FINANCIAL STATEMENTS WITH
REPORT OF INDEPENDENT AUDITORS

EAST TEXAS ELECTRIC COOPERATIVE, INC.

December 31, 2020 and 2019

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REPORT OF INDEPENDENT AUDITORS

The Board of Directors
East Texas Electric Cooperative, Inc.
Nacogdoches, Texas

We have audited the accompanying financial statements of East Texas Electric Cooperative, Inc. (the "Cooperative") which comprise the balance sheets as of December 31, 2020 and 2019 and the related statements of revenue and expense, comprehensive income, patronage capital and other equities and cash flows for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards for financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. These standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Cooperative's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of East Texas Electric Cooperative, Inc. as of December 31, 2020 and 2019, and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

In accordance with *Government Auditing Standards*, we have also issued our report dated June 22, 2021, on our consideration of the Cooperative's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Axley & Rode LLP
CERTIFIED PUBLIC ACCOUNTANTS

Lufkin, Texas
June 22, 2021

EAST TEXAS ELECTRIC COOPERATIVE, INC.
BALANCE SHEETS
December 31, 2020 and 2019

	2020	2019
ASSETS		
Utility Plant:		
Utility plant in service	$ 1 073 855 376	$ 908 168 469
Construction work in progress	29 165 661	165 455 314
	1 103 021 037	1 073 623 783
Less accumulated provision for depreciation	425 296 740	391 093 994
	677 724 297	682 529 789
Investments and Other Assets:		
Investments in associated organizations	42 487 650	42 808 923
Other investments - RUS cushion of credit	-	64 911 744
Funds held in escrow	-	3 363 921
	42 487 650	111 084 588
Current Assets:		
Cash and cash equivalents	15 594 356	7 948 651
Accounts receivable from member cooperatives	47 197 733	45 183 773
Accounts receivable - Other	1 861 327	1 371 316
Certificates of deposit	7 228 500	7 201 900
Investment securities - Available for sale	3 239 524	3 053 573
Fuel stock	6 081 107	6 141 607
Materials and supplies	13 382 587	13 979 713
Other current assets	2 431 540	1 485 217
	97 016 674	86 365 750
Deferred debits	156 394 650	162 147 060
	$ 973 623 271	$ 1 042 127 187
EQUITIES AND LIABILITIES		
Equity and Margin:		
Patronage capital	$ 199 433 211	$ 189 240 686
Accumulated comprehensive income (loss)	28	(44 222)
	199 433 239	189 196 464
Long-term debt, less current maturities	648 342 278	745 875 966
Current Liabilities:		
Accounts payable - Purchased power	18 533 537	15 399 471
Accounts payable - Other	18 366 227	17 845 447
Accrued expenses	10 948 837	9 227 606
Line of credit - General	-	16 500 000
Current maturities of long-term debt	74 998 724	43 195 114
	122 847 325	102 167 638
Deferred credits	3 000 429	4 887 119
	$ 973 623 271	$ 1 042 127 187

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

EAST TEXAS ELECTRIC COOPERATIVE, INC.
STATEMENTS OF REVENUE AND EXPENSE
For the Years Ended December 31, 2020 and 2019

	2020	2019
Operating Revenues:		
Power sales - Members	$ 292 181 251	$ 312 588 368
Other electric revenues	25 561 227	18 117 488
	317 742 477	330 705 856
Operating Expenses:		
Purchased power	95 591 936	101 382 979
Power Generation:		
Fuel	43 363 990	51 012 697
Other production expenses	35 984 015	34 457 448
Transmission	55 946 636	58 706 524
Administrative and general	10 636 406	11 470 603
Depreciation	34 393 588	32 185 859
Amortization of regulatory asset	8 816 612	8 054 547
Other deductions - Plant impairment	-	1 285 488
	284 773 183	298 556 145
OPERATING MARGINS BEFORE INTEREST EXPENSE	33 009 294	32 149 711
Interest expense	28 362 879	29 062 485
OPERATING MARGINS	4 646 415	3 087 226
Nonoperating Margins:		
Other income	95 000	25 000
Interest income	3 106 218	4 571 147
Capital credits and patronage capital allocations	2 344 892	2 284 471
NET MARGINS	$ 10 192 525	$ 9 967 844

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

EAST TEXAS ELECTRIC COOPERATIVE, INC.
STATEMENTS OF COMPREHENSIVE INCOME
For the Years Ended December 31, 2020 and 2019

	2020	2019
NET MARGINS	$ 10 192 525	$ 9 967 844
Other Comprehensive Income (Loss):		
Unrealized gains (losses) on available for sale securities	44 250	89 965
OTHER COMPREHENSIVE INCOME (LOSS)	44 250	89 965
COMPREHENSIVE INCOME	$ 10 236 775	$ 10 057 809

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

EAST TEXAS ELECTRIC COOPERATIVE, INC.
STATEMENTS OF PATRONAGE CAPITAL AND OTHER EQUITIES
For the Years Ended December 31, 2020 and 2019

	PATRONAGE CAPITAL	ACCUMULATED COMPREHENSIVE INCOME (LOSS)	TOTAL
Balance, December 31, 2018	$ 179 272 842	$ (134 187)	$ 179 138 655
Net margins	9 967 844	-	9 967 844
Other comprehensive income (loss)	-	89 965	89 965
Balance, December 31, 2019	189 240 686	(44 222)	189 196 464
Net margins	10 192 525	-	10 192 525
Other comprehensive income (loss)	-	44 250	44 250
Balance, December 31, 2020	$ 199 433 211	$ 28	$ 199 433 239

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

EAST TEXAS ELECTRIC COOPERATIVE, INC.
STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2020 and 2019

	2020	2019
Operating Activities:		
Net margins	$ 10 192 525	$ 9 967 844
Adjustments to Reconcile Net Margins to Net Cash Provided by Operating Activities:		
Depreciation	34 393 588	32 185 859
Amortization	8 816 612	8 054 547
Plant impairment	-	1 285 488
Asset regulatory obligations	-	53 202
Patronage capital credits - Non-cash	(984 890)	(1 007 784)
Reinvested dividends on investment securities	(13 274)	(20 212)
Cash Provided by (Used for) the Change in:		
Accounts receivable - Members	(2 097 171)	3 510 130
Accounts receivable - Other	(490 011)	(47 444)
Fuel stock	60 499	(2 614 708)
Materials and supplies	597 125	(2 147 864)
Other current assets	(879 466)	(297 086)
Deferred debits	198 866	198 866
Accounts payable	3 134 068	340 916
Accounts payable - Other	(604 175)	2 485 477
Accrued expenses	1 721 226	913 364
Deferred credits	(5 312 263)	(3 415 382)
NET CASH PROVIDED BY OPERATING ACTIVITIES	48 733 259	49 445 213
Investing Activities:		
Capital expenditures (including interest capitalized)	(28 334 278)	(26 024 061)
Redemption of CFC loan certificates	1 356 163	1 346 898
RUS cushion of credit	64 911 744	(3 146 642)
Funds held in escrow	3 363 921	8 986 919
Certificates of deposit	(26 600)	(1 573 900)
Other investments	(128 427)	1 420 220
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES	41 142 523	(18 990 566)
Financing Activities:		
Loan advances - RUS	-	7 008 410
Loan advances - CFC	12 347 646	-
Loan advances - CoBank	92 900 000	-
Loan payments - RUS	(116 057 686)	(19 717 117)
Loan payments - Others	(17 396 824)	(15 347 543)
Clean Renewable Energy Bonds	(7 523 213)	(7 523 212)
Net activity - Syndicated facility/lines of credit	(46 500 000)	12 491 370
NET CASH USED BY FINANCING ACTIVITIES	(82 230 077)	(23 088 092)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	7 645 705	7 366 555
Cash and cash equivalents, beginning of year	7 948 651	582 096
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 15 594 356	$ 7 948 651
Supplemental Disclosures of Cash Flow Information:		
Cash paid for interest	$ 30 900 782	$ 30 066 743
Supplemental Schedule of Non-Cash Investing and Financing Activities:		
Unrealized gain/(loss) on investment available for sale	$ 44 250	$ 89 965
Increase in accounts payable for capital expenditures	$ 8 056 589	$ 8 775 452
Increase in deferred debits from utility plant	$ -	$ 13 797 551

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

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF ACCOUNTING POLICIES

Nature of Operations:

East Texas Electric Cooperative, Inc. ("Cooperative") is an electric generating and transmission cooperative formed and operating pursuant to the Texas Electric Cooperative Corporation Act for the purpose of providing wholesale electric service to the Members. The Cooperative's members consist of one electric generating and transmission cooperative, Northeast Texas Electric Cooperative, Inc. ("NTEC"), and seven distribution cooperatives, Cherokee County Electric Cooperative Association ("CCECA"), Deep East Texas Electric Cooperative, Inc. ("DETEC"), Houston County Electric Cooperative, Inc. ("HCEC"), Jasper-Newton Electric Cooperative, Inc. ("JNEC"), Rusk County Electric Cooperative, Inc. ("RCEC"), Sam Houston Electric Cooperative, Inc. ("SHECO") and Wood County Electric Cooperative, Inc. ("WCEC") ("Members").

The Cooperative was formed principally to provide dependable power to its Members at the lowest cost possible. In doing so, the Cooperative works closely with its Members in determining their power requirements.

Use of Estimates:

The preparation of the financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities. The estimates and assumptions used in the accompanying financial statements are based upon management's evaluation of the relevant facts and circumstances as of the date of the financial statements. Actual results may differ from the estimates and assumptions used in preparing the accompanying financial statements.

System of Accounts:

The Cooperative maintains its accounting records in accordance with the Federal Energy Regulatory Commission's ("FERC") Uniform System of Accounts as adopted by the USDA Rural Development's Rural Utilities Service ("RUS"), which conforms with U.S. generally accepted accounting principles in all material respects. The more significant accounting policies are described below.

Revenue Recognition:

Revenue from Contracts with Customers

On January 1, 2019, the Cooperative adopted the Financial Accounting Standards Board, Accounting Standards Update 2014-09, Revenue from Contracts with Customers (Topic 606), using the modified retrospective method applied to contracts that were not completed as of the adoption date. The Cooperative performed an analysis of the cumulative effect of initially applying the new standard to the opening balance of accumulated patronage capital and determined that because it incurs no significant costs associated with acquiring a contract with customers and offers little to no incentives requiring deferral over the lives of uncompleted contracts that there was no material impact on previously reported balances. As a result, no adjustment was recorded. Following the adoption of the new standard, the Cooperative's revenue recognition of its contracts with customers remains materially consistent with its historical practice. The comparative information has not been restated and continues to be reported under the accounting standards in effect for those periods. The Cooperative's policies with respect to its various revenue streams are detailed below. In general, the Cooperative applies the invoicing practical expedient method, specified by Topic 606, to recognize revenue for the revenue streams detailed below, except in circumstances where the invoiced amount does not represent the value transferred to the customer.

Energy Revenue

Electric energy revenue is recognized upon transmission to the customer over time, using the output method for measuring progress of satisfaction of performance obligations. The sale of electricity is recorded on a gross basis in the Cooperative's statements of revenue. The Cooperative applies the invoicing practical expedient, where applicable, in recognizing electric revenue. Under the practical expedient, revenue is recognized based on the invoiced amount which is equal to the value to the customer of the Cooperative's performance obligation completed to date.

The Cooperative's tariffs provide that rates are to be adjusted from time to time based on changes in estimated power costs. At the end of the year, the estimated power costs are compared to actual power costs. At the discretion of the Board of Directors, an over-collection is either refunded to the members over the subsequent year or in a lump sum; under-collections are collected from the members over the subsequent year. In 2020 and 2019, there was an under-collection of $196,360 and an over-collection of $3,778,095, respectively, included in deferrals.

As contracts for wholesale electricity can be for multi-year periods, the Cooperative has performance obligations under these contracts that have not yet been satisfied. These performance obligations have transaction prices that are expected to vary based on customer usage, ultimate duration of the contract, and future over or under recoveries, which will vary with the larger power market. Therefore, it is not practicable to estimate such amounts.

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF ACCOUNTING POLICIES - CONTINUED

Renewable Energy Certificates

The Cooperative receives renewable energy certificates, also known as renewable energy credits, (RECs) in connection with its power purchases from wind farms, which are discussed in Note 11 - Power Contracts. The Cooperative holds these certificates in a trading account and sells them periodically. Balances held and revenues from the sale of RECs were not material to the balance sheet or operating results in 2020 or 2019. REC sales are reported as reductions of purchased power cost.

Cash Flows Statement:

For purposes of reporting cash flows, cash and cash equivalents consist of cash and temporary cash investments with original maturities of three months or less.

Accounts Receivable:

Accounts receivable from member cooperatives are recorded from the billings of the sale of electricity to the Members. The Cooperative considers accounts receivable to be fully collectible; accordingly, no allowance for doubtful accounts has been established. If accounts become uncollectible, they will be charged to operations when that determination is made. No accounts receivable from Member Cooperatives were past due more than 90 days as of December 31, 2020.

Utility Plant:

The utility plant is stated at original cost. The cost of additions to the electric plant includes contracted work, direct labor, materials, allocable overhead and interest on debt used for construction. The cost of retirements, replacements, or betterments are removed from utility plant and, in accordance with industry practice, the cost of the unit and its removal cost, less salvage, are charged to accumulated depreciation. Maintenance and repairs are charged to operating expenses as incurred.

Depreciation of the utility plant is provided on the composite straight-line method over the estimated useful lives of the various components. The method and rates are prescribed by RUS or as approved for rate-making purposes. The annual depreciation rates are:

Transmission	2.75%
Office Building	2.00%
Production plant	3.226% - 6.67%
Load dispatching equipment	6.67%

In accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 360-10, *Impairment of Long-Lived Assets,* the Cooperative evaluates, when indicators of impairment are identified, the carrying amount of its long-lived assets. Recoverability is determined by comparing the projected undiscounted net cash flows of the long-lived assets against their respective carrying amounts. The amount of impairment, if any, is measured based upon the excess of the carrying value over the fair value.

Asset Retirement Obligations

Accounting standards require entities to record liabilities for all legal obligations associated with the retirement of long-lived assets that result from the normal operation of the assets. The Cooperative has recognized an Asset Retirement Obligation (ARO) for legal obligations primarily for the retirement of certain ash disposal facilities, reclamation of landfill sites and asbestos removal and disposal at four jointly owned coal-fired power plants. These liabilities are recorded at their fair values (which are the present values of the estimated future cash outflows).

For the years ended December 31, 2020 and 2019, there are no assets legally restricted for the purpose of settling any AROs. These AROs are recorded as deferred credits on the balance sheet in the amount of $1,165,805 and $1,109,024, respectively.

Investments in Associated Organizations:

Investments in patronage capital credits of associated organizations are accounted for under the equity method. Patronage capital is recorded at the stated amount of the certificate when allocated by the associated organization.

Investment Securities:

The Cooperative's investment securities are classified as available for sale. These securities are carried at estimated fair value with any unrealized gains or losses excluded from net margin and reported in accumulated other comprehensive income (loss), which is reported as a separate component of members' equity.

Premiums and discounts on securities available for sale are recognized in interest income using a method approximating the interest method over the period to expected maturity. Purchases and sales of securities are accounted for on a trade date basis on a specific identification basis.

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF ACCOUNTING POLICIES - CONTINUED

Declines in the estimated fair value of individual securities below their cost that are other-than-temporary are accounted for as a write-down of the individual securities to their fair value. Any related write-downs are included in earnings as realized losses.

Unrealized holding gains and losses on securities available for sale are reported in other comprehensive income. Realized gains and losses on securities available for sale are included in gains and losses on sale of available for sale securities in the statement of operations and, when applicable, are reported as a reclassification adjustment in other comprehensive income. Gains and losses on the sale of securities are determined using the specific-identification method.

Fair Value Measurements:

The fair value of financial assets and liabilities is measured according to the *Fair Value Measurements and Disclosure* topic of FASB Accounting Standards Codification. Fair value is required to be evaluated and adjusted according to the following valuation techniques.

Level 1 - Fair value is determined using quoted market prices in active markets for identical assets and liabilities.

Level 2 - Fair value is determined using quoted market prices in active markets for similar assets and liabilities, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant inputs are observable in the market for substantially the full term of the assets or liabilities.

Level 3 - Fair value is determined using inputs that are generally unobservable and typically reflect management's estimates of assumptions that market participants would use in pricing the asset or liability. The market for assets and liabilities using Level 3 measures is typically inactive.

Inventories:

Inventory consists of fuel stock (primarily coal) for operation of the electric plants. Fuel inventory is carried at weighted average cost. Materials and supplies inventory used for the operation of the electric plants is valued at average cost and is stated at the lower of average cost or net realizable value (NRV), with NRV determined to be the estimated selling price in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. Cost is determined using the average cost method and includes all costs related to acquisition.

Allowance for Borrowed Funds Used During Construction:

The Cooperative capitalizes the carrying costs on certain significant construction and development projects while in progress. Interest is capitalized based on the debt specifically borrowed to finance projects during construction and is reflected as a credit to interest expense in the Statement of Revenue and Patronage Capital. For the years ended December 31, 2020 and 2019, capitalized interest was approximately $1,495,767 and $1,179,000, respectively.

Income Taxes:

The Cooperative is exempt from Federal income tax under the provisions of Section 501(c)(12) of the Internal Revenue Code of 1986.

Uncertain Tax Positions:

FASB ASC 740 requires recognition, measurement, and disclosure of uncertain tax positions. The Cooperative currently accounts for uncertain tax positions based on the estimated likelihood of assessment and has not determined that any tax positions require an accrual based on current standards of accounting. For federal income tax purposes, the tax returns essentially remain open for possible examination for a period of three years after the date on which those returns are filed.

Comprehensive Income:

Accounting principles generally require that recognized revenue, expenses, gains, and losses be included in net margin. Although certain changes in assets and liabilities, such as unrealized gains and losses on available-for-sale securities are reported as a separate component of the equity section of the balance sheet, such items, along with net margin, are components of comprehensive income.

Deferred Debits/Credits:

In accordance with FASB ASC 980: *Regulated Operations* (formerly FASB Statement No. 71, *Accounting for the Effects of Certain Types of Regulation*), certain costs have been capitalized as deferred debits that would otherwise be charged to expense. Such deferred debits are recorded when it is probable that future revenue in an amount at least equal to the capitalized costs will result from inclusion of those costs in future rates. Accordingly, certain obligations have been accrued as deferred credits that would otherwise be charged to income. Such deferred credits are recorded when it is probable that future expenses in an amount at least equal to the accrued liabilities will result from inclusion of those revenues in future rates.

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF ACCOUNTING POLICIES - CONTINUED

Derivative Instruments:

The accounting standards for derivative instruments and hedging activities require that all derivatives be recognized at fair value on the balance sheet, either as assets or liabilities, unless they meet the normal purchase, normal sales criteria. The changes in the fair value of recognized derivatives are recorded each period in current margins or other comprehensive income, depending on whether a derivative is designated as part of a hedge transaction and the type of hedge transaction. The Cooperative's policy is that derivatives are to be used only for hedging purposes and Management does not engage in transactions unrelated to the underlying financial exposures. The Cooperative does not enter into derivative financial instruments for trading purposes.

There were no derivative instruments outstanding as of December 31, 2020 or 2019.

Regional Transmission Organizations:

The Cooperative is a member of and participates in three Regional Transmission Organizations ("RTO"), which include the Midcontinent Independent System Operator ("MISO") RTO, Southwest Power Pool ("SPP") RTO and Electric Reliability Council of Texas ("ERCOT") RTO. The RTOs operate wholesale electric markets and are responsible for moving electricity over large areas. They also coordinate, control, and monitor the electric transmission grid within their areas. As a result of this, the Cooperative now sells all plant generation into the RTO markets and purchases power to serve a large portion of its load from markets. The Cooperative records RTO transactions on an hour-to-hour basis. Transactions within each individual hour are netted to a single purchase or sale based on actual load and net megawatt-hour generation.

New Authoritative Accounting Guidance:

In May 2014, FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers.* ASU 2014-09 introduces new, increased requirements for disclosure of revenue in financial statements and is intended to eliminate inconsistencies in revenue recognition and thereby improve financial reporting comparability across entities, industries, and capital markets. The new standard was effective for annual reporting periods beginning after December 15, 2018 and was adopted on January 1, 2019. The most substantial impact on the Cooperative was enhancement of qualitative disclosures related to revenue recognition. See Note 1 - Significant Accounting Policies, Revenue Recognition.

In February 2016, FASB issued ASU 2016-02, *Leases.* The standard introduces a new lessee model that brings substantially all leases onto the balance sheet. Additionally, the guidance retains most of the principles of the existing lessor model in principles generally accepted in the United States of America, and it aligns many of those principles with *Revenue from Contracts with Customers.* This will be effective for annual reporting periods beginning after December 15, 2021. The Cooperative is still evaluating the impact that this standard will have on its financial statements.

Subsequent Events:

Management has evaluated subsequent events through June 22, 2021, the date the financial statements were available to be issued.

NOTE 2 - UTILITY PLANT

The following summarizes utility plant as of December 31, 2020 and 2019:

	2020	2019
Utility Plant, at Cost:		
Transmission	$ 101 150 011	$ 100 927 318
Production plant	969 814 865	804 272 462
Distribution and telemetering	696 921	693 115
Asset retirement obligations - Generation	788 143	922 205
Office building	698 312	698 312
Office equipment	707 124	655 057
	1 073 855 376	908 168 469
Construction work in progress	29 165 661	165 455 314
	1 103 021 037	1 073 623 783
Less accumulated depreciation	425 296 740	391 093 994
	$ 677 724 297	$ 682 529 789

The Cooperative has an undivided ownership in and is responsible for providing its share of the costs for its jointly owned and other power plant facilities. The Cooperative's share of each facility as of December 31, 2020 and 2019, is as follows:

Nelson Unit 6 (155Mw)	19.10%
Independence Steam Electric Station Unit 2 ("ISES 2") (60Mw)	7.13%
Plum Point Energy Station ("Plum Point") (50Mw)	7.52%
John W. Turk Power Plant ("Turk") (50Mw)	8.33%
Harrison County Power Project ("HCPP") (248Mw)	45.03%
Hardin County Units 1 and 2 (150Mw)	100.00%
San Jacinto Units 1 and 2 (150Mw)	100.00%
Hilton Lively Renewable Power Project (49Mw)	100.00%
R.C. Thomas Hydroelectric Project (24Mw) (construction completed in 2020)	100.00%

NOTE 2 - UTILITY PLANT - CONTINUED

In addition to the above plants that are currently in operation, the Cooperative has significant additional investments in the following power plant projects under construction or development:

R.C. Thomas Hydroelectric Project

In 2020, the Cooperative completed construction, in cooperation with the Trinity River Authority of Texas ("Authority") and the City of Houston, Texas, a hydropower facility with an installed capacity of approximately 24Mw located at the Lake Livingston Dam. The total cost to construct the hydropower facility was approximately $156,000,000. The Cooperative has been approved for and has issued a total of $106,355,693 in Clean Renewable Energy Bonds (CREBS) (Note 9). The Cooperative has financed the project with the use of allocated CREBS related to the project and used RUS funds for their remaining financing needs.

Montgomery County Power Station

The Cooperative has entered into an Asset Purchase Agreement (APA) with Entergy Texas, Inc. for the purchase of 7.55% of the Montgomery County Power Station (MCPS). MCPS is a nominal 993Mw combined-cycle generating unit in Willis, Texas. The total cost of MCPS is $870,786,137 with the Cooperative's share $65,831,432. The facility achieved commercial operation January 1, 2021. The Cooperative funded its ownership share of MCPS on June 4, 2021 and closed on the transaction. The Cooperative has applied for financing with RUS to fund its ownership in the facility.

Hilton Lively Renewable Power Project

During the year ended December 31, 2016, the Cooperative elected to temporarily suspend operations at the Hilton Lively Renewable Power Project. Due to several operational challenges including steep declines in natural gas prices and lower wholesale energy prices in the MISO market, the Project was determined to no longer be economically viable to operate under current conditions. During the year ended December 31, 2019, the three-year suspension period ended and the Board elected to disconnect the Lively Project from the MISO transmission system. This was a result of continued poor economic conditions and a negative outlook for the Lively Project moving forward. The Cooperative does not at this time anticipate economic conditions to change, absent a major environmental or political change, that would result in reconnecting to MISO.

As a result of the suspension and subsequent disconnection from MISO, the Cooperative applied the provisions of ASC 360-10, *Impairment of Long-Lived Assets,* and performed an impairment analysis. Under generally accepted accounting principles the determination of an asset's recoverability is based on the probability-weighted net cash flows expected to be generated. The projected net cash flows primarily depend on the status of operations as well as projections of future revenues and costs over the estimated remaining life of the Project. The Cooperative performed an impairment analysis based upon energy and capacity price curves as well as anticipated salvage values for the project, as applicable, which were developed internally with both observable Level 2 quotations and unobservable Level 3 inputs, as well as management's forecasts of fuel, operating, and capital expenditures. A separate impairment analysis was performed in both 2016 and 2019 due to the separate triggering events of suspension of operations and the subsequent disconnection from MISO.

During the year ended December 31, 2016, the Cooperative estimated fair value of the Project to be $17,766,600, while the carrying value was $182,655,457, resulting in an impairment charge of $164,888,857. The Cooperative applied for and received approval from RUS to defer $163,925,311 of the impairment charge for future rate recovery as a regulatory asset. The Cooperative was approved to amortize and recover the regulatory asset over a period of twenty-one years beginning January 2017 using a regulatory method based on the bonds outstanding.

During the year ended December 31, 2019, the second impairment analysis resulted in an estimated fair value of the Project to be $1,500,000, while the carrying value was $16,583,039, resulting in an additional impairment charge of $15,083,039. The Cooperative again applied for and received approval from RUS to defer $13,797,551 of the impairment charge for future rate recovery as a regulatory asset. The Cooperative will amortize and recover the regulatory asset over a period of seventeen years beginning January 2020 using a regulatory method based on the bonds outstanding. The remaining net impairment of $1,285,488 was written-off.

For the years ended December 31, 2020 and 2019, the amount amortized and recovered through rates was $8,816,612 and $8,054,547, respectively. As of December 31, 2020 and 2019, the balance of the regulatory asset including both impairment deferrals was $144,670,540 and $153,559,229, respectively.

NOTE 3 - INVESTMENTS IN ASSOCIATED ORGANIZATIONS

Investments in associated organizations as of December 31, 2020 and 2019 consisted of the following:

	2020	2019
National Rural Utilities Cooperative Finance Corporation (CFC):		
Patronage capital and membership	$ 7 863 020	$ 7 300 394
Member capital securities	500 000	500 000
Loan capital term certificates	22 641 548	23 997 711
CoBank:		
Patronage capital and membership	6 415 385	5 993 122
Sam Rayburn Dam Electric Cooperative, Inc. (Note 11)	5 065 586	5 015 586
Memberships	2 110	2 110
	$ 42 487 649	$ 42 808 923

NOTE 3 - INVESTMENTS IN ASSOCIATED ORGANIZATIONS - CONTINUED

Patronage capital allocations reported in the Statements of Revenue and Expense in the amount of $2,344,892 and $2,284,471 for the fiscal years ended December 31, 2020 and 2019, respectively, represent patronage capital allocations from CoBank and CFC.

NOTE 4 - OTHER INVESTMENTS - RUS CUSHION OF CREDIT

The Cooperative had previously maintained a Cushion of Credit Account with RUS which represented voluntary payments to RUS in excess of amounts due, intended to enable the Cooperative to have funds available to make scheduled payments on RUS debt. Funds could only be used to make installments on RUS mortgage notes. Provisions of the 2018 Farm Bill passed on December 20, 2018 modified the RUS cushion of credit program. No new deposits into the cushion of credit account were allowed after December 20, 2018. The Cooperative made deposits of $30,000,000 into the cushion of credit on December 17, 2018. The Farm Bill allowed for cushion of credit holders to prepay their RUS debt without a prepayment penalty through September 30, 2020. In January 2020, the Board of Directors approved the use of the cushion of credit funds to pay off RUS notes in the amount of $13,100,000 related to HCPP and $89,400,000 related to San Jacinto Units 1 & 2 and Hardin Units 1 & 2. As of December 31, 2020 and 2019, the Cooperative had $-0- and $64,911,744, respectively, in the Cushion of Credit with RUS.

NOTE 5 - INVESTMENT SECURITIES AND FAIR VALUE MEASUREMENTS

Investment securities consisted of investments in fixed income mutual funds and government bonds with an estimated fair value of $3,239,524 and $3,053,573 as of December 31, 2020 and 2019, respectively. The amount of unrealized gain or (loss) included in other comprehensive income is $28 and $(44,222) for the years ended December 31, 2020 and 2019.

Mutual funds are valued at the net asset value (NAV) of shares held which is considered a Level 1 valuation technique.

Government bonds are valued using quoted market prices in active markets for identical assets which is considered a Level 1 valuation technique.

The amortized costs and estimated fair values of investment securities are as follows:

	AMORTIZED COST	GROSS UNREALIZED GAINS	GROSS UNREALIZED LOSSES	ESTIMATED FAIR VALUE
Securities Available for Sale December 31, 2020:				
Money Market Mutual Fund	$ 273 628	$ -	$ -	$ 273 628
U.S. Government Obligations	2 200 920	11 806	(8 359)	2 204 367
Mutual Fund Bond	764 948	-	(3 419)	761 529
TOTALS	$ 3 239 496	$ 11 806	$ (11 778)	$ 3 239 524
Securities Available for Sale December 31, 2019:				
Money Market Mutual Fund	$ 322 332	$ -	$ -	$ 322 332
U.S. Government Obligations	2 010 515	14 801	(34 614)	1 990 702
Mutual Fund Bond	764 948	-	(24 409)	740 539
TOTALS	$ 3 097 795	$ 14 801	$ (59 023)	$ 3 053 573

The scheduled maturities of securities to be held to maturity and securities available for sale as of December 31, 2020 were as follows:

	AVAILABLE FOR SALE SECURITIES	
	AMORTIZED COST	ESTIMATED FAIR VALUE
Due in one year or less	$ -	$ -
Due from one to five years	764 948	761 529
Due from five to ten years	-	-
Over ten years	-	-
Money Market Mutual Fund	273 628	273 628
Mutual Fund Bond	2 200 920	2 204 367
	$ 3 239 496	$ 3 239 524

Information pertaining to securities with gross unrealized losses as of December 31, 2020 and 2019 aggregated by investment category and length of time that individual securities have been in a continuous loss position follows:

	LESS THAN 12 MONTHS		12 MONTHS OR GREATER		TOTAL	
2020 Description of Securities:	FAIR VALUE	UNREALIZED LOSSES	FAIR VALUE	UNREALIZED LOSSES	FAIR VALUE	UNREALIZED LOSSES
U.S. Governments	$ 638 592	$ (7 674)	$ 99 629	$ (685)	$ 738 221	$ (8 359)
Mutual Fund Bonds	$ -	$ -	$ 761 529	$ (3 419)	$ 761 529	$ (3 419)
2019 Description of Securities:						
U.S. Governments	$ 134 943	$ (7 910)	$ 691 604	$ (26 703)	$ 826 547	$ (34 614)
Mutual Fund Bonds	$ -	$ -	$ 740 539	$ (24 409)	$ 740 539	$ (24 409)

NOTE 5 - INVESTMENT SECURITIES AND FAIR VALUE MEASUREMENTS - CONTINUED

Management evaluates securities for other-than-temporary impairment on a periodic basis. Consideration is given to (1) the length of time and the extent to which the fair value has been less than cost, (2) the financial condition and near-term prospects of the issuer, and (3) the intent and ability of the Cooperative to retain its investment in the issuer for a period of time sufficient to allow for any anticipated recovery in fair value. As the Cooperative has the ability to hold investment securities until maturity, or the foreseeable future, none of the declines are deemed to be other-than-temporary.

As of December 31, 2020, the majority of the securities are guaranteed by the U.S. Government, agencies thereof or municipalities. These unrealized losses relate principally to current interest rates for similar types of securities. In analyzing an issuer's financial condition, management considers whether the securities are issued by the federal government or its agencies, whether downgrades by bond rating agencies have occurred, and the results of reviews of the issuer's financial condition. As management has the ability to hold debt securities until maturity, or for the foreseeable future, none of the declines are deemed to be other-than-temporary.

NOTE 6 - FUNDS HELD IN ESCROW

The Cooperative has issued $106,355,693 in CREBS related to the R.C. Thomas Hydroelectric Project. Bond proceeds of $3,363,921 were held in escrow by CoBank until utilized. As of December 31, 2020, the funds held in escrow were utilized entirely on construction for the project.

NOTE 7 - DEFERRED DEBITS/CREDITS

The following is a summary of the amounts recorded as deferred debits/credits as of December 31, 2020 and 2019:

	2020	2019
DEFERRED DEBITS		
Debt issuance costs	$ 98 283	$ 123 377
Retirement security plan	72 900	106 547
Prepayment premium on settlement of derivative	3 518 784	3 692 556
Due from member - Billing correction	1 375 028	2 029 462
Due from members - Levelized billing	196 360	-
Overhead and maintenance	-	2 635 889
Regulatory asset - Impairment (Note 2)	144 670 540	153 559 229
Prepayment premium on early payoff of debt	6 034 913	-
Provision for property insurance (Note 15)	427 842	-
	$ 156 394 650	$ 162 147 060
DEFERRED CREDITS		
Overhead and maintenance	$ 1 834 624	$ -
Asset retirement obligations (Note 1)	1 165 805	1 109 024
Due to members - Levelized billing	-	3 778 095
	$ 3 000 429	$ 4 887 119

Debt issuance costs represent the unamortized costs associated with the issuance of CREBS and refinancing of debt. The costs are being amortized over the life of the bonds and the life of the loan, respectively.

The NRECA Board of Directors approved an option to allow participating cooperatives to make a prepayment and reduce future required contributions to the NRECA Retirement Security Plan ("RS Plan"). The prepayment amount is the Cooperative's share of future contributions required to fund the RS Plan's unfunded value of benefits earned to date using Plan actuarial valuation assumptions. The Cooperative elected to accept the option and made a prepayment to the NRECA RS Plan. The Cooperative recorded the prepayment as a miscellaneous deferred debit and is amortizing the prepayment over ten years as stipulated by RUS.

In connection with the Cooperative's long-term financing for a 50Mw interest in the Turk power plant, the Cooperative entered into an interest rate swap that effectively fixed the interest rate for this loan. The interest rate swap agreement effectively converted floating rates into fixed rates so that the Cooperative could predict with greater assurance what its future interest costs will be and protect itself against increases in floating rates. During 2016, the Cooperative refinanced the debt associated and settled the interest rate swap. The Cooperative incurred a prepayment premium for settling the swap in the amount of $4,344,200. The premium was deferred and is being amortized over the remaining term of the new debt.

During the year ended December 31, 2013, the Cooperative discovered a billing correction related to previous years' power billings. For several years, there was a misallocation of power costs between the Cooperative's Members. Several of the Cooperative's Members were over-allocated purchased power costs while one Cooperative Member was under-allocated power costs. The total correction approximated $7,064,410. The Cooperative has implemented an adder to collect the billing correction from the Member that was under-allocated power costs with $1,375,028 remaining to be collected as of December 31, 2020. The Cooperative refunded the $7,064,410 to the other Members in three annual installments of $2,354,803. The final installment was paid in February 2015.

NOTE 7 - DEFERRED DEBITS/CREDITS - CONTINUED

The Board of Directors approves the Cooperative's rates, which allow recovery of overhead and maintenance ("O & M") expenses, including administrative and general expenses incurred by the Cooperative on behalf of the Members. Under this provision, the difference in the allowable customer charge computed under the Cooperative's rate and the actual amount of O & M expenses incurred by the Cooperative is to be accumulated by the Cooperative in a deferred account. The allowable customer charge is a monthly average of O & M expenses as budgeted by the Cooperative at the beginning of each twelve-month billing period. Subsequent periods reflect the adjustments between actual and estimated O & M expenses.

The Cooperative's tariff includes a levelized billing rate plan. Under the levelized billing rate plan, each of the Cooperative's Members has the option to pay a monthly levelized bill computed using the actual kilowatt-hours and a levelized billing rate. The difference between the actual monthly power cost computed under the Cooperative's Board approved wholesale rate and the amount paid to the Cooperative under the levelized billing rate plan is recorded on monthly billing statements to the Members and accumulated by the Cooperative in a designated deferred account.

Under the levelized billing plan, a Member's levelized billing factor is recalculated each month. The levelized billing rate is calculated using actual data for the year to date and projected figures for the remainder of the year. At the end of each twelve-month period, the Cooperative computes a new projected cost of power. The new projected cost of power and the accumulated deferred billing for the previous twelve-month period are combined to determine the levelized billing rate for the next twelve-month period. The Board of Directors of the Cooperative may revise the levelized billing rate due to unforeseen fluctuations in the cost of purchased power.

During the year ended December 31, 2020, the Cooperative utilized the RUS Cushion of Credit to pay off RUS notes related to HCPP, San Jacinto Units 1 and 2 and Hardin Units 1 and 2. The Cooperative obtained unsecured financing from CoBank and CFC to refinance the remaining amount outstanding. A prepayment premium was incurred for paying off the RUS debt prior to maturity in the amount of $6,179,751. The premium was deferred and is being amortized over the remaining term of the new debt.

NOTE 8 - PATRONAGE CAPITAL

Patronage capital as of December 31, 2020 and 2019 consists of the following:

	2020	2019
Assignable patronage capital	$ 10 192 525	$ 9 967 844
Assigned patronage capital	189 240 686	179 272 842
	$ 199 433 211	$ 189 240 686

The by-laws of the Cooperative provide that all amounts received and receivable from the furnishing of electric energy in excess of the sum of operating costs and expenses are to be assigned to Members' patronage capital credit accounts on a patronage basis. The bylaws permit the Cooperative to allocate losses to Members, offset losses with margins from future years, or offset losses with certain nonoperating margins from current or future years.

Pursuant to the RUS mortgage and related loan agreements, until the total of equities and margins equal or exceed 30% of total assets, the distribution of capital contributed by members in each year is limited generally to 25% of patronage capital and margins of the preceding year provided that, after giving effect to such distribution, the total equity will equal or exceed 20% of total assets. The equities and margins of the Cooperative represent 20% and 18% of total assets as of December 31, 2020 and 2019, respectively. For the years ended December 31, 2020 and 2019, no patronage capital was retired.

NOTE 9 - LONG-TERM DEBT

Long-term debt as of December 31, 2020 and 2019 consisted of the following:

	2020	2019
Federal Financing Bank ("FFB") mortgage notes guaranteed by RUS, fixed rates 1.94% to 5.27%, maturing at various times through 2040	$ 247 593 911	$ 363 651 601
CFC Fixed Rate Notes - 3.35% to 7.15%, maturing at various times through 2041	192 224 084	193 180 197
CFC Financing Notes - Capital term certificates, fixed rates from 4.52% to 5.72%, maturing 2024-2041	21 046 284	22 279 265
CFC/Regions Syndicated Revolving Credit Facility - variable interest rates, maturing 2021	17 875 239	47 875 239
Clean Renewable Energy Bonds - Hilton Lively Renewable Power Plant, CFC, effective rate of 1.36%, maturing 2035	35 659 341	38 076 923
Clean Renewable Energy Bonds - R.C. Thomas Facility CFC, effective rate of 2.95%, maturing 2024	2 550 000	3 187 501
Clean Renewable Energy Bonds - R.C. Thomas Facility CoBank, effective rate of 1.25%, maturing 2035-2040	70 338 399	74 461 056
CoBank Fixed Rate Note - 3.06%, maturing 2021	36 000 000	-
CoBank Fixed Rate Note - 3.92%, maturing 2031	9 648 802	10 525 966
CoBank Fixed Rate Notes - 2.75% to 5.64%, maturing 2041	90 404 942	35 833 332
	723 341 002	789 071 080
Less current maturities	74 998 724	43 195 114
	$ 648 342 278	$ 745 875 966

The Cooperative has secured long-term financing from RUS to finance an ownership interest in several power projects including HCPP, Nelson 6, San Jacinto, Hardin, and the Hilton Lively Renewable Power Project. The RUS mortgage secures existing RUS debt in an amount up to $509,995,264, in the form of eight separate RUS promissory notes. During the year ended December 31, 2020, the Cooperative made an advance in the amount of $40,754,724 related to the R.C. Thomas Hydroelectric Project. The Cooperative has an approved commitment from RUS for an additional $32,245,276 for the permanent financing of the R.C. Thomas Hydroelectric Project. As of December 31, 2020, the RUS notes aggregated $247,593,911.

NOTE 9 - LONG-TERM DEBT - CONTINUED

The Cooperative has a senior credit facility with CFC. The facility includes fixed rate notes that have been utilized to finance construction projects including the Cooperative's undivided ownership interest in Nelson Unit No. 6, Plum Point, and the Turk power plant. The Cooperative receives a performance discount rate reduction of 0.125% and a volume discount rate reduction of 0.125% on CFC fixed rate notes. The notes feature a combination of level debt service and level principal payment arrangements.

The Cooperative has a syndicated revolving credit facility with CFC, Regions Bank, and BancorpSouth for a five year term. The facility consists of an aggregate commitment of $115,000,000. The facility has been utilized for general corporate purposes and to provide unsecured interim financing for the R.C. Thomas Hydroelectric Project. The Cooperative had $17,875,239 outstanding on this facility as of December 31, 2020. In March 2021, the Cooperative closed the $115,000,000 facility with CFC and secured a three year revolving facility for $100,000,000 with CoBank. This facility will be utilized for general corporate purposes and to provide unsecured interim financing for MCPS.

The Cooperative has received an allocation and CFC issued $55,000,000 of CREBS related to the Hilton Lively Renewable Power Project. The funds were utilized to finance the construction of the facility and had a balance of $35,659,341 as of December 31, 2020.

The Cooperative has been allocated and has issued a total of $106,355,693 in CREBS in coordination with R.C. Thomas Hydroelectric Project. The initial issue of CREBS was in the amount of $10,200,000 and was issued by CFC. The Cooperative utilized the funds to finance the initial stages of development of the hydropower facility. As of December 31, 2020, the balance of the CREBS amounted to $2,550,000. The Cooperative applied for and was approved for three issuances of CREBS. The three separate CREBS allocations were issued in coordination with CoBank in the total amount of $96,155,693. The funds have been utilized to finance construction of the hydropower facility (Note 6). As of December 31, 2020, the balance of the CREBS amounted to $70,338,399.

The Cooperative has an unsecured financing facility with CoBank. The facility includes a fixed rate note that was utilized to refinance and combine two existing facilities held by CoBank. The CoBank term loan had a balance of $9,648,802 as of December 31, 2020.

The Cooperative has also secured long-term financing from CoBank to finance an ownership interest in Plum Point power plant. The facility consists of a fixed rate note with level principal payment arrangements. As of December 31, 2020, the Cooperative had a balance of $34,166,667 on this facility.

On July 14, 2020, the Cooperative refinanced the Cooperative's ownership interest in Hardin, Jacinto and HCPP held at RUS with CoBank and CFC. The Cooperative secured financing with CoBank for the ownership interest of Hardin and Jacinto. The financing consists of a twenty-one year fixed rate loan of $56,900,000 and a short-term fixed rate loan for $36,000,000 maturing October 2021. CFC provided a twenty-one year fixed rate loan for HCPP in the amount of $12,347,647.

The long-term debt agreements with lenders contain certain restrictive covenants and restrictions on payment of patronage capital. The covenants require the Cooperative to maintain certain annual minimum financial ratios. The restrictions on payment of patronage capital are related in general to the Cooperative's equity and assets as defined in the agreements. For the years ended December 31, 2020 and 2019, the Cooperative was in compliance with all restrictive covenants.

Substantially all owned assets of the Cooperative are pledged as collateral for the above-mentioned secured debt.

The approximate annual maturities of long-term debt for the next five years that are not expected to be refinanced are as follows:

2021	$	74 998 724
2022	$	39 847 193
2023	$	40 231 095
2024	$	38 423 285
2025	$	37 327 562

The Cooperative has a $12,000,000 line of credit with CFC that matures on May 28, 2023. As of December 31, 2020 and 2019, no funds were advanced or owed under this line of credit.

The Cooperative also has an additional line of $25,000,000 with CoBank that matures on October 31, 2021. As of December 31, 2020 and 2019, no funds were advanced or owed under this line of credit.

The Cooperative has an additional line of credit with Bank of America for amounts up to $11,000,000 that matured October 12, 2020 and was not renewed. As of December 31, 2019, the Cooperative had $5,500,000 outstanding on the Bank of America line of credit.

NOTE 10 - OPERATING LEASES AND FACILITIES AGREEMENTS

The Cooperative has accepted an assignment of a transmission lease obligation between one of its Members, NTEC, and a distribution cooperative, Wood County Electric Cooperative, Inc., in connection with a 5Mw load served by the Cooperative. The annual lease payments are based upon an estimate using various factors. An annual true-up of this estimate is performed once actual amounts have been determined. This lease obligation has no fixed term, but will remain in effect until terminated by the mutual agreement of both parties. For the years ended December 31, 2020 and 2019, the total transmission lease payments were $112,636 and $139,904, respectively. Estimated lease payments for each of the next five (5) years will approximate $130,000.

NOTE 11 - POWER CONTRACTS

The Cooperative has entered into Wholesale Power Contracts (the "Contracts") with each of its Members extending through December 31, 2044. Pursuant to the Contracts, the Cooperative has agreed to serve all of the Members' power needs, except for the power supply responsibility that is specifically retained in the Contracts by the Members. The Cooperative's Board of Directors, as well as the Cooperative's lenders, have approved amendments to the Contracts permitting the Members to purchase renewable distributed generation resources in an amount not to exceed one percent of the Member's annual summer peak purchases from the Cooperative.

The Cooperative has a power supply agreement with SWEPCO, whereby SWEPCO agrees to provide the Cooperative's requirements at certain points of delivery. SWEPCO, the Cooperative and NTEC entered into an agreement dated November 2, 2009, that has a twenty (20) year term and provides for the sale of partial requirements service for the first five years and 80Mw for the remaining fifteen years. During 2020 and 2019, the Cooperative paid $22,382,312 and $18,061,869, respectively, to SWEPCO for the purchase requirements.

The Cooperative is a party to power supply agreement to acquire power from NextEra Energy Marketing that entitles the Cooperative to purchase a fixed amount of energy per hour at a fixed cost during the delivery period. The Cooperative was required to purchase approximately 249Mw during the years ending December 31, 2020 and 2019, respectively. The Cooperative paid $21,568,282 and $23,390,732 in 2020 and 2019, respectively, for purchased power associated with this agreement. This power supply agreement terminates at the end of 2021.

In October 2015, the Cooperative entered into a purchase power agreement with Grant Wind, LLC, a subsidiary of Southern Renewable Energy, Inc., to purchase 50Mw of output from a wind-powered generating facility for a fixed price. The facility has a total of 150Mw of installed capacity and the agreement is for a 20-year term. In November 2016, the Cooperative has also entered into a purchase power agreement with Redbed Plains Wind Farm, LLC, a subsidiary of EDP Renewables, to purchase 50Mw of output from a wind-powered generating facility for a fixed price. The facility has a total of 100Mw of installed capacity and the agreement is for a 20-year term.

The Cooperative purchases power from the Southwestern Power Administration ("SWPA"), an agency of the Department of Energy, through Sam Rayburn Dam Electric Cooperative, Inc. ("SRDEC"). SRDEC has entered into a contract whereby the Cooperative acquired an entitlement to the hydroelectric output of the Sam Rayburn Hydroelectric Plant with the term of the agreement expiring December 2027. In the event that SRDEC is not able to receive enough power (primarily as a result of inadequate rainfall) to cover operating costs (primarily entitlement to SWPA), the Cooperative is obligated to absorb 66-2/3 percent of the deficiency. In 2020 and 2019, $3,354,478 was paid for power and energy purchased from SRDEC.

Sam Rayburn Municipal Power Agency ("Agency") and the Cooperative have an agreement for the Agency to sell to the Cooperative a 24.89% share (1.49 MW) of the output of the Robert Douglas Willis Hydropower Project (the "Project") with the term of the agreement expiring December 2039. Under the assignment arrangement, the Cooperative will pay 24.89% of all the Project costs and expenses, including debt service, which amounted to $656,400 for both 2020 and 2019. The assignment arrangement provides that the Cooperative is to receive 24.89% of any power made available to the Agency from the Project each month.

NOTE 12 - RETIREMENT PLANS

All employees of the Cooperative participate in the NRECA RS 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 Employer 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. The Cooperative's contributions to the RS Plan in 2020 represented less than 5 percent of the total contributions made to the plan by all participating employers. The Cooperative made contributions to the plan of $143,695 and $186,543 in 2020 and 2019, respectively.

NOTE 12 - RETIREMENT PLANS - CONTINUED

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 RS Plan was over 80 percent funded on January 1, 2019 based on the 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 also participates in a 401(k) plan offered to similar cooperatives by the NRECA. The Cooperative matches certain employee contributions. Such matching contributions amounted to $22,834 and $31,387 in 2020 and 2019, respectively.

NOTE 13 - RELATED PARTY TRANSACTIONS

The Cooperative has various electrical facility operating agreements with its Members for the operation and maintenance of certain transmission facilities and telemetering equipment. During 2020 and 2019, the Cooperative paid approximately $408,000 and $401,000, respectively, to its Members for operations and maintenance services. There were no amounts payable for the years ended December 31, 2020 and 2019 to these Members.

NOTE 14 - RATE MATTERS

In 1999, the Texas Legislature approved Senate Bill 7, which provided, among other things, that the Cooperative's rates for the sale of wholesale power are no longer regulated by the Public Utility Commission of Texas ("PUCT"). Similarly, the rates of the Members for the sale of electricity are no longer regulated by the PUCT. The law permits cooperatives' boards of directors to set rates.

Investor-owned utilities in the Electric Reliability Council of Texas ("ERCOT") were required to allow their retail customers to select generation suppliers of electricity as of January 2002. The law gives cooperatives' boards of directors sole authority to allow, or not allow, generating suppliers to attempt to sell electricity to retail customers of a cooperative. Allowing retail customer choice is called "opting in". Even if a cooperative's board decides to opt in, retail customers will continue to use the transmission and distribution facilities of the Cooperative's Members. The Cooperative monitors whether any of its Members will decide to opt in and thus evaluate the potential effects of a change in generation sales. The law allows the Cooperative to recover stranded costs if it experiences a loss of load which would impair payment of debt service and payment of purchased power fixed charges. As of December 31, 2020, none of the distribution cooperatives who are served by the Cooperative's Members have elected to opt in.

NOTE 15 - COMMITMENTS AND CONTINGENCIES

General

The Cooperative is not a party to any pending legal proceedings that management or the Cooperative's legal counsel believe are material to its financial condition, results of its operations, or cash flows. The Cooperative maintains liability insurance against risks, subject to certain self-insurance limits, arising out of the normal course of its business.

In addition, in the normal course of business the Cooperative has ongoing disputes with some of its power suppliers. Some of the billings received by the Cooperative for purchased power are subject to adjustment based on the actual costs of the seller.

Power Supply

On July 15, 2019, SWEPCO filed an application at the PUCT requesting approval to acquire three wind farms totaling 1,485Mw, along with the possibility of transmission of approximately 150 miles. The total cost of SWEPCO's share of the project, excluding the transmission line, was estimated to be $1.09 billion. The Cooperative has filed testimony taking the position that the project contains risks with speculative benefits and should therefore be rejected as not in the public interest. Management believes the project could have a significant negative impact on the Cooperative's power supply agreements with SWEPCO. On July 2, 2020, the PUCT denied SWEPCO’s application. SWEPCO received approval from regulators in Arkansas and Louisiana and plans to continue with the project, but is not expected to have any impact upon the Cooperative or its operations.

Investments in Utility Plant Projects

The Cooperative has experienced three significant flood events that have impacted the construction of the R.C. Thomas Hydroelectric Project. The events delayed the commercial operations date from an initial estimate of May 2019 to July 2020. The contract for construction of the project is a fixed price contract; however, it is subject to force majeure events. The Cooperative is seeking relief from its insurance carrier and from the Federal Emergency Management Agency (FEMA). During the years ended December 31, 2020 and 2019, the Cooperative received approximately $2.3 million and $7.5 million, respectively, from the insurance carrier associated with the flood events.

NOTE 15 - COMMITMENTS AND CONTINGENCIES - CONTINUED

In addition, on March 11, 2020, the World Health Organization assessed and characterized the novel coronavirus (COVID-19) outbreak as a pandemic. Subsequent to the declaration of a pandemic, a variety of federal, state, and local governments have taken actions in response to the pandemic, which have ranged by jurisdiction, but generally included travel restrictions and quarantine orders. As a result of these events along with certain contested construction and warranty issues, the Cooperative has asserted liquidated damage claims and warranty claims against the construction contractor in the amount of approximately $6,700,000. Concurrently, the construction contractor has also asserted certain delay and additional work claims against the Cooperative in the amount of $15,700,000, which includes $7,300,000 in contract retainage. The delays in completion of the project and uncertainty with associated force majeure delay claims could result in the cost of the project exceeding the current project total of approximately $156,000,000.

Entergy Texas completed construction on a 993Mw combined-cycle generating unit in Montgomery County, Texas. The total cost of the MCPS is $871 million. MCPS was approximately 65% complete as of December 31, 2019 and achieved commercial operation on January 1, 2021. The Cooperative funded its ownership in MCPS (75Mw) on June 4, 2021 with a total cost of approximately $65,800,000. See Note 2.

The Cooperative has entered into an Asset Purchase Agreement with Entergy Texas, Inc. to sell Hardin Units 1 and 2 at the Cooperative's net book value as of closing. This transaction occurred at the same time the Cooperative acquired its ownership in MCPS June 4, 2021. The net book value total at closing is $36,534,118. The Cooperative has received approval from RUS, CFC and CoBank for this transaction.

Due to economic reasons, the Cooperative elected to temporarily suspend operations at the Hilton Lively Renewable Power Project (Note 2). The MISO market requires that plants within the RTO operate in two out of every five years on a rolling basis. The Hilton Lively Renewable Power Project began suspended operations in August 2016 and will therefore have been in suspended operations status for three years as of August 2019. In 2019, the Board elected to disconnect the Hilton Lively Renewable Power Project from the MISO market, losing its interconnection service.

In August and October 2020, Hurricane Laura, Hurricane Delta, and Hurricane Zeta caused significant damage to portions of the Utility's service territories in Louisiana, including New Orleans, Texas, and to a lesser extent, in Arkansas and Mississippi. The storms resulted in significant damage to distribution and transmission infrastructure to Nelson Unit 6. Additionally, as a result of Hurricane Laura's extensive damage to the grid infrastructure serving the impacted area, large portions of the underlying transmission system required nearly a complete rebuild. Total restoration costs for the repair and/or replacement of the electrical system damaged by Hurricane Laura, Hurricane Delta, and Hurricane Zeta are currently estimated to be $5,240,000 for the Cooperative.

Environmental Regulation

The Cooperative's facilities and operations are subject to regulation by various governmental authorities having jurisdiction over air quality, water quality, control of toxic substances and hazardous and solid wastes, and other environmental matters. Management believes that the Cooperative is in substantial compliance with environmental regulations currently applicable to its facilities and operations. Because environmental regulations are subject to change, future compliance requirements and costs cannot be precisely estimated.

There have been significant efforts in the United States to regulate greenhouse gas emissions through regulatory changes. These efforts culminated in the issuance by the Environmental Protection Agency of a final rule for both new and existing power plants in August 2015 (the "Clean Power Plan"). The Clean Power Plan provided standards and guidelines for the development of state implementation plans that would reduce carbon emissions from existing power plants. The standards and guidelines have been challenged by several dozen states as well as industry groups and other stakeholders. In February 2016, the US Supreme Court issued a stay on implementation of the rule, including all of the deadlines for submission of initial or final state plans. In 2017, the Federal EPA issued a proposal to repeal the Clean Power Plan and an advance notice of proposed rulemaking seeking information that should be considered in the development of new emission guidelines. The EPA issued the proposed Affordable Clean Energy ("ACE") rule in August 2018 to replace the Clean Power Plan. The ACE rule was finalized by EPA in June 2019 and the rule provides the states wide latitude to formulate unit-specific standards and focuses primarily on efficiency upgrades at coal units. The ACE rule was vacated by the U.S. Court of Appeals for the DC Circuit in January 2021, with the EPA being directed to develop a new plan that is consistent with existing federal guidelines. There is currently no anticipated timeline for the development of this new rule.

Reduced carbon emission standards could result in increases in capital expenditures and operating costs and could impact the dates for retirement of Cooperative coal-fired power plants. The Cooperative is currently unable to predict with any degree of certainty when (or if) a comprehensive regulatory scheme for greenhouse gases will be in place.

NOTE 16 - CONCENTRATIONS OF CREDIT RISK

The Cooperative's financial instruments that are exposed to concentrations of credit risk consist primarily of cash equivalents and accounts receivable.

NOTE 16 - CONCENTRATIONS OF CREDIT RISK - CONTINUED

The Cooperative places its cash and cash equivalents on deposit with financial institutions in the United States. The Federal Deposit Insurance Corporation (FDIC) provides coverage to $250,000 for substantially all depository accounts, per depositor, per depository institution. At various times during the year, cash balances may exceed insured limits. The Cooperative has not experienced any losses in such accounts.

The Cooperative's accounts receivable are subject to concentration of credit risk due to the Cooperative's customer base. Substantially all of the accounts receivable balance is due from the Cooperative's Members.

NOTE 17 - SUBSEQUENT EVENTS

In February 2021, a severe winter storm with extremely cold temperatures affected much of the U.S., including Texas. This severe weather resulted in surging demand for power, gas supply shortages, operational challenges for generators, widespread power outages, and disruption to the wholesale and retail energy markets. The Cooperative was required to purchase power during the storm at significantly escalated prices in order to meet supply obligations. As a result, the Cooperative incurred unbudgeted and unforeseen additional power purchase expenses of approximately $207 million. This estimate is preliminary and based on currently available information. The full financial impact still remains uncertain as it is subject to proposed regulatory changes including potential repricing, finalizing meter and settlement data, and potential customer and counterparty risk including shortfall payments and uplift charges.

In order to fund the additional power purchases incurred, the Cooperative utilized an existing $100 million credit facility with CoBank and obtained an additional short term loan from CoBank. The additional financing consisted of a $100 million term loan, which carries a variable interest rate and an initial termination date of March 2022. Management is currently evaluating long-term financing options. In addition to the credit facilities, the Cooperative requested the Members fund approximately twenty-five percent of the unbudgeted power cost. The Cooperative received from the Members approximately $51.7 million in March 2021 for this share.

The Cooperative’s tariff provides for a power cost recovery mechanism that allows for the recovery of incurred purchased power expenses. Given the significance of these costs and in order to mitigate their impact on the Members, the Cooperative anticipates deferring these costs over an extended period of time. Management believes these costs are probable of future recovery. The recovery of these costs from Members; however, may be extended over longer than usual time periods. If the Cooperative is unable to recover these purchased power expenses, it could reduce future net margins and cash flows and impact the Cooperative’s financial condition.

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*

The Board of Directors
East Texas Electric Cooperative, Inc.
Nacogdoches, Texas

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of East Texas Electric Cooperative, Inc. which comprise the balance sheet as of December 31, 2020 and 2019 and the related statement of revenue and expenses, comprehensive income, patronage capital and cash flow for the year then ended and the related notes to the financial statements and have issued our report thereon dated June 22, 2021.

Internal Control Over Financial Reporting

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

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

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

Compliance

As part of obtaining reasonable assurance about whether East Texas Electric Cooperative, Inc.'s financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance 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 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.

Axley & Rode LLP
CERTIFIED PUBLIC ACCOUNTANTS

Lufkin, Texas
June 22, 2021

INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH ASPECTS OF CONTRACTUAL AGREEMENTS AND REGULATORY REQUIREMENTS FOR RUS ELECTRIC BORROWERS

AXLEY&RODE LLP
CERTIFIED PUBLIC ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT

Board of Directors
East Texas Electric Cooperative, Inc.
Nacogdoches, Texas

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of East Texas Electric Cooperative, Inc. (the Cooperative), which comprise the balance sheet as of December 31, 2020 and the related statements of revenue and expenses, patronage capital and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated June 22, 2021. In accordance with *Government Auditing Standards*, we have also issued our report dated June 22, 2021, 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 recommendation 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*, section 1773.33 and clarified in RUS policy memorandum dated February 7, 2014, insofar as they relate to accounting matters as enumerated below. However, our audit was not directed primarily toward obtaining knowledge of noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Cooperative's noncompliance with the above-referenced terms, covenants, provisions, or conditions of the contractual agreements and regulatory requirements, insofar as they relate to accounting matters. In connection with our audit, we noted no matters regarding the Cooperative's accounting and records to indicate that the Cooperative did not:

Maintain adequate and effective accounting procedures;

Utilize adequate and fair methods of accumulating and recording labor, material, and overhead costs, and the distribution of these costs to construction, retirement, and maintenance or other expenses 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 financial statements, in accordance with requirements for related parties in generally accepted accounting principles;

Record depreciation in accordance with RUS requirements (See RUS Bulletin 183-1, Depreciation Rates and Procedures);

Comply with the requirements for the detailed schedule of deferred debits and deferred credits; and

Comply with the requirements for the detailed schedule of investments.

This report is intended solely for the information and use of the board of directors, management, and the RUS and supplemental lenders and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Axley & Rode LLP
CERTIFIED PUBLIC ACCOUNTANTS

Lufkin, Texas
June 22, 2021

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