

Warren Rural Electric Cooperative Corporation

FINANCIAL STATEMENTS AND SUPPLEMENTARY INFORMATION

June 30, 2019 and 2018



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Warren Rural Electric Cooperative Corporation
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June 30, 2019 and 2018

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REPORT





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Independent Auditors' Report

Board of Directors
Warren Rural Electric Cooperative Corporation
Bowling Green, Kentucky

Report on the Consolidated Financial Statements

We have audited the accompanying consolidated financial statements of the Warren Rural Electric Cooperative Corporation and subsidiaries (the "Cooperative"), which comprise the consolidated balance sheets as of June 30, 2019 and 2018, and the related consolidated statements of income, equities, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated 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.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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 auditors' 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, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Cooperative as of June 30, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Other Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The information in the consolidating statements is presented for purposes of additional analysis, and it 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 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 consolidated 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 our opinion, the information is fairly stated, in all material respects in relation to the consolidated financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 22, 2019, on our consideration of the Cooperative's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Cooperative's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Cooperative's internal control over financial reporting and compliance.

Carr, Riggs & Ingram, L.L.C.

CARR, RIGGS & INGRAM, LLC
Bowling Green, Kentucky
October 22, 2019



FINANCIAL STATEMENTS

Warren Rural Electric Cooperative Corporation
Consolidated Balance Sheets

<i>June 30,</i>	2019	2018
Assets		
Utility plant		
Plant in service	\$ 323,255,457	\$ 300,103,931
Construction in progress	14,757,812	19,017,260
Less accumulated depreciation	(145,374,624)	(137,009,202)
Net utility plant	192,638,645	182,111,989
Other property and investments		
Non-utility plant, net of accumulated depreciation	1,033,194	959,886
Investments in associated companies	2,129,930	2,134,371
Other investments	422,313	385,380
Goodwill	503,260	503,260
Total other property and investments	4,088,697	3,982,897
Current assets		
Cash and cash equivalents	20,507,308	20,724,345
Accounts receivable, net of allowance	15,141,963	16,095,395
Other accounts receivable	1,522,048	869,466
Materials and supplies	3,857,737	3,835,060
Prepaid expenses	1,149,882	1,105,659
Total current assets	42,178,938	42,629,925
Other assets		
TVA Energy Services loans receivable	3,106	4,090
Deferred debits	868,490	682,267
Total other assets	871,596	686,357
Total assets	\$ 239,777,876	\$ 229,411,168

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

Warren Rural Electric Cooperative Corporation
Consolidated Balance Sheets

<i>June 30,</i>	2019	2018
Equities and Liabilities		
Equities		
Membership fees	\$ 567,660	\$ 561,165
Patronage capital	109,339,632	107,226,956
Other equities	107,634	107,629
Total equities	110,014,926	107,895,750
Long-term liabilities		
Long-term debt - net of current portion	81,939,748	75,566,151
Accrued post-retirement benefits	4,711,098	4,149,047
Total other liabilities	86,650,846	79,715,198
Current liabilities		
Accounts payable - purchased power	24,430,213	25,583,492
Accounts payable - other	3,630,552	2,236,350
Self-insured fund	280,444	248,136
Customer deposits	4,012,398	3,837,128
Accrued interest	149,377	164,228
Accrued vacation and sick leave	1,515,516	1,577,293
Current portion of post-retirement liability	469,000	350,000
Accrued taxes and other current liabilities	1,836,476	1,955,492
Current portion of long-term debt	5,467,461	4,722,269
Total current liabilities	41,791,437	40,674,388
Other liabilities		
Advances for TVA Energy Services loans	2,759	3,741
Deferred income taxes	180,686	138,631
Deferred credits	1,137,222	983,460
Total other liabilities	1,320,667	1,125,832
Total equities and liabilities	\$ 239,777,876	\$ 229,411,168

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

Warren Rural Electric Cooperative Corporation
Consolidated Statements of Income

<i>For the years ended June 30,</i>	2019	2018
Operating revenues		
Electric sales	\$ 196,361,987	\$ 193,972,883
Forfeited discounts	1,159,059	1,133,704
Rent from electric property	2,273,486	2,101,101
Other electric revenues	658,534	625,043
Natural gas sales	683,254	739,886
Propane and related sales	2,944,898	2,908,749
Total operating revenue	204,081,218	201,481,366
Purchased power and expenses		
Purchased power	151,632,183	149,844,707
Operation	7,295,290	6,929,300
Maintenance	6,805,954	6,956,436
Facilities rental	103,011	100,161
Customer accounts	3,321,740	3,393,047
Customer service and information	727,007	675,195
Administrative and general	6,540,215	5,818,476
Depreciation and amortization	10,397,641	9,666,261
Taxes and tax equivalents	5,576,102	5,530,426
Natural gas purchases	437,911	460,264
Propane gas and related cost of goods sold	1,478,620	1,480,323
Total purchased power and expenses	194,315,674	190,854,596
Total operating income	9,765,544	10,626,770
Other revenues		
Interest income	111,354	166,965
Income of unconsolidated entities	133	147
Miscellaneous	286,192	325,768
Total other revenues	397,679	492,880
Other deductions		
Interest on long-term debt	3,373,118	3,285,598
Post-retirement benefits	469,000	350,000
Loss from disposition of utility plant	4,010,836	-
Total other deductions	7,852,954	3,635,598

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

Warren Rural Electric Cooperative Corporation
Consolidated Statements of Income

<i>For the years ended June 30,</i>	2019	2018
Income before income taxes	2,310,269	7,484,052
Income tax expense	197,593	165,581
Net Income	\$ 2,112,676	\$ 7,318,471

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

Warren Rural Electric Cooperative Corporation
Consolidated Statements of Equities

For the years ended June 30, 2019 and 2018

	Memberships	Patronage Capital	Other Equities	Total Equities
Balance - July 1, 2017	\$ 551,605	\$ 99,908,485	\$ 107,658	\$ 100,567,748
Net income for the year	-	7,318,471	-	7,318,471
Investment from (returned to) members	9,560	-	(29)	9,531
Balance - June 30, 2018	561,165	107,226,956	107,629	107,895,750
Net income for the year	-	2,112,676	-	2,112,676
Investment from members	6,495	-	5	6,500
Balance, June 30, 2019	\$ 567,660	\$ 109,339,632	\$ 107,634	\$ 110,014,926

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

Warren Rural Electric Cooperative Corporation
Consolidated Statements of Cash Flows

<i>For the years ended June 30,</i>	2019	2018
Cash flows from operating activities		
Net income	\$ 2,112,676	\$ 7,318,471
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	10,397,641	9,666,261
Loss on disposition of utility plant	4,010,836	-
(Increase) decrease in assets:		
Receivables	300,850	(2,124,716)
Materials and supplies	(22,677)	(851,687)
Prepaid expenses	(44,223)	83,864
Other assets	(185,239)	(187,391)
Increase (decrease) in liabilities:		
Accounts payable	240,923	1,841,553
Customer deposits	175,270	268,395
Accrued expenses and other liabilities	(10,556)	284,914
Accretion in post-retirement benefit obligation	681,051	459,508
Provision for deferred income taxes	42,055	(109,424)
Total adjustments	15,585,931	9,331,277
Net cash provided by operating activities	17,698,607	16,649,748
Cash flows from investing activities		
Additions to utility plant, net of disposals	(25,008,441)	(24,943,722)
Purchase of other investments	(36,933)	(75,629)
Change in investment in associated organizations	4,441	6,204
Net cash used in investing activities	(25,040,933)	(25,013,147)
Cash flows from financing activities		
Proceeds from long-term debt	12,000,000	13,000,000
Payments on principal of long-term debt	(4,881,265)	(4,423,356)
Use of RUS cushion of credit	54	108,104
Investment from members	6,500	9,531
Net cash provided by financing activities	7,125,289	8,694,279

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

Warren Rural Electric Cooperative Corporation
Consolidated Statements of Cash Flows

<i>For the years ended June 30,</i>	2019	2018
Increase (decrease) in cash and cash equivalents	(217,037)	330,880
Cash and cash equivalents – beginning of year	20,724,345	20,393,465
Cash and cash equivalents – end of year	\$ 20,507,308	\$ 20,724,345

Supplemental disclosures of cash flow information:

Cash paid during the year for interest	\$ 3,387,969	\$ 3,298,552
Cash paid for income taxes, net	\$ 198,855	\$ 22,576

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

Warren Rural Electric Cooperative Corporation Notes to Consolidated Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Warren Rural Electric Cooperative Corporation (“WRECC”) and its subsidiaries (hereinafter referred to collectively as “the Cooperative”) were organized under Kentucky laws and exist for the purpose of distributing various utility services to its members, primarily in south central Kentucky. Counties included in its service area include Warren, Simpson, Butler, Ohio, Grayson, Logan, Edmonson, and Barren.

Measuring Focus, Basis of Accounting, and Financial Statement Presentation

The Cooperative's consolidated financial statements are presented on the full accrual basis of accounting. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.

The accounting policies of the Cooperative are in accordance with the system of accounts prescribed by the United States Department of Agriculture, the Rural Utility Service (RUS) and the Tennessee Valley Authority (TVA), which do not differ materially from accounting principles generally accepted in the United States of America.

The consolidated financial statements include the accounts of WRECC and its wholly-owned for-profit subsidiaries, Propane Energy Service, Inc. (“PES”) and Millennium Energy, Inc. (“Millennium”). PES is involved with propane distribution and Millennium is a natural gas distributor. All significant intercompany activity has been eliminated in consolidation.

Through the business of providing services to customers, nearly all of whom are regional residents, the Cooperative grants credit to those customers, which is basically unsecured. This results in the Cooperative incurring monthly losses associated with uncollectible accounts and is reflected in the Cooperative’s operating expenses.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Estimates and assumptions are reviewed periodically and the effects of revisions are reflected in the consolidated financial statements in the period that are determined to be necessary. Actual results could differ from the estimates.

Warren Rural Electric Cooperative Corporation Notes to Consolidated Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Concentrations of Credit Risk

Financial instruments that potentially subject the Cooperative to concentrations of credit risk consist principally of cash deposits and accounts receivable. The Cooperative maintains its cash balances in institutions whose deposits are covered by the FDIC. Deposits are insured up to \$250,000 per financial institution. At June 30, 2019 and 2018, the Cooperative had deposits of \$1,439,737 and \$2,015,836 in excess of the FDIC insured amount, respectively. The Cooperative has a geographical concentration in accounts receivable because most of the balances are due from individuals and businesses located in the same geographical region.

Cash and Cash Equivalents

For the purposes of the statements of cash flows, the Cooperative considers all liquid investments with original maturities of three months or less to be cash equivalents. At June 30, 2019 and 2018, cash equivalents consisted primarily of commercial paper and repurchase agreements.

Accounts Receivable

Accounts receivable result from unpaid billings and accrued unbilled amounts for service to customers and from unpaid billings related to work performed or materials sold to certain entities. Accounts receivable are stated at amounts expected to be collected from customers, less an allowance for uncollectible accounts that includes unpaid balances in excess of 90 days plus an additional amount based on management's estimation of future doubtful accounts. The allowance for doubtful accounts was \$4,652,457 and \$4,454,874 at June 30, 2019 and 2018, respectively.

Utility bills are due 15 days after the billing date, with a 5% penalty assessed for late payments. A cut-off notice is sent, allowing the customer seven days to pay before their service is disconnected. The customer then has five days to pay before the meter is read and entered to create a final bill. A collection letter is sent if the account remains unpaid after the due date of the final bill. A second collection letter is sent after ten days. The account is turned over to a collection agency ten days after the issuance of the second collection letter.

Materials and Supplies

All materials and supplies inventories are valued at average cost. WRECC performs semi-annual physical inventory counts.

Prepaid Expenses

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in the consolidated financial statements.

Warren Rural Electric Cooperative Corporation Notes to Consolidated Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Utility Plant and Depreciation Procedures

Utility plant, which includes property, plant, equipment, and construction in progress, is stated at original cost and includes direct labor, materials, overhead, and special services (contract labor, etc.). Work orders are used to accumulate these costs, which are closed into plant when complete. Replacing only part of an installation is considered a repair and charged to maintenance expense.

Depreciation expense is computed on the composite-rate method at rates recommended by TVA and RUS. Retirements of property from service have been charged to the accumulated provision for depreciation accounts at the original cost of the units plus cost of removal. Salvage value of the units retired is returned to inventory.

Investments in Associated Enterprises

Investments in other cooperative's equities are carried at cost plus the Cooperative's share of allocated equities. Capital term certificates issued by the National Rural Utilities Cooperative Finance Corporation (CFC) are required investments for cooperatives that borrow funds from CFC. The required investment amount is based on a predetermined formula. Since there is not a market for these securities, management has determined that it is not practicable to estimate the fair value of these investments.

The Cooperative has a 50% investment in Penwar, Inc., which is accounted for under the equity method. Penwar provides billing and collection services for the Cooperative and one other electric utility. The Cooperative's share of income from Penwar for the years ended June 30, 2019 and 2018 was \$133 and \$147, respectively.

Goodwill

The Cooperative's goodwill represents the excess of the purchase price over the fair value of assets acquired in business combinations. Goodwill is evaluated annually for impairment, or whenever impairment indicators arise.

Compensated Absences

It is the Cooperative's policy to permit employees to accumulate earned but unused personal benefits. Personal leave earned by employees is accrued based on years of continuous service. All personal leave pay has been accrued and is reflected as a liability in the consolidated financial statements. When an employee ceases to be employed, all benefits shall cease to accrue.

Unearned Revenue

Unearned revenue arises when assets are recognized before revenue recognition criteria have been satisfied.

Warren Rural Electric Cooperative Corporation Notes to Consolidated Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Revenues and Purchased Power

Revenues are recognized for power delivered but unbilled at the end of each month, which coincides with billings from TVA for purchased power in the month delivered.

Income Taxes and Uncertain Tax Positions

WRECC is exempt from income taxes under section 501(c)12 of the Internal Revenue Code and applicable state laws and regulations. For the Cooperative's wholly-owned, for-profit enterprises, income taxes are provided for the tax effects of transactions reported in the consolidated financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the bases of certain assets and liabilities for financial statement and income tax reporting. The deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled.

It is the Cooperative's policy to recognize interest and penalties related to income taxes in income tax expense, when applicable.

As of June 30, 2019 and 2018, the Cooperative believes it has no uncertain tax positions that qualify for either recognition or disclosure in the financial statements.

Reclassification

Certain amounts in the 2018 financial statements have been reclassified to conform to the 2019 presentation. The reclassification did not have any effect on the change in equity for 2018.

Subsequent Events

The Cooperative has evaluated any recognized or unrecognized subsequent events for consideration in the accompanying consolidated financial statements through October 22, 2019, which was the date the consolidated financial statements were made available.

Warren Rural Electric Cooperative Corporation
Notes to Consolidated Financial Statements

NOTE 2: INVESTMENTS

Investments in Associated Enterprises

The Cooperative had the following investments in associated enterprises at June 30, 2019 and 2018:

<i>June 30,</i>	2019	2018
CFC capital term certificates	\$ 2,083,880	\$ 2,090,525
Penwar, Inc.	45,050	42,846
Co-Bank stock	1,000	1,000
	<u>\$ 2,129,930</u>	<u>\$ 2,134,371</u>

Investments in Subsidiaries

WRECC holds investments in two wholly-owned for-profit entities, PES and Millennium. PES is involved with propane distribution and Millennium is a natural gas distributor. For the years ended June 30, 2019 and 2018, PES reported a net income after tax of \$331,904 and \$367,185, respectively. For the years ended June 30, 2019 and 2018, Millennium reported a net income after tax of \$24,738 and \$112,004, respectively.

NOTE 3: UTILITY PLANT

Utility plant at June 30, 2019 and 2018 is summarized as follows:

<i>June 30,</i>	2019	2018
Electric plant in service:		
Transmission plant	\$ 27,987,381	\$ 27,630,661
Distribution plant	263,798,531	242,685,041
General plant	31,469,545	29,788,229
Total electric plant in service	<u>323,255,457</u>	300,103,931
Construction work in progress	14,757,812	19,017,260
Total utility plant	<u>338,013,269</u>	319,121,191
Accumulated depreciation	<u>(145,374,624)</u>	(137,009,202)
Net utility plant	<u>\$ 192,638,645</u>	<u>\$ 182,111,989</u>

Warren Rural Electric Cooperative Corporation
Notes to Consolidated Financial Statements

NOTE 3: UTILITY PLANT (CONTINUED)

Depreciation rates have been applied to the general plant, distribution plant, and transmission plant on a straight-line basis ranging as follows:

General Plant	3.00% to 20.00%
Distribution Plant	2.50% to 6.70%
Transmission Plant	2.75% to 3.34%

NOTE 4: LINES OF CREDIT

The Cooperative has a line of credit for \$8,000,000 with CFC that renews annually each year unless terminated by either party. The note has a variable interest rate and is unsecured. The Cooperative also has a revolving line of credit with Co-Bank for \$1,000,000 that also has a variable interest rate and is unsecured. There were no outstanding balances against either of these notes at June 30, 2019 or 2018.

NOTE 5: LONG-TERM DEBT

At June 30, 2019 and 2018, long-term debt consisted of the following:

<i>June 30,</i>	2019	2018
Mortgage notes payable to CFC due in quarterly installments ranging from approximately \$3,000 to \$728,000 including interest at fixed rates ranging from 4.15% to 6.15%, maturing August 2019 through August 2034; secured by all assets.	\$ 38,804,567	\$ 42,434,376
Mortgage notes payable to Federal Financing Bank, RUS, due in quarterly installments of approximately \$579,000 including interest at fixed rates ranging from 2.65% to 6.14%, maturing March 2028 through December 2047; secured by all assets.	35,942,557	36,984,736
Mortgage notes payable to CoBank due in monthly installments of approximately \$95,000 including interest at rates ranging from 3.26% to 3.76%, maturing December 2021 through 2034; secured by all assets not otherwise securing pre-existing loans.	12,660,087	869,366
Total long-term debt	87,407,211	80,288,478
Less current maturities	5,467,461	4,722,269
Less RUS cushion of credit	2	58
Net long-term debt	\$ 81,939,748	\$ 75,566,151

Warren Rural Electric Cooperative Corporation
Notes to Consolidated Financial Statements

NOTE 5: LONG-TERM DEBT (CONTINUED)

The provisions of the mortgage notes payable place certain restrictions and limitations upon the Cooperative. These include maintenance of certain financial ratios, as well as restrictions or limitations on the payment of distributions, rentals of property, and additional borrowings. The Cooperative was in compliance with these covenants at June 30, 2019 and 2018.

The annual debt service requirements of principal to maturity at June 30 are as follows:

<i>For the year ending June 30,</i>	
	Principal
2020	\$ 5,467,461
2021	5,688,532
2022	6,552,335
2023	6,135,690
2024	5,689,886
Thereafter	57,873,305
Total	\$ 87,407,209

NOTE 6: DEFERRED DEBITS AND CREDITS

The Cooperative's deferred debits and credits as presented in the balance sheets consisted of the following items:

<i>June 30,</i>	2019	2018
Deferred debits:		
Computer software, amortized over 1 to 5 years	\$ 494,580	\$ 415,916
WRECC rebate program	373,910	257,571
Transportation overhead clearing	-	8,780
	\$ 868,490	\$ 682,267
Deferred credits:		
Refundable contributions	\$ 561,366	\$ 447,662
Unearned revenue	195,085	148,064
Advance receipts of subdivision street light assessments	380,771	387,734
	\$ 1,137,222	\$ 983,460

Warren Rural Electric Cooperative Corporation Notes to Consolidated Financial Statements

NOTE 7: INCOME TAXES

On December 22, 2017, comprehensive tax reform legislation known as the Tax Cuts and Jobs Act (the "Tax Reform Act") was signed into law. The Tax Reform Act amends the Internal Revenue Code to reduce U.S. tax rates and modify policies, credits, and deductions for individuals and businesses.

The Tax Reform Act permanently reduces the U.S. federal corporate income tax rate from 34% to 21%, effective for tax years beginning after 2017. GAAP requires an adjustment to deferred taxes as a result of a change in the corporate tax rate in the period that change in enacted, with the change recorded to the current year tax provision. Accordingly, the Cooperative has re-measured its deferred tax assets and liabilities at the new tax rate and recorded a one-time noncash tax benefit of \$78,092 to deferred income taxes for the year ended June 30, 2018. This benefit resulted from the Cooperative's lower effective tax rate for that year.

The provision for income taxes for the years ended June 30, 2019 and 2018 consisted of the following:

<i>For the years ended June 30,</i>	2019	2018
Current tax expense	\$ 155,538	\$ 275,005
Deferred taxes	42,055	(109,424)
Total	\$ 197,593	\$ 165,581

The Cooperative has net deferred tax liabilities of \$180,686 and \$138,631 at June 30, 2019 and 2018, respectively, primarily related to the use of accelerated methods of depreciation of property and equipment for income tax purposes.

NOTE 8: RETIREMENT PLANS

Defined Benefit Pension Plan

The Cooperative participates in the National Rural Electrification Cooperative Association (NRECA) Retirement Security Plan (RS Plan). The NRECA RS Plan is a defined benefit pension plan qualified under Section 401 and tax-exempt under Section 501 (a) of the Internal Revenue Code. It is a multi-employer plan under accounting standards. The plan sponsor's Employer Identification Number is 53-0116145 and the Plan Number is 333.

A unique characteristic of a multi-employer plan compared 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.

Warren Rural Electric Cooperative Corporation Notes to Consolidated Financial Statements

NOTE 8: RETIREMENT PLANS (CONTINUED)

The Cooperative made contributions to the plan of \$2,327,634 for the year ended June 30, 2019, and \$2,146,907 for the year ended June 30, 2018. There have been no significant changes that affect the comparability of 2019 and 2018 contributions.

In the RS Plan, a "zone status" determination is not required, and therefore, not determined, under the Pension Protection Act (PPA) of 2006. In addition, the accumulated benefit obligations and plan assets are not determined or allocated separately by individual employer. In total, the Retirement Security Plan was approximately 95 percent funded on January 1, 2018, and approximately 97 percent funded on January 1, 2017, based on the PPA funding target and PPA actuarial value of assets on those dates.

Because the provisions of the PPA do not apply to the RS Plan, funding improvement plans and surcharges are not applicable. Future contribution requirements are determined each year as part of the actuarial valuation of the plan and may change as a result of plan experience. The Cooperative's normal retirement age is 62.

Deferred Compensation Retirement Plans

The Cooperative has a 401(k) plan which is available to all employees who have completed one month of service. The Cooperative contributes 1% of the employees' base pay if the employee contributes 4%.

For employees hired after January 1, 2014, the Cooperative contributes 1% of the employee's base salary. In addition, the Cooperative will provide a matching contribution of 3% if the employee contributes 4% of his/her base pay.

The Cooperative made contributions to the plan of \$157,401 for 2019 and \$117,362 for 2018.

The Cooperative also has a 457(b) Plan which is administered by Homestead Funds. The Plan is for management or highly compensated employees of the Cooperative. The Plan is for participant contributions only; the Cooperative does not contribute. The Plan's assets will remain solely the property of the Cooperative, subject only to the claims of the Cooperative's creditors until made available to the participant or beneficiary of the Plan's assets. Amounts at June 30, 2019 and 2018 were \$419,967 and \$383,034, respectively.

NOTE 9: POSTRETIREMENT HEALTHCARE BENEFITS

The Cooperative provides certain healthcare benefits for retired employees hired prior to January 1, 2014. In order to receive retiree medical and dental benefits, an employee must be at least 55 years of age, with a minimum of 5 years of service, and the sum of age plus years of service must be at least 75. The Cooperative will pay up to five years of benefits for the retiree, or until age 65 is attained. Employees hired after January 1, 2014, will not be eligible for postretirement healthcare benefits.

Warren Rural Electric Cooperative Corporation
Notes to Consolidated Financial Statements

NOTE 9: POSTRETIREMENT HEALTHCARE BENEFITS (CONTINUED)

The annual measurement date is July 1 for the postretirement benefits. The following summarizes the postretirement benefits plan for the years ended June 30, 2019 and 2018.

<i>For the year ended June 30,</i>	2019	2018
Reconciliation of funded status		
Benefit obligation at June 30	\$ 4,760,131	\$ 4,115,013
Fair value of plan assets at June 30	-	-
Unfunded benefit obligation	<u>\$ 4,760,131</u>	<u>\$ 4,115,013</u>
Benefits paid	\$ 4,790	\$ 109,732
Employer contributions	\$ 4,790	\$ 109,732
Reconciliation of net periodic benefit cost		
Net loss	\$ 106,229	\$ 100,892
Prior service cost	148,881	158,386
Interest cost	187,234	160,548
Net periodic benefit cost	<u>\$ 442,344</u>	<u>\$ 419,826</u>

The weighted average assumptions used in the accounting for the Cooperative's postretirement benefit plan was as follows:

<i>For the year ended June 30,</i>	2019	2018
Discount rate	3.50%	4.15%

The following benefit payments, which reflect expected future service, as appropriate, as expected to be paid:

<i>For the year ending June 30,</i>	
2020	\$ 469,000
2021	418,000
2022	332,000
2023	356,000
2024	477,000
Thereafter	1,956,000
<hr/>	
Total	<u>\$ 4,008,000</u>

Warren Rural Electric Cooperative Corporation Notes to Consolidated Financial Statements

NOTE 10: SELF-INSURANCE

The Cooperative is self-insured for a significant portion of its employee healthcare claims. During 2019 and 2018, the Cooperative paid claims of \$3,569,541 and \$3,073,141, respectively. Management has recorded an estimate for an amount it considers reasonable related to its obligation for claims incurred but not reported as of year-end. At June 30, 2019 and 2018, the Cooperative had accrued \$280,444 and \$248,136, respectively, for these projected claims.

NOTE 11: COMMITMENTS

The Cooperative has a wholesale power contract with Tennessee Valley Authority (TVA) whereby the electric system purchases all of its electric power from TVA. The rates paid for such purchases are subject to review periodically. A five-year notice to TVA is required to terminate the contract.

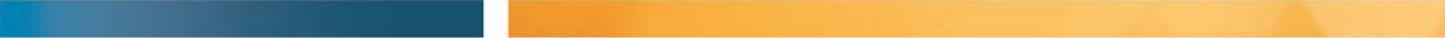
On October 8, 2015, the Cooperative signed a five-year contract with A&G Tree Service for right-of-way clearing services. After one contract amendment dated January 15, 2019, the contract price totaled \$8,732,230. As of June 30, 2019, the Cooperative has one year remaining on the contract, totaling \$1,816,588 for services provided between July 1, 2019 and June 30, 2020.

On August 21, 2017, the Cooperative signed a contract with Tantalus for the installation of network equipment and services for the Cooperative's advanced metering infrastructure ("AMI") installation and deployment. After two contract amendments, dated September 29, 2017 and December 6, 2017, the contract price totaled \$9,834,981. As of June 30, 2019, the Cooperative had a remaining balance of \$559,296 to pay on the contract for services to be provided. Management expects the AMI system to be fully functional by June 30, 2020.

On November 15, 2017, the Cooperative secured a loan commitment with CoBank for \$20,000,000. The loan commitment expires December 31, 2021. As of June 30, 2019, the Cooperative has borrowed \$12,000,000 of the \$20,000,000 loan commitment.

On December 21, 2017, the Cooperative secured a loan commitment with National Rural Utilities Cooperative Finance Corporation ("CFC") for \$20,000,000, available to be drawn down over a period of 5 years. As of June 30, 2019, the Cooperative has not borrowed any of the available funds.

On March 1, 2019, the Cooperative signed a two-year contract with Ervin Cable Construction for the installation of 400 linear miles of fiber optic backbone. The contract is for approximately \$4,500,000.



Warren Rural Electric Cooperative Corporation Notes to Consolidated Financial Statements

NOTE 12: RISK MANAGEMENT

The Cooperative is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. During the years ended June 30, 2019 and 2018, the Cooperative purchased commercial insurance for all of the above risks. The Cooperative is involved in lawsuits from time to time, which are considered to be in the normal course of business. In the opinion of management, based on information furnished by counsel, the ultimate liability, if any, will have no material effect on the financial position of the Cooperative.

Warren Rural Electric Cooperative Corporation
Consolidating Balance Sheets

<i>June 30, 2019</i>	WRECC	PES	Millennium	Eliminations	Total
Assets					
Utility plant					
Plant in service	\$ 323,255,457	\$ -	\$ -	\$ -	\$ 323,255,457
Construction in progress	14,757,812	-	-	-	14,757,812
Less accumulated depreciation	(145,374,624)	-	-	-	(145,374,624)
Net utility plant	192,638,645	-	-	-	192,638,645
Other property and investments					
Non-utility plant, net of accumulated	-	603,177	430,017	-	1,033,194
Investments in associated companies	5,729,030	-	-	(3,599,100)	2,129,930
Other investments	422,313	-	-	-	422,313
Goodwill	503,260	-	-	-	503,260
Total other property and investments	6,654,603	603,177	430,017	(3,599,100)	4,088,697
Current assets					
Cash and cash equivalents	17,777,748	1,817,213	912,347	-	20,507,308
Accounts receivable, net of allowance	15,014,135	99,086	27,628	1,114	15,141,963
Other accounts receivable	1,522,048	-	-	-	1,522,048
Materials and supplies	3,761,287	91,402	5,048	-	3,857,737
Prepaid expenses	1,074,138	59,302	16,442	-	1,149,882
Total current assets	39,149,356	2,067,003	961,465	1,114	42,178,938
Other assets					
TVA Energy Services loans receivable	3,106	-	-	-	3,106
Deferred debits	868,490	-	-	-	868,490
Total other assets	871,596	-	-	-	871,596
Total assets	\$ 239,314,200	\$ 2,670,180	\$ 1,391,482	\$ (3,597,986)	\$ 239,777,876

Warren Rural Electric Cooperative Corporation
Consolidating Balance Sheets

<i>June 30, 2019</i>	WRECC	PES	Millennium	Eliminations	Total
Equities and Liabilities					
Equities					
Membership fees	\$ 567,660	\$ -	\$ -	\$ -	\$ 567,660
Patronage capital	109,339,632	-	-	-	109,339,632
Other equities	107,634	2,357,591	1,241,509	(3,599,100)	107,634
Total equities	110,014,926	2,357,591	1,241,509	(3,599,100)	110,014,926
Long-term liabilities					
Long-term debt - net of current portion	81,939,748	-	-	-	81,939,748
Accrued post-retirement benefits	4,711,098	-	-	-	4,711,098
Total other liabilities	86,650,846	-	-	-	86,650,846
Current liabilities					
Accounts payable - purchased power	24,430,213	-	-	-	24,430,213
Accounts payable - other	3,576,017	13,780	39,641	1,114	3,630,552
Self-insured fund	280,444	-	-	-	280,444
Customer deposits	4,005,068	-	7,330	-	4,012,398
Accrued interest	149,377	-	-	-	149,377
Accrued vacation and sick leave	1,515,516	-	-	-	1,515,516
Current portion of post-retirement liability	469,000	-	-	-	469,000
Accrued taxes and other current liabilities	1,810,436	16,594	9,446	-	1,836,476
Current portion of long-term debt	5,467,461	-	-	-	5,467,461
Total current liabilities	41,703,532	30,374	56,417	1,114	41,791,437

Warren Rural Electric Cooperative Corporation
Consolidating Balance Sheets

<i>June 30, 2019</i>	WRECC	PES	Millennium	Eliminations	Total
Other liabilities					
Advances for TVA Energy Services loans	2,759	-	-	-	2,759
Deferred income taxes	-	87,130	93,556	-	180,686
Deferred credits	942,137	195,085	-	-	1,137,222
Total other liabilities	944,896	282,215	93,556	-	1,320,667
Total equities and liabilities	\$ 239,314,200	\$ 2,670,180	\$ 1,391,482	\$ (3,597,986)	\$ 239,777,876

Warren Rural Electric Cooperative Corporation
Consolidating Statements of Income

For the year ended June 30, 2019

	WRECC	PES	Millennium	Eliminations	Total
Operating Revenues					
Electric sales	\$ 196,361,987	\$ -	\$ -	\$ -	\$ 196,361,987
Forfeited discounts	1,159,059	-	-	-	1,159,059
Rent from electric property	2,273,486	-	-	-	2,273,486
Other electric revenues	658,534	-	-	-	658,534
Natural gas sales	-	-	683,254	-	683,254
Propane and related sales	-	2,944,898	-	-	2,944,898
Total operating revenue	200,453,066	2,944,898	683,254	-	204,081,218
Purchased power and expenses					
Purchased power	151,632,183	-	-	-	151,632,183
Operation	6,523,773	729,926	41,591	-	7,295,290
Maintenance	6,804,523	-	1,431	-	6,805,954
Facilities rental	103,011	-	-	-	103,011
Customer accounts	3,321,740	-	-	-	3,321,740
Customer service and information	726,099	-	908	-	727,007
Administrative and general	6,383,025	100,543	56,647	-	6,540,215
Depreciation and amortization	10,227,424	132,632	37,585	-	10,397,641
Taxes and tax equivalents	5,462,735	57,716	55,651	-	5,576,102
Natural gas purchases	-	-	437,911	-	437,911
Propane gas and related cost of goods sold	-	1,478,620	-	-	1,478,620
Total purchased power and expenses	191,184,513	2,499,437	631,724	-	194,315,674
Total operating income	9,268,553	445,461	51,530	-	9,765,544

Warren Rural Electric Cooperative Corporation
Consolidating Statements of Income

<i>For the year ended June 30, 2019</i>	WRECC	PES	Millennium	Eliminations	Total
Other revenues					
Interest income	95,066	15,904	384	-	111,354
Income of unconsolidated entities	133	-	-	-	133
Miscellaneous	601,878	33,631	7,325	(356,642)	286,192
Total other revenues	697,077	49,535	7,709	(356,642)	397,679
Other deductions					
Interest on long-term debt	3,373,118	-	-	-	3,373,118
Post-retirement benefits	469,000	-	-	-	469,000
Loss from disposition of utility plant	4,010,836	-	-	-	4,010,836
Total other deductions	7,852,954	-	-	-	7,852,954
Income before income taxes	2,112,676	494,996	59,239	(356,642)	2,310,269
Income tax expense	-	163,082	34,511	-	197,593
Net Income	\$ 2,112,676	\$ 331,914	\$ 24,728	\$ (356,642)	\$ 2,112,676



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**Independent Auditors' 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***

Board of Directors
Warren Rural Electric Cooperative Corporation
Bowling Green, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of the Warren Rural Electric Cooperative Corporation and subsidiaries (the "Cooperative") (a nonprofit organization), which comprise the consolidated balance sheet as of June 30, 2019 and the related consolidated statements of income, equities, and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated October 22, 2019.

Internal Control Over Financial Reporting

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

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

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

did identify certain deficiencies in internal control, described in the accompanying schedule of findings and recommendations that we consider to be a significant deficiency: 2019-001.

Compliance and Other Matters

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

We noted other matters involving internal control over financial reporting that we have reported to management of the Cooperative in a separate letter dated October 22, 2019.

The Cooperative's Response to Findings

The Cooperative's response to the findings identified in our audit is described in the accompanying schedule of findings and recommendations. The Cooperative's response was not subjected to the auditing procedures applied in the audit of the consolidated financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

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

Carr, Riggs & Ingram, L.L.C.

CARR, RIGGS & INGRAM, LLC
Bowling Green, Kentucky
October 22, 2019



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

Board of Directors
Warren Rural Electric Cooperative Corporation
Bowling Green, Kentucky

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of Warren Rural Electric Cooperative Corporation and subsidiaries (the "Cooperative"), which comprise the consolidated balance sheet as of June 30, 2019, and the related consolidated statements of income, equities, and cash flows for the year then ended, and the related notes to the consolidated financial statements, and have issued our report thereon dated October 22, 2019. In accordance with *Government Auditing Standards*, we have also issued our report dated October 22, 2019, on our consideration of the Cooperative's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. No reports other than the reports referred to above and our schedule of findings and recommendations related to our audit have been furnished to management.

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

- Maintain adequate and effective accounting procedures;
- Utilize adequate and fair methods for accumulating and recording labor, material, and overhead costs, and the distribution of these costs to construction, retirement, and maintenance or other expense accounts;

- Reconcile continuing property records to the controlling general ledger plant accounts;
- Clear construction accounts and accrue depreciation on completed construction
- Record and properly price the retirement of plant;
- Seek approval of the sale, lease, or transfer of capital assets and disposition of proceeds for the sale or lease of plant, material, or scrap;
- Maintain adequate control over materials and supplies;
- Prepare accurate and timely Financial and Operating Reports;
- Obtain written RUS approval to enter into any contract for the management, 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 consolidated 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) and other Federal agency (TVA) requirements;
- 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.

The purpose of this report is solely to communicate, in connection with the audit of the consolidated 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.

Carr, Riggs & Ingram, L.L.C.

CARR, RIGGS & INGRAM, LLC
Bowling Green, Kentucky
October 22, 2019

Warren Rural Electric Cooperative Corporation Schedule of Findings and Recommendations

2019-001 SEGREGATION OF DUTIES

Criteria and Condition: Proper segregation of duties is a significant component to the internal control structure. There is a lack of segregation of duties in relation to the cash disbursements. Compensating controls have been implemented in an attempt to reduce this risk.

Cause: Select employees have access to the Cooperative's assets and financial records.

Effect or Potential Effect: Misappropriations could occur and not be detected by the Cooperative's internal controls.

Recommendation: We recommend management strengthen internal controls in relation to cash disbursements by segregating access to the Cooperative's assets and financial records.

Views of Responsible Officials and Planned Corrective Actions: In our opinion, the Accounting department is not large enough to have full segregation of duties. The Manager of Accounting acts as backup for accounts payable, payroll and all other functions within the Accounting Department. The VP of Administrative Services reviews all checks written to ensure that all checks are accounted for. Bank reconciliations are performed by individuals who do not have access to the bank accounts. There are no planned corrective actions, other than continuous review of procedures for reasonableness.



THOUGHT LEADERSHIP



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CRI's website features financial calculators, current tax and estate tax guides, a record retention schedule, glossary of common financial terms, and hundreds of articles with topics ranging from current legislation to industry-specific news.



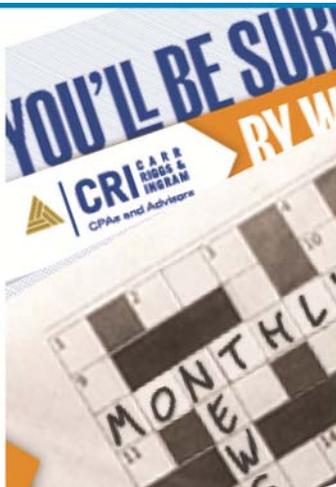
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Our team is dedicated to keeping our clients informed, and we prove it by creating a custom monthly e-newsletter with widely-applicable topics. The articles are designed to help you improve your business and personal finances. Popular recent topics include:

- Reportable Health Care Coverage on W-2s
- Navigating Alternative Minimum Tax (AMT)
- Key Considerations of Health Care Law
- Six Commandments of Estate Planning