FINANCIAL STATEMENTS WITH
REPORT OF INDEPENDENT AUDITORS

EAST TEXAS ELECTRIC COOPERATIVE, INC.

December 31, 2021 and 2020

C O N T E N T S

REPORT OF INDEPENDENT AUDITORS

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

Opinion

We have audited the accompanying financial statements of East Texas Electric Cooperative, Inc. (the "Cooperative") which comprise the balance sheets as of December 31, 2021 and 2020 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.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Cooperative as of December 31, 2021 and 2020, and the results of operations and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis of Opinion

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Cooperative and to meet our other ethical responsibilities in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis of our audit opinion.

Responsibility of Management 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Cooperative's ability to continue as a going concern within one year after the date that the financial statements are available to be issued.

Auditor's Responsibility for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements, including omission, are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgement made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards, we:

- Exercise professional judgement and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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, no such opinion is expressed.

- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Cooperative's ability to continue as a going concern for a reasonable period of time.

Other Matters

In accordance with *Government Auditing Standards*, we have also issued our report dated April 13, 2022, 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.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Axley & Rode LLP
CERTIFIED PUBLIC ACCOUNTANTS

Lufkin, Texas
April 13, 2022

axleyrode.cpa

EAST TEXAS ELECTRIC COOPERATIVE, INC.
BALANCE SHEETS
December 31, 2021 and 2020

	2021	2020
ASSETS		
Utility Plant:		
Utility plant in service	$ 1 103 916 752	$ 1 073 855 376
Construction work in progress	823 834	29 165 661
	1 104 740 586	1 103 021 037
Less accumulated provision for depreciation	417 205 857	425 296 740
	687 534 729	677 724 297
Investments and Other Assets:		
Investments in associated organizations	42 152 647	42 487 650
	42 152 647	42 487 650
Current Assets:		
Cash and cash equivalents	24 410 682	15 594 356
Accounts receivable from member cooperatives	47 062 813	47 197 733
Accounts receivable - Other	1 145 712	1 861 327
Certificates of deposit	6 908 163	7 228 500
Investment securities - Available for sale	33 612 260	3 239 524
Fuel stock	5 873 534	6 081 107
Materials and supplies	15 251 811	13 382 587
Other current assets	6 211 287	2 431 540
	140 476 262	97 016 674
Deferred debits	248 371 014	156 394 650
	$ 1 118 534 652	$ 973 623 271
EQUITIES AND LIABILITIES		
Equity and Margin:		
Patronage capital	$ 209 965 777	$ 199 433 211
Accumulated comprehensive income (loss)	(56 726)	28
	209 909 051	199 433 239
Long-term debt, less current maturities	734 479 481	648 342 278
Current Liabilities:		
Accounts payable - Purchased power	12 067 973	18 533 537
Accounts payable - Other	6 972 957	18 366 227
Accrued expenses	11 229 723	10 948 837
Line of credit - General	100 000 000	-
Current maturities of long-term debt	41 619 274	74 998 724
	171 889 927	122 847 325
Deferred credits	2 256 193	3 000 429
	$ 1 118 534 652	$ 973 623 271

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, 2021 and 2020

	2021	2020
Operating Revenues:		
Power sales - Members	$ 459 164 458	$ 292 181 251
Other electric revenues	41 330 958	25 561 227
	500 495 416	317 742 477
Operating Expenses:		
Purchased power	210 321 556	95 591 936
Power Generation:		
Fuel	101 526 342	43 363 990
Other production expenses	36 590 175	35 984 015
Transmission	60 511 666	55 946 636
Administrative and general	9 337 145	10 636 406
Depreciation	36 487 248	34 393 588
Amortization of regulatory asset	8 816 612	8 816 612
	463 590 744	284 773 183
OPERATING MARGINS BEFORE INTEREST EXPENSE	36 904 672	33 009 294
Interest expense	30 207 436	28 362 879
OPERATING MARGINS	6 697 236	4 646 415
Nonoperating Margins:		
Other income	-	95 000
Interest income	1 186 342	3 106 218
Capital credits and patronage capital allocations	2 648 988	2 344 892
NET MARGINS	$ 10 532 566	$ 10 192 525

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, 2021 and 2020

	2021	2020
NET MARGINS	$ 10 532 566	$ 10 192 525
Other Comprehensive Income (Loss):		
Unrealized gains (losses) on available for sale securities	(56 754)	44 250
OTHER COMPREHENSIVE INCOME (LOSS)	(56 754)	44 250
COMPREHENSIVE INCOME	$ 10 475 812	$ 10 236 775

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, 2021 and 2020

	PATRONAGE CAPITAL	ACCUMULATED COMPREHENSIVE INCOME (LOSS)	TOTAL
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
Net margins	10 532 566	-	10 532 566
Other comprehensive income (loss)	-	(56 754)	(56 754)
Balance, December 31, 2021	$ 209 965 777	$ (56 726)	$ 209 909 051

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, 2021 and 2020

	2021	2020
Operating Activities:		
Net margins	$ 10 532 566	$ 10 192 525
Adjustments to Reconcile Net Margins to Net Cash Provided by Operating Activities:		
Depreciation	36 487 248	34 393 588
Amortization	8 816 612	8 816 612
Patronage capital credits - Non-cash	(1 031 918)	(984 890)
Reinvested dividends on investment securities	(14 860)	(13 274)
Cash Provided by (Used for) the Change in:		
Accounts receivable - Members	134 920	(2 097 171)
Accounts receivable - Other	648 915	(490 011)
Fuel stock	207 574	60 499
Materials and supplies	(1 524 507)	597 125
Other current assets	(3 920 159)	(1 814 671)
Deferred debits	198 863	198 866
Accounts payable	(6 465 565)	3 134 068
Accounts payable - Other	(3 336 682)	(604 175)
Accrued expenses	598 038	1 721 226
Deferred credits	(4 323 126)	(5 312 263)
NET CASH PROVIDED BY OPERATING ACTIVITIES	36 665 204	47 798 054
Investing Activities:		
Capital expenditures (including interest capitalized)	(90 916 408)	(27 399 073)
Redemption of CFC loan certificates	1 366 921	1 356 163
RUS cushion of credit	-	64 911 744
Funds held in escrow	-	3 363 921
Proceeds from disposition of Hardin facility	36 534 117	-
Regulatory asset – Winter Storm Uri	(97 496 969)	-
Certificates of deposit	320 337	(26 600)
Other investments	(30 414 630)	(128 427)
NET CASH (USED) PROVIDED BY INVESTING ACTIVITIES	(180 606 632)	42 077 728
Financing Activities:		
Loan advances - RUS	46 392 072	-
Loan advances - CFC	-	12 347 646
Loan advances - CoBank	100 000 000	92 900 000
Loan payments - RUS	(12 202 240)	(116 057 686)
Loan payments - Others	(56 033 626)	(17 396 824)
Clean Renewable Energy Bonds	(7 523 213)	(7 523 213)
Net activity - Syndicated facility/lines of credit	82 124 761	(46 500 000)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	152 757 754	(82 230 077)
NET INCREASE IN CASH AND CASH EQUIVALENTS	8 816 326	7 645 705
Cash and cash equivalents, beginning of year	15 594 356	7 948 651
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 24 410 682	$ 15 594 356
Supplemental Disclosures of Cash Flow Information:		
Cash paid for interest	$ 30 370 450	$ 30 900 782
Supplemental Schedule of Non-Cash Investing and Financing Activities:		
Unrealized gain/(loss) on investment available for sale	$ (56 754)	$ 44 250
(Decrease)/Increase in accounts payable for capital expenditures	$ (7 452 738)	$ 9 102 480

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

The Cooperative's policies with respect to its various revenue streams are detailed below. In general, the Cooperative applies the invoicing practical expedient 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 2021 and 2020, there was an under-collection of $1,727,376 and $196,360, 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.

Renewable Energy Certificates

The Cooperative receives renewable energy certificates, also known as renewable energy credits, (RECs) in connection with generation from its hydroelectric facility and its power purchases from wind farms, which are discussed in Note 9 - 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 2021 or 2020. 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.

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

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, 2021.

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, 2021 and 2020, 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 $1,216,179 and $1,165,805, 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.

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 revenue and expenses 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.

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

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, 2021 and 2020, capitalized interest was approximately $-0- and $1,495,767, 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.

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.

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

There were no derivative instruments outstanding as of December 31, 2021 or 2020.

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.

Significant Events Impacting Operations

In February 2021, a severe winter storm (“Winter Storm Uri”) 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. As a result, the Cooperative experienced increased cost of power, which will be recovered on a deferred basis over a period not to exceed ten years. Refer to Notes 5 for additional details.

New Authoritative Accounting Guidance:

In February 2016, FASB issued ASU 2016-02, *Leases.* The standard introduced 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 *ASU 2014-09, 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 April 13, 2022, the date the financial statements were available to be issued.

NOTE 2 - UTILITY PLANT

The following summarizes utility plant as of December 31, 2021 and 2020:

		2021		2020
Utility Plant, at Cost:				
Transmission	$	132 947 756	$	101 150 011
Production plant		968 087 770		969 814 865
Distribution and telemetering		696 921		696 921
Asset retirement obligations - Generation		736 452		788 143
Office building		698 312		698 312
Office equipment		749 541		707 124
		1 103 916 752		1 073 855 376
Construction work in progress		823 834		29 165 661
		1 104 740 586		1 103 021 037
Less accumulated depreciation		417 205 857		425 296 740
	$	687 534 729	$	677 724 297

The Cooperative outright owns or holds partial ownership in multiple power plant facilities. The Cooperative is responsible for its share of operating and capital costs for each facility it jointly owns with other entities. The Cooperative's ownership share of each facility as of December 31, 2021 and 2020, 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%
Montgomery County Power Station (75Mw)	7.56%
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

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 7). 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 entered into an Asset Purchase Agreement (APA) with Entergy Texas, Inc. for the purchase of 7.56% 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. On June 4, 2021, the Cooperative funded its ownership share of MCPS with available cash and closed on the transaction. The Cooperative has applied for financing with RUS to fund its ownership in the facility with an anticipated closing date no later than June 2022.

Hardin County Units 1 and 2

In 2021, the Cooperative entered into a sales agreement with Entergy Texas, Inc. for its ownership in Hardin County Units 1 and 2 at the historical book value of $36,534,117. This sale occurred as a simultaneous transaction with the purchase of its participation in Montgomery County Power Station as detailed above, which also closed on June 4, 2021. A portion of the proceeds from this sale were used by the Cooperative to pay off its debt related to Hardin County Units 1 and 2.

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, 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, 2021 and 2020, the amount amortized and recovered through rates was $8,816,612 and $8,816,612, respectively. As of December 31, 2021 and 2020, the balance of the regulatory asset including both impairment deferrals was $135,853,928 and $144,670,540, respectively.

NOTE 3 - INVESTMENTS IN ASSOCIATED ORGANIZATIONS

Investments in associated organizations as of December 31, 2021 and 2020 consisted of the following:

		2021		2020
National Rural Utilities Cooperative Finance Corporation (CFC):				
Patronage capital and membership	$	8 355 966	$	7 863 020
Member capital securities		500 000		500 000
Loan capital term certificates		21 274 627		22 641 549
CoBank:				
Patronage capital and membership		6 954 358		6 415 385
Sam Rayburn Dam Electric Cooperative, Inc. (Note 9)		5 065 586		5 065 586
Memberships		2 110		2 110
	$	42 152 647	$	42 487 650

Patronage capital allocations reported in the Statements of Revenue and Expense in the amount of $2,648,988 and $2,344,892 for the fiscal years ended December 31, 2021 and 2020, respectively, represent patronage capital allocations from CoBank and CFC.

NOTE 4 - 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 $33,612,260 and $3,239,524 as of December 31, 2021 and 2020, respectively. The amount of unrealized gain or (loss) included in other comprehensive income is $(56,726) and $28 for the years ended December 31, 2021 and 2020.

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, 2021:								
Money Market Mutual Fund	$	30 015 652	$	-	$	-	$	30 015 652
U.S. Government Obligations		2 888 386		16 392		(51 597)		2 853 181
Mutual Fund Bond		764 948		-		(21 521)		743 427
TOTALS	$	33 668 986	$	16 392	$	(73 118)	$	33 612 260
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

The scheduled maturities of securities to be held to maturity and securities available for sale as of December 31, 2021 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		743 427
Due from five to ten years		-		-
Over ten years		-		-
Money Market Mutual Fund		30 015 652		30 015 652
Mutual Fund Bond		2 888 386		2 853 181
	$	33 668 986	$	33 612 260

NOTE 4 - INVESTMENT SECURITIES AND FAIR VALUE MEASUREMENTS - CONTINUED

Information pertaining to securities with gross unrealized losses as of December 31, 2021 and 2020 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	
2021 Description of Securities:	FAIR VALUE	UNREALIZED LOSSES	FAIR VALUE	UNREALIZED LOSSES	FAIR VALUE	UNREALIZED LOSSES
U.S. Governments	$ 974 428	$ (9 311)	$ 1 246 900	$ (50 379)	$ 2 221 328	$ (59 690)
Mutual Fund Bonds	$ -	$ -	$ 743 427	$ (21 521)	$ 743 427	$ (21 521)
2020 Description of Securities:						
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)

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, 2021, 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 5 - DEFERRED DEBITS/CREDITS

The following is a summary of the amounts recorded as deferred debits/credits as of December 31, 2021 and 2020:

	2021	2020
DEFERRED DEBITS		
Debt issuance costs	$ 73 190	$ 98 283
Retirement security plan	39 254	72 900
Prepayment premium on settlement of derivative	3 345 014	3 518 784
Due from member - Billing correction	697 686	1 375 028
Due from members - Levelized billing	1 727 376	196 360
Regulatory asset - Impairment (Note 2)	135 853 928	144 670 540
Regulatory asset - Winter Storm Uri	97 496 969	-
Prepayment premium on early payoff of debt	5 745 238	6 034 913
Provision for property insurance (Note 13)	3 392 359	427 842
	$ 248 371 014	$ 156 394 650
DEFERRED CREDITS		
Overhead and maintenance	$ 1 040 014	$ 1 834 624
Asset retirement obligations (Note 1)	1 216 179	1 165 805
	$ 2 256 193	$ 3 000 429

Debt Issuance Costs

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.

Retirement Security Plan

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.

Prepayment Premium on Settlement of Derivative

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.

NOTE 5 - DEFERRED DEBITS/CREDITS - CONTINUED

Due from Member - Billing Correction

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 $697,686 remaining to be collected as of December 31, 2021. 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.

Due from Members - Levelized Billing

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.

Regulatory Asset - Winter Storm Uri

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 $199,519,080. The Cooperative received $102,022,111 of the unbudgeted power cost from the Members during the year ending December 31, 2021 and, as a result, the Cooperative recorded $102,022,111 of winter storm related power cost and related revenue in 2021. The Cooperative applied for and received approval from RUS to defer the remaining $97,496,969 power purchases incurred for future rate recovery as a regulatory asset. The Cooperative was approved to amortize and recover the regulatory asset over a period not to exceed 10 years beginning January 2022. The short-term and permanent financing associated with the regulatory asset are described in Notes 7 and 15.

Prepayment Premium of Early Payoff of Debt

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 amounts 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.

Overhead and Maintenance

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.

NOTE 6 - PATRONAGE CAPITAL

Patronage capital as of December 31, 2021 and 2020 consists of the following:

	2021	2020
Assignable patronage capital	$ 10 532 566	$ 10 192 525
Assigned patronage capital	199 433 211	189 240 686
	$ 209 965 777	$ 199 433 211

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.

NOTE 6 - PATRONAGE CAPITAL

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 19% and 20% of total assets as of December 31, 2021 and 2020, respectively. For the years ended December 31, 2021 and 2020, no patronage capital was retired.

NOTE 7 - LONG-TERM DEBT

Long-term debt as of December 31, 2021 and 2020 consisted of the following:

	2021	2020
Federal Financing Bank ("FFB") mortgage notes guaranteed by RUS, fixed rates 1.94% to 5.27%, maturing at various times through 2044	$ 281 783 745	$ 247 593 911
CFC Fixed Rate Notes - 3.35% to 7.15%, maturing at various times through 2041	178 268 690	192 224 084
CFC Financing Notes - Capital term certificates, fixed rates from 4.52% to 5.72%, maturing 2024-2041	19 813 302	21 046 284
CFC/Regions Syndicated Revolving Credit Facility - variable interest rates, maturing 2021	-	17 875 239
Clean Renewable Energy Bonds - Hilton Lively Renewable Power Plant, CFC, effective rate of 1.36%, maturing 2035	33 241 758	35 659 341
Clean Renewable Energy Bonds - R.C. Thomas Facility CFC, effective rate of 2.95%, maturing 2024	1 912 500	2 550 000
Clean Renewable Energy Bonds - R.C. Thomas Facility CoBank, effective rate of 1.25%, maturing 2035-2040	66 215 741	70 338 399
CoBank Variable Rate Note - maturing 2022	100 000 000	-
CoBank Fixed Rate Note - 3.06%, maturing 2021	-	36 000 000
CoBank Fixed Rate Note - 3.92%, maturing 2031	8 771 639	9 648 802
CoBank Fixed Rate Notes - 2.75% to 5.64%, maturing 2041	86 091 380	90 404 942
	776 098 755	723 341 002
Less current maturities	41 619 274	74 998 724
	$ 734 479 481	$ 648 342 278

The Cooperative has secured long-term financing from RUS to finance an ownership interest in several power projects including HCPP, Nelson Unit 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, 2021, the Cooperative received an advance in the amount of $46,392,072 related to the R.C. Thomas Hydroelectric Project. The Cooperative has an approved commitment from RUS for an additional $19,519,518 for the permanent financing of the R.C. Thomas Hydroelectric Project. As of December 31, 2021, the RUS notes aggregated $281,783,745.

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 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 with 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. The facility has been utilized to fund the additional power purchases incurred during Winter Storm Uri (Note 5). The Cooperative had $100,000,000 outstanding on this facility as of December 31, 2021.

On March 9, 2021, the Cooperative also obtained a short-term loan from CoBank to fund the additional power purchases incurred during Winter Storm Uri (Note 5). This short-term financing consists of a $100,000,000 term loan, which carries a variable interest rate and a termination date of June 2022.

The Cooperative has received an allocation and has issued $55,000,000 in CREBS related to the Hilton Lively Renewable Power Project from CFC. The funds were utilized to finance the construction of the facility and had a balance of $33,241,758 as of December 31, 2021.

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 $1,912,500. 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. As of December 31, 2021, the balance of the CREBS amounted to $66,215,741.

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 $8,771,639 as of December 31, 2021.

NOTE 7 - LONG-TERM DEBT - CONTINUED

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, 2021, the Cooperative had a balance of $32,500,000 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 long-term financing consists of fixed rate loan with CoBank with a balance of $53,591,382 as of December 31, 2021 and a fixed rate note with CFC with a balance of $11,566,150 as of December 31, 2021.

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, 2021 and 2020, 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:

2022	$	41 619 274
2023	$	42 004 282
2024	$	38 789 018
2025	$	37 936 418
2026	$	38 214 030

The Cooperative has a $12,000,000 line of credit with CFC that matures on May 28, 2023. As of December 31, 2021 and 2020, no funds were advanced or owed under this line of credit. In January 2022, the Cooperative increased the line of credit with CFC from $12,000,000 to $75,000,000 with the maturity date extended to May 28, 2025.

The Cooperative also has an additional line of $25,000,000 with CoBank that matures on October 31, 2024. As of December 31, 2021 and 2020, no funds were advanced or owed under this line of credit.

NOTE 8 - 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, 2021 and 2020 the total transmission lease payments were $133,517 and $112,636, respectively. Estimated lease payments for each of the next five (5) years will approximate $130,000.

NOTE 9 - 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 2021 and 2020, the Cooperative paid $46,673,803 and $22,382,312, respectively, to SWEPCO for the purchase requirements.

The Cooperative is also obligated under several power purchase agreements with third-party suppliers to purchase fixed quantities of energy at fixed rates in the ERCOT region. The Cooperative paid $26,566,534 and $13,014,036 in 2021 and 2020, respectively, for purchased power associated with these agreements. These agreements are for varying quantities and lengths, terminating from 2022 to 2031.

NOTE 9 - POWER CONTRACTS - CONTINUED

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 2021 and 2020, $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 2021 and 2020. 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 10 - 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 2021 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 $99,792 and $143,695 in 2021 and 2020, respectively.

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, 2020 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 $24,702 and $22,834 in 2021 and 2020, respectively.

NOTE 11 - 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 2021 and 2020, the Cooperative paid approximately $672,000 and $408,000, respectively, to its Members for operations and maintenance services. There were no amounts payable as of the years ended December 31, 2021 and 2020 to these Members.

NOTE 12 - 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.

NOTE 12 - RATE MATTERS - CONTINUED

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, 2021, none of the distribution cooperatives who are served by the Cooperative's Members have elected to opt in.

NOTE 13 - 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 adjustments based on the actual costs of the seller.

Power Supply

On October 14, 2020, SWEPCO filed an application at the PUCT requesting approval to change its Texas retail rates. Certain decisions by the PUCT concerning the depreciation rates of SWEPCO's generation assets have a flow-through effect on the power supply charges paid by the Cooperative under the applicable power supply agreements. Thus, the Cooperative participated in this PUCT ratemaking proceeding in order to protect its interests related to these power supply charges. On January 14, 2022, the PUCT issued its order, which, among other things, substantially adopted the Cooperative's recommendations concerning the appropriate ratemaking treatment of the depreciation of certain generation assets. Management believes this favorable outcome could have a positive effect on the Cooperative's power supply agreements with SWEPCO. The positive effect would be reflected in SWEPCO’s wholesale formulary rates filed at FERC. The case is expected to be appealed which may affirm or reverse and remand the PUCT's January 14, 2022 order.

Investments in Utility Plant Projects

The Cooperative has experienced three significant flood events that 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, 2021 and 2020, the Cooperative received approximately $136,000 and $2,254,268 million, respectively, from the insurance carrier associated with the flood events.

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. Concurrently, the construction contractor has also asserted certain delay and additional work claims against the Cooperative. As of December 31, 2021, all project claims between the Cooperative and the construction contractor have been resolved in mediation and no further construction defect, design or delay claims are pending on the project.

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 achieved commercial operation on January 1, 2021. The Cooperative funded its ownership in MCPS (75Mw) on June 4, 2021 with a total cost of $65,832,432. See Note 2.

The Cooperative 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 $36,534,117. The Cooperative 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 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.

NOTE 13 - COMMITMENTS AND CONTINGENCIES - CONTINUED

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 approximately $4,200,000 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. Although the new administration's EPA withdrew the ACE Rule upon taking office, several parties appealed the DC Circuit's decision to invalidate it, and the US Supreme Court heard oral arguments on these appeals on February 28, 2022. A decision is expected by the end of the Court's term in June.

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 14 - 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. 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 15 - SUBSEQUENT EVENTS

On September 27, 2021, RUS approved a loan guarantee commitment from FFB in the amount of $101,000,000, designated as an operating loan, with the proceeds to be used to replace the CoBank term loan maturing June 2022. Subsequent to the year ended December 31, 2021, the Cooperative plans to advance a combined total of $97,496,969 on the operating loan that will consist of three separate fixed rate term loans with various maturities. A five-year fixed rate term loan of $35,351,840, a seven-year fixed rate term of $45,988,365 and a ten-year fixed rate term loan of $16,156,764. As of the date of this report, no funds have been advanced on this loan.

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, 2021 and 2020 and the related statements 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 April 13, 2022.

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
April 13, 2022

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, 2021 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 April 13, 2022. In accordance with *Government Auditing Standards*, we have also issued our report dated April 13, 2022, 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
April 13, 2022

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