

Shenandoah Valley Electric Cooperative

Financial Statements

December 31, 2019 and 2018



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SHENANDOAH VALLEY ELECTRIC COOPERATIVE

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REPORT OF INDEPENDENT ACCOUNTANTS

The Board of Directors of
Shenandoah Valley Electric Cooperative
Rockingham, Virginia

Report on the Financial Statements

We have audited the accompanying financial statements of Shenandoah Valley Electric Cooperative (the "Cooperative"), which comprise the balance sheets as of December 31, 2019 and 2018, 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; 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 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 audits 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 Shenandoah Valley Electric Cooperative as of December 31, 2019 and 2018, 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.

Emphasis of a Matter

As discussed in Note 1 to the financial statements, in 2019, Shenandoah Valley Electric Cooperative adopted Accounting Standards Codification (ASC) Topic 606, *Revenue from Contracts with Customers*. 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 March 27, 2020, on our consideration of the Cooperative's internal control over financial reporting and on 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 the 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

A handwritten signature in black ink, appearing to read "Keiter", with a long, sweeping horizontal stroke extending to the right.

March 27, 2020
Glen Allen, Virginia

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Balance Sheets December 31, 2019 and 2018

<u>Assets</u>	<u>2019</u>	<u>2018</u>
Electric plant:		
Electric plant	\$ 593,352,814	\$ 570,793,720
Less accumulated provision for depreciation	<u>(197,778,508)</u>	<u>(185,949,561)</u>
Net electric plant	<u>395,574,306</u>	<u>384,844,159</u>
Other property and investments:		
Investments in associated organizations	59,493,495	56,819,075
Other investments	<u>389,187</u>	<u>331,323</u>
Total other property and investments	<u>59,882,682</u>	<u>57,150,398</u>
Current assets:		
Cash and cash equivalents	1,706,088	1,152,001
Short-term investments	23,367,576	16,230,385
Accounts receivable, net	16,781,612	17,630,047
Accrued unbilled revenue	12,062,059	11,788,272
Materials and supplies	7,120,033	7,896,059
Other current assets	<u>602,309</u>	<u>229,157</u>
Total current assets	61,639,677	54,925,921
Deferred charges	<u>4,515,340</u>	<u>3,270,777</u>
Total assets	<u>\$ 521,612,005</u>	<u>\$ 500,191,255</u>

See accompanying notes to financial statements.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Balance Sheets, Continued
December 31, 2019 and 2018

<u>Liabilities and Equities</u>	<u>2019</u>	<u>2018</u>
Equities:		
Patronage capital	\$ 162,287,410	\$ 156,963,820
Other equities	24,480,050	22,278,494
Memberships	<u>395,980</u>	<u>392,645</u>
 Total equities	 <u>187,163,440</u>	 <u>179,634,959</u>
Current liabilities:		
Accounts payable	18,593,362	18,793,068
Current maturities of long-term debt	8,937,882	8,789,744
Consumer deposits	6,064,526	7,162,129
Other current and accrued liabilities	1,941,693	1,552,367
Lines of credit	<u>15,500,000</u>	<u>8,000,000</u>
 Total current liabilities	 51,037,463	 44,297,308
Long-term debt, net of current maturities	278,261,904	272,414,847
Deferred credits	<u>5,149,198</u>	<u>3,844,141</u>
 Total liabilities and equities	 <u>\$ 521,612,005</u>	 <u>\$ 500,191,255</u>

See accompanying notes to financial statements.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Statements of Operations Years Ended December 31, 2019 and 2018

	2019	2018
Operating revenues	\$ 257,230,242	\$ 247,033,126
Operating expenses:		
Cost of power	180,537,126	169,482,360
Transmission	85,992	77,378
Distribution - operation	9,306,849	8,262,146
Distribution - maintenance	14,971,197	13,802,994
Consumer accounts	6,941,316	5,207,703
Customer service and information	1,470,634	1,343,303
Sales expense	201,756	280,109
Administrative and general	8,075,375	8,497,432
Depreciation and amortization	19,033,528	18,721,632
Taxes	351,805	391,886
Interest on long-term debt	10,332,308	10,159,175
Other	451,471	270,663
Total operating expenses	251,759,357	236,496,781
Operating margins before patronage allocations	5,470,885	10,536,345
Patronage allocations:		
Generation and transmission	3,072,278	2,355,038
Other	189,727	218,286
Total patronage allocations	3,262,005	2,573,324
Net operating margins	8,732,890	13,109,669
Nonoperating income (expense):		
(Loss) gain on sale of assets	(7,421)	115,900
Investment income, net	2,030,103	2,419,387
Other	6,184	210
Total nonoperating income	2,028,866	2,535,497
Net margins	\$ 10,761,756	\$ 15,645,166

See accompanying notes to financial statements.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Statements of Equities Years Ended December 31, 2019 and 2018

	Patronage Capital	Other Equities	Memberships	Total
Balance, January 1, 2018	\$ 150,530,219	\$ 18,315,443	\$ 387,465	\$ 169,233,127
Net margins	13,109,669	2,535,497	-	15,645,166
Assignment of 2017 capital credits	(1,173,415)	1,173,415	-	-
Retirement of capital credits	(5,502,653)	-	-	(5,502,653)
Net change in donated capital	-	254,139	-	254,139
Net change in memberships	-	-	5,180	5,180
Balance, December 31, 2018	156,963,820	22,278,494	392,645	179,634,959
Net margins	8,732,890	2,028,866	-	10,761,756
Retirement of capital credits	(3,409,300)	-	-	(3,409,300)
Net change in donated capital	-	172,690	-	172,690
Net change in memberships	-	-	3,335	3,335
Balance, December 31, 2019	<u>\$ 162,287,410</u>	<u>\$ 24,480,050</u>	<u>\$ 395,980</u>	<u>\$ 187,163,440</u>

See accompanying notes to financial statements.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Statements of Cash Flows Years Ended December 31, 2019 and 2018

	2019	2018
Cash flows from operating activities:		
Cash received from members	\$ 255,694,588	\$ 248,253,682
Cash paid to suppliers and employees	(222,081,148)	(212,741,271)
Interest received	637,362	396,966
Interest paid	(1,856,258)	(2,064,007)
Net cash provided by operating activities	32,394,544	33,845,370
Cash flows from investing activities:		
Extension and replacement of plant	(28,652,435)	(38,618,677)
Plant removal costs	(3,161,438)	(2,968,647)
Proceeds from the sale of plant	149,290	115,900
Contribution in aid of construction	2,228,387	1,633,269
Proceeds from retirement of investments in CTC's	2,144	2,104
Purchase of short-term investments	(7,137,191)	(16,230,385)
Net cash used in investing activities	(36,571,243)	(56,066,436)
Cash flows from financing activities:		
Proceeds from long-term debt	-	23,776,000
Advance payments to RUS cushion of credit	-	(500,000)
Principal payments on long-term debt	(1,517,340)	(6,661,958)
Proceeds from lines of credit	205,000,000	89,500,000
Payments on lines of credit	(197,500,000)	(84,800,000)
Capital credits paid to members, net	(743,047)	(1,477,413)
Proceeds from capital credits and other investments	585,441	143,456
Net change in consumer deposits	(1,097,603)	56,522
Net change in memberships	3,335	5,180
Net cash provided by financing activities	4,730,786	20,041,787
Net change in cash and cash equivalents	554,087	(2,179,279)
Cash and cash equivalents, beginning of year	1,152,001	3,331,280
Cash and cash equivalents, end of year	\$ 1,706,088	\$ 1,152,001

See accompanying notes to financial statements.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Statements of Cash Flows, Continued Years Ended December 31, 2019 and 2018

	2019	2018
Cash from operating activities:		
Net margins	\$ 10,761,756	\$ 15,645,166
Adjustments to reconcile net margins to net cash provided by operating activities:		
Depreciation and amortization	19,033,528	18,721,632
Increase in cash value of life insurance	(14,680)	(15,180)
Noncash capital credits received	(3,247,325)	(2,558,144)
Capital credits applied to member accounts	(2,110,302)	(3,232,429)
Interest expense applied from cushion of credit	8,911,461	10,409,345
Interest income earned from cushion of credit	(1,398,925)	(2,022,631)
Loss (gain) on sale of assets	7,421	(115,900)
Changes in:		
Accounts receivable, net	574,648	4,452,985
Other current assets	(373,152)	(15,764)
Deferred charges	(1,244,563)	726,756
Accounts payable	(199,706)	(1,971,700)
Other current and accrued liabilities	389,326	(1,867,097)
Deferred credits	1,305,057	(4,311,669)
Net cash provided by operating activities	\$ 32,394,544	\$ 33,845,370

See accompanying notes to financial statements.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements

1. Summary of Significant Accounting Policies:

Nature of Cooperative: Shenandoah Valley Electric Cooperative (the “Cooperative”) is a member-owned, not-for-profit company organized to provide electric service to its members essentially residing in the counties of Rockingham, Augusta, Shenandoah, Clarke, Frederick, Highland, Page, Warren, and the City of Winchester in the Commonwealth of Virginia.

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).

Adoption of a New Accounting Standard: In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, “Revenue from Contracts with Customers (Topic 606)”. The ASU and subsequently issued clarifying ASUs established Accounting Standards Codification (ASC) Topic 606 replaced most existing revenue recognition guidance in GAAP. ASC Topic 606 requires expanded disclosures relating to the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The Cooperative adopted the new standard effective January 1, 2019, the first day of the Cooperative’s fiscal year, using the modified retrospective approach. The adoption of this ASU did not have a significant impact on the Cooperative’s financial statements and no changes were required to previously reported revenues as a result of the adoption.

Cash and Cash Equivalents: The Cooperative considers all highly liquid investments with a maturity of three months or less to be cash equivalents. The Cooperative maintains the majority of its cash in one financial institution with balances that regularly exceed federally insured limits.

Short-Term Investments: Short-term investments consist of select notes with National Rural Cooperatives Finance Corporation (CFC) that mature within twelve months of December 31, 2019.

Regulatory Assets and Liabilities: The Cooperative complies with the accounting guidance set forth by the ASC Topic 980 regarding the effect of certain types of regulation. This guidance allows a regulated Cooperative to record certain costs and 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.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

1. Summary of Significant Accounting Policies, Continued:

Use of Estimates: The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods reported. 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. Acquired plant was recorded based on information received pursuant to purchase contracts as approved by the SCC. 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 repairs of transportation and service equipment are charged to clearing accounts and redistributed to operating expenses and other accounts.

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 existing plant over the service lives, were as follows for the years ended December 31, 2019 and 2018:

Transmission plant	2.75%
Distribution plant	2.53 - 9.06%
General plant	3.00 - 25.00%
Office furniture and equipment	7.00 - 25.00%

Materials and Supplies: Materials and supplies inventories are generally used for construction, operation and maintenance work, and are not for resale. They are valued at the lower of moving average unit cost or market.

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.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

1. Summary of Significant Accounting Policies, Continued:

Advertising Costs: Advertising costs are expensed as incurred. Advertising expense was approximately \$202,000 for 2019 and \$280,000 for 2018.

Revenue Recognition: The Cooperative sells electricity to residential and commercial members. The Cooperative recognizes revenue over time as energy is delivered to members on a monthly basis. Payment terms generally require that members pay for services within the month following delivery of electricity. The billing rate schedules of the Cooperative contain provisions to either increase or decrease the members' billing from the base level billing schedule dependent on the cost of the wholesale power adjustment passed on from the vendor for electrical energy purchased for resale.

The Cooperative is responsible for certain excise taxes levied by state and local governments. These taxes are collected from members and remitted to the appropriate government. The Cooperative does not recognize these taxes as a component of revenue; upon collection, they are accrued as liabilities until remittance.

Cost of Power: The Cooperative utilizes a deferred method of accounting for power costs. Under this method, any amounts collected over or below the Cooperative's monthly power costs are recorded as a deferred charge or credit as applicable on the balance sheets.

Income Taxes: The Cooperative has been granted exemption from federal income taxation under Internal Revenue Service Code Section 501(c)(12). 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 treatment as a tax-exempt utility will be sustained and does not anticipate any adjustment that will result in a material change to its financial position. The Cooperative is not currently under audit by any tax jurisdiction.

Reclassifications: Certain prior year balances have been reclassified to conform with current year presentation

Subsequent Events: Subsequent to December 31, 2019, an outbreak of a novel strain of coronavirus (COVID-19) was declared a pandemic by World Health Organization. The situation is evolving with many cities and countries around the world responding in different ways to address the outbreak. There are direct and indirect economic effects developing for all industries and individual organizations throughout the world. As of the date of issuance, the Cooperative has not had any material delays in services or indications of material impact. Management will continue to monitor the impact of the outbreak and recovery on the Cooperative and reflect the consequences as appropriate in the Cooperative's accounting and financial reporting.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

1. Summary of Significant Accounting Policies, Continued:

Subsequent Events, Continued: Management has evaluated subsequent events through March 27, 2020, the date the financial statements were available for issuance and has determined that, other than noted above, the note payable agreements and the pension freeze disclosed in Notes 11 and 14, respectively, there are no other subsequent events to be reported in the accompanying financial statements.

2. Assets Pledged:

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

3. Electric Plant:

Electric plant consisted of the following at December 31:

	<u>2019</u>	<u>2018</u>
Distribution plant	\$ 457,389,888	\$ 444,805,386
Acquisition adjustments	43,229,911	43,229,911
General plant	65,970,282	66,100,144
Transmission plant	<u>5,445,767</u>	<u>5,445,767</u>
Electric plant in service	572,035,848	559,581,208
Construction work in progress	<u>21,316,966</u>	<u>11,212,512</u>
Total electric plant	<u>\$ 593,352,814</u>	<u>\$ 570,793,720</u>

In accordance with GAAP and FERC as adopted by the RUS, the Cooperative has determined that it had no legal asset retirement obligations for the years ended December 31, 2019 and 2018. Regarding non-legal retirement costs, 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.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

4. 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. Investments in associated organizations consisted of the following at December 31:

	2019	2018
Patronage capital:		
ODEC (Old Dominion Electric Cooperative)	\$ 54,301,742	\$ 51,634,515
CFC	2,083,914	2,053,469
CoBank	112,711	129,767
Other	408,724	412,776
	56,907,091	54,230,527
Capital Term Certificates (CTC):		
Subscriptions (SCTC's)	1,213,509	1,213,509
Loan (LCTC's)	300,950	300,950
Loan (ZCTC's)	563,239	565,383
	2,077,698	2,079,842
Other:		
TEC Trading, Inc.	470,365	470,365
Investment in building - Virginia, Maryland, Delaware Association of Electric Cooperatives	36,320	36,320
Membership fees	2,021	2,021
	508,706	508,706
 Total investment in associated organizations	 \$ 59,493,495	 \$ 56,819,075

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.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

5. 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, 2019, the Cooperative had \$1,206,088 of deposits that exceed the insured limits.

At December 31, 2019, the Cooperative had invested in CFC Select Notes totaling \$23,367,474 which were not insured. These Select Notes are senior unsecured debt securities and mature at various dates during 2020. The Select Notes are classified as short-term investments on the balance sheets.

Concentrations of credit risk with respect to member accounts receivable generally are limited due to the large number of members comprising the member base. The Cooperative services ten members that represented approximately 15% of total operating revenues for the years ended December 31, 2019 and 2018. Generally, the rate structure of the Cooperative is designed in such a manner that all classes of members contribute equitably to net margins.

6. Accounts Receivable:

Accounts receivable consisted of the following at December 31:

	<u>2019</u>	<u>2018</u>
Member accounts receivable	\$ 15,390,155	\$ 15,271,356
Other accounts receivable	<u>2,424,428</u>	<u>3,237,931</u>
	17,814,583	18,509,287
Less provision for uncollectible accounts	<u>(1,032,971)</u>	<u>(879,240)</u>
Total accounts receivable, net	<u>\$ 16,781,612</u>	<u>\$ 17,630,047</u>

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

7. Other Current Assets:

Other current assets consisted of the following at December 31:

	2019	2018
Prepayments	\$ 585,509	\$ 211,757
Interest receivable	16,800	17,400
Total other current assets	\$ 602,309	\$ 229,157

8. Deferred Charges:

Deferred charges consisted of the following at December 31:

	2019	2018
NRECA prepayment (Note 14)	\$ 2,345,746	\$ 3,127,661
Radio tower purchase	1,325,964	142,189
Storm restoration costs	840,775	-
Other	2,855	927
Total deferred charges	\$ 4,515,340	\$ 3,270,777

9. Patronage Capital:

Patronage capital consisted of the following at December 31:

	2019	2018
Assigned	\$ 232,898,509	\$ 219,788,840
Assignable	8,732,890	13,109,669
	241,631,399	232,898,509
Retired	(79,343,989)	(75,934,689)
Total patronage capital	\$ 162,287,410	\$ 156,963,820

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

9. Patronage Capital, Continued:

Under provisions of the long-term debt agreements 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 preceding year. Total equities and margins amounted to 36% of total assets for 2019 and 2018.

10. Other Equities:

Other equities consisted of the following at December 31:

	2019	2018
Permanent equity	\$ 21,458,749	\$ 19,429,883
Donated capital	3,021,301	2,848,611
 Total other equities	 \$ 24,480,050	 \$ 22,278,494

11. Long-Term Debt:

Long-term debt consisted of the following at December 31:

	2019	2018
FFB		
Mortgage notes, fixed	\$ 257,780,300	\$ 264,662,012
Advanced payments, unapplied	(17,491,795)	(31,852,095)
	240,288,505	232,809,917
 CFC		
Mortgage notes, fixed	32,957,265	34,474,606
 RUS		
Mortgage notes, fixed	14,969,798	15,824,555
Advanced payments, unapplied	(1,015,782)	(1,904,487)
	13,954,016	13,920,068
 Total long term debt	 \$ 287,199,786	 \$ 281,204,591

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

11. Long-Term Debt, Continued:

Long-term debt is presented on the accompanying balance sheets as follows at December 31:

	2019	2018
Total long term debt	\$ 287,199,786	\$ 281,204,591
Less current maturities	(8,937,882)	(8,789,744)
Total long term debt, net of current maturities	\$ 278,261,904	\$ 272,414,847

Long-term debt payable to RUS is represented by mortgage notes with rates ranging from 1.63% to 2.00%. The notes have 35-year maturity periods and mature from 2029 through 2037. The notes are subject to periodic repricing by RUS and are payable on an installment basis. Principal and interest payments are due monthly in the amount of \$92,493. During 2019 and 2018, the Cooperative elected to participate in the RUS cushion of credit program, whereby a portion of principal and interest payments are prepaid to RUS and FFB and earn interest at a rate of 5.00%.

For the years ended December 31, 2019 and 2018, the Cooperative had prepaid \$18,507,577 and \$33,756,582, respectively, which has been reflected in the financial statements as a reduction of long-term debt payable to RUS and FFB.

Long-term debt payable to FFB is represented by mortgage notes with rates ranging from 1.71% to 3.88%. The notes mature from 2044 to 2048. Principal and interest installments are due quarterly in the amount of approximately \$3,577,000. At December 31, 2019, the Cooperative had no unadvanced funds available from FFB. At December 31, 2018, the Cooperative had unadvanced funds available from FFB of \$251,000.

Long-term debt payable to CFC is represented by mortgage notes with rates ranging from 3.75% to 4.25%. The notes mature from 2027 to 2046. Principal and interest installments are due quarterly in the amount of approximately \$595,000. In 2018, the Cooperative converted and paid off outstanding serial mortgage notes earlier than their scheduled maturity in the amount of \$5,500,000.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

11. Long-Term Debt, Continued:

The scheduled maturities consisted of the following at December 31, 2019:

<u>Year</u>	<u>Amount</u>
2020	\$ 8,937,882
2021	9,223,634
2022	9,519,205
2023	9,824,953
2024	10,141,245
Thereafter	<u>239,552,867</u>
	<u>\$ 287,199,786</u>

In addition to the mortgage notes, the Cooperative has established unsecured lines of credit in the amounts of \$20,000,000 with CFC and \$15,000,000 with Pinnacle Bank ("Pinnacle") at variable interest rates. At December 31, 2018, the Cooperative had an unsecured line of credit in the amount of \$5,000,000 with Wells Fargo. This line of credit matured and was not renewed in 2019. For the years ended December 31, 2019 and 2018, the Cooperative had outstanding borrowings of \$11,500,000 and \$8,000,000, respectively, on the CFC line of credit with an interest rate of 3.25% at December 31, 2019, and 3.75% at December 31, 2018. At December 31, 2019, the Cooperative had \$4,000,000 in outstanding balances against the Pinnacle line of credit with an interest rate of 2.78%. At December 31, 2018, there were no outstanding balances against the Wells Fargo line of credit with an interest rate of 3.50%.

In January 2020, the Cooperative entered into a term note for \$5,000,000 with Pinnacle. The note will bear interest at 3.38% and matures on December 31, 2024. Principal payments are due in monthly installments of \$83,333 with remaining unpaid principal and accrued interest payable in full upon maturity. As the financing was received subsequent to December 31, 2019, the related note payable is not included in the accompanying 2019 financial statements.

In January 2020, the Cooperative agreed in principle to enter into an uncommitted master note facility with New York Life for draws totaling up to \$50,000,000. As the financing was received subsequent to December 31, 2019, the related notes payable are not included in the accompanying 2019 financial statements.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

11. Long-Term Debt, Continued:

Under the terms of the loan agreements with RUS, FFB and CFC, there are certain restrictions, which include requirements to maintain average coverage ratios in the two best years out of the three most recent calendar years of OTIER (operating times interest earned ratio) of 1.1, ODSC (operating debt service coverage) of 1.1, TIER (times interest earned ratio) of 1.25 and DSC (debt service coverage) of 1.25. As of December 31, 2019 and 2018, the Cooperative was in compliance with these requirements. There were also no restrictions on the return of capital to patrons as discussed in Note 9.

12. Other Current and Accrued Liabilities:

Other current and accrued liabilities consisted of the following at December 31:

	2019	2018
Accrued interest	\$ 17,434	\$ 1,374
Accrued taxes and amounts withheld from employees	642,571	635,468
Accrued vacation	667,826	444,734
Accrued salaries and wages	504,068	371,181
Deferred compensation	109,794	99,610
Total other current and accrued liabilities	\$ 1,941,693	\$ 1,552,367

13. Deferred Credits:

Deferred credits consisted of the following at December 31:

	2019	2018
Wholesale power cost adjustment	\$ 4,804,828	\$ 3,348,970
Consumer advances	86,314	233,790
Advance pole rentals	251,204	253,821
Other	6,852	7,560
Total deferred credits	\$ 5,149,198	\$ 3,844,141

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

14. Retirement Plans:

Defined Benefit Retirement Security 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 2019 and in 2018 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 \$3,161,000 in 2019 and \$2,941,000 in 2018. There have been no significant changes that affect the comparability of 2019 and 2018 contributions.

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, 2019, and January 1, 2018, 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 contributions requirements are determined each year as part of the actuarial valuation of the plan and may change as a result of plan experience.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

14. Retirement Plans, Continued:

Defined Benefit Retirement Security Plan, Continued: 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 cooperatives is reduced by approximately 25%, retroactive to 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.

In March 2013, the Cooperative made a prepayment of \$7,819,154 to the NRECA RS Plan. The Cooperative elected to finance the prepayment as part of a note bearing a fixed interest rate of 3.21%. Interest expense associated with the prepayment loan is being accounted for in accordance with RUS. The Cooperative is amortizing the prepayment over 10 years.

Deferred Income Plan – 401(k): In addition to the NRECA Retirement and Security Program, substantially all employees of the Cooperative are eligible to participate in the NRECA SelectRE pension plan, a defined contribution multi-employer deferred income plan qualified under Section 401(k) of the Internal Revenue Code. The Cooperative's required contribution to the Plan and its net pension cost was approximately \$561,000 in 2019 and \$551,000 in 2018.

Effective January 1, 2020, the Cooperative transitioned from the RS Plan and the NRECA SelectRE pension plan to an enhanced 401(k) plan. The intent is to provide a sustainable retirement plan that allows the Cooperative to remain competitive for talent in the electric utility industry, while balancing the need for predictable costs associated with the plan. The RS Plan benefits have been frozen and employees will no longer accrue additional benefits under the plan. The new 401(k) plan provides for safe-harbor and non-elective Cooperative contributions based on a tiered schedule, with tiers varying based on age and years of service.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

15. 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. Accordingly, the following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate that value:

Cash and Cash Equivalents: The carrying amount of cash and cash equivalents approximates fair value.

Short-Term Investments: The carrying amount of short-term investments approximates fair value due to the short maturity of the instruments.

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

Investments in Associated Organizations: Fair value of capital term certificates and member capital certificates was determined by computing the present value of estimated future cash flows, discounted at the long-term treasury rate of 2.39% for 2019 and 3.02% for 2018. 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 long-term debt includes certain interest rates that are below quoted market prices for the same or similar issues. Therefore, the fair value of 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 4.19% for 2019 and 5.90% for 2018.

Consumer Deposits: The carrying amount approximates fair value due to the relatively short maturity of the deposits.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

15. Financial Instruments Carried at Cost, Continued:

The estimated fair values of the Cooperative's financial instruments consisted of the following at December 31:

	2019		2018	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets:				
Investments in associated organizations:				
Capital term certificates	\$ 2,077,698	\$ 3,080,000	\$ 2,079,842	\$ 2,770,000
Liabilities:				
RUS, CFC, and FFB long-term debt including current portion				
	\$ 287,199,786	\$ 266,434,522	\$ 281,204,591	\$ 209,102,000

16. Related Party Transactions:

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

The Cooperative is a member of CFC and CoBank, national financing organizations, and had investment assets and long-term debt 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 rates for wholesale power sales to members are determined by the Board of Directors of ODEC.

The Cooperative is 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.

17. Commitments:

Purchased 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.

SHENANDOAH VALLEY ELECTRIC COOPERATIVE

Notes to Financial Statements, Continued

17. Commitments, Continued:

Purchased Power, Continued: The Cooperative has entered into a long-term contract with Morgan Stanley Capital Group (“Morgan Stanley”) for a 25 megawatt block of power through April 2024. The cost of power purchases through Morgan Stanley is fixed through the duration of the contract.

Construction Contracts: At December 31, 2019, the Cooperative had approximately \$1,084,600 due associated with various contracted construction projects that were not yet completed. At December 31, 2018, the Cooperative had approximately \$4,600,000 due associated with various contracted construction projects that were not yet completed.

18. Other:

During 2018, the Cooperative completed construction on its new headquarters campus in Rockingham County. The Cooperative had entered into a short-term lease agreement with the purchaser of the old headquarters building to lease at \$22,700 per month while the new headquarters campus was under construction. During 2017, the Cooperative sold its Dayton building and entered into a short-term lease agreement with the purchaser to lease the building at \$20,000 per month while the new headquarters campus was under construction. The Cooperative ceased both short-term lease agreements in July 2018. Rent expense was \$239,480 in 2018.

**SUPPLEMENTAL MATTERS REQUIRED BY THE
RURAL UTILITIES SERVICE**

REPORT OF INDEPENDENT ACCOUNTANTS 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 of
Shenandoah Valley Electric Cooperative
Rockingham, 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 Shenandoah Valley Electric Cooperative (the “Cooperative”), which comprise the balance sheet as of December 31, 2019, 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 March 27, 2020.

Internal Control Over Financial Reporting

In planning and performing our audit 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 audit 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 audit, 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 Shenandoah Valley Electric Cooperative in a separate letter dated March 27, 2020.

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 *Government 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 black ink, appearing to read "Keita", with a long, sweeping horizontal stroke extending to the right.

March 27, 2020
Glen Allen, Virginia

REPORT OF INDEPENDENT ACCOUNTANTS ON COMPLIANCE WITH ASPECTS OF CONTRACTUAL AGREEMENTS AND REGULATORY REQUIREMENTS FOR ELECTRIC BORROWERS

The Board of Directors of
Shenandoah Valley Electric Cooperative
Rockingham, 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 Shenandoah Valley Electric Cooperative (the "Cooperative"), which comprise the balance sheet as of December 31, 2019, 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 March 27, 2020. In accordance with *Government Auditing Standards*, we have also issued a report dated March 27, 2020 on our consideration of the Cooperative's 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.

A handwritten signature in black ink, appearing to read "Keita", with a stylized flourish at the end.

March 27, 2020
Glen Allen, Virginia