

# **Associated Electric Cooperative Inc.**

A Touchstone Energy<sup>®</sup> Cooperative 

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## **Financial Statements**

**For the Quarterly Periods Ended**

**June 30, 2020 and 2019**

## **MANAGEMENT'S DISCUSSION AND ANALYSIS**

Associated Electric Cooperative, Inc. (Associated) is pleased to present the enclosed interim financial statements, which include balance sheets, statements of revenues and expenses, and statements of cash flows as of, or for the periods ended June 30, 2020 and 2019. The discussion below is not meant to be comprehensive but rather to identify significant aspects in the current quarter and year-to-date performance of Associated.

### **Overview**

Net margin for the three and six-month period ended June 30, 2020, was \$21.2 and \$67.5 million, respectively, compared to \$30.3 and \$69.3 million in the same periods of 2019. Total assets were \$3.2 billion at June 30, 2020, and \$3.1 billion at June 30, 2019. Significant factors contributing to Associated's financial performance for these periods are discussed in the paragraphs below.

On March 11, 2020, the Novel Coronavirus Disease, COVID-19, was declared a pandemic by the World Health Organization. On March 13, 2020, a national emergency was declared in the United States concerning the COVID-19 outbreak. The spread of COVID-19 has brought unique challenges to Associated and cooperatives across the country. To date, the COVID-19 pandemic has not significantly impacted Associated's business operations or financial performance. However, the extent of the impact of the COVID-19 pandemic will depend on future developments which are uncertain at this time and cannot be predicted.

Associated has taken measures to implement health and safety policies for employees, members and contractors in response to these challenges. In addition, Associated remained focused on the mission to provide an economical and reliable power supply and support services to members. Associated followed or exceeded the Center for Disease Control guidelines specific for critical infrastructure organizations to ensure safe continuity of operations.

During the first six months of 2020, Associated incurred \$1.9 million in expenses related to pandemic preparedness. In accordance with the Stafford Act, eligible emergency protective measures taken to respond to the COVID-19 emergency at the direction or guidance of public health officials may be reimbursed by the Federal Emergency Management Agency (FEMA) Public Assistance program. While it is anticipated that a portion of pandemic-related expenses may be reimbursed by the FEMA, no receivable has been recorded as of June 30, 2020. Associated has worked diligently in documenting expenses that are eligible for recovery and will continue to monitor these expenses going forward.

### **Operating Revenues**

Revenue from members decreased \$2.9 million and \$24.3 million, or 1.3% and 5.0%, respectively, for the second quarter and the six-month period ended June 30, 2020, as compared to the same periods of 2019. Member revenue consists of an energy and a demand

component. Energy sales volume increased 3.6% for the second quarter of 2020 as compared to 2019 but decreased 3.4% for the first six months of 2020 as compared to 2019. Additionally, there is a \$0.50/MWh energy discount in place for 2020 that reduced member revenue by \$2.0 million and \$4.6 million, respectively, for the three and six-month periods of 2020 as compared to 2019. Demand revenue decreased \$5.0 and \$10.2 million, respectively, due to a decrease in billing demand determinants, as compared to the same periods of 2019. Associated's board approved a demand rate discount of \$1.12/kW for both 2019 and 2020.

Revenue from nonmembers decreased \$37.1 million and \$38.0 million, or 39.4% and 22.6%, respectively, for the second quarter and the six-month period ended June 30, 2020, as compared to the same periods of 2019. The decrease for both periods was primarily due to a \$35.9 and \$37.0 million decrease in nonmember energy sales. Interchange sales volume decreased 29.1% and 5.5%, respectively. Additionally, the weighted average sales price decreased 19.6% and 20.6%, respectively, due in large part to the impact of decreased natural gas prices for the three and six-month periods ended June 30, 2020, as compared to the same periods of 2019.

### **Generation Operation**

Generation operations expense decreased \$31.3 million and \$59.6 million, or 22.6% and 19.9%, respectively, for the three and six-month periods ended June 30, 2020, as compared to the same periods of 2019. This decrease was primarily due to lower coal and gas fuel expense.

Coal fuel expense decreased \$24.4 million and \$39.6 million, or 34.4% and 26.3%, respectively, and coal generation decreased 1,184,681 MWh and 1,758,723 MWh, or 34.0% and 23.5%, respectively for the three and six-month periods. Additionally, the weighted average cost of coal burned was 2.8% lower for the first six months of 2020 as compared to the same period of 2019.

Gas generation increased 73,943 MWh and 570,800 MWh, or 2.8% and 10.5%, respectively, for the three and six-month periods, primarily at the Chouteau power plant due to low natural gas prices in the Oklahoma market and the Dell power plant due to additional sales into the MISO market over 2019. The increased gas generation was more than offset by lower natural gas prices, which resulted in a 26.8% decrease in the average fuel costs/MWh for the gas fleet for the six-month period, and a decrease in gas fuel expense of \$7.1 million and \$20.2 million, or 15.9% and 19.2%, respectively, for the three and six-month periods, as compared to the same periods of 2019.

## Generation Maintenance

Generation maintenance expense decreased \$1.7 million and \$5.6 million, or 6.8% and 11.9%, respectively, for the three and six-month periods ended June 30, 2020, as compared to the same periods of 2019. The decrease for both periods was primarily due to the elimination of the deferred maintenance program at the end of 2019. The first and second quarters of 2019 included amortization of deferred maintenance projects, but Associated's board approved the recovery of previously deferred maintenance costs at the end of 2019. Partially offsetting this decrease was an increase in variable fees for the gas plants due to increased generation for the three and six-month periods ending June 30, 2020 as compared to the same periods of 2019.

## Financial Position:

Significant changes in the balance sheet at June 30, 2020, as compared to the prior year include the following:

- Utility plant, including construction work in progress, increased \$128.4 million, or 3.0%, primarily due to boiler component, generator and environmental projects at the New Madrid power plant and various ongoing projects at the Thomas Hill and Dell power plants. Accumulated depreciation increased \$98.2 million, resulting in an increase in utility plant, net of accumulated depreciation, of \$30.2 million, or 1.5%.
- Other restricted assets and designated assets and restricted short-term investments decreased \$212.4 million, or 42.8%, primarily due to the prepayment of Federal Financing Bank (FFB) debt out of the cushion of credit in the amount of \$227.4 million.
- Cash and cash equivalents increased \$342.7 million, or 558.8%, primarily due to funds provided by financing activities, partially offset by expenditures for plant additions.
- Accounts receivable decreased \$62.2 million, or 36.6%, primarily due to lower member sales resulting from lower sales volume, a \$0.50/MWh energy discount and lower nonmember energy sales.
- Fuel inventories increased \$19.2 million, or 48.4%, primarily due to a 99.2% increase in tons of coal on the ground as compared to June 30, 2019.
- Deferred regulatory debits, including the current portion, decreased by \$19.0 million, or 20.5%, primarily due to the elimination of \$39.8 million in deferred expenses as a result of the elimination of several deferred expense programs at the end of 2019 and a \$5.3 million decrease in deferred loss on disposal due to the write off of the remaining deferred impairment loss on generation equipment at the end of 2019. The decreases were partially offset by a \$23.4 million increase in deferred mark-to market losses on diesel, natural gas and interest rate hedging activity and a \$2.6 million increase in the deferral of asset retirement obligation costs.

- Patronage capital increased \$23.9 million, or 3.5%, due to margins offset by the retirement of \$23.9 million in patronage capital in May of 2020.
- Long-term debt, including current maturities, increased \$27.3 million or 1.5%. The increase was due to \$250.0 million in private placement notes issued in 2020 and two FFB advances, \$77.4 million for a plant equipment loan and \$44.4 million for a New Madrid Unit 1 project. The increases were partially offset by a principal prepayment of \$227.4 million of FFB debt through use of the Cushion of Credit investment. The Agriculture Improvement Act of 2018 allowed balances in the cushion of credit to be used to pay FFB debt without penalty. Debt was further reduced by principal payments of \$87.4 million and a reduction in the line of credit balance of \$30.0 million.
- Asset retirement obligation, including the current portion, increased \$9.2 million, or 16.9%, primarily due to changes in the estimates of the amounts and timing of retirement costs related to coal combustion residual storage facilities at Thomas Hill.
- Deferred regulatory credits, including the current portion, increased by \$33.1 million, or 13.3%, primarily due to the deferral in December of 2019 of \$34.0 million of member revenue subject to future refund in the form of lower rate requirements. Additionally, deferred gains on diesel and natural gas swaps increased \$0.4 million. Partially offsetting the increase was a \$1.4 million recognition of previously deferred revenue related to the New Madrid Unit 1 purchase.
- Other deferred liabilities increased \$15.6 million, or 39.4%, primarily due to increases in the derivative liabilities related to an interest rate swap and diesel and natural gas hedging activity.

Associated Electric Cooperative, Inc.  
Statement of Operations  
For the Six Months Ending 6/30/2020  
(In thousands of dollars)

	Three Months Ended June 30		Six Months Ended June 30	
	2020	2019	2020	2019
Operating revenues:				
Members	\$215,028	\$217,878	\$458,771	\$483,029
Nonmembers	57,170	94,295	130,466	168,469
	<u>272,198</u>	<u>312,173</u>	<u>589,237</u>	<u>651,498</u>
Operating expenses:				
Generation operation	107,345	138,610	239,898	299,519
Contracted generation	10,661	10,257	22,223	21,461
Power purchased	32,576	29,301	65,010	60,193
Depreciation and amortization	22,685	22,334	45,212	44,638
Transmission Expense	22,491	23,233	45,664	46,230
Generation maintenance	23,019	24,710	41,007	46,566
Administrative and general	17,435	18,753	36,281	35,604
Taxes	1,343	1,340	2,972	3,038
Accretion of asset retirement obligations	403	421	796	833
	<u>237,958</u>	<u>268,959</u>	<u>499,063</u>	<u>558,082</u>
Operating margin before interest expense	<u>34,240</u>	<u>43,214</u>	<u>90,174</u>	<u>93,416</u>
Interest Expense:				
Interest on long-term debt	17,438	19,825	33,843	39,918
Less: interest capitalized	(633)	(503)	(1,274)	(995)
	<u>16,805</u>	<u>19,322</u>	<u>32,569</u>	<u>38,923</u>
Operating margin	<u>17,435</u>	<u>23,892</u>	<u>57,605</u>	<u>54,493</u>
Nonoperating:				
Interest and dividend income	3,438	6,424	9,338	14,822
Other nonoperating income	412	362	957	727
Interest expense	(133)	(413)	(441)	(722)
Total nonoperating	<u>3,717</u>	<u>6,373</u>	<u>9,854</u>	<u>14,827</u>
Net margin (loss)	<u><u>21,152</u></u>	<u><u>30,265</u></u>	<u><u>67,459</u></u>	<u><u>69,320</u></u>

These interim financial statements are unaudited. In the opinion of management all adjustments, which are normal recurring accruals, necessary for a fair presentation of results for interim periods have been included. The interim financial statements should be read in conjunction with the Notes to the Financial Statements included in the 2019 Annual Report.

Associated Electric Cooperative, Inc.  
Statement of Operations  
For the Six Months Ending 6/30/2020  
(In thousands of dollars)

Assets	<u>Current Month</u>	<u>Prior Year</u>
Utility Plant:		
Electric plant in service	\$4,290,538	\$4,198,795
Construction work in progress	137,483	100,790
	<u>4,428,021</u>	<u>4,299,585</u>
Less accumulated depreciation	<u>(2,333,704)</u>	<u>(2,235,459)</u>
	<u>2,094,317</u>	<u>2,064,126</u>
Other property and investments:		
Nonutility property	31,663	31,663
Net investment in direct financing leases	3,119	3,436
Advanced construction funds	18,695	19,879
	<u>53,477</u>	<u>54,978</u>
Restricted assets:		
Investments in associated organizations	29,036	27,980
Other restricted assets and designated assets	208,225	374,994
	<u>237,261</u>	<u>402,974</u>
Current assets:		
Cash and cash equivalents	404,059	61,331
Restricted short-term investments	75,256	120,844
Accounts receivable, net	107,657	169,814
Fuel inventories	58,953	39,716
Materials and supplies inventories	88,019	86,755
Other current assets	14,267	14,018
Current portion of deferred regulatory debits	12,460	4,518
	<u>760,671</u>	<u>496,996</u>
Deferred regulatory debits	61,489	88,475
Other deferred assets	28,123	35,420
	<u>89,612</u>	<u>123,895</u>
 Total Assets	 <u><u>3,235,338</u></u>	 <u><u>3,142,968</u></u>

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Associated Electric Cooperative, Inc.  
Statement of Operations  
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(In thousands of dollars)

	Current Month	Prior Year
<b>Capitalization and Liabilities</b>		
Patronage capital and other equities:		
Memberships	12	12
Patronage capital	704,129	680,247
Other equities	55,561	55,561
Accumulated other comprehensive inc. (exp)	(19,198)	(14,322)
	740,504	721,498
Long-term debt, excluding current maturities:		
Federal Financing Bank	1,030,918	1,164,274
CoBank	165,529	216,132
Other long-term debt	576,625	345,185
	1,773,072	1,725,591
Asset retirement obligation	48,346	39,777
Accumulated provision for postretirement benefits	40,399	35,438
Current Liabilities:		
Payable to member cooperatives	70,949	77,792
Accounts payable	81,115	90,004
Other current and accrued liabilities	48,231	49,271
Current maturities of long-term debt	81,387	101,559
Current portion of asset retirement obligation	15,226	14,619
Current portion of deferred regulatory credits	2,535	1,706
	299,443	334,951
Deferred regulatory credits	278,280	246,052
Other deferred liabilities	55,294	39,661
	333,574	285,713
<b>Total Capitalization and Liabilities</b>	<b>3,235,338</b>	<b>3,142,968</b>

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Associated Electric Cooperative, Inc.  
Statement of Operations  
For the Six Months Ending 6/30/2020  
(In thousands of dollars)

	Six Months Ended June 30, 2020	Six Months Ended June 30, 2019
Cash flows from operating activities:		
Net margin(loss)	\$67,458	\$69,321
Adjustments to reconcile net margin to net		
Cash provided by operating activities:		
Provision for depreciation and amortization	49,402	47,158
Amortization of loan expenses and other costs	(50)	283
Decrease (increase) in deferred debits	(4,436)	2,566
Increase (decrease) in deferred credits	766	2,702
Increase (decrease) in asset retirement obligation	(1,073)	851
Change in assets and liabilities:		
Accounts receivable	18,916	(39,328)
Fuel inventories	(14,566)	7,905
Materials and supplies inventories	417	(2,589)
Accounts payable	(41,638)	(36,071)
Other current and accrued liabilities	12,699	19,838
Other operating activities, net	2,146	2,434
Net cash provided by operating activities	90,041	75,070
Cash flows from investing activities:		
Construction expenditures for utility plant	(69,813)	(36,258)
Sale (purchase) of investments	(5,935)	(11,331)
Investments in associated organizations	(268)	(136)
Direct financing lease proceeds	162	149
Other investments	548	384
Reimbursement of capital expenditures	(18)	(10)
Net cash (used) in investing activities	(75,324)	(47,202)
Cash flows from financing activities:		
Increase (decrease) in net borrowings from member cooperatives	24,250	42,681
Issuance (retirement) of long-term debt, including change in current maturity	256,007	(87,831)
Retirement of patronage capital	(23,926)	(23,504)
Net cash (used) in financing activities	256,331	(68,654)
Net increase (decrease) in cash and cash equivalents	271,048	(40,786)
Cash and cash equivalents, beginning of period	133,011	102,115
Cash and cash equivalents, end of period	404,059	61,331
Supplemental disclosure of noncash activities:		
Change in plant expenditures included in accounts payable	(11,245)	(6,554)
Supplemental disclosure of cash flow information:	32,242	27,260
Cash paid for interest (net of amount capitalized)		

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