumptions used to determine benefit obligations for the years ended December 31, 2018, and 2017, were as follows:

	Pension Plans		Other Plans	
	2018	2017	2018	2017
Discount rate	4.27%	3.65%	4.14%	3.47%
Rate of compensation increase	3.00%	3.00%	—	—

The weighted-average assumptions used to determine net periodic benefit cost for the years were as follows:

	Pension Plans		Other Plans	
	2018	2017	2018	2017
Discount rate	3.65%	4.25%	3.47%	4.05%
Rate of compensation increase	3.00%	3.89%	—	—
Expected return on plan assets	5.75%	5.75%	—	—

The assumptions above are used to develop the benefit obligations at year end and to develop the net periodic benefit cost for the subsequent year. Therefore, the assumptions used to determine benefit obligations are established at each year end while the assumptions used to determine net periodic benefit cost for each year are established at the end of each previous year. The expected return on plan assets that will be used in the determination of 2019 net periodic benefit cost is 6.10 percent.

The benefit obligations and the net periodic benefit cost are based on actuarial assumptions that are reviewed on an annual basis. We revise these assumptions based on an annual evaluation of long-term trends, as well as market conditions, which may have an impact on the cost of providing retirement benefits.

PLAN ASSETS

We fund our ERP obligation, and we have established an irrevocable rabbi trust to fund our SERP obligation. The retiree medical and postretirement life insurance benefit plans are unfunded plans.

The trust related to the SERP obligation is included in our consolidated financial statements. As of December 31, 2018, and 2017, $4.4 million and $6.1 million of investments were included in available-for-sale securities in the consolidated balance sheets, representing the amounts contributed by FINRA, plus earned income and market value gains, less distributions to retirees and market value losses.

The investment policy and strategy of the ERP assets are established by the Pension Committee, which is composed of a cross-representative body of FINRA officers assisted by outside counsel, investment advisors and actuaries. The Management Compensation and Investment Committees of the Board have oversight responsibilities with respect to the ERP and its assets. The investment policy and strategy strive to achieve a rate of return on plan assets that will, over the long term, in concert with Company contributions, fund the plan's liabilities to provide for required benefits. As the funded status of the plan improves, the plan will assume less risk through reductions in return-seeking exposure and/or improved matching of fixed income assets with liabilities.

7. EMPLOYEE BENEFIT LIABILITIES (CONTINUED)

The ERP assets are allocated among a diversified portfolio of equity investments, fixed income securities, alternative investments and cash equivalents with both domestic and international strategies. Derivatives are permitted on a limited scale for hedging or creation of market exposures. Direct debt and equity interests are prohibited in any broker-dealer, exchange, contract market, regulatory client, alternative or electronic trading system or entity that derives a certain threshold of revenue from broker-dealer activities. Asset allocations are reviewed quarterly and adjusted, as appropriate, to remain within target allocations. The Pension Committee reviews the investment policy annually, under the guidance of an investment consultant, to determine whether a change in the policy or asset allocation targets is necessary.

The ERP assets consisted of the following as of December 31, 2018 and 2017:

	2018 Target Allocation	2018	2017
Equity securities:			
U.S. equity	16.0%	15.8%	17.9%
Non-U.S. equity	14.0%	14.1%	16.3%
Global equity	21.0%	20.1%	23.3%
U.S. fixed income securities	44.0%	45.6%	38.2%
Alternative investments	3.0%	2.7%	2.8%
Cash equivalents	2.0%	1.7%	1.5%
Total	100.0%	100.0%	100.0%

The expected long-term rate of return for the plan's total assets is based on the expected returns of each of the above categories, weighted based on the current target allocation for each class. Based on historical experience, the Pension Committee expects that the ERP's active asset managers overall will provide a modest premium to their respective market benchmark indexes. At least annually, the Pension Committee evaluates whether adjustments are needed based on historical returns to more accurately reflect expectations of future returns.

7. EMPLOYEE BENEFIT LIABILITIES (CONTINUED)

The following tables present information about the fair value of the Company's ERP assets at December 31, 2018 and 2017, by asset category, and indicate the fair value hierarchy of the valuation techniques used to determine fair value:

	Fair Value Measurement at December 31, 2018 Measured Using		
Description	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Total
	(in millions)		
Money market funds	$ 9.0	$ —	$ 9.0
Corporate stocks	10.0	—	10.0
Common/collective trusts (a):			
Equity	—	193.3	193.3
Fixed income	—	104.3	104.3
Registered investment companies:			
Equity	42.3	—	42.3
Fixed income	132.0	—	132.0
Total assets in the fair value hierarchy	193.3	297.6	490.9
Partnership/joint venture interests measured at net asset value (b):	—	—	1.6
Total	$193.3	$297.6	$492.5

	Fair Value Measurement at December 31, 2017 Measured Using		
Description	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Total
	(in millions)		
Money market funds	$ 8.0	$ —	$ 8.0
Corporate stocks	15.3	—	15.3
Common/collective trusts (a):			
Equity	—	233.2	233.2
Fixed income	—	48.4	48.4
Registered investment companies:			
Equity	50.8	—	50.8
Fixed income	164.0	—	164.0
Total assets in the fair value hierarchy	238.1	281.6	519.7
Partnership/joint venture interests measured at net asset value (b):	—	—	1.9
Total	$238.1	$281.6	$521.6

(a) Includes both domestic and international equity and fixed income securities. Fair values are readily available and have been estimated using the net asset value per unit of the funds. Investment managers are not constrained by any particular investment style and may invest in either "growth" or "value" securities. Units of this investment are valued daily and a unit-holder's ability to transact in the trusts' units occurs daily; however, units are not available on an active exchange. As the fair value per unit is readily determinable, the valuation of these securities is categorized in Level 2 of the fair value hierarchy.

7. EMPLOYEE BENEFIT LIABILITIES (CONTINUED)

(b) In accordance with ASC Subtopic 820–10, a certain investment that is measured at fair value using the net asset value per share practical expedient has not been classified in the fair value hierarchy. The fair value amount presented in this table is intended to permit reconciliation of the fair value hierarchy to the fair value of plan assets presented in the plan disclosures section of this footnote.

The investment included in this category is a private equity fund that invests in the natural resources and real estate industries. The investment is nonredeemable. The fair value of the investment has been estimated using the net asset value per share of the investment.

For the years ended December 31, 2018 and 2017, there were no transfers between Level 1, Level 2 or Level 3 of the fair value hierarchy.

The valuation techniques and inputs used to measure fair value of the ERP assets are consistent with the Company's valuation procedures as disclosed in Note 5, "Fair Value Measurement." For alternative investments, net asset value is used as a practical expedient to measure fair value unless it is probable that an investment will be sold for a different amount. In these cases, fair value is measured based on recent observable transaction information for similar investments, the consideration of non-binding bids from potential buyers and third-party valuations.

EXPECTED FUTURE BENEFIT PAYMENTS

We measure our plans as of the end of each fiscal year. The ERP's funding policy is to fund at least 100 percent of the ERP's funding target liability as set forth by the Internal Revenue Service. In 2019, we expect to contribute $15.5 million to the ERP. We do not expect to contribute to the SERP in 2019. In addition, we expect to make the following benefit payments to participants over the next 10 years:

	Pension Plans	Other Plans
	(in millions)	
Year ending December 31,		
2019	$ 30.6	$ 5.1
2020	30.9	5.2
2021	29.3	5.6
2022	31.1	5.9
2023	33.4	7.9
2024 through 2028	200.9	56.4
Total	$356.2	$86.1

8. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following is a summary of changes in accumulated other comprehensive income (loss) as of December 31, 2018, and 2017.

	Unrealized gain (loss) on available-for-sale investments	Net unrecognized employee benefit plan amounts	Total
	(in millions)		
Balance, January 1, 2017	$ 0.7	$ (82.7)	$ (82.0)
Other comprehensive income (loss) before reclassifications	32.5	(32.4)	0.1
Amounts reclassified from accumulated other comprehensive (income) loss (a)	(1.2)	3.7	2.5
Net current-period other comprehensive income	31.3	(28.7)	2.6
Balance, December 31, 2017	32.0	(111.4)	$ (79.4)
Other comprehensive (loss) income before reclassifications	(30.7)	25.4	(5.3)
Amounts reclassified from accumulated other comprehensive (income) loss (a)	(1.9)	4.4	2.5
Net current-period other comprehensive (loss) income	(32.6)	29.8	(2.8)
Balance, December 31, 2018	$ (0.6)	$ (81.6)	$ (82.2)

(a) Reclassified amounts for gains (losses) on available-for-sale investments were recorded in net realized and unrealized investment (losses) gains in the consolidated statements of operations—see Note 4, "Investments," for additional information. Reclassified net unrecognized employee benefit plan amounts were included as a component of net periodic benefit cost and recorded in compensation and benefits expense in the consolidated statements of operations—see Note 7, "Employee Benefit Liabilities," for additional information.

9. LEASES

FINRA leases certain office space and equipment in connection with its operations. The majority of these leases contain escalation clauses based on increases in rent, property taxes and building operating costs. Certain of these leases also contain renewal options. Rent expense for operating leases was $25.8 million and $24.5 million for the years ended December 31, 2018, and 2017, which was included in occupancy expense in the consolidated statements of operations.

Future minimum lease payments under non-cancelable operating leases with initial or remaining terms of one year or more consisted of the following at December 31, 2018:

Year ending December 31,	*(in millions)*
2019	$ 28.8
2020	22.9
2021	8.8
2022	6.7
2023	6.8
Remaining years	10.8
Total minimum lease payments	$ 84.8

Future minimum lease payments drop significantly in 2021 with the expiration of our lease at One Liberty Plaza in New York City, New York.

On May 22, 2019, we executed a lease to occupy 203,583 square feet of space over a ten-year period in New York City, New York. The rent commencement date for the leased space is July 16, 2021. Future minimum lease payments will total approximately $131.3 million over the ten-year lease term.

9. LEASES (CONTINUED)

On June 4, 2019, we executed a lease to occupy 48,981 square feet of space over a ten year period in Jersey City, New Jersey. The rent commencement date for the leased space is November 15, 2020. Future minimum lease payments will total approximately $22.4 million over the ten year lease term.

10. DEBT

FINRA maintains a seasonal unsecured line of credit agreement and has the option to borrow up to $150 million at the LIBOR Daily Floating Rate plus 0.45 percent (2.83 percent at December 31, 2018). As of December 31, 2018, and December 31, 2017, no line of credit amounts were outstanding. Our latest line of credit renewal commenced on February 1, 2019 and expired on May 31, 2019.

As of December 31, 2018 and 2017, we had outstanding debt of $14.6 million and $15.5 million, respectively, on our unsecured 2.99 percent fixed rate seven-year term loan related to our 2015 purchase of the Omega Building in Rockville, Maryland.

11. COMMITMENTS AND CONTINGENCIES

General Litigation

Management is not aware of any unasserted claims or assessments that would have a material adverse effect on the Company's financial position and the results of operations. Currently, there are certain legal proceedings pending against us. While the outcome of any pending litigation cannot be predicted, management does not believe that any such matter will have a material adverse effect on our business or financial position. As of December 31, 2018, there were no material estimated losses requiring disclosure related to pending legal proceedings, because we believe that any litigation contingency from these matters involves a chance of loss that is either remote or not reasonably possible. Such pending legal matters involve unspecified claim amounts, in which the respective plaintiffs seek an indeterminate amount of damages. The outcome of such matters is always uncertain, and unforeseen results can occur. It is possible that such outcomes could require us to pay damages or make other expenditures or establish accruals in amounts that we could not estimate as of December 31, 2018.

Indemnities

The general partner and investment manager of the Consolidated Entity, on behalf of the Consolidated Entity, enter into certain contracts that contain a variety of indemnifications. The Consolidated Entity's maximum exposure under these arrangements is unknown. However, the Consolidated Entity has not had prior claims or losses pursuant to these contracts and expects any risk of loss to be remote.

12. SUBSEQUENT EVENTS

On February 27, 2019, FINRA was selected as the Plan Processor for the Consolidated Audit Trail (CAT) and the contract was formalized the following month. As Plan Processor, FINRA is responsible for all aspects of the build, maintenance and operation of the CAT, which will allow regulators to improve securities market surveillance by creating an extensive audit trail of trades, quotes and orders for all U.S. exchange-listed and over-the-counter equity securities across all U.S. markets and trading venues. The CAT will also collect the same data for U.S. exchange-listed options contracts. To perform its duties as Plan Processor for the CAT, FINRA established a new wholly-owned consolidated subsidiary, FINRA CAT, LLC, and made a $50 million capital contribution to FINRA CAT, LLC in April 2019.

Subsequent events have been evaluated through June 25, 2019, the date these financial statements became available to be issued. These financial statements have been approved by management, who has determined that no subsequent event occurred that would require disclosure in the financial statements or accompanying notes.

FINRA Board of Governors as of May 21, 2019

William H. Heyman (Public)
Chairman
The Travelers Companies, Inc.
New York, NY

Robert W. Cook
President and CEO
FINRA
Washington, DC

Lance F. Drummond (Public)
Retired
Charlotte, NC

Andrew S. Duff (Industry)
Piper Jaffray & Co.
Minneapolis, MN

John (Jack) Ehnes (Public)
CalSTRS
West Sacramento, CA

Stephen A. Kohn (Industry)
Stephen A. Kohn & Associates, Ltd.
Lakewood, CO

Brian J. Kovack (Industry)
Kovack Securities, Inc.
Ft. Lauderdale, FL

Rochelle B. Lazarus (Public)
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Joshua S. Levine (Public)
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Greenwich, CT

Brigitte C. Madrian (Public)
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Joseph M. Mecane (Industry)
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Robert A. Muh (Industry)
Sutter Securities, Inc.
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Kathleen A. Murphy (Industry)
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Eileen K. Murray (Public)
Bridgewater Associates
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James D. Nagengast (Industry)
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LaVista, NE

Paige W. Pierce (Industry)
Larimer Capital Corporation
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Amelia Island, FL

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Amy L. Webber (Industry)
Cambridge Investment Research, Inc.
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Susan Wolburgh Jenah (Public)
Former President and CEO
Investment Industry Regulatory Organization of Canada
Toronto, ON

FINRA Officers as of May 21, 2019

Robert W. Cook
President and Chief Executive Officer

Marcia E. Asquith
Executive Vice President, Board and External Relations and Corporate Secretary

Richard W. Berry
Executive Vice President and Director of Dispute Resolution

Robert L. D. Colby
Executive Vice President and Chief Legal Officer

Gene DeMaio
Executive Vice President, Options Regulation and Market Regulation

Todd T. Diganci
Executive Vice President—Chief Financial and Chief Administrative Officer

Cameron K. Funkhouser
Executive Vice President, Office of Fraud Detection and Market Intelligence

Thomas R. Gira
Executive Vice President, Market Regulation and Transparency Services

Bari Havlik
Executive Vice President, Member Supervision

Derek W. Linden
Executive Vice President, Registration and Disclosure

Steven J. Randich
Executive Vice President and Chief Information Officer

Michael G. Rufino
Executive Vice President, Head of Member Supervision—Sales Practice

Susan Schroeder
Executive Vice President, Enforcement

Thomas M. Selman
Executive Vice President, Regulatory Policy and Legal Compliance Officer

William J. Wollman
Executive Vice President, Member Regulation—Risk Oversight and Operational Regulation

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