

Hornor, Townsend & Kent, Inc.

**Statement of Financial Condition
With Report of Independent Registered Public
Accounting Firm
December 31, 2017**

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

ANNUAL AUDITED REPORT
FORM X-17A-5
PART III

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FACING PAGE

Information Required of Brokers and Dealers Pursuant to Section 17 of the
Securities Exchange Act of 1934 and Rule 17a-5 Thereunder

REPORT FOR THE PERIOD BEGINNING 01/01/17 AND ENDING 12/31/17
MM/DD/YY MM/DD/YY

A. REGISTRANT IDENTIFICATION

NAME OF BROKER-DEALER: **Hornor, Townsend & Kent, Inc.**

ADDRESS OF PRINCIPAL PLACE OF BUSINESS: (Do not use P.O. Box No.)

600 Dresher Road

OFFICIAL USE ONLY
FIRM I.D. NO.

(No. and Street)

HORSHAM

PA

19044

(City)

(State)

(Zip Code)

NAME AND TELEPHONE NUMBER OF PERSON TO CONTACT IN REGARD TO THIS REPORT

Charles J. Ingulli Jr., CPA

(215) 956-8735

(Area Code - Telephone Number)

B. ACCOUNTANT IDENTIFICATION

INDEPENDENT PUBLIC ACCOUNTANT whose opinion is contained in this Report*

PricewaterhouseCoopers, LLP

(Name - if individual, state last, first, middle name)

Two Commerce Square Suite 1800 Philadelphia

Pennsylvania 19103

(Address)

(City)

(State)

(Zip Code)

CHECK ONE:

- ☒ Certified Public Accountant
☐ Public Accountant
☐ Accountant not resident in United States or any of its possessions.

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*Claims for exemption from the requirement that the annual report be covered by the opinion of an independent public accountant must be supported by a statement of facts and circumstances relied on as the basis for the exemption. See Section 240.17a-5(e)(2)

OATH OR AFFIRMATION

I, Timothy N. Donahue, swear (or affirm) that, to the best of my knowledge and belief the accompanying financial statement and supporting schedules pertaining to the firm of Hornor, Townsend & Kent, Inc., as of December 31, 2017, are true and correct. I further swear (or affirm) that neither the company nor any partner, proprietor, principal officer or director has any proprietary interest in any account classified solely as that of a customer, except as follows:

Commonwealth of Pennsylvania - Notary Seal
Marianne C. Bechtel, Notary Public
Montgomery County
My commission expires December 26, 2021
Commission number 1008805
Member, Pennsylvania Association of Notaries

Timothy N. Donahue
Signature

CEO / President

Title

Marianne C. Bechtel
Notary Public

This report ** contains (check all applicable boxes):

- ☒ (a) Facing Page.
- ☒ (b) Statement of Financial Condition.
- ☐ (c) Statement of Income (Loss).
- ☐ (d) Statement of Changes in Financial Condition.
- ☐ (e) Statement of Changes in Stockholders' Equity or Partners' or Sole Proprietors' Capital.
- ☐ (f) Statement of Changes in Liabilities Subordinated to Claims of Creditors.
- ☐ (g) Computation of Net Capital.
- ☐ (h) Computation for Determination of Reserve Requirements Pursuant to Rule 15c3-3.
- ☐ (i) Information Relating to the Possession or Control Requirements Under Rule 15c3-3.
- ☐ (j) A Reconciliation, including appropriate explanation of the Computation of Net Capital Under Rule 15c3-1 and the Computation for Determination of the Reserve Requirements Under Exhibit A of Rule 15c3-3.
- ☐ (k) A Reconciliation between the audited and unaudited Statements of Financial Condition with respect to methods of consolidation.
- ☒ (l) An Oath or Affirmation.
- ☐ (m) A copy of the SIPC Supplemental Report.
- ☐ (n) A report describing any material inadequacies found to exist or found to have existed since the date of the previous audit.

****For conditions of confidential treatment of certain portions of this filing, see section 240.17a-5(e)(3).**

Hornor, Townsend & Kent, Inc.

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The accompanying notes are an integral part of this financial statement.



Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholder of Hornor, Townsend & Kent, Inc.:

Opinion on the Financial Statement – Statement of Financial Condition

We have audited the accompanying statement of financial condition of Hornor, Townsend & Kent, Inc. as of December 31, 2017, including the related notes (collectively referred to as the “financial statement”). In our opinion, the financial statement presents fairly, in all material respects, the financial position of the Company as of December 31, 2017 in conformity with accounting principles generally accepted in the United States of America.

Basis for Opinion

The financial statement is the responsibility of the Company’s management. Our responsibility is to express an opinion on the Company’s financial statement based on our audit. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (“PCAOB”) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audit of this financial statement in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statement is free of material misstatement, whether due to error or fraud.

Our audit included performing procedures to assess the risks of material misstatement of the financial statement, 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 statement. Our audit also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the financial statement. We believe that our audit provides a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

February 28, 2018

We have served as the Company’s auditor since 2004.

Hornor, Townsend & Kent, Inc.
Statement of Financial Condition
As of December 31, 2017

Assets

Cash and cash equivalents	\$ 5,803,606
Segregated cash	250,000
Deposits with clearing organizations	120,029
Receivables from brokers/dealers and clearing organizations	1,859,577
Commissions receivable	1,215,793
Equipment and capitalized software, at cost (net of accumulated depreciation and amortization of \$ 1,343,653)	573,682
Prepaid expenses	1,051,898
Receivable from Parent	509,248
Deferred tax asset, net	60,864
Other assets	531,742
Total assets	<u>\$ 11,976,439</u>

Liabilities and Stockholder's Equity

Liabilities

Commissions payable	\$ 2,926,381
Accounts payable and accrued expenses	770,065
Payable to Parent	791,020
Total liabilities	<u>4,487,466</u>

Stockholder's Equity

Common stock, \$1.00 par value; 1,000 shares authorized, issued and outstanding	1,000
Additional paid-in capital	33,158,264
Accumulated deficit	(25,670,291)
Total stockholder's equity	<u>7,488,973</u>
Total liabilities and stockholder's equity	<u>\$ 11,976,439</u>

The accompanying notes are an integral part of this financial statement.

Hornor, Townsend & Kent, Inc.
Notes to Statement of Financial Condition
As of December 31, 2017

1. Organization and Basis of Presentation

Hornor, Townsend & Kent, Inc. (the "Company") is an introducing broker-dealer registered with the Securities and Exchange Commission ("SEC"), a member of the Financial Industry Regulatory Authority, the Depository Trust Clearing Corporation and the National Securities Clearing Corporation. The Company is a wholly owned subsidiary of The Penn Mutual Life Insurance Company ("Penn Mutual" or "Parent"). The Company has one wholly owned subsidiary, HTK Insurance Agency, Inc. that is inactive. The Company selects, trains, and supervises personnel of Penn Mutual and independent registered representatives in connection with the sale of registered products.

As of December 31, 2017, the Company had an accumulated deficit of \$25,670,291. To the extent that sufficient capital is not generated through the Company's normal operating activities, Penn Mutual would provide any incremental capital to fund the Company's ongoing business. Penn Mutual has provided the Company with an ongoing support letter through March 31, 2019.

2. Summary of Significant Accounting Policies

Basis of Presentation

The financial statement is prepared in conformity with accounting principles generally accepted in the United States.

Use of Estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates.

Cash and Cash Equivalents

Cash and cash equivalents include cash and money market instruments with original maturities of three months or less and have no redemption restrictions. At December 31, 2017, the company had \$2,540,987 in cash equivalents.

Segregated Cash

Segregated Cash represents cash in a bank account established exclusively for the benefit of customers.

Deposits with Clearing Organizations

Deposits with clearing organizations include \$100,000 in deposits with Pershing LLC, the Company's clearing organization and \$20,029 with the Depository Trust Clearing Corporation.

Receivable from Brokers/Dealers and Clearing Organizations

Receivable from brokers/dealers and clearing organizations contains a receivable from Pershing, LLC in the amount of \$918,177 at December 31, 2017. The Company clears certain of its customer transactions through Pershing, LLC on a fully disclosed basis. The amount receivable from the clearing broker relates to commissions and other fees earned for the aforementioned transactions. It also contains a 12b-1 receivable related to various mutual fund carriers for \$941,400 for business processed directly with those carriers.

Equipment and Capitalized Software

Equipment and capitalized software is carried at depreciated or amortized cost. Capitalized software consists primarily of costs related to the firm's implementation of certain operational and financial systems. Costs related to planning and analysis have been expensed.

Federal Income Taxes

The Company files a consolidated federal income tax return with its Parent. Federal income taxes are charged or credited to operations based upon amounts estimated to be payable or recoverable as a result of taxable operations for the current year. Beginning in 2014, the Company modified the tax sharing agreement with its Parent. In connection with this agreement, the Company will compute its federal tax liability on a benefits for loss basis. The Company will pay for any taxable income it contributes to the Parent's consolidated income tax return, or receive a reimbursement of income taxes for net operating losses actually used to reduce the tax liability of the Parent's consolidated income tax return. Deferred income tax assets and liabilities are established to reflect the impact of temporary differences between the amount of assets and liabilities recognized for financial reporting purposes and such amounts recognized for tax purposes. These deferred tax assets or liabilities are measured by using the enacted tax rates expected to apply to taxable income in the period in which the deferred tax liabilities or assets are expected to be settled or realized.

3. Valuation of Company Assets

Fair Value Measurements

The Company's financial instruments recorded at fair value have been categorized based upon a fair value hierarchy in accordance with ASC 820.

ASC 820 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used by the Company to measure fair value:

Level 1 – Quoted prices in active markets for identical assets or liabilities without adjustment.

Level 2 – Observable inputs other than Level 1 prices, such as quoted prices for similar assets, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. The Company does not hold any assets carried at fair value in Level 2 assets.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, or similar techniques, as well as instruments for which the determination of fair value requires significant judgment by management. The Company does not hold any assets carried at fair value in Level 3.

The Company had no transfers of financial instruments between Levels during the fiscal year ended December 31, 2017.

Hornor, Townsend & Kent, Inc.
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Money Market - The fair value of money market funds, which are included in Cash and cash equivalents, is based upon daily quoted net asset values of shares held at the reporting date.

The following table presents information about the Company's financial instruments measured at Fair Value on a recurring basis as of December 31, 2017:

Financial Assets	Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Totals
Cash equivalents				
Money Market	\$ 2,540,987	\$ -	\$ -	\$ 2,540,987
Total	\$ 2,540,987	\$ -	\$ -	\$ 2,540,987

The following financial instruments are not carried at fair value on our Statement of Financial Condition.

Cash and cash equivalents, Segregated cash, Deposits with clearing organizations, Receivables from brokers/dealers and clearing organizations, Commissions Receivable, Clearing Organizations and certain Other assets - These assets are generally short-term in nature and with credit worthy counterparties. Carrying value approximates fair value.

Commissions Payable, Accounts payable and accrued expenses and certain Other liabilities - These liabilities are generally short-term in nature. Carrying value approximates fair value.

4. Related Party Transactions

The Company supports Penn Mutual's professional agents and financial advisors and sells Penn Mutual Variable Life and Variable Annuity Products.

Under the terms of an expense allocation agreement, the Company reimbursed Penn Mutual for services provided on behalf of the Company, including direct and allocated expenses.

As a marketing allowance, the Company pays an 87% ratio of commission expense on commission revenue. Commission Revenue is defined as Commissions from sale of investment company shares, variable insurance products and securities and fee income from investment advisory and asset management. After commissions are paid to registered representatives the residual amount is paid to Penn Mutual.

As of December 31, 2017, the Company had a receivable of \$509,248 for Federal Income Taxes and a payable of \$791,020 to Penn Mutual resulting from related party transactions.

5. Credit Risk

The Company clears approximately 24% of their securities transactions through a clearing broker, with whom the Company maintains a Proprietary Accounts for Introducing Brokers ("PAIB") agreement. Accordingly, a substantial portion of the Company's credit exposures is concentrated with its clearing broker. In accordance with industry practice, the clearing agent records customer transactions on a settlement-date basis, which is generally three business days after trade date. The clearing agent is therefore exposed to risk of loss on these transactions in the event of a customer's inability to meet the terms of their contracts, in which case the clearing agent may have

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Notes to Statement of Financial Condition
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to purchase or sell the underlying financial instruments at prevailing market prices. Any loss incurred by the clearing agent, on behalf of a customer of the Company, is charged to the Company.

6. Income Taxes

Deferred income taxes reflect the impact for financial statement reporting purposes of temporary differences between the financial statement carrying values and tax basis of assets and liabilities. The tax effects of temporary differences and carryforwards that give rise to the deferred tax asset are the following as of December 31, 2017:

Deferred tax asset, Net:

Net Operating Losses	\$ 146,631
Other	41,554
Total Deferred Tax Assets	<u>\$ 188,185</u>
<i>Deferred Tax Liability</i>	
Capitalized Software	<u>(127,321)</u>
Total Deferred Tax Liability	<u>\$ (127,321)</u>

Deferred Tax Asset, Net **\$ 60,864**

On December 22, 2017, the U.S. government enacted new tax legislation. The legislation makes broad and complex changes to the U.S. tax code and accordingly it will take time to assess and interpret the changes. Given the timing of the enactment date and impact of the legislation, the SEC issued Staff Accounting Bulletin ("SAB") 118, with similar provisions extended by the FASB staff for non-public companies. SAB 118 provisions allow registrants to implement elements of tax reform under three scenarios:

1. Measurement of certain income tax effects are complete in accordance with the new tax law.
2. Measurement of certain income tax effects can be reasonably estimated (also referred to as "provisional" amounts).
3. Measurement of certain income tax effects cannot be reasonably estimated.

SAB 118 provides that the measurement period is complete when a company's accounting is complete and in no circumstances should the measurement period extend beyond one year from the enactment date. If a company discloses elements of tax reform under scenario 2 or 3 and new information or further analysis is needed which results in a revised estimate, the revision will be considered a change in estimate recorded in the period identified rather than an error during this one year relief period.

The company has adopted the provisions of SAB 118 as of the balance sheet date December 31, 2017. The Deferred tax asset, net may change significantly in the future, following a more comprehensive review of the legislation.

The Company files a consolidated federal income tax return with its parent, Penn Mutual, and is subject to taxation in the U.S. and various state jurisdictions. Based on the inter-company tax allocation agreements, each subsidiary's tax liability or refund is accrued on a benefits for loss

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basis. As of December 31, 2017, the Company has a current tax receivable of \$509,248 from Penn Mutual.

The Company is required to evaluate the recoverability of deferred tax assets and to establish a valuation allowance if necessary to reduce the deferred tax asset to an amount which is more likely than not to be realized. Considerable judgment is required in determining whether a valuation allowance is necessary, and if so, the amount of such valuation allowance. In evaluating the need for a valuation allowance, the Company considers many factors, including: (1) the nature of the deferred tax assets and liabilities; (2) whether they are ordinary or capital; (3) the timing of their reversal; (4) taxable income in prior carryback years as well as projected taxable income exclusive of reversing temporary differences and carryforwards; (5) the length of time that carryovers can be utilized; (6) unique tax rules that would impact the utilization of the deferred tax assets; and (7) any tax planning strategies that the Company would employ to avoid a tax benefit from expiring unused.

Additionally, the benefits for loss approach also enables a standalone entity to consider certain criteria of its consolidated parent when evaluating the realizability of its deferred tax assets. Given this, a valuation allowance is not required in a company's standalone financial statements if it is determined that a valuation allowance was not required for its parent consolidated group. The Company's parent consolidated group has not recorded a valuation allowance as of December 31, 2017. As such, although the realization is not assured, management believes it is more likely than not that the deferred tax assets will be realized and, therefore, the Company has not recorded a valuation allowance as of December 31, 2017.

The Company remains subject to examinations by U.S. Federal and state tax authorities for the tax years 2014 through 2016.

7. Employee Benefit Plan

Pension Plan

Certain employees of the Company are covered under Penn Mutual's funded defined benefit pension plan. Penn Mutual's policy is to fund qualified pension costs in accordance with the Employee Retirement Income Security Act of 1974. Penn Mutual may increase its contribution above the minimum based upon an evaluation of the tax and cash positions and the plan's funded status.

Penn Mutual froze the benefits under its qualified pension plans effective December 31, 2005. Therefore no further benefits are accrued for participants.

Other Retirement and Post Employment Benefits

The Company provides, through Penn Mutual, certain life insurance and health care benefits for its retired employees, their beneficiaries and covered dependents.

Defined Contribution Plan

Substantially all the employees of the Company are covered by Penn Mutual's defined contribution plan. Designated contributions of up to 6% of annual compensation are eligible to be matched by the Company.

Hornor, Townsend & Kent, Inc.
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8. Commitments and Contingencies

The Company leases its office from Penn Mutual under a non-cancelable operating lease expiring December 31, 2018.

As of December 31, 2017, aggregate minimum rental commitments under all non-cancelable leases through December 31, 2018 are \$194,361.

The Company is involved in litigation arising in and out of the normal course of business. In addition, the regulators within the brokerage industry continue to focus on market conduct and compliance issues. The Company would establish a provision for estimated losses from pending complaints, legal actions, investigations and proceedings when fully analyzed, indicating it is both probable that a liability will be incurred and the amount of loss can be reasonably estimated. The ultimate costs of litigation-related charges can vary significantly from period to period, depending on such factors as market conditions, the size and volume of customer complaints and claims and recoveries from indemnification, contribution or insurance reimbursements. As of December 31, 2017, the Company has no recorded liability related to these matters.

9. Concentrations

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of bank deposits and money market funds. The Company maintains cash balances with one financial institution that exceeds the federally insured limit of \$250,000 per institution. The Company also maintains money market funds that are not federally insured. Management of the Company believes it has adequately mitigated this risk by only investing in or through major financial institutions.

10. Equipment and Capitalized Software, at cost

Equipment	\$ 5,061
Capitalized software	<u>1,912,274</u>
	1,917,335
Less: Accumulated depreciation and amortization	<u>(1,343,653)</u>
Equipment and Capitalized Software, net	<u>\$ 573,682</u>

11. Net Capital Requirements

As a registered broker-dealer, the Company is subject to the Uniform Net Capital Rule under Rule 15c3-1 of Securities Exchange Act of 1934. The Company computes its net capital requirement using the basic method of computation. Under this method, the Company's requirement may not be less than 6 2/3% of aggregate indebtedness or \$250,000 whichever is greater. The regulations also require that the ratio of aggregate indebtedness to net capital not to exceed 15 to 1. At December 31, 2017, the Company had net capital of \$4,304,257 which was \$4,005,092 in excess of its requirement of \$299,165. The Company's aggregate Indebtedness to Net Capital Ratio was 1.04 to 1. The Company claims the exemption provision of SEC Rule 15c3-3(k)(2)(ii).

Hornor, Townsend & Kent, Inc.
Notes to Statement of Financial Condition
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12. Subsequent Events

Management has evaluated the events and transactions that have occurred through February 28, 2018, the date the financial statements were available to be issued, and noted no items requiring adjustment of the financial statements or additional disclosures.