

**Kentucky 3**  
**Jackson Energy Cooperative Corporation**  
**and Subsidiary**  
**McKee, Kentucky**

**Audited Financial Statements**  
**February 28, 2019 and 2018**

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**Independent Auditor's Report**

To the Board of Directors  
Jackson Energy Cooperative Corporation  
McKee, Kentucky

**Report on the Financial Statements**

I have audited the accompanying consolidated financial statements of Jackson Energy Cooperative Corporation and Subsidiary, which comprise the balance sheet as of February 28, 2019 and 2018, and the related consolidated statements of revenue and comprehensive income, changes in members' equities, and cash flows for the year then ended, and the related notes to the consolidated 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 consolidated 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 consolidated financial statements based on my audit. I conducted my audit 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 consolidated financial statements.

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

To the Board of Directors  
Jackson Energy Cooperative Corporation

## **Opinion**

In my opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Jackson Energy Cooperative Corporation and Subsidiary as of February 28, 2019 and 2018, and the results of their operations and cash flows for the year 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 May 14, 2019, on my consideration of Jackson Energy Cooperative Corporation'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 and should be considered in assessing the results of my audit.

## **Other Matters**

My audit was conducted for the purpose of forming an opinion on the consolidated financial statements that collectively comprise the Cooperative's consolidated financial statements. The consolidating schedules on pages 16-17 are presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The supplementary information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In my opinion, the supplementary information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

*Alan M. Zumstein*

Alan M. Zumstein, CPA  
May 14, 2019

Jackson Energy Cooperative Corporation and Subsidiary  
Consolidated Balance Sheets, February 28, 2019 and 2018

<u>Assets</u>	<u>2019</u>	<u>2018</u>
Utility Plant, net	\$ 170,093,644	\$ 169,551,692
Investments and Other Assets:		
Associated organizations and others	63,027,152	60,088,040
Goodwill	262,177	262,177
	63,289,329	60,350,217
Current Assets:		
Cash and cash equivalents	7,741,508	6,587,773
Accounts receivable, less allowance for uncollectible accounts	13,560,902	14,556,904
Material and supplies	2,195,338	2,067,518
Prepayments	402,824	779,998
	23,900,572	23,992,193
Deferred Debits	9,448,313	10,404,812
Total	\$ 266,731,858	\$ 264,298,914
<u>Members' Equities and Liabilities</u>		
Members' Equities:		
Memberships and capital	\$ 1,309,950	\$ 1,311,060
Patronage capital and retained earnings	109,828,384	102,716,696
Accumulated other comprehensive income	(587,036)	(635,612)
Other equities	4,034,195	4,046,869
	114,585,493	107,439,013
Long Term Debt	126,079,725	127,851,825
Accumulated Postretirement Benefits	8,956,515	8,834,362
Current Liabilities:		
Accounts payable	6,584,659	7,268,731
Short term borrowings	-	1,600,000
Current portion of long term debt	5,700,000	6,385,000
Consumer deposits	817,488	719,202
Other current and accrued liabilities	2,680,177	2,871,882
	15,782,324	18,844,815
Consumer advances and others	1,327,801	1,328,899
Total	\$ 266,731,858	\$ 264,298,914

The accompanying notes are an integral part of these statements.

Jackson Energy Cooperative Corporation and Subsidiary  
Consolidated Statements of Revenue and Comprehensive Income  
for the years ended February 28, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Operating Revenues	<u>\$ 107,666,160</u>	<u>\$ 105,414,753</u>
Operating Expenses:		
Cost of purchases	65,532,325	65,566,363
Distribution - operations	5,962,472	5,678,438
Distribution - maintenance	7,400,417	6,270,970
Sales	627,224	769,085
Administrative and general	5,122,570	4,889,010
Depreciation, excluding \$635,907 in 2019 and \$686,887 in 2018 charged to clearing account	10,204,958	9,878,032
Amortization of deferred property retirements	470,772	470,772
Interest on long-term debt	4,554,953	4,411,339
Other interest	15,942	55,398
Taxes	173,911	172,312
Other	141,735	86,097
	<u>103,420,479</u>	<u>101,511,060</u>
Operating Margins	<u>4,245,681</u>	<u>3,903,693</u>
Nonoperating Margins		
Interest income	146,375	112,801
Subsidiary and others	(97,431)	34,628
	<u>48,944</u>	<u>147,429</u>
Patronage Capital assigned, associated organizations		
G&T capital credits	3,291,092	1,963,643
Other capital credits	178,275	148,043
	<u>3,469,367</u>	<u>2,111,686</u>
Net Margins	7,763,992	6,162,808
Other Comprehensive Income:		
Postretirement benefits	48,576	48,576
Total Comprehensive income	<u><u>\$ 7,812,568</u></u>	<u><u>\$ 6,211,384</u></u>

The accompanying notes are an integral part of these statements.

Jackson Energy Cooperative Corporation and Subsidiary  
 Statements of Changes in Members' Equities  
 for the years ended February 28, 2018 and 2019

	<u>Memberships and Capital</u>	<u>Patronage Capital</u>	<u>Other Equities</u>	<u>Accumulated Comprehensive Income</u>	<u>Total Members' Equities</u>
Balance - February 28, 2017	\$ 1,307,365	\$ 97,108,401	\$ 4,053,617	\$ (684,188)	\$ 101,785,195
Comprehensive income:					
Net margins		6,162,808			6,162,808
Postretirement benefit obligation					
Amortization				48,576	
Adjustments				-	48,576
Total comprehensive income				<u>48,576</u>	<u>6,211,384</u>
Refunds of capital credits		(554,513)			(554,513)
Transfers to other equity					-
Memberships, net	3,695				3,695
Other equities			(6,748)		(6,748)
Balance - February 28, 2018	1,311,060	102,716,696	4,046,869	(635,612)	107,439,013
Comprehensive income:					
Net margins		7,763,992			7,763,992
Postretirement benefit obligation					
Amortization				48,576	
Adjustments				-	48,576
Total comprehensive income				<u>48,576</u>	<u>7,812,568</u>
Refunds of capital credits		(652,304)			(652,304)
Transfers to other equity					-
Memberships, net	(1,110)				(1,110)
Other equities			(12,674)		(12,674)
Balance - February 28, 2019	<u>\$ 1,309,950</u>	<u>\$ 109,828,384</u>	<u>\$ 4,034,195</u>	<u>\$ (587,036)</u>	<u>\$ 114,585,493</u>

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

Jackson Energy Cooperative Corporation and Subsidiary  
Consolidated Statements of Cash Flows  
for the years ended February 28, 2019 and 2018

	<u>2019</u>	<u>2018</u>
Cash Flows from Operating Activities:		
Net margins	\$ 7,763,992	\$ 6,162,808
Adjustments to reconcile to net cash provided by operating activities:		
Depreciation and amortization		
Charged to expense	10,675,730	10,348,804
Charged to clearing accounts	635,907	686,887
Patronage capital allocated	(3,469,367)	(2,111,686)
Accumulated postretirement benefits	170,729	42,362
Change in assets and liabilities:		
Receivables	996,002	(601,177)
Material and supplies	(127,820)	(70,280)
Prepayments	862,901	79,364
Payables	(684,072)	637,036
Consumer deposits and advances	97,188	(14,415)
Accrued expenses	(191,705)	263,036
	<u>16,729,485</u>	<u>15,422,739</u>
Cash Flows from Investing Activities:		
Plant additions	(10,076,392)	(11,905,605)
Plant removal costs	(1,370,386)	(1,414,049)
Salvage recovered from plant retirements	54,537	72,476
Other investments, net	539,679	570,603
	<u>(10,852,562)</u>	<u>(12,676,575)</u>
Cash Flows from Financing Activities:		
Memberships, capital and other equities	(13,784)	(3,053)
Retirement of patronage capital	(652,304)	(554,513)
Additional long-term borrowings	6,940,000	10,000,000
Payments on long-term debt	(9,397,100)	(7,004,534)
Short term borrowings (repayments)	(1,600,000)	(2,400,000)
	<u>(4,723,188)</u>	<u>37,900</u>
Net increase in cash	1,153,735	2,784,064
Cash and cash equivalents - beginning of period	<u>6,587,773</u>	<u>3,803,709</u>
Cash and cash equivalents - end of period	<u>\$ 7,741,508</u>	<u>\$ 6,587,773</u>
Supplemental cash flows information:		
Interest paid on long-term debt	\$ 4,466,520	\$ 4,251,949
Income taxes paid	\$ 120,000	\$ 28,176

The accompanying notes are an integral part of these statements.



Jackson Energy Cooperative and Subsidiary  
Notes to Financial Statements

**Note 1. Summary of Significant Accounting Policies**

Jackson Energy Cooperative Corporation and Subsidiary (“Jackson Energy”) 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 with generally accepted accounting principles as applied to regulated entities. The more significant of these policies are as follows:

**Principles of Consolidation** The accompanying consolidated financial statements include the accounts of Jackson Energy Cooperative Corporation and Jackson Energy Propane Plus, LLC (“Propane Plus”). All significant inter-company accounts and transactions have been eliminated. Jackson Energy uses an audit date of February 28. The Subsidiary operates on a fiscal year ending December 31. The consolidated financial statements reflect the year end of February 28 for Jackson Energy and December 31 for the Subsidiary, respectively.

**Utility Plant** Jackson Energy’s 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.

Propane Plus’ fixed assets consist primarily of propane tanks located on customers’ premises, bulk tanks, and trucks used in the delivery of propane.

Utility plant consists of:

	<u>2019</u>	<u>2018</u>
Electric Plant:		
Distribution plant	\$234,443,284	\$227,911,938
General plant	<u>22,884,818</u>	<u>22,743,948</u>
	257,328,102	250,655,886
Plant under construction	<u>597,815</u>	<u>759,742</u>
	257,925,917	251,415,628
Less accumulated depreciation	<u>90,709,267</u>	<u>84,582,223</u>
Net electric plant	<u>167,216,650</u>	<u>166,833,405</u>
Propane Plant:		
Propane tanks on customers' premises	2,108,130	1,956,990
Bulk tanks	928,643	849,979
Delivery and other trucks	1,531,374	1,348,734
Buildings and land	616,544	590,606
Office and other equipment	<u>229,439</u>	<u>221,465</u>
	5,414,130	4,967,774
Less accumulated depreciation	<u>2,537,136</u>	<u>2,249,487</u>
Net propane plant	<u>2,876,994</u>	<u>2,718,287</u>
Net utility plant	<u>\$170,093,644</u>	<u>\$169,551,692</u>

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.

Jackson Energy Cooperative and Subsidiary  
Notes to Financial Statements

**Note 1. Summary of Significant Accounting Policies**, continued

**Depreciation** Provision has been made for depreciation on the basis of the estimated lives of assets, using the straight-line method. Depreciation rates range from 1.44% to 10.0%, with a composite rate of 4.1% for distribution plant. General plant rates range from 2.5% to 20%. Propane Plus's depreciation is computed using the straight-line method over the useful lives of its assets.

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

**Off Balance Sheet Risk** Jackson Energy has off-balance sheet risk in that they maintain cash deposits in financial institutions in excess of the amounts insured by the Federal Deposit Insurance Corporation (FDIC). At February 28, 2019, the financial institutions reported deposits in excess of the \$250,000 FDIC insured limit several times during the audit period. These financial institutions have strong credit ratings and management believes that credit risk related to the accounts is minimal.

**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.

**Revenue** Jackson Energy records revenue as billed to its consumers based on monthly meter-reading cycles. Under certain circumstances, consumers are required to pay a refundable deposit. Jackson Energy's sales are concentrated in a fifteen (15) county area of southeastern Kentucky. Consumers must pay their bill within 20 days of billing, at which time a disconnect notice is sent with payment to be within 10 days. If not paid, then consumers are subject to disconnect. Accounts are written off when they are deemed to be uncollectible. The allowance for uncollectible accounts is based on the aging of receivables. The balance in the allowance account was \$82,721 at 2019 and \$95,798 at 2018. There were no individual account balances that exceeded 10% of outstanding accounts receivable at 2019 or 2018.

Propane Plus recognizes revenue when earned, regardless of the period in which customers are billed. Propane sales are recognized when deliveries are made, tank rental each month, and sales of related accessories at the time of sale. Accounts are written off when they are deemed to be uncollectible. The allowance for uncollectible accounts is based on the aging of receivables. The balance in the allowance account was \$38,792 for 2019 and \$25,000 for 2018. There were no individual account balances that exceeded 10% of outstanding accounts receivable at 2019 or 2018.

The Companies are required to collect, on behalf of the Commonwealth 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. The Company'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.

**Advertising** Jackson Energy expenses advertising costs as incurred.

**Cost of Power** Jackson Energy is one of sixteen (16) members of East Kentucky. Under a wholesale power agreement, Jackson Energy 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.

Jackson Energy Cooperative and Subsidiary  
Notes to Financial Statements

**Note 1. Summary of Significant Accounting Policies**, continued

**Cost of Propane** Propane Plus purchases all of its propane requirements from an unrelated party through Kentucky Propane Plus, LLC, a related party. Propane is delivered in bulk tanks owned by Propane Plus, then delivered to customers on an as needed basis.

**Propane Inventory** Propane is measured at the end of each month and valued based on the current purchase price of propane.

**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.

Jackson Energy 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.

The carrying amounts of Jackson Energy's cash and cash equivalents, other receivables, inventory, accounts payable, accrued expenses and 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, other liabilities, and investments are not considered financial instruments because they represent activities specifically related to Jackson Energy. 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.

**Goodwill** The goodwill was recorded in connection with the purchase of one-half (1/2) interest from an unrelated party on June 30, 2000. The excess of the purchase price over the value of assets acquired has been recorded as goodwill. Goodwill was tested for impairment and it was determined that goodwill has not been impaired; therefore, there was no impairment of goodwill for 2019 or 2018.

Jackson Energy Cooperative and Subsidiary  
Notes to Financial Statements

**Note 1. Summary of Significant Accounting Policies, continued**

**Deferred Property Retirement** During 1994, Jackson Energy initiated a Geographic Information System (“GIS”) project to establish detailed maps of its distribution electric system and provide a database containing detailed information on the facilities and quantities installed. A physical inventory was performed and the difference between the facilities reported on the GIS base map and the accounting records resulted in an adjustment to decrease plant by \$14,535,593, and a reduction in accumulated depreciation of \$2,530,647. This resulted in a net adjustment of \$12,004,946. The PSC required this amount to be amortized over 25.5 years, which results in annual amortization of \$470,782.

**Risk Management** Jackson Energy 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.

**Income Tax Status** Jackson Energy is exempt from federal and state income taxes under provisions of Section 501(c)(12). Accordingly, the financial statements for Jackson Energy include no provision for income taxes. Propane Plus is a limited liability company treated as a partnership for federal income tax purposes. Income taxes for Propane Plus are provided on income as reported in the accompanying statements regardless of when such taxes are payable. Propane Plus uses the same depreciation for book and taxes, therefore, deferred taxes are considered immaterial and are not recorded.

Management evaluates its potential exposures from tax positions taken that have or could be challenged by taxing authorities. These potential exposures result because taxing authorities may take positions that differ from those taken by management in the interpretation and application of statutes, regulations, and rules. There are no tax positions for which the ultimate deductibility is highly uncertain included in the accompanying financial statements. Jackson Energy recognizes interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. Jackson Energy did not recognize any interest or penalties during the years ended February 28, 2019 or 2018. Jackson Energy’s income tax return is subject to possible examination by taxing authorities until the expiration of related statutes of limitations on the return, which is generally three years.

**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.

**Subsequent Events** Management has evaluated subsequent events through May 14, 2019, the date the financial statements were available to be issued. There were no significant subsequent events to report.

**Note 2. Investments in Associated Organizations and Others**

Jackson Energy 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 0%, 3% and 5% and are scheduled to mature at varying times from 2020 to 2080. Interest is paid each April 1 and October 1. The economic development loans are through RUS at low interest rates to local businesses and are secured by either/or a portion of the assets pledged by Jackson Energy’s consumers, or guarantees from local banks.

Jackson Energy Cooperative and Subsidiary  
Notes to Financial Statements

**Note 2. Investments in Associated Organizations and Others, continued**

Investments in associated organizations and others consist of:

	<u>2019</u>	<u>2018</u>
East Kentucky, patronage capital	\$56,247,251	\$52,956,158
CFC - CTC's	1,637,967	1,680,559
Other associated organizations	3,322,211	3,218,636
Economic development loans	<u>1,819,723</u>	<u>2,232,687</u>
	<u>\$63,027,152</u>	<u>\$60,088,040</u>

**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, Jackson Energy may distribute the difference between 25% and the payments made to such estates. The equity at February 28, 2019 was 41% of total assets. Prior year's deficits are being carried forward and will be offset with future years' non operating margins.

Patronage capital consists of:

	<u>2019</u>	<u>2018</u>
Assigned to date	\$136,386,050	\$128,271,067
Assignable	2,220,369	2,624,615
Prior year's deficits	(4,076,654)	(4,129,907)
Retired to date	<u>(24,701,381)</u>	<u>(24,049,079)</u>
	<u>\$109,828,384</u>	<u>\$102,716,696</u>

**Note 4. Long Term Debt**

All assets, except vehicles, are pledged as collateral on the long term debt to RUS, Federal Financing Bank ("FFB"), and CFC under a joint mortgage agreement. The Economic Development Loans are due to RUS and are secured by a portion of the assets pledged by Jackson Energy's consumers.

The interest rates on the notes to CFC are subject to change every seven years from the repricing date for each individual note. The long term debt is due in quarterly and monthly installments of varying amounts through 2040. Jackson Energy has loan funds available from FFB in the amount of \$36,000,000. RUS assesses 12.5 basis points to administer the FFB loans.

The note due National Bank for Cooperatives ("CoBank") is a 15 year note and represents amounts to refinance higher rate RUS loans.

Propane Plus has advanced funds from Cumberland Valley National Bank to open facilities at a new location.

Jackson Energy Cooperative and Subsidiary  
Notes to Financial Statements

**Note 4. Long Term Debt**, continued

Long term debt consists of:

	<u>2019</u>	<u>2018</u>
RUS, cushion of credit earns 5%	(\$3,411,061)	(\$481,950)
Notes due FFB, 2.399% to 4.51%	101,105,206	97,291,071
Economic Development, RUS, 0% interest	2,132,807	2,493,922
Notes due CoBank, 15 years at 3.47%	24,186,228	25,595,099
Notes due CFC:		
6.20% to 6.70%	7,570,903	8,153,179
Refinance RUS loans 6.05%	-	917,859
	<u>131,584,083</u>	<u>133,969,180</u>
Current portion	<u>5,685,000</u>	<u>6,370,000</u>
Long term portion for Jackson Energy	<u>125,899,083</u>	<u>127,599,180</u>
 Fifteen year note to Cumberland Valley National Bank bearing interest at 5.75% and due in monthly installments of \$2,532.	 195,642	 267,645
Current portion	<u>15,000</u>	<u>15,000</u>
Long term portion for Propane Plus	<u>180,642</u>	<u>252,645</u>
Total long term portion	<u><u>\$126,079,725</u></u>	<u><u>\$127,851,825</u></u>

As of February 28, 2019, the annual principal payments of Jackson Energy for the next five years are as follows: 2020 - \$5,700,200; 2021 - \$5,915,000; 2022 - \$6,155,000; 2023 - \$6,410,000; 2023 - \$6,670,000.

**Note 5. Short Term Borrowings**

At February 28, 2019, Jackson Energy had a short term line of credit of \$10,000,000 available from CFC and \$5,000,000 from CoBank. At February 28, 2019 all advances against the CFC line of credit were repaid.

**Note 6. Pension Plan**

All eligible employees of Jackson 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.

Employees hired prior to December 1, 2013 participate in Cost of Living Allowance (“COLA”) benefits for contributions made prior to February 2014 and have a contribution rate of 2.0%. All contributions after February 2014 are not covered by COLA. Employees hired after December 1, 2013 do not participate in COLA and have a contribution rate of 1.7%.

Jackson Energy Cooperative and Subsidiary  
Notes to Financial Statements

**Note 6. Pension Plan, continued**

Jackson's contributions to the R&S Plan in 2019 and 2018 represent less than 5 percent of the total contributions made to the plan by all participating employers. Jackson made contributions to the plan of \$1,804,890 in 2019 and \$1,791,415 in 2018. There have been no significant changes that affect the comparability of 2019 and 2018. During 2012, Jackson Energy purchased ("COLA") benefits for participating employees at a cost of \$2,040,627. This amount is being amortized over 30 years.

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 over 85 percent funded at January 1, 2019 and 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 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 chooses 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 March 15, 2013, the Corporation made a prepayment of \$6,383,300 to the R&S Plan. The amount is being amortized over 16 years. Interest expense associated with the prepayment loan is being accounted for in accordance with the RUS USoA.

Jackson Energy Cooperative and Subsidiary  
Notes to Financial Statements

**Note 6. Pension Plan, continued**

All eligible employees of Jackson Energy participate in the NRECA Retirement and Security Program, a defined contribution pension plan qualified under section 401(k) and tax-exempt under section 501(a) of the Internal Revenue Code. Jackson Energy makes annual contributions to the Program equal to the amounts accrued for pension expense. There have been no significant changes that affect the comparability of 2019 and 2018. Jackson Energy contributed \$154,064 in 2019 and \$151,658 in 2018 to this plan.

Propane Plus has a profit sharing plan of 10% of net profits, before the pension amount, where managers receive 5% of the plan amount and the remaining employees share the remaining 5%. The pension amount for 2019 was \$67,709 and 2018 was \$72,623.

**Note 7. Postretirement Benefits**

Jackson Energy sponsors a defined benefit plan that provides medical insurance coverage to retired employees and their dependents. The plan calls for benefits to be paid at retirement based primarily upon years of service with Jackson Energy. Participating retirees and dependents retiring prior to January 4, 2016 do not contribute to the projected cost of coverage. Participating retirees after January 4, 2016 are provided with a single coverage plan. The following is a reconciliation of the postretirement obligation.

The funded status of the plan is as follows:

	<u>2019</u>	<u>2018</u>
Projected benefit obligation	(\$8,956,515)	(\$8,834,362)
Fair value of plan assets	-	-
Funded status	<u>(\$8,956,515)</u>	<u>(\$8,834,362)</u>

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

	<u>2019</u>	<u>2018</u>
Benefit obligation - beginning of period	\$8,834,362	\$8,840,576
Net periodic benefit cost:		
Service cost	273,061	275,670
Interest cost	400,295	397,686
Net period cost	<u>673,356</u>	<u>673,356</u>
Actuarial adjustments	-	-
Benefit payments for participants	<u>(551,203)</u>	<u>(679,570)</u>
Benefit obligation - end of period	<u>\$8,956,515</u>	<u>\$8,834,362</u>

Amounts included in accumulated other comprehensive income:

Unrecognized actuarial gain (loss)	<u>(\$587,036)</u>	<u>(\$635,612)</u>
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Effect of 1% increase in the health care trend:

Postemployment benefit obligation	\$9,540,000
Net periodic benefit cost	717,000

Projected retiree benefit payments for the next five years are expected to be as follows: 2020 - \$700,000; 2021 - \$711,000; 2022 - \$750,000; 2023 - \$792,000; 2023 - \$835,000.



Jackson Energy Cooperative and Subsidiary  
Notes to Financial Statements

**Note 7. Postretirement Benefits, continued**

The discount rate used in determining the APBO was 4.5% for 2019 and 2018. The health care cost trend rate used to compute the APBO is a 6% annual rate of increase for 2019, and decreasing gradually to 4.5%, they then remain at that level thereafter.

**Note 8. Related Party Transactions**

Several of the Directors of Jackson Energy, its President & CEO, and another employee are on the boards of directors of various associated organizations.

**Note 9. Environmental Contingency**

Jackson Energy, from time to time, is required to work with and handle PCB's, herbicides, automotive fluids, lubricants, and other hazardous materials in the normal course of business. As a result, there is a possibility that environmental conditions may arise which would require Jackson Energy 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 Jackson Energy's financial position or its future cash flows.

**Note 10. Commitments**

Jackson Energy has various 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 11. Contingencies**

Jackson Energy 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.

\* \* \* \* \*

Jackson Energy Cooperative Corporation and Subsidiary  
Consolidating Balance Sheet, February 28, 2019

<u>Assets</u>	<u>Energy</u>	<u>Propane</u>	<u>Eliminations</u>	<u>Consolidated</u>
Net Utility Plant	\$ 167,216,650	\$ 2,876,994		\$ 170,093,644
Investments and Other Assets:				
Associated organizations and others	63,027,152			63,027,152
Goodwill, net of amortization		262,177		262,177
Propane company	4,117,433		(4,117,433)	-
	<u>67,144,585</u>	<u>262,177</u>	<u>(4,117,433)</u>	<u>63,289,329</u>
Current Assets:				
Cash and cash equivalents	7,155,800	585,708		7,741,508
Accounts receivable, less allowance for uncollectible accounts	13,357,983	202,919		13,560,902
Material and supplies, at average cost	1,745,554	449,784		2,195,338
Prepayments	363,824	39,000		402,824
	<u>22,623,161</u>	<u>1,277,411</u>		<u>23,900,572</u>
Deferred Debits	<u>9,448,313</u>			<u>9,448,313</u>
Total	<u>\$ 266,432,709</u>	<u>\$ 4,416,582</u>	<u>\$ (4,117,433)</u>	<u>\$ 266,731,858</u>
<u>Members' Equities and Liabilities</u>				
Members' and Stockholder's Equities:				
Memberships and capital	\$ 1,309,950	\$ 1,293,141	\$ (1,293,141)	\$ 1,309,950
Patronage capital and retained earnings	109,828,384	2,824,292	(2,824,292)	109,828,384
Accum other comprehensive income	(587,036)			(587,036)
Other equities	4,034,195			4,034,195
	<u>114,585,493</u>	<u>4,117,433</u>	<u>(4,117,433)</u>	<u>114,585,493</u>
Long Term Debt	<u>125,899,083</u>	<u>180,642</u>		<u>126,079,725</u>
Accumulated Postretirement Benefits	<u>8,956,515</u>			<u>8,956,515</u>
Current Liabilities:				
Accounts payable	6,481,152	103,507		6,584,659
Short term borrowings	-			-
Current portion of long term debt	5,685,000	15,000		5,700,000
Consumer deposits	817,488			817,488
Accrued expenses	2,680,177			2,680,177
	<u>15,663,817</u>	<u>118,507</u>		<u>15,782,324</u>
Consumer Advances and Others	<u>1,327,801</u>			<u>1,327,801</u>
Total	<u>\$ 266,432,709</u>	<u>\$ 4,416,582</u>	<u>\$ (4,117,433)</u>	<u>\$ 266,731,858</u>

The accompanying notes are an integral part of these statements.

Consolidating Statement of Revenue and Comprehensive Income  
for the year ended February 28, 2019

	<u>Energy</u>	<u>Propane</u>	<u>Eliminations</u>	<u>Consolidated</u>
Operating Revenues	\$ 102,779,487	\$ 4,910,535	\$ (23,862)	\$ 107,666,160
Operating Expenses:				
Cost of purchases	63,139,985	2,392,340		65,532,325
Distribution - operations	4,680,749	1,281,723		5,962,472
Distribution - maintenance	7,400,417			7,400,417
Consumer accounts	2,923,081	290,119		3,213,200
Customer service and information	587,041	40,183		627,224
Administrative and general	4,988,347	158,085	(23,862)	5,122,570
Depreciation, excluding \$635,907 charged to clearing accounts	9,873,534	331,424		10,204,958
Amortization of deferred retirements	470,772			470,772
Interest on long term debt	4,541,143	13,810		4,554,953
Other interest	15,942			15,942
Taxes	134,393	39,518		173,911
Other	141,735			141,735
	<u>98,897,139</u>	<u>4,547,202</u>	<u>(23,862)</u>	<u>103,420,479</u>
Operating Margins	<u>3,882,348</u>	<u>363,333</u>		<u>4,245,681</u>
Nonoperating Margins:				
Interest income	144,788	1,587		146,375
Subsidiary and others	267,489	29,275	(394,195)	(97,431)
	<u>412,277</u>	<u>30,862</u>	<u>(394,195)</u>	<u>48,944</u>
Patronage Capital, associated organizations				
G&T capital credits	3,291,092			3,291,092
Other capital credits	178,275			178,275
	<u>3,469,367</u>	<u>-</u>	<u>-</u>	<u>3,469,367</u>
Net Margins	7,763,992	394,195	(394,195)	7,763,992
Other Comprehensive Income:				
Postretirement benefits	48,576			48,576
Total Comprehensive Income	<u>\$ 7,812,568</u>	<u>\$ 394,195</u>	<u>\$ (394,195)</u>	<u>\$ 7,812,568</u>

The accompanying notes are an integral part of these statements.

**ALAN M. ZUMSTEIN**  
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MEMBER  
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• KENTUCKY SOCIETY OF CPA'S  
• AICPA DIVISION FOR FIRMS

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  
Jackson Energy Cooperative Corporation  
McKee, Kentucky

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 consolidated financial statements of Jackson Energy Cooperative Corporation and Subsidiary ("the Cooperative"), as of and for the year ended February 28, 2019 and 2018, and the related notes to the consolidated financial statements, which collectively comprise the Cooperative's basic consolidated financial statements, and have issued my report thereon dated May 14, 2019.

**Internal Control Over Financial Reporting**

In planning and performing my audit of the financial statements, I 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 my opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control. Accordingly, I 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 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 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 and, therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during my audit I did not identify any deficiencies in internal control that I consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

To the Board of Directors  
Jackson Energy Cooperative Corporation

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Cooperative's financial statements are free of material misstatement, I 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 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**

The purpose of this report is solely to describe the scope of my testing on internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the organization'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 organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Alan Zumstein*

Alan M. Zumstein, CPA  
May 14, 2019

**ALAN M. ZUMSTEIN**  
**CERTIFIED PUBLIC ACCOUNTANT**

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

Board of Directors  
Jackson Energy Cooperative Corporation  
McKee, Kentucky

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 Jackson Energy Cooperative Corporation ("the Cooperative"), which comprise the balance sheet as of February 28, 2019, and the related statements of revenue and comprehensive income, changes in members' equities, 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 May 14, 2019. In accordance with *Government Auditing Standards*, we have also issued my report dated May 14, 2019, 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 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;

Board of Directors  
Jackson Energy Cooperative Corporation

- 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, which are listed below.

The deferred debits are as follows:

Deferred property retirements	\$3,648,489
Past service pension benefits	1,553,144
Accelerated pension benefit payment	<u>4,246,680</u>
	<u><u>\$9,448,313</u></u>

The deferred credits are as follows:

Consumer advances for construction	\$376,072
Joint use attachments paid in advance	<u>951,729</u>
	<u><u>\$1,327,801</u></u>

Jackson Energy is a 100% owner of a subsidiary, Jackson Energy Propane Plus, LLC, which is engaged in the distribution sales of propane gas in and around the areas in which the Cooperative provides electric service and other areas in southeastern Kentucky. The investment is accounted for using the equity method of accounting. The original investment was \$7,500. The investment is as follows:

	<u>Investment</u>	<u>Profits</u>
Beginning balance	\$2,526,836	\$1,205,826
Activity for 2019	<u>-</u>	<u>384,771</u>
Ending balance	<u><u>\$2,526,836</u></u>	<u><u>\$1,590,597</u></u>

The purpose of this report is solely to communicate, in connection with the audit of the financial statements, on compliance with aspects of contractual agreements and the regulatory requirements for electric borrowers based on the requirements of 7 CFR Part 1773, Policy on Audits of Rural Utilities Service Borrowers and Grantees. Accordingly, this report is not suitable for any other purpose.

*Alan Zumstein*

Alan M. Zumstein, CPA  
May 14, 2019