Kentucky 27
Inter County Energy Cooperative
Danville, Kentucky

Audited Financial Statements
December 31, 2013 and 2012

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CONTENTS

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Independent Auditor's Report

To the Board of Directors
Inter County Energy Cooperative

Report on the Financial Statements

I have audited the accompanying financial statements of Inter County Energy Cooperative, which comprise the balance sheets as of December 31, 2013 and 2012, and the related statements of revenue and comprehensive income, changes in 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

My responsibility is to express an opinion on these financial statements based on my audits. I conducted my 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 I 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 entity'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 entity's internal control. Accordingly, I 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.

I believe the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Inter County Energy Cooperative as of December 31, 2013 and 2012, and the results of their operations and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, I have also issued a report dated March 28, 2014, on my consideration of Inter County Energy Cooperative's internal control over financial reporting and my 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 my 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 internal control over financial reporting and compliance.

Alan M. Zumstein

Alan M. Zumstein, CPA
March 28, 2014

Inter County Energy Cooperative
Balance Sheets, December 31, 2013 and 2012

Assets	2013	2012
Electric Plant, at original cost:		
In service	$ 110,728,807	$ 106,959,524
Under construction	472,071	403,504
	111,200,878	107,363,028
Less accumulated depreciation	28,128,161	25,774,272
	83,072,717	81,588,756
Investments in Associated Organizations	19,871,849	16,995,307
Current Assets:		
Cash and cash equivalents	32,624	2,526,072
Accounts receivable, less allowance for 2013 of $147,345 and 2012 of $107,397	5,579,932	4,698,665
Other receivables	158,898	496,960
Material and supplies, at average cost	323,142	353,133
Other current assets	443,786	482,547
	6,538,382	8,557,377
Deferred Pension Costs	2,000,886	-
Total	$ 111,483,834	$ 107,141,440

Members' Equities and Liabilities	2013	2012
Members' Equities:		
Memberships	$ 1,035,515	$ 1,030,965
Patronage capital	38,872,237	35,022,527
Other equities	541,158	73,922
Accumulated other comprehensive income	(233,676)	(305,676)
	40,215,234	35,821,738
Long Term Debt	59,540,956	60,130,194
Accumulated Postretirement Benefits	3,138,675	2,991,632
Current Liabilities:		
Notes payable	400,000	-
Accounts payable	3,871,923	3,957,804
Current portion of long term debt	2,800,000	2,700,000
Consumer deposits	513,331	505,016
Accrued expenses	1,003,715	1,035,056
	8,588,969	8,197,876
Total	$ 111,483,834	$ 107,141,440

The accompanying notes are an integral part of the financial statements.

Statements of Revenue and Patronage Capital
for the years ended December 31, 2013 and 2012

	2013	2012
Operating Revenues:		
Sale of electric energy	$ 48,458,730	$ 45,173,350
Other electric revenue	1,541,617	1,388,474
	50,000,347	46,561,824
Operating Expenses:		
Cost of power	34,101,047	32,248,546
Distribution - operations	2,563,545	2,379,025
Distribution - maintenance	1,712,386	1,844,153
Consumer accounts	1,681,241	1,729,618
Customer services	528,255	536,701
Administrative and general	2,204,548	2,303,916
Depreciation, excluding $296,897 in 2013 and $279,770 in 2012 charged to clearing accounts	3,676,467	3,567,809
Taxes	54,331	56,742
Other deductions	22,180	33,822
	46,544,000	44,700,332
Operating margins before interest charges	3,456,347	1,861,492
Interest Charges:		
Long-term debt	1,620,273	1,622,375
Other	7,616	18,468
	1,627,889	1,640,843
Operating margins after interest charges	1,828,458	220,649
Nonoperating Margins		
Interest income	74,430	77,413
Others	16,418	57,627
	90,848	135,040
Patronage Capital Credits	2,976,949	2,265,304
Net Margins	4,896,255	2,620,993
Comprehensive Income:		
Postretirement benefits	72,000	60,000
Total Comprehensive Income	$ 4,968,255	$ 2,680,993

The accompanying notes are an integral part of the financial statements.

Statement of Changes in Members' Equity
for the years ended December 31, 2012 and 2013

	Memberships	Patronage Capital	Other Equity	Accumulated Other Comprehensive Income	Total Members' Equity
Balance - Beginning of year	$ 1,022,385	$ 33,572,896	$ 74,379	$ (365,676)	$ 34,303,984
Comprehensive income:					
Net margins		2,620,993			2,620,993
Postretirement benefit obligation					
Amortization				60,000	
Adjustments				-	60,000
Total comprehensive income					2,680,993
Net change in memberships	8,580				8,580
Refunds to estates		(260,395)			(260,395)
Transfers to other equity and prior year's deficits		(1,135,622)			(1,135,622)
Other equities		224,198			224,198
Balance - December 31, 2012	1,030,965	35,022,070	74,379	(305,676)	35,821,738
Comprehensive income:					
Net margins		4,896,255			4,896,255
Postretirement benefit obligation					
Amortization				72,000	
Adjustments				-	72,000
Total comprehensive income					4,968,255
Net change in memberships	4,550				4,550
Refunds to estates		(282,313)			(282,313)
General refund of capital credits		(763,775)			(763,775)
Transfers to other equity and prior year's deficits			-		-
Other equities			466,779		466,779
Balance - December 31, 2013	$ 1,035,515	$ 38,872,237	$ 541,158	$ (233,676)	$ 40,215,234

The accompanying notes are an integral part of the financial statements.

Statements of Cash Flows
for the years ended December 31, 2013 and 2012

	2013	2012
Cash Flows from Operating Activities:		
Net margins	$ 4,896,255	$ 2,620,993
Adjustments to reconcile to net cash provided by operating activities:		
Depreciation:		
Charged to expense	3,676,467	3,567,809
Charged to clearing accounts	296,897	279,770
Patronage capital credits assigned	(2,976,949)	(2,265,304)
Accumulated postretirement benefits	219,043	206,347
Change in assets and liabilities:		
Receivables	(543,205)	(483,612)
Material and supplies	29,991	(30,328)
Other assets	(1,962,125)	4,699
Payables	(85,881)	120,316
Consumer deposits	8,315	51,575
Accrued expenses	(31,341)	(23,981)
	3,527,467	4,048,284
Cash Flows from Investing Activities:		
Plant additions	(4,985,100)	(4,814,962)
Plant removal costs	(567,683)	(622,118)
Salvage recovered from retired plant	95,458	101,107
Receipts from other investments, net	100,407	54,024
	(5,356,918)	(5,281,949)
Cash Flows from Financing Activities:		
Net increase in memberships	4,550	8,580
Refund of patronage capital to members	(1,046,088)	(1,396,017)
Increase in other equities	466,779	455,302
Advances of short term borrowings	400,000	-
Advances of long term debt	2,202,011	4,068,630
Advance payments	100,247	(96,360)
Payments on long term debt	(2,791,496)	(2,378,399)
	(663,997)	661,736
Net increase in cash	(2,493,448)	(571,929)
Cash and cash equivalents, beginning of year	2,526,072	3,098,001
Cash and cash equivalents, end of year	$ 32,624	$ 2,526,072
Supplemental cash flows information:		
Interest paid on long-term debt	$ 1,621,803	$ 1,625,595

The accompanying notes are an integral part of the financial statements.

Note 1. Summary of Significant Accounting Policies

Inter County Energy Cooperative ("Inter County") maintains its records in accordance with the policies prescribed or permitted by the Kentucky Public Service Commission ("PSC") and the United States Department of Agriculture, Rural Utilities Service ("RUS"), which conform in all material respects with generally accepted accounting principles. The more significant of these policies are as follows:

Electric Plant Electric plant is stated at original cost, which is the cost when first dedicated to public service. Such amount includes applicable supervisory and overhead cost including any construction period interest and taxes. There was no interest required to be capitalized during the year.

The cost of maintenance and repairs, including renewals of minor items of property, is charged to operating expense. The cost of replacement of depreciable property units, as distinguished from minor items, is charged to electric plant. The units of property replaced or retired, including cost of removal, net of any salvage value, is charged to accumulated depreciation. Electric plant consists of:

	2013	2012
Distribution plant	$97,283,211	$93,863,366
General plant	13,445,596	13,096,158
Total	$110,728,807	$106,959,524

Depreciation Provision has been made for depreciation on the basis of the estimated lives of assets, using the straight-line method. Distribution plant depreciation is based on a composite rate of 3.35% per annum. General plant rates range from 2.5% to 18%.

Cash and Cash Equivalents Inter County considers all short-term, highly liquid investments with original maturities of three months or less to be cash equivalents.

Off Balance Sheet Risk Inter County maintains its cash balances, which may exceed the federally insured limit, with several financial institutions. These financial institutions have strong credit ratings and management believes that the credit risk related to the accounts is minimal.

Revenue Inter County records revenue as billed to its consumers based on monthly meter-reading cycles. All consumers are required to pay a refundable deposit, however, it may be waived under certain circumstances. Inter County's sales are concentrated in a six county area of southeastern Kentucky. There were no consumers whose individual account balance exceeded 10% of outstanding accounts receivable at December 31, 2013 or 2012. Consumers must pay their bill within 20 days of billing, then are subject to disconnect after another 10 days. Accounts are written off when they are deemed to be uncollectible. The allowance for uncollectible accounts is based on the aging of receivables.

Inter County is required to collect, on behalf of the State of Kentucky, sales taxes based on 6 percent of gross sales from non-residential consumers, a 3 percent school tax from certain counties on most gross sales, and franchise fees in certain cities. Inter County's policy is to exclude sales tax from revenue when collected and expenses when paid and instead, record collection and payment of sales taxes through a liability account.

Cost of Power Inter County is one of sixteen members of East Kentucky Power Cooperative, Inc. ("East Kentucky"). Under a wholesale power agreement, Inter County is committed to purchase its electric power and energy requirements from East Kentucky until 2051. The rates charged by East Kentucky are subject to approval of the PSC. The cost of purchased power is recorded monthly during the period in which the energy is consumed, based upon billings from East Kentucky.

Note 1. Summary of Significant Accounting Policies, continued

Estimates The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates used in the preparation of the financial statements.

Fair Value Measurements The Fair Value Measurements and Disclosures Topic of the FASB ASC 820, *Fair Value Measurements and Disclosures,* defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal, or most advantageous, market for the asset or liability in an orderly transaction between market participants at the measurement date. The Fair Values Measurements Topic establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs when possible. The three levels of inputs used to measure fair value are as follows:

Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities

Level 2: Quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly.

Level 3: Prices or valuations that require inputs that are both significant to the fair value measure and unobservable.

A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

The carrying amounts of Inter County's cash and cash equivalents, other receivables, investments, inventories, other assets, trade accounts payable, accrued expenses and liabilities, and other liabilities approximate fair value due to their short maturity. Investments in associated organizations are not considered a financial instrument because they represent nontransferable interests in associated organizations. Other assets and liabilities are not considered financial instruments because they represent activities specifically related to Inter County. Long term debt can not be traded in the market, and is specifically for electric cooperatives and, therefore, a value other than its outstanding principal cannot be determined.

Inter County may, and also does, invest idle funds in local banks and in National Rural Utilities Cooperative Finance Corporation ("CFC") commercial paper. The inputs used to measure idle funds are Level 1 measurements, as these funds are exchange traded funds in an active market.

Income Tax Status Inter County is exempt from federal and state income taxes under provisions of Section 501(c)(12). Accordingly, the financial statements for Inter County include no provision for income taxes. Inter County's accounting policy provides that a tax expense/benefit from an uncertain tax position may be recognized when it is more likely than not that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes, based on the technical merits. Management believes Inter County has no uncertain tax positions resulting in an accrual of tax expense or benefit. Inter County recognizes interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. Inter County did not recognize any interest or penalties during the years ended December 31, 2013 and 2012. Inter County's income tax return is subject to possible examination by taxing authorities until the expiration of related statues of limitations on the return, which is generally three years.

Note 1. Summary of Significant Accounting Policies, continued

Comprehensive Income Comprehensive income includes both net margin and other comprehensive income. Other comprehensive income represents the change in funded status of the accumulated postretirement benefit obligation.

Risk Management Inter County is exposed to various forms of losses of assets associated with, but not limited to, fire, personal liability, theft, vehicular accidents, errors and omissions, fiduciary responsibility, workers compensation, etc. Each of these areas is covered through the purchase of commercial insurance.

Advertising Inter County expenses advertising costs as incurred.

Subsequent Events Management has evaluated subsequent events through March 28, 2014, the date the financial statements were available to be issued. There were no significant subsequent events to report.

Note 2. Investments in Associated Organizations

Investments in associated organizations consist of:

	2013	2012
East Kentucky, patronage capital	$17,707,583	$14,883,013
CFC, patronage capital and CTCs	1,255,094	1,243,684
Others	909,172	868,610
Total	$19,871,849	$16,995,307

Inter County records patronage capital assigned by associated organizations in the year in which such assignments are received.

The Capital Term Certificates ("CTCs") of CFC are recorded at cost. The CTCs were purchased from CFC as a condition of obtaining long-term financing. The CTCs bear interest at 3% and 5% and are scheduled to mature at varying times from 2020 to 2080.

Note 3. Patronage Capital

Under provisions of the long-term debt agreement, return to patrons of capital contributed by them is limited to amounts which would not allow the total equities and margins to be less than 30% of total assets, except that distributions may be made to estates of deceased patrons. The debt agreement provides, however, that should such distributions to estates not exceed 25% of the net margins for the next preceding year, Inter County may distribute the difference between 25% and the payments made to such estates.

The equity at December 31, 2013 was 36% of total assets. Patronage capital consists of:

	2013	2012
Assigned to date	$41,486,707	$39,124,656
Assignable margins	4,896,255	2,620,993
Unassigned	150,817	150,817
Prior years deficits	(469,511)	(728,453)
Retirements to date	(7,192,031)	(6,145,486)
Total	$38,872,237	$35,022,527

Note 4. Long Term Debt

The long term debt is due in quarterly and monthly installments of varying amounts through 2039. The 6.25% to 6.46% notes due CFC are available for repricing every 7 years to either a variable or fixed rate. RUS assesses 12.5 basis points to administer the Federal Financing Bank ("FFB") loans. Inter County Energy has loan funds available from FFB in the amount of $7,000,000. These funds will be used for future plant additions. Inter County refinanced $2,354,391 during 2011 and $5,002,175 during 2010 of 5% interest notes from RUS with proceeds from National Bank for Cooperatives ("CoBank"). The 2.25% interest rate notes to CoBank are for the accelerated R&S payment to NRECA as described in Note 6.

All assets, except vehicles, are pledged as collateral on the long term debt to RUS, FFB, CFC, and CoBank under a joint mortgage agreement. First mortgage notes consist of:

	2013	2012
RUS:		
0.25% - 5.125%	$22,645,663	$23,162,757
Cushion of credit, earns 5%	(420,117)	(520,364)
	22,225,546	22,642,393
FFB, 0.02% and 2.748% (0.104% in 2012)	28,248,609	29,415,768
CFC, 6.0% to 6.50% notes	4,359,983	4,660,204
CoBank, 4.55% and 4.48%	5,485,238	6,011,125
CoBank, 2.25%	1,910,496	-
East Kentucky, 1.5% various 5 years	111,084	100,704
	62,340,956	62,830,194
Less current portion	2,800,000	2,700,000
Long term portion	$59,540,956	$60,130,194

As of December 31, 2013, the annual principal portion of long term debt outstanding for the next five years are as follows: 2014 - $2,800,000; 2015 - $2,850,000; 2016 - $2,900,000; 2017 - $2,950,000; 2018 - $3,000,000.

Note 5. Short Term Borrowings

At December 31, 2013, Inter County Energy had a short term line of credit of $5,000,000 available from CFC. Inter County Energy has advances against the line of credit with CFC in the amount of $400,000 with an interest rate of 2.90%.

Note 6. Pension Plan

All eligible employees of Inter County Energy participate in the NRECA Retirement and Security Plan ("R&S Plan"), a defined benefit pension plan qualified under section 401 and tax exempt under section 501(a) of the Internal Revenue Code. It is a multiemployer plan under the accounting standards. The Plan sponsor's identification number is 53-0116145 and the Plan Number is 333. A unique characteristic of a multiemployer plan compared to 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.

Note 6. Pension Plan, continued

Inter County Energy's contributions to the R&S Plan in 2013 and 2012 represent less than 5 percent of the total contributions made to the plan by all participating employers. Inter County Energy made contributions to the plan of $641,963 in 2013 and $804,543 in 2012. There have been no significant changes that affect the comparability of 2013 and 2012.

In the R&S 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 R&S Plan was between 65 percent and 80 percent funded at January 1, 2013 and 2012 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 R&S 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 the December 2012 meeting of the I&FS Committee of the NRECA Board of Directors, the Committee approved an option to allow participating cooperatives in the Retirement Security ("R&S") Plan (a defined benefit multiemployer pension plan) to make a prepayment and reduce future required contributions. The prepayment amount is a cooperative share, as of January 1, 2013, of future contributions required to fund the R&S Plan's unfunded value of benefits earned to date using Plan actuarial valuation assumptions. The prepayment amount will typically equal approximately 2.5 times a cooperative's annual R&S Plan required contribution as of January 1, 2013. After making the prepayment, for most cooperatives the billing rate is reduced by approximately 25%, retroactive to January 1, 2013. The 25% differential in billing rates is expected to continue for approximately 15 years. However, changes in interest rates, asset returns and other plan experience different from that expected, plan assumptions changes, and other factors may have an impact on the differential in billing rates and the 15 year period.

Two prepayment options were available to participating cooperatives:

1. Use current assets to make the prepayment over a period of not more than 4 years, or,
2. Borrow funds sufficient to make the prepayment in a lump sum, with the prepayment of the borrowed amount determined by the loan's amortization schedule.

On February 14, 2013, RUS issued a memorandum to all of its borrowers regarding the proper accounting treatment of the R&S Plan prepayment. RUS stipulated that the prepayment shall be recorded as a long term prepayment in Account 186, Miscellaneous Deferred Debits. This prepaid expense shall be amortized to Account 926, Employee Pensions and Benefits, over a ten year period. Alternatively, RUS borrowers may calculate the amortization period by subtracting the cooperative's average age of its workforce as provided by NRECA from the cooperative's normal retirement age under the R&S Plan, up to a maximum period of 20 years. If the entity choses to finance the prepayment, interest expense associated with the loan shall be recorded in the year incurred as is required under the RUS Uniform System of Accounts ("USoA").

Section 6.13(e) of the RUS Loan Contract limits the amount of unsecured debt that a borrower may incur to 15% on Net Utility Plant if the equity level of the borrower, after considering such unsecured debt, is below 30% of its Total Assets, unless the borrower obtains RUS consent. RUS will consider any unsecured debt associated with the R&S Plan prepayment to be "Permitted Debt" and accordingly, it will be excluded from the application of Section 6.13(e). On April 22, 2013, the Corporation made a prepayment of $2,163,206 to the R&S Plan. The amount is being amortized over 10 years.

Note 7. Postretirement Benefits

Inter County Energy sponsors a defined benefit plan that provides medical insurance coverage to retirees and their dependents. Participating retirees and dependents do not contribute to the projected cost of coverage until eligible for Medicare at which time they contribute 50% of the cost of coverage. For measurement purposes, an annual rate of increase of 8% in 2012, then decreasing by 0.5% per year until 5% per year, in the per capita cost of covered health care benefit was assumed. The discount rate used in determining the accumulated postretirement benefit obligation was 5.5%.

The funded status of the plan is as follows:

	2013	2012
Projected benefit obligation	($3,138,675)	($2,991,632)
Plan assets at fair value	-	-
Total	($3,138,675)	($2,991,632)

The components of net periodic postretirement benefit costs are as follows:

	2013	2012
Benefit obligation at beginning of year	$2,991,632	$2,845,285
Components of net periodic benefit cost:		
Service cost	119,436	127,485
Interest cost	168,564	160,515
Net periodic benefit cost	288,000	288,000
Benefits paid	(140,957)	(141,653)
Accumulated other comprehensive income	-	-
Benefit obligation at end of year	$3,138,675	$2,991,632

Projected retiree benefit payments for the next five years are expected to be as follows: 2014 - $143,000; 2014 - $145,000; 2015 - $147,000; 2016 - $149,000; 2017 - $141,000.

Note 8. Related Party Transactions

Several of the Directors of Inter County and its President & General Manager are on the Boards of Directors of various associated organizations.

Note 9. Commitments

Inter County Energy has various other agreements outstanding with local contractors. Under these agreements, the contractors will perform certain construction and maintenance work at specified hourly rates or unit cost, or on an as needed basis. The duration of these contracts are one to three years.

Note 10. Environmental Contingency

Inter County from time to time is required to work with and handle PCBs, herbicides, automotive fluids, lubricants, and other hazardous materials in the normal course of business. As a result, there is the possibility that environmental conditions may arise which would require Inter County to incur cleanup costs. The likelihood of such an event, or the amount of such costs, if any, cannot be determined at this time. However, management does not believe such costs, if any, would materially affect Inter County's financial position or its future cash flows.

Note 11. Contingencies

Inter County, on occasion, is involved in litigation arising in the normal course of business. While the results of such litigation cannot be predicted with certainty, management, based upon advice of counsel, believes that the final outcome will not have a material adverse effect on the financial statements.

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Supplementary Information

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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*

To the Board of Directors
Inter County Energy Cooperative

I 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 Inter County Energy Cooperative, which comprise the balance sheets as of December 31, 2013 and 2012, and the related statements of revenue and comprehensive income, members' equities and cash flows for the years then ended, and related notes to the financial statements, and have issued my report thereon dated March 28, 2014.

Internal Control Over Financial Reporting

Management is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing my audit, I considered Inter County's internal control over financial reporting as a basis for designing my auditing procedures for the purpose of expressing my opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Inter County's internal control over financial reporting. Accordingly, I do no express an opinion on the effectiveness of Inter County's internal control over financial reporting.

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 a 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.

My consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. I did not identify any deficiencies in internal control over financial reporting that I consider to be material weaknesses, as defined previously.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Inter County's financial statements are free of material misstatement, I performed test 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 my audit, and accordingly, I do not express such an opinion. The results of my tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

This report is intended solely for the information and use of the audit committee, management, the Rural Utilities Service, and supplemental lenders, and is not intended to be and should not be used by anyone other than these specified parties.

Alan M. Zumstein

Alan M. Zumstein, CPA
March 28, 2014

ALAN M. ZUMSTEIN
CERTIFIED PUBLIC ACCOUNTANT

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To the Board of Directors
Inter County Energy Cooperative

I have audited the financial statements of Inter County Energy Cooperative for the year ended December 31, 2012, and have issued my report thereon dated March 28, 2014. I conducted my audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, and 7 CFR Part 1773, Policy on audits of the Rural Utilities Service (RUS) Borrowers. Those standards require that I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

In planning and performing my audit of the financial statements of Inter County for the year ended December 31, 2012, I considered its internal control over financial reporting in order to determine my auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control over financial reporting.

My consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be a material weakness. A material weakness is a condition in which the design or operation of the specific internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. I noted no matters involving the internal control over financial reporting that I consider to be a material weakness.

7 CFR Part 1773.3 requires comments on specific aspects of the internal control over financial reporting, compliance with specific RUS loan and security instrument provisions and other additional matters. I have grouped my comments accordingly. In addition to obtaining reasonable assurance about whether the financial statements are free from material misstatements, at your request, I performed tests of specific aspects of the internal control over financial reporting, of compliance with specific RUS loan and security instrument provisions and of additional matters. The specific aspects of the internal control over financial reporting, compliance with specific RUS loan and security instrument provisions, and additional matters tested include, among other things, the accounting procedures and records, material control, compliance with specific RUS loan and security instrument provisions set forth in 7 CFR Part 1773.3(d)(1) related transactions, depreciation rates, a schedule of deferred debits and credits and a schedule of investments, upon which I express an opinion. In addition, my audit of the financial statements also included the procedures specified in 7 CFR Part 1773.38-.45. My Objective was not to provide an opinion on these specific aspects of the internal control over financial reporting, compliance with specific RUS loan and security instrument provisions, or additional matters, and accordingly, I express no opinion thereon.

No reports, other than my independent auditor's report, and my independent auditor's report on internal control over financial reporting and compliance and other matters, all dated March 28, 2014, or summary of recommendations related to my audit have been furnished to management.

My comments on specific aspects of the internal control over financial reporting, compliance with specific RUS loan and security instrument provisions and other additional matters as required by 7 CFR Part 1773.33 are presented below.

Comments on Certain Specific Aspects of the Internal Control Over Financial Reporting

I noted no matters regarding Inter County's internal control over financial reporting and its operation that I consider to be a material weakness as previously defined with respect to:

- The accounting procedures and records;
- the process for accumulating and recording labor, material and overhead costs, and the distribution of these costs to construction, retirement, and maintenance and other expense accounts, and;
- the material controls.

Comments on Compliance with Specific RUS Loan and Security Instrument Provisions

At your request, I have performed the procedures enumerated below with respect to compliance with certain provisions of laws, regulations, and contracts. The procedures I performed are summarized as follows:

- Procedures performed with respect to the requirement for a borrower to obtain written approval of the mortgagee to enter into any contract for the operation or maintenance of property, or for the use of mortgaged property by others for the year ended December 31, 2013, of Inter County.
    1. Inter County has not entered into any contract during the year for the operation or maintenance of its property, or for the use of its property by others as defined in 1773.33(e)(1)(i).
- Procedures performed with respect to the requirement to submit RUS *Financial and Operating Report Electric Distribution* to RUS:
    1. Agreed amounts reported in RUS *Financial and Operating Report Electric Distribution* to Inter County Energy's records as of December 31, 2013.

The results of my tests indicate that, with respect to the items tested, Inter County complied in all material respects, with the specific RUS loan and security instrument provisions referred to below. With respect to items not tested, nothing came to my attention that caused me to believe that Inter County Energy had not complied, in all material respects, with those provisions. The specific provisions tested, as well as any exceptions noted, include the requirements that:

- The borrower has submitted its RUS *Financial and Operating Report Electric Distribution* to RUS and the *Financial and Operating Report Electric Distribution* as of December 31, 2013, represented by the borrower as having been submitted to RUS appears to be in agreement with its audited records in all material respects.
- During the period of this review, Inter County received no long term advances from CFC on loans controlled by the RUS/CFC Mortgage and Loan Agreement.

Comments on Other Additional Matters

In connection with my audit of Inter County, nothing came to my attention that caused me to believe that Inter County failed to comply with respect to:

- The reconciliation of continuing property records to controlling general ledger plant accounts addressed at 7 CFR Part 1773.33(c)(1);
- The clearing of the construction accounts and the accrual of depreciation on completed construction addressed at 7 CFR Part 1773.33(c)(2);
- The retirement of plant addressed at 7 CFR 1773.33(c)(3) and (4);
- Approval of the sale, lease, or transfer of capital assets and disposition of proceeds for the sale or lease of plant, material, or scrap addressed at 7 CFR Part 1773.33(c)(5);
- The disclosure of material related party transactions, in accordance with Statement of Financial Accounting Standard No. 57, Related party Transactions, for the year ended December 31, 2013, in the financial statements referenced in the first paragraph of this report addressed at 7 CFR Part 1773.33(f);
- The depreciation rates addressed at 7 CFR Part 1773.33(g);
- The detailed schedule of deferred debits and deferred credits, and
- The detailed schedule of investments, of which there were none.

Deferred debits are as follows:

Prepaid pension cost	$2,000,866

My audit was made for the purpose of forming an opinion on the basic financial statements taken as a whole. The detailed schedule of deferred debits and deferred credits required by 7 CFR Part 1773(h) and provided below is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information has been subjected to the auditing procedures applied in my audit of the basic financial statements and, in my opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the Board of Directors, management, RUS, and supplemental lenders and is not intended to be and should not be used by anyone other than these specified parties.

Alan M. Zumstein

Alan M. Zumstein, CPA
March 28, 2014

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

Board of Directors
Inter County Energy

Independent Auditor's Report

I 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 Inter County Energy ("the Cooperative"), which comprise the balance sheet as of December 31, 2013, and the related statements of revenue and comprehensive income, patronage capital, and changes in cash flows for the year then ended, and the related notes to the financial statements, and have issued my report thereon dated March 28, 2014. In accordance with *Government Auditing Standards*, we have also issued my report dated March 28, 2014, on my consideration of the Cooperative's internal control over financial reporting and on my 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 and my schedule of findings and recommendations related to my audit have been furnished to management.

In connection with my audit, nothing came to my attention that caused me 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, my audit was not directed primarily toward obtaining knowledge of noncompliance. Accordingly, had I performed additional procedures, other matters may have come to my 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 relate to accounting matters. In connection with my audit, I 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 material and supplies;
- Prepare accurate and timely Financial and Operating Reports;
- Obtain written RUS approval to enter into any contract for the management, operation, 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, 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 distributions is not limited.

Alan Zumstein

Alan M. Zumstein, CPA
March 28, 2014