

**A & N Electric Cooperative**  
**Financial Statements**  
**December 31, 2018 and 2017**

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## **Independent Auditor's Report**

The Board of Directors  
A & N Electric Cooperative  
Tasley, Virginia

We have audited the accompanying financial statements of A & N Electric Cooperative (the "Cooperative") which comprise the balance sheets as of December 31, 2018 and 2017 and the related statements of operations, equities and cash flows for the years then ended, and the related notes to the financial statements.

### **Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Cooperative's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of A & N Electric Cooperative as of December 31, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## **Change in Accounting Principle**

We draw attention to Note A of the financial statements, which describes a change in accounting principle related to revenue recognition of unbilled revenue. The financial statements for 2017 have been retrospectively adjusted to reflect this change of accounting principle adopted in 2018. Our opinion is not modified with respect to this matter.

## **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated February 10, 2019, on our consideration of the Cooperative's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Cooperative's internal control over financial reporting and compliance.



Richmond, Virginia  
February 10, 2019

## Balance Sheets

### A & N Electric Cooperative

	December 31,	
	2018	As Adjusted 2017
<b>Assets</b>		
Electric plant		
Electric plant	\$ 194,261,426	\$ 189,082,790
Less accumulated provision for depreciation	67,450,919	65,317,956
	<u>126,810,507</u>	<u>123,764,834</u>
Investments		
Investments in associated organizations	20,569,966	19,674,833
Special funds	2,578,191	2,340,644
Investments in economic development project	25,000	50,000
	<u>23,173,157</u>	<u>22,065,477</u>
Current assets		
Cash and cash equivalents	5,973,804	10,334,133
Accounts receivable, net	12,477,802	12,717,283
Materials and supplies	2,393,574	1,204,589
Other current assets	903,774	862,643
	<u>21,748,954</u>	<u>25,118,648</u>
Deferred charges	<u>1,337,547</u>	<u>1,374,112</u>
	<u>\$ 173,070,165</u>	<u>\$ 172,323,071</u>

See Independent Auditor's Report and Notes to Financial Statements

	December 31,	
	2018	As Adjusted 2017
<b>Equities and Liabilities</b>		
Equities		
Patronage capital	\$ 55,621,417	\$ 54,188,461
Other equities	12,696,342	10,887,155
Memberships	137,750	137,500
	<u>68,455,509</u>	<u>65,213,116</u>
Noncurrent liabilities		
Long-term debt	89,396,603	92,525,167
Other noncurrent liabilities	2,815,620	2,694,620
	<u>92,212,223</u>	<u>95,219,787</u>
Current liabilities		
Accounts payable	5,755,308	5,460,909
Current maturities of long-term debt	3,700,379	3,626,000
Consumer deposits	2,314,245	2,257,035
Other current and accrued liabilities	610,169	463,090
	<u>12,380,101</u>	<u>11,807,034</u>
Deferred credits	<u>22,332</u>	<u>83,134</u>
	<u>\$ 173,070,165</u>	<u>\$ 172,323,071</u>

# Statements of Operations

## A & N Electric Cooperative

	Year Ended December 31,	
	2018	2017
Operating revenues	\$ 79,267,236	\$ 69,991,587
Operating expenses		
Cost of power	53,020,748	46,428,354
Transmission	23,099	18,746
Distribution - operation	2,484,313	2,180,900
Distribution - maintenance	4,728,322	4,678,528
Consumer accounts	2,818,681	2,238,913
Customer service and informational	51,782	54,152
Administrative and general	3,563,342	3,146,349
Depreciation and amortization	5,696,046	5,552,453
Interest on long-term debt	4,033,879	4,040,132
Interest - other	24,707	11,105
Other	258,739	281,076
	<u>76,703,658</u>	<u>68,630,708</u>
Operating Margins Before Patronage Allocations	2,563,578	1,360,879
Patronage allocations		
Generation and transmission	821,342	1,630,439
Other	132,638	117,617
	<u>953,980</u>	<u>1,748,056</u>
Net Operating Margins	3,517,558	3,108,935
Nonoperating income		
Interest income	1,573,787	1,400,214
Other, net	156,395	
	<u>1,730,182</u>	<u>1,400,214</u>
Net Margins	<u>\$ 5,247,740</u>	<u>\$ 4,509,149</u>

See Independent Auditor's Report and Notes to Financial Statements

## Statements of Equities

### A & N Electric Cooperative

#### Years Ended December 31, 2018 and 2017

	Patronage Capital	Other Equities	Memberships	Total
Balance, December 31, 2016, as previously reported	\$ 46,953,316	\$ 9,289,524	\$ 137,100	\$ 56,379,940
Adjustment for cumulative effect on prior years of retroactively applying a change in accounting principle	6,070,641			6,070,641
Balance, December 31, 2016, as adjusted	53,023,957	9,289,524	137,100	62,450,581
Net margins	3,108,935	1,400,214		4,509,149
Retirement of capital credits	(1,944,431)	21,604		(1,922,827)
Net change in memberships			400	400
Unclaimed capital credits		175,813		175,813
Balance, December 31, 2017, as adjusted	54,188,461	10,887,155	137,500	65,213,116
Net margins	3,673,953	1,573,787		5,247,740
Retirement of capital credits	(2,240,997)	21,503		(2,219,494)
Net change in memberships			250	250
Unclaimed capital credits		213,897		213,897
Balance, December 31, 2018	<u>\$ 55,621,417</u>	<u>\$ 12,696,342</u>	<u>\$ 137,750</u>	<u>\$ 68,455,509</u>

See Independent Auditor's Report and Notes to Financial Statements



# Statements of Cash Flows

## A & N Electric Cooperative

	Year Ended December 31,	
	2018	2017
<b>Cash Flows from Operating Activities</b>		
Cash received from members	\$ 79,506,717	\$ 70,307,914
Cash paid to suppliers and employees	(66,533,068)	(59,346,680)
Interest received	286,635	178,498
Interest paid	(4,058,586)	(4,051,237)
Net Cash Provided by Operating Activities	9,201,698	7,088,495
<b>Cash Flows from Investing Activities</b>		
Extension and replacement of plant	(9,141,684)	(8,525,545)
Plant removal costs	(1,713,984)	(1,577,147)
Contribution in aid of construction	924,964	690,777
Proceeds from retirement of investments in CTC's	7,088	6,971
Collections on economic development loan	25,000	25,000
Net Cash Used by Investing Activities	(9,898,616)	(9,379,944)
<b>Cash Flows from Financing Activities</b>		
Capital credits received from suppliers	51,759	525,644
Capital credits paid to members	(2,005,597)	(1,747,014)
Principal payments of long-term debt	(3,790,033)	(3,328,294)
Proceeds from long-term borrowings	2,023,000	9,034,000
Net change in memberships	250	400
Net change in consumer deposits	57,210	(30,506)
Net Cash Provided (Used) by Financing Activities	(3,663,411)	4,454,230
Net Increase (Decrease) in Cash and Cash Equivalents	(4,360,329)	2,162,781
Cash and cash equivalents - beginning of year	10,334,133	8,171,352
Cash and Cash Equivalents - End of Year	<u>\$ 5,973,804</u>	<u>\$ 10,334,133</u>

See Independent Auditor's Report and Notes to Financial Statements

	Year Ended December 31,	
	2018	2017
<b>Net Margins</b>	\$ 5,247,740	\$ 4,509,149
Adjustments to reconcile net margins to net cash provided by operating activities:		
Depreciation and amortization	5,494,830	5,351,237
Acquisition adjustment amortization	201,216	201,216
Noncash capital credits	(953,980)	(1,748,056)
Noncash interest received from cushion of credit	(1,287,152)	(1,221,701)
(Increase) decrease in:		
Accounts receivable	239,481	316,327
Other current assets	(41,131)	(293,979)
Special funds	(237,547)	(243,561)
Deferred charges	36,565	388,026
Increase (decrease) in:		
Accounts payable	294,399	(491,186)
Other current and accrued liabilities	147,079	65,976
Deferred credits	(60,802)	63,047
Other noncurrent liabilities	121,000	192,000
Net Cash Provided by Operating Activities	<u>\$ 9,201,698</u>	<u>\$ 7,088,495</u>
<b>Non-Cash Investing and Financing Activity</b>		
Refinance of RUS debt to CFC	<u>\$ 8,045,183</u>	

## **Notes to Financial Statements**

### **A & N Electric Cooperative**

#### **December 31, 2018 and 2017**

##### **Note A - Summary of Significant Accounting Policies**

###### Nature of Operations

A & N Electric Cooperative (the “Cooperative”) is a member owned, not-for-profit company organized to provide electric service to its members residing in the counties of Accomack and Northampton in Virginia, along with Smith Island in Maryland.

###### Basis of Presentation

These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), including GAAP for regulated operations.

The system of accounts of the Cooperative are maintained in accordance with the Uniform System of Accounts as prescribed by the Federal Energy Regulatory Commission (FERC) for Class A and B electric utilities modified for electric borrowers of the Rural Utilities Service (RUS) and the State Corporation Commission of the Commonwealth of Virginia (SCC).

###### Accounting Estimates

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

###### Electric Plant

Electric plant is stated at the original cost of construction, which includes the cost of contracted services, direct labor, materials and overhead items. Contributions from others toward the construction of electric plant are credited to the applicable plant accounts.

When property, which represents a retirement unit, is replaced or removed, the average cost of such property as determined from the continuing property records is credited to electric plant and such cost, together with cost of removal less salvage is charged to the accumulated provision for depreciation.

Maintenance and repairs, including the renewal of minor items of plant not comprising a retirement unit, are charged to the appropriate maintenance accounts, except that repairs of transportation and service equipment are charged to clearing accounts and redistributed to operating expenses and other accounts.

###### Accounts Receivable

Accounts receivable are uncollateralized obligations of members which are stated at the amount billed. The carrying amount of accounts receivable is reduced by accounts considered uncollectible. The Cooperative provides for the uncollectible accounts monthly, based on a percentage of sales which past experience has indicated will be uncollectible. When accounts are deemed to be uncollectible, they are charged against the provision for uncollectible accounts.

## Notes to Financial Statements

### A & N Electric Cooperative

#### December 31, 2018 and 2017

##### Note A - Summary of Significant Accounting Policies - Continued

###### Depreciation

Provision for depreciation has been made by application of the straight-line method to the original cost, by groups of depreciable properties in service. Current depreciation rates, which are estimated to amortize the cost of plant over the service lives, were as follows:

Production plant	3.00 - 7.00%
Transmission plant	4.72%
Distribution plant	1.70 - 8.13%
General plant	2.00 - 20.00%

###### Inventories

Inventories are generally used for construction, operation and maintenance work, and are not for resale. They are valued at the lower of market value or moving average unit cost.

###### Revenues

Revenue is recognized at the time energy is delivered to consumers on a monthly basis.

The billing rate schedules of the Cooperative contain provisions to either increase or decrease the consumers' billing from the base level billing schedules dependent upon the cost of the power cost adjustment and wholesale power adjustment passed on from the vendor for electrical energy purchased for resale.

###### Cost of Power

The Cooperative utilizes a deferred method of accounting for power cost and wholesale power fuel adjustments. Under this method, the cost of power is adjusted to recognize as expense that portion of the pass-through power cost and fuel charge that is billed to consumers. Any amounts collected in advance or not billed to consumers are recorded as a deferred charge or deferred credit as applicable.

###### Accounting Changes

During 2018, management and the Board of Directors of the Cooperative changed the way they accounted for unbilled revenue by electing to recognize revenue for utility service rendered to customers, but not yet billed to customers until the subsequent year. As a result of this accounting change for unbilled revenue, accounts receivable and patronage capital assignable increased \$6,070,641 for the year ending December 31, 2017. The financial statements for the year ending December 31, 2017 have been adjusted to reflect this accounting change with the following changes:

As of December 31, 2017, accounts receivable was originally reported as \$6,646,642, patronage capital was reported as \$48,117,820. As a result of this accounting change, accounts receivable has been adjusted to \$12,717,283 and patronage capital has been adjusted to \$54,188,461.

## Notes to Financial Statements

### A & N Electric Cooperative

#### December 31, 2018 and 2017

##### Note A - Summary of Significant Accounting Policies - Continued

###### Regulatory Accounting

The Cooperative currently complies with accounting guidance set forth by the Accounting Standards Codification (ASC) Topic 980 regarding the effect of certain types of regulation. This guidance allows a regulated cooperative to record certain costs or credits that have been or are expected to be allowed in the ratemaking process in a period different from the period in which the costs would be charged to expense or income by a non-regulated enterprise. Accordingly, the Cooperative records certain assets and liabilities that result from the regulated ratemaking process that would not be recorded under GAAP for non-regulated entities.

###### Income Taxes

The Cooperative has been granted exemption from income tax under Internal Revenue Service Code Section 501(c)(12) of the Internal Revenue Code. The Cooperative evaluates the filing positions in all federal and state jurisdictions where it is required to file income tax returns, including its status as a tax-exempt electric cooperative entity. The Cooperative believes its income tax filing positions, including its status as a tax-exempt entity will be sustained and does not anticipate any adjustment that will result in a material change to its financial position. Tax filing ending on or after December 31, 2015 remain subject to examination by federal and state taxing authorities.

###### Cash and Cash Equivalents

The Cooperative considers all highly liquid investments with a maturity of three months or less to be cash equivalents.

###### Investments in Associated Organizations

Investments in associated organizations are primarily composed of patronage capital assigned from associated organizations. These investments are recorded at costs plus allocated equities.

###### Advertising Costs

Advertising costs were expensed as incurred.

###### Subsequent Events

Subsequent events have been evaluated through February 10, 2019, which is the date the financial statements were available to be issued.

###### Reclassifications

Certain reclassifications were made to the 2017 financial statements to conform to the 2018 presentation. As a result of these reclassifications, there were no changes to 2017 net margins or total equities.

## Notes to Financial Statements

### A & N Electric Cooperative

#### December 31, 2018 and 2017

##### Note B - Assets Pledged

All assets are pledged as security for the long-term debt to National Rural Utilities Cooperative Finance Corporation (CFC) and Federal Financing Bank (FFB).

##### Note C - Electric Plant

Listed below are the major classes of electric plant:

	December 31,	
	2018	2017
Distribution plant	\$ 159,727,559	\$ 154,547,453
General plant	18,212,140	18,004,005
Acquisition adjustments	6,438,902	6,438,902
Transmission plant	3,821,253	3,870,966
Production plant	3,045,725	2,631,344
Intangible plant	2,026	2,026
Electric plant in service	191,247,605	185,494,696
Construction work in progress	3,013,821	3,588,094
	<u>\$ 194,261,426</u>	<u>\$ 189,082,790</u>

In accordance with accounting for Asset Retirement Obligations and FERC Order 631 as adopted by the RUS, the Cooperative has determined that it had no legal asset retirement obligations for the years ended December 31, 2018 and 2017. Regarding non-legal retirement obligations, the Cooperative follows the regulatory principle of inter-generational cost allocation by including net salvage (gross salvage less cost of removal) as a component of depreciation rates. For the year ended December 31, 2018, the Cooperative collected approximately \$1,400,000 from consumers for net salvage. As of December 31, 2018, it was estimated that the Cooperative had approximately \$14,800,000 as a component of accumulated depreciation, which represented the difference in the timing of recognition of period costs associated with non-legal retirement obligations.

## Notes to Financial Statements

### A & N Electric Cooperative

#### December 31, 2018 and 2017

##### Note D - Investments in Associated Organizations

Investments in associated organizations consisted of the following:

	December 31,	
	2018	2017
Patronage capital:		
Old Dominion Electric Cooperative (ODEC)	\$ 17,957,885	\$ 17,136,563
National Rural Telecommunications Cooperative	862,154	862,225
CFC	389,878	376,292
Federated Insurance	365,717	324,245
National Information Solutions Cooperative	218,138	200,016
Other	86,684	80,909
	<u>19,880,456</u>	<u>18,980,250</u>
Capital Term Certificates (CTC):		
Subscriptions (SCTC's)	416,306	416,306
Loan (ZCTC's)	22,253	29,341
Loan (LCTC's)	8,850	8,850
	<u>447,409</u>	<u>454,497</u>
Other:		
Investment - TEC Trading	202,500	202,500
Investment in building - Virginia, Maryland and		
Delaware Association of Electric Cooperatives	12,880	12,880
Membership fees	2,000	2,000
Other	24,721	22,706
	<u>242,101</u>	<u>240,086</u>
	<u>\$ 20,569,966</u>	<u>\$ 19,674,833</u>

The capital term certificates invested in CFC are unsecured and subordinated. The SCTC's bear interest at an annual rate of 5% payable semiannually and the LCTC's bear interest at an annual rate of 3% payable semiannually. The ZCTC's are non-interest bearing.

The investment in TEC Trading, Inc. represents an unconsolidated joint venture with other members of ODEC. The Cooperative has a non-controlling ownership interest that has been accounted for under the cost method.

## Notes to Financial Statements

### A & N Electric Cooperative

#### December 31, 2018 and 2017

##### Note E - Concentrations of Credit Risk

The Cooperative places its cash on deposit with financial institutions located in the United States of America, which are insured by the Federal Deposit Insurance Corporation (FDIC). The FDIC provides insurance coverage for up to \$250,000 of cash held by the Cooperative in each separate FDIC insured bank and savings institution. From time to time, the Cooperative may have amounts on deposit in excess of the insured limits. As of December 31, 2018, the Cooperative had approximately \$3,500,000 of deposits that exceed the insured limits. The Cooperative also had ODEC power bill prepayments and CFC Select Notes of approximately \$4,800,000, which were not insured.

##### Note F - Accounts Receivable

Accounts receivable consisted of the following:

	December 31,	
	2018	As Adjusted 2017
Unbilled revenue	\$ 6,250,896	\$ 6,070,641
Consumer accounts receivable	5,924,464	4,862,963
Other accounts receivable	1,023,034	2,051,350
	13,198,394	12,984,954
Less provision for uncollectible accounts	720,592	267,671
	<u>\$ 12,477,802</u>	<u>\$ 12,717,283</u>

##### Note G - Deferred Charges

Deferred charges consisted of the following:

	December 31,	
	2018	2017
NRECA R&S prepayment	\$ 989,102	\$ 1,236,378
Other	266,237	137,734
Deferred power costs	52,167	
Deferred fuel costs	30,041	
	<u>\$ 1,337,547</u>	<u>\$ 1,374,112</u>



## Notes to Financial Statements

### A & N Electric Cooperative

#### December 31, 2018 and 2017

##### Note H - Patronage Capital

Patronage capital consisted of the following:

	December 31,	
	2018	As Adjusted 2017
Assigned	\$ 71,798,150	\$ 68,689,215
Assignable	9,744,594	9,179,576
	81,542,744	77,868,791
Retired	(25,921,327)	(23,680,330)
	<u>\$ 55,621,417</u>	<u>\$ 54,188,461</u>

Under provisions of the long-term debt agreement and Title 7 of the Code of Federal Regulations (Part 1717.617), the Cooperative may refund capital to patrons without limitation if total equity is equal to or greater than 30% of total assets and there are no instances of default. If equities are between 20% and 30% of total assets, general refunds are limited to 25% (adjusted for returns to estates, which are not limited) of patronage capital or margins received in the next preceding year. Total equities and margins amounted to approximately 40% and 38% of total assets for 2018 and 2017, respectively.

##### Note I - Other Equities

Other equities consisted of the following:

	December 31,	
	2018	2017
Interest	\$ 10,633,778	\$ 9,059,991
Donated capital	1,663,257	1,449,360
Other	399,307	377,804
	<u>\$ 12,696,342</u>	<u>\$ 10,887,155</u>

## Notes to Financial Statements

### A & N Electric Cooperative

#### December 31, 2018 and 2017

##### Note J - Long-Term Debt

Long-term debt consisted of the following:

	December 31,	
	2018	2017
FFB		
Mortgage notes, fixed	\$ 108,952,450	\$ 109,766,917
Advanced payments, unapplied	<u>(26,552,511)</u>	<u>(25,265,360)</u>
	82,399,939	84,501,557
CFC		
Mortgage notes, fixed	10,697,043	3,604,427
RUS		
Mortgage notes, fixed		<u>8,045,183</u>
	93,096,982	96,151,167
Less current maturities	<u>3,700,379</u>	<u>3,626,000</u>
	<u>\$ 89,396,603</u>	<u>\$ 92,525,167</u>

Long-term debt payable with FFB is represented by mortgage notes with rates ranging from 1.94% to 5.56%. The notes generally have 35-year maturity periods and are payable on an installment basis. Principal and interest payments are due quarterly in the amount of approximately \$1,615,000. The Cooperative had no unadvanced funds available from FFB as of December 31, 2018. The Cooperative has elected to participate in the RUS cushion of credit program, whereby a portion of principal and interest payments are prepaid to RUS and earn interest at a rate of 5.00%. For the year ended December 31, 2018 and 2017, the Cooperative had prepaid approximately \$27,000,000 and \$25,000,000, respectively, which has been reflected in the financial statements as a reduction of long-term debt to FFB.

The security and terms for the CFC notes, except for interest rates which range from 3.25% to 7.25%, are the same as the FFB notes. Principal and interest payments are due in monthly installments of approximately \$172,000 and quarterly installments of approximately \$226,000. The Cooperative had \$7,875,255 of unadvanced funds available from CFC as of December 31, 2018.

In 2018, the Cooperative refinanced outstanding RUS debt with CFC and all outstanding principal was curtailed in the refinance. Long-term debt payable to RUS was represented by mortgage notes with rates ranging from 4.00% to 5.13%. The notes generally had 35-year maturity periods and were payable on an installment basis. Principal and interest payments are due monthly in the amount of approximately \$51,000.

Under the terms of the loan agreements with RUS, CFC, and FFB there are certain restrictions, which include requirements to maintain a TIER (times interest earned ratio) of 1.25 and DSC (debt service coverage) of 1.25. There were also restrictions on the return of capital to patrons as discussed in Note H. As of December 31, 2018 and 2017, the Cooperative was in compliance with all covenants and restrictions.

## Notes to Financial Statements

### A & N Electric Cooperative

#### December 31, 2018 and 2017

##### Note J - Long-Term Debt - Continued

Annual maturities of long-term debt were as follows:

<u>Year Ending December 31,</u>	
2019	\$ 3,700,379
2020	3,735,321
2021	3,746,680
2022	3,876,613
2023	3,973,765
Thereafter	<u>74,064,224</u>
	<u>\$ 93,096,982</u>

The Cooperative has a line of credit with CFC in the amount of \$7,012,000, there were no advances outstanding at December 31, 2018 and 2017. The Cooperative has an unsecured line of credit with CoBank in the amount of \$7,000,000, there were no advances outstanding at December 31, 2018 and 2017.

The Cooperative had unused letters of credit from CFC in the amount of \$100,000 at December 31, 2018 and 2017.

##### Note K - Deferred Credits

Deferred credits consisted of the following:

	<u>December 31,</u>	
	<u>2018</u>	<u>2017</u>
Deferred sales tax surcharge	\$ 18,582	\$ 17,633
Consumer advances and other	3,750	3,750
Deferred fuel costs		<u>61,751</u>
	<u>\$ 22,332</u>	<u>\$ 83,134</u>

##### Note L - Contingencies

The Cooperative and Local 1307 of the International Brotherhood of Electrical Workers have a collective bargaining agreement, which covers approximately 54% of the Cooperative's employees and substantially all non-administrative hourly employees. The current agreement expires on December 31, 2021.

##### Note M - Cost of Power

The Cooperative, as a member of ODEC, an organization composed of electric cooperatives in Virginia, Maryland and Delaware, has entered into a long-term contract with ODEC for the acquisition of wholesale power through ODEC as have other members of the organization. The cost of wholesale power purchases through ODEC may increase or decrease based upon rates established by the Board of Directors of ODEC.

## **Notes to Financial Statements**

### **A & N Electric Cooperative**

#### **December 31, 2018 and 2017**

##### **Note N - Retirement Plans**

###### Pension Plan

The retirement Security Plan (RS Plan), sponsored by the National Rural Electric Cooperative Association (NRECA) is a defined benefit pension plan qualified under Section 401 and tax-exempt under Section 501(a) of the Internal Revenue Code. It is considered a multi-employer plan under the accounting standards.

The plan sponsor's Employer Identification Number is 53-0116145 and the Plan Number is 333.

A unique characteristic of a multi-employer plan compared with a single employer plan is that all plan assets are available to pay benefits of any plan participant. Separate asset accounts are not maintained for participating employers. This means that assets contributed by one employer may be used to provide benefits to employees of other participating employers.

The Cooperative's contributions to the RS Plan in 2018 and in 2017 represented less than 5% of the total contributions made to the RS Plan by all participating employers. The Cooperative made contributions to the RS Plan of approximately \$1,013,000 and \$996,000 in 2018 and 2017, respectively.

For the RS Plan, a "zone status" determination is not required, and therefore not determined, under the Pension Protection Act (PPA) of 2006. In addition, the accumulated benefit obligations and plan assets are not determined or allocated separately by individual employer. In total, the RS Plan was over 80% funded at January 1, 2018 and over 80% funded on January 1, 2017 based on the PPA funding target and PPA actuarial value of assets on those dates.

Because the provisions of the PPA do not apply to the RS Plan, funding improvement plans and surcharges are not applicable. Future contribution requirements are determined each year as part of the actuarial valuation of the plan and may change as a result of plan experience.

At its December 2012 meeting, the I&FS Committee of the NRECA Board of Directors approved an option to allow participating cooperatives in the RS Plan to make a contribution prepayment and reduce future required contributions. The prepayment amount is a cooperative's share, as of January 1, 2013, of future contributions required to fund the RS Plan's unfunded value of benefits earned to date using RS Plan actuarial valuation assumptions. The prepayment amount will typically equal approximately 2.5 times a cooperative's annual RS Plan required contribution as of January 1, 2013. After making the prepayment, the billing rate for most co-ops is reduced by approximately 25%, retroactive to the January 1 of the year in which the amount is paid to the RS Plan. The 25% differential in billing rates is expected to continue for approximately 15 years from January 1, 2013. However, unexpected changes in interest rates, asset returns and other plan experience, plan assumption changes and other factors may have an impact on the differential in billing rates and the 15-year period.

## **Notes to Financial Statements**

### **A & N Electric Cooperative**

#### **December 31, 2018 and 2017**

##### **Note N - Retirement Plans - Continued**

On April 23, 2013 the Cooperative made a prepayment of \$2,431,316 to the NRECA RS Plan, which is being amortized over a period of 10 years as part of deferred charges.

##### Deferred Income Plan

In addition to the NRECA RS Plan, substantially all employees of the Cooperative are eligible to participate in the NRECA SelectRE pension plan (the "Plan"), a defined contribution multi-employer deferred income plan qualified under Section 401(k) of the Internal Revenue Code. For the years ended December 31, 2018 and 2017, the Cooperative's required contribution to the Plan and its net pension cost was approximately \$173,000 and \$171,000, respectively.

##### **Note O - Financial Instruments Carried at Cost**

The Cooperative has recorded all financial instruments based on the carrying amount (book value) in the financial statements in accordance with *ASC Topic 825*. According to this guidance, the Cooperative is required to disclose the fair value of financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using discounted cash flow analysis. This technique involves subjective judgment and is significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. As a result, the derived fair value estimates cannot be substantiated by comparison to independent markets, and in many cases, could not be realized in immediate settlement of the instrument. Accordingly, the following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it was practicable to estimate that value.

##### Cash and Cash Equivalents

The carrying amount of cash and cash equivalents approximates fair value due to the short maturity of these instruments.

##### Accounts Receivable

The carrying amount of accounts receivable approximates fair value due to the short period of time amounts are outstanding.

## Notes to Financial Statements

### A & N Electric Cooperative

#### December 31, 2018 and 2017

##### Note O - Financial Instruments Carried at Cost - Continued

###### Investments in Associated Organizations

Fair value of capital term certificates was determined by computing the present value of estimated future cash flows, discounted at the long-term treasury rate of 2.98% and 2.74% for the years ending December 31, 2018 and 2017, respectively. The fair value of patronage capital is not determinable since no legal obligation exists to retire capital credits. The fair value of the cost method investment is not estimated since there are no identified events or changes in circumstances that may have a significant adverse effect on the fair value, and it is not practicable to estimate fair value. The carrying value of memberships approximates fair value.

###### Accounts Payable

The carrying amount of accounts payable approximates fair value due to the short period of time amounts are outstanding.

###### Long-Term Debt

The carrying amount of the Cooperative's fixed long-term debt includes certain interest rates that are below quoted market prices for the same or similar issues. Therefore, the fair value of fixed long-term debt is estimated based on current market prices for the same or similar issues offered for debt of the same and remaining maturities which was 5.90% and 5.50% for the years ending December 31, 2018 and 2017, respectively.

The carrying amount of lines of credit approximates fair value due to the short maturity of these instruments.

###### Consumer Deposits

The carrying amount of consumer deposits approximates fair value due to the short maturity of these instruments.

The estimated fair value of the Cooperative's financial instruments are as follows:

	December 31,			
	2018		2017	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets:				
Capital term certificates	\$ 447,409	\$ 673,000	\$ 454,497	\$ 722,000
Liabilities:				
RUS, CFC, and FFB notes payable including current portion	\$ 93,096,982	\$ 75,381,000	\$ 96,151,167	\$ 77,944,000

## **Notes to Financial Statements**

### **A & N Electric Cooperative**

#### **December 31, 2018 and 2017**

##### **Note P - Related Party Transactions**

The Cooperative was a member of the following organizations and conducted business transactions during the current and prior years as set forth below:

The Cooperative was a member of CFC, a national financing organization, and had investment assets and mortgage notes payable at various interest rates and maturities.

The Cooperative, as a member of ODEC, an organization composed of electric cooperatives, has entered into a contract for the acquisition of wholesale power. The cost of wholesale power to members is determined by the Board of Directors of ODEC. The Cooperative also maintains transmission assets owned by ODEC in the Cooperative's service territory.

The Cooperative was a member of the Virginia, Maryland and Delaware Association of Electric Cooperatives, an association organized to serve rural electrification in those three state areas by providing group efforts on a regional basis in public and member relations, government affairs, human resource development, technical services, and legal services.

The Cooperative was a member of National Rural Telecommunications Cooperative (NRTC), a telecommunications cooperative, and purchases various equipment from NRTC.

**Supplemental Matters Required by the  
Rural Utilities Service**





**Independent Auditor's Report on Internal Control Over Financial  
Reporting and on Compliance and Other Matters Based on  
an Audit of Financial Statements Performed  
in Accordance with Government Auditing Standards**

The Board of Directors  
A & N Electric Cooperative  
Tasley, Virginia

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of A & N Electric Cooperative (the "Cooperative"), which comprise the balance sheets as of December 31, 2018 and 2017, and the related statements of operations, equities and cash flows for the years then ended, and the related notes to the financial statements, and have issued our report thereon dated February 10, 2019.

**Internal Control Over Financial Reporting**

In planning and performing our audits of the financial statements, we considered the Cooperative's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control. Accordingly, we do not express an opinion on the effectiveness of the Cooperative's internal control.

*A deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audits we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Cooperative's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we reported to management of A & N Electric Cooperative in a separate letter dated February 10, 2019.

## **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Cooperative's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Governmental Auditing Standards* in considering the Cooperative's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in cursive script that reads "Adams, Jenkins & Cheatham".

Richmond, Virginia  
February 10, 2019



**Independent Auditor's Report on Compliance with  
Aspects of Contractual Agreements and Regulatory  
Requirements for Electric Borrowers**

The Board of Directors  
A & N Electric Cooperative  
Tasley, Virginia

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of A & N Electric Cooperative (the "Cooperative"), which comprise the balance sheet as of December 31, 2018, and the related statements of operations, equities, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated February 10, 2019. In accordance with *Government Auditing Standards*, we have also issued a report dated February 10, 2019 on our consideration of the Cooperative's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. No reports other than the reports referred to above have been furnished to management.

In connection with our audit, nothing came to our attention that caused us to believe that the Cooperative failed to comply with the terms, covenants, provisions, or conditions of their loan, grant, and security instruments as set forth in 7 CFR Part 1773, *Policy on Audits of Rural Utilities Service Borrowers*, §1773.33 and clarified in the RUS policy memorandum dated February 7, 2014, insofar as they relate to accounting matters as enumerated below. However, our audit was not directed primarily toward obtaining knowledge of noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Cooperative's noncompliance with the above-referenced terms, covenants, provisions, or conditions of the contractual agreements and regulatory requirements, insofar as they related to accounting matters. In connection with our audit, we noted no matters regarding the Cooperative's accounting and records to indicate that the Cooperative did not:

- Maintain adequate and effective accounting procedures;
- Utilize adequate and fair methods for accumulating and recording labor, material, and overhead costs, and the distribution of these costs to construction, retirement, and maintenance or other expense accounts;
- Reconcile continuing property records to the controlling general ledger plant accounts;
- Clear construction accounts and accrue depreciation on completed construction;
- Record and properly price the retirement of plant;

- Seek approval of the sale, lease or transfer of capital assets and disposition of proceeds for the sale or lease of plant, material, or scrap;
- Maintain adequate control over materials and supplies;
- Prepare accurate and timely Financial and Operating Reports;
- Obtain written RUS approval to enter into any contract for the management, operations, or maintenance of the borrower's system if the contract covers all or substantially all of the electric system;
- Disclose material related party transactions in the financial statements, in accordance with requirements for related parties in generally accepted accounting principles;
- Record depreciation in accordance with RUS requirements (See RUS Bulletin 183-1, Depreciation Rates and Procedures);
- Comply with the requirements for the detailed schedule of deferred debits and deferred credits; and
- Comply with the requirements for the detailed schedule of investments.

This report is intended solely for the information and use of the board of directors, management, and the RUS and supplemental lenders and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

*Alama, Jenkins & Cheatham*

Richmond, Virginia  
February 10, 2019