



PEDERNALES ELECTRIC COOPERATIVE

2019 ANNUAL REPORT



President's message



Paul Graf

President
District 6 Director

It is an understatement to say 2019 was a remarkable year at PEC.

We experienced accelerated account growth, economic boom within our communities, and celebrated several notable accomplishments. While adding an average of 1,300 meters a month — an increase of over 15,000 for the entire year — our commitment to our membership and communities remained intact while increasing reliability. Members, on average, experienced less than one outage lasting no more than 45 minutes!

Our pledge to maintain competitive rates was also top of mind. We are continuously reviewing existing policies and revised rates, power supply, and energy management programs. With continuous power demand monitoring, PEC is able to set some of the lowest rates possible. In fact, the most recent metrics available from the Public Utility Commission of Texas place PEC's rates at 8% lower than those paid by the average Texas residential customer. Additionally, the board has approved a permanent 1% rate decrease that takes effect June 2020.

PEC's financial stability and investment was also evident in our communities. The entire PEC Board of Directors stands strong with practical decisions that benefit our entire membership. In 2019, we returned more than \$12 million in capital credits to our members. To mark the 20th year of our scholarship program, we gave a record \$120,000 in scholarships to local graduates. And our employees gave \$250,000 to local charities through the PEC United Charities program.

Personally, I would like to acknowledge not just the board, but a very strong leadership team that is empowered to make day-to-day decisions in the best interest of the cooperative. This guidance starts at the top with Chief Executive Officer Julie Caruthers Parsley. Julie has pushed this culture down into the ranks and across the cooperative. Her leadership was well noted by the Austin Business Journal when they named her 2019 Best CEO in the nonprofit category. We're very proud of her and the entire PEC team for serving the membership with utmost professionalism and integrity.

It has been a pleasure to serve as board president for PEC. As many of you know, the board operated with only six directors during the latter part of 2019, and with only five directors in the first part of 2020. We are eager to get back to a full board with the 2020 elections in Districts 2, 3, and 4. Moving forward, we pledge to continue down the strong path we found ourselves in 2019, especially as the early part of 2020 brought on the coronavirus and its challenges. PEC is your cooperative, and we greatly value your membership and partnership.

Thank you!

As the Texas Hill Country grew in 2019, we kept the lights on 99.9% of the time, with three out of four members experiencing no planned outages.

CEO's message



Julie C. Parsley
Chief Executive Officer

For more than 81 years, Pedernales Electric Cooperative has been committed to improving the quality of life for our members in the Texas Hill Country. These challenging times are no exception. As we work through COVID-19 and its impact, we're focused on remaining resilient and well-positioned to support you and the communities you call home. We have entered this crisis in a position of strength, and we are acting quickly for the safety of our members and employees.

During 2019, we realigned our focus and recommitted to "Think Like a Member," building member engagement campaigns and discovering fresh ways to serve you better. We also invested in more employee training and development; as a result, our member responsiveness metrics and service levels not only rebounded, but we are now recording the highest customer service levels on record. You recognized these efforts, helping PEC rank in the top 10 of all electric cooperatives in the 2019 JD Power Syndicated Survey of Overall Satisfaction.

We also focused on our operations and strategic capital projects, allowing us to provide the outstanding, safe, reliable service we're known for while planning strategically for the future. As the Texas Hill Country grew in 2019, we kept the lights on 99.9% of the time, with three out of four members experiencing no unplanned outages. When an interruption did occur, our skilled crews were on the scene quickly and safely, keeping outages to an average of 45 minutes. For these and other achievements, PEC was selected by the Texas Public Power Association for its esteemed System Achievement Award, marking the first time an electric cooperative received such recognition.

It's been a pleasure to serve you and lead a dynamic organization powered by the best of the best in our industry. We closed 2019 stronger than ever, and I have every confidence we will continue to build on that strength for years to come.

Our membership makes us PEC Proud, and keeps us PEC Strong.





Empowered record growth

To accommodate record growth, we expanded – building more than 500 new miles of distribution line.

In 2019, we added more new meters and welcomed more members than ever before. By the end of the year, we reached nearly 330,000 accounts. In July alone, we added more than 2,000 accounts – a cooperative record. To accommodate this growth, we expanded – building more than 500 new miles of distribution line.

Keeping our members in mind, we introduced new virtual hold callback technology, and we completed upgrades at our Bertram, Oak Hill, Dripping Springs, and Cedar Park offices. Serving our members has been our priority for over 80 years, and no matter how large we grow, we will always think about each and every individual.

Supported record giving

Investing in our communities and giving back is part of who we are as your cooperative. Last year, we proudly awarded a record amount of funds to local nonprofits in our service territory. Through our Power of Change program, \$55,000 in PEC Community Grants went to 11 area nonprofits to support those helping the places we call home. PEC also sponsored and participated in nine volunteer events.

Celebrating 20 years of our scholarship program, we provided \$120,000 in scholarships, and sent 10 students to Washington, D.C., for NRECA's annual Youth Tour. Our employees gave too — through our United Charities organization, PEC staff donated more than \$250,000 to 222 local charities.

We proudly awarded a record \$55,000 to local nonprofits in our service territory.

PEC EMPLOYEE
CAROLE HALL AT
THE CENTRAL TEXAS
FOOD BANK.





Delivered record reliability

PEC members in 2019 experienced less than one outage, on average, lasting no more than 45 minutes.

As we continue to serve our expanding communities and growing membership, your cooperative is focused on delivering power you can count on. That's why we upgraded infrastructure and have ongoing projects in place to ensure dependability not just today, but for years to come.

On average, PEC members in 2019 experienced less than one outage, lasting no more than 45

minutes. We installed and upgraded five distribution substations, finished two voltage conversion projects, and more than 860 substation inspections.

Through our unmanned aerial vehicle program, we inspected more than 480 miles of distribution line and 300 miles of transmission line. These efforts are just part of our commitment to ensure we're able to power our members today, tomorrow, and beyond.

PEC Board of Directors



Milton Rister
District 1 Director &
Secretary-Treasurer



Emily Pataki
District 2 Director &
Vice President



James Oakley
District 5 Director



Paul Graf
District 6 Director &
President



Amy Lea SJ Akers
District 7 Director



Since 1938, Pedernales Electric Cooperative has served its members, supported its communities, and helped extend electric service throughout the Texas Hill Country. Photo taken in Leander, Texas.



PEDERNALES
ELECTRIC
COOPERATIVE
**2019
FINANCIAL
REPORT**


Pedernales
Electric Cooperative, Inc.



TECGENER

**PEDERNALES ELECTRIC COOPERATIVE, INC.
JOHNSON CITY, TEXAS**

FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS
LUBBOCK, TEXAS

PEDERNALES ELECTRIC COOPERATIVE, INC.

JOHNSON CITY, TEXAS

FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

PEDERNALES ELECTRIC COOPERATIVE, INC.
JOHNSON CITY, TEXAS
FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018

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BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

PHONE: (806) 747-3806

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8215 NASHVILLE AVENUE

LUBBOCK, TEXAS 79423-1954

Independent Auditor's Report

Board of Directors
Pedernales Electric Cooperative, Inc.
Johnson City, Texas

Report on the Financial Statements

We have audited the accompanying financial statements of Pedernales Electric Cooperative, Inc. (the Cooperative), which comprise the balance sheets as of December 31, 2019 and 2018, and the related statements of income and patronage capital, 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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, 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 Pedernales Electric Cooperative, Inc. as of December 31, 2019 and 2018, and the results of their operations and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

Lubbock, Texas

April 6, 2020

PEDERNALES ELECTRIC COOPERATIVE, INC.

BALANCE SHEETS
DECEMBER 31, 2019 AND 2018

ASSETS

	December 31,	
	2019	2018
UTILITY PLANT AT COST		
Utility Plant in Service	\$ 1,852,689,244	\$ 1,784,158,237
Construction Work in Progress	105,448,674	63,244,834
	<u>\$ 1,958,137,918</u>	<u>\$ 1,847,403,071</u>
Less: Accumulated Provision for Depreciation	310,728,192	298,206,899
	<u>\$ 1,647,409,726</u>	<u>\$ 1,549,196,172</u>
OTHER PROPERTY AND INVESTMENTS - AT COST OR STATED VALUE		
Investments in Associated Organizations	\$ 14,853,345	\$ 13,845,105
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 768,768	\$ 2,354,840
Accounts Receivable - Energy (Less allowance for uncollectibles of \$474,031 in 2019 and \$590,046 in 2018)	19,626,978	22,034,976
Accounts Receivable - Other (Less allowance for uncollectibles of \$224,355 in 2019 and \$347,851 in 2018)	2,500,851	2,989,733
Accrued Unbilled Revenue	26,250,305	27,772,229
Materials and Supplies Inventory	17,921,711	19,443,659
Other Current and Accrued Assets	3,524,991	3,026,820
Total Current Assets	<u>\$ 70,593,604</u>	<u>\$ 77,622,257</u>
DEFERRED CHARGES AND OTHER ASSETS	\$ 75,147,217	\$ 62,351,825
TOTAL ASSETS	<u>\$ 1,808,003,892</u>	<u>\$ 1,703,015,359</u>

EQUITIES AND LIABILITIES

EQUITIES		
Memberships	\$ 13,456,187	\$ 12,784,618
Patronage Capital	467,174,912	458,957,514
Other Equities	253,848,966	215,912,613
Total Equities	<u>\$ 734,480,065</u>	<u>\$ 687,654,745</u>
LONG-TERM DEBT		
Mortgage Bonds Less Current Maturities and Issuance Costs	\$ 269,311,308	\$ 283,726,168
CFC Mortgage Notes Less Current Maturities	460,917,422	389,866,921
Chase Notes Less Current Maturities	6,050,000	11,650,000
Line of Credit to be Refinanced	8,200,000	51,500,000
Total Long-Term Debt	<u>\$ 744,478,730</u>	<u>\$ 736,743,089</u>
ACCUMULATED PROVISION FOR PENSIONS AND BENEFITS	\$ 85,965,102	\$ 81,905,157
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 48,740,433	\$ 45,101,040
Current Portion of Accumulated Provision for Pensions and Benefits	2,095,220	2,339,615
Purchased Power - Payable and Accrued	28,980,423	28,869,914
Accounts Payable - Other	29,709,181	20,009,772
Power Cost Adjustments - Over-Recovered	34,014,504	12,026,220
Tax Payable	10,531,239	11,460,895
Interest Payable	3,750,407	3,648,042
Member Deposits	5,811,779	6,332,614
Other Current and Accrued Liabilities	13,035,015	11,294,402
Total Current Liabilities	<u>\$ 176,668,201</u>	<u>\$ 141,082,514</u>
DEFERRED CREDITS	\$ 66,411,794	\$ 55,629,854
TOTAL EQUITIES AND LIABILITIES	<u>\$ 1,808,003,892</u>	<u>\$ 1,703,015,359</u>

See accompanying notes to financial statements.

PEDERNALES ELECTRIC COOPERATIVE, INC.

STATEMENTS OF INCOME AND PATRONAGE CAPITAL
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018

	December 31,	
	2019	2018
OPERATING REVENUES		
Residential	\$ 464,321,990	\$ 449,967,045
Small Power	72,022,314	68,893,327
Large Power	95,140,860	91,541,220
Public Authorities	1,066,308	1,028,840
Other Operating Revenues	29,792,556	27,875,809
Accrued Unbilled Revenue	(1,521,924)	1,408,028
Power Cost Adjustment	(42,905,099)	(2,166,977)
Total Operating Revenues	<u>\$ 617,917,005</u>	<u>\$ 638,547,292</u>
OPERATING EXPENSES		
Purchased Power	\$ 336,358,046	\$ 366,572,110
Transmission - Operation	2,581,131	2,059,774
Transmission - Maintenance	3,117,569	3,138,412
Distribution - Operation	45,427,226	44,469,102
Distribution - Maintenance	20,272,723	16,227,348
Consumer Accounts	27,803,227	25,081,591
Customer Service and Information	3,821,042	3,678,406
Sales	1,693,704	1,673,282
Administrative and General	27,003,121	25,987,568
Depreciation	57,620,272	53,392,308
Taxes	(108,236)	2,062,305
Other Interest	1,740,606	421,055
Other Deductions	124,329	224,650
Total Operating Expenses	<u>\$ 527,454,760</u>	<u>\$ 544,987,911</u>
OPERATING MARGINS - Before Fixed Charges	<u>\$ 90,462,245</u>	<u>\$ 93,559,381</u>
FIXED CHARGES		
Interest and Amortization on Long-Term Debt	\$ 35,809,236	\$ 36,342,026
Interest Charged to Construction	(235,555)	(2,140,472)
	<u>\$ 35,573,681</u>	<u>\$ 34,201,554</u>
OPERATING MARGINS - After Fixed Charges	\$ 54,888,564	\$ 59,357,827
Capital Credits	<u>2,080,747</u>	<u>1,990,368</u>
NET OPERATING MARGINS	<u>\$ 56,969,311</u>	<u>\$ 61,348,195</u>
NON-OPERATING MARGINS		
Interest and Dividend Income	\$ 278,796	\$ 267,146
Miscellaneous Non-Operating Income	508,549	293,514
Disposal of Assets	430,821	(1,413,057)
	<u>\$ 1,218,166</u>	<u>\$ (852,397)</u>
NET MARGINS	\$ 58,187,477	\$ 60,495,798
PATRONAGE CAPITAL - BEGINNING OF YEAR	458,957,514	436,437,823
Patronage Capital Retired	(12,033,727)	(11,897,906)
Transfers to Other Equities	<u>(37,936,352)</u>	<u>(26,078,201)</u>
PATRONAGE CAPITAL - END OF YEAR	<u>\$ 467,174,912</u>	<u>\$ 458,957,514</u>

See accompanying notes to financial statements.

PEDERNALES ELECTRIC COOPERATIVE, INC.

**STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2019 AND 2018**

	December 31,	
	2019	2018
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margins	\$ 58,187,477	\$ 60,495,798
Adjustments to Reconcile Net Margins to Net Cash From Operating Activities		
Depreciation and Amortization Charged to Expense	57,885,412	53,657,448
Provision for Uncollectible Accounts	1,066,559	1,035,622
Capital Credits	(2,080,747)	(1,990,368)
Deferral/Accrual/Asset Activity for Pension/Post-Retirement Plans	7,439,787	9,460,439
Payments on Post-Retirement Benefits	(1,997,063)	(2,336,647)
Payments to Defined Benefit Plan	(7,037,451)	(6,277,802)
Changes in Assets and Liabilities:		
Accounts Receivable - Net	1,830,321	(1,396,478)
Accrued Unbilled Revenue	1,521,924	(1,408,027)
Power Cost Adjustments	21,988,284	329,419
Materials & Supplies	1,521,948	1,564,463
Prepayments & Other Current Assets	(498,171)	(302,617)
Deferred Charges & Other Assets	(14,569,167)	7,335,929
Accrued & Accounts Payable	9,809,918	(2,555,801)
Member Deposits	(520,835)	70,661
Accrued Taxes	(929,656)	1,187,712
Accrued Interest	102,365	(142,007)
Other Current Liabilities	1,740,614	1,155,533
Other Deferred Credits & Liabilities	17,965,992	2,760,683
Net Cash From Operating Activities	\$ 153,427,511	\$ 122,643,960
CASH FLOWS FROM INVESTING ACTIVITIES		
Net Additions to Property, Plant & Equipment	\$ (155,833,826)	\$ (139,923,834)
Capital Credit Retirements from Associated Organizations	1,072,507	1,028,706
Net Cash From Investing Activities	\$ (154,761,319)	\$ (138,895,128)
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on Long-Term Debt	\$ (45,590,106)	\$ (43,546,070)
Advances on Long-Term Debt	100,000,000	
Net Activity on Line of Credit	(43,300,000)	51,500,000
Retirement of Patronage Capital	(12,033,727)	(11,897,906)
Increase in Memberships - Net	671,569	619,290
Net Cash From Financing Activities	\$ (252,264)	\$ (3,324,686)
CHANGE IN CASH AND CASH EQUIVALENTS	\$ (1,586,072)	\$ (19,575,854)
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	2,354,840	21,930,694
CASH AND CASH EQUIVALENTS - END OF YEAR	\$ 768,768	\$ 2,354,840
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash Paid During the Year for:		
Interest on Long-Term Debt	\$ 35,432,397	\$ 36,239,312
Patronage Capital Retired by Noncash Discounting	\$ 37,936,352	\$ 26,078,201

See accompanying notes to financial statements.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Pedernales Electric Cooperative, Inc. (the Cooperative) is a non-profit corporation organized to provide electric service at the retail level to primarily residential and commercial accounts in a designated service area. As of December 31, 2019, the Cooperative served approximately 329,702 meters.

Power delivered at retail is purchased wholesale from the Lower Colorado River Authority (LCRA) and other third-party wholesale power suppliers. Any revenues earned in excess of costs incurred are allocated to members of the Cooperative and are reflected as patronage capital on the balance sheet.

Regulatory Accounting

The Cooperative utilizes the Uniform System of Accounts established by the Rural Utilities Service (RUS). In accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 980, Regulated Operations, the Cooperative records certain assets and liabilities in accordance with the economic effects of the rate making process. See Notes 6 and 10 that describe the most significant amounts accounted for under this standard.

Utility Plant

Plant is stated at the original cost of construction which includes the cost of contracted services, direct labor, materials, overhead items and capitalized interest. During 2019, the Cooperative discontinued capitalizing interest amounts. Contributions from others toward the construction of electric plant are credited to the applicable plant accounts.

When property, which represents a retirement unit, is replaced or removed, the average cost of such property as determined from the continuing property records is credited to electric plant and such cost, together with cost of removal less salvage, is charged to the accumulated provision for depreciation.

Maintenance and repairs, including the renewal of minor items of plant not comprising a retirement unit, are charged to the appropriate maintenance accounts, except that repairs of transportation and service equipment are charged to clearing accounts and redistributed to operating expense and other accounts.

Cash and Cash Equivalents

For purposes of the statements of cash flows, cash and short term investments are considered cash and cash equivalents.

Accounts Receivable

In the normal course of business, the Cooperative recognizes accounts receivable for energy delivered and billed. The Cooperative provides a statement with a due date that will not be less than 16 days after the statement date. Payments not received by the due date are considered delinquent.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

The Cooperative provides an allowance for uncollectible accounts to recognize the portion of receivables considered uncollectible. The allowance is estimated based on historical trends, aging of receivables, and a review of potential bad debts. Accounts remaining unpaid 120 days after the due date of the final bill are written off.

Materials and Supplies Inventory

Materials and supplies inventories are valued at average unit cost.

Electric Revenues from Contracts with Customers

Substantially all operating revenues and customer accounts receivables are derived from contracts with customers. Performance obligations related to the sale of energy are satisfied as energy is delivered to customers. The Cooperative recognizes electric revenue that corresponds to the price of the energy delivered to the customer. The measurement of energy sales to customers is generally based on the reading of their meters, which occurs on a systematic basis throughout the month. At the end of each month, amounts of energy delivered to customers since the date of the last meter reading are estimated, and the corresponding unbilled revenue is recognized. The Cooperative has calculated that its unbilled revenue for delivered power usage which has not been billed to customers at December 31, 2019 and 2018 amounted to \$26,250,305 and \$27,772,229, respectively.

The Cooperative does not recognize a separate financing component of its collections from customers as contract terms are short-term in nature. The Cooperative presents its revenues net of any excise or sales taxes or fees.

The Cooperative's tariffs for electric service include adjustment clauses under which billings to customers are adjusted to reflect changes in the cost of purchased power. In order to match power cost and related revenues, these amounts to be billed to consumers in subsequent periods are included with the revenue accrual described above.

Federal Income Taxes

The Cooperative is exempt from federal income taxes under Section 501(c)(12) of the Internal Revenue Code. More than 85% of the gross income is collected from members.

The Cooperative follows the "uncertain tax positions" provisions of accounting principles generally accepted in the United States of America. The primary tax position of the Cooperative is its filing status as a tax exempt entity. The Cooperative determined that it is more likely than not that its tax positions will be sustained upon examination by the Internal Revenue Service (IRS) and that all tax benefits are likely to be realized upon settlement with taxing authorities.

The Cooperative files income tax returns in the U.S. federal jurisdiction. The Cooperative is no longer subject to examinations by federal taxing authorities for years before 2016. In 2019 and 2018, the Cooperative did not incur tax related interest or penalties.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Group Concentration of Credit Risk

The Cooperative's headquarters facility is located in Johnson City, Texas. The service area extends into 24 counties in the Central Texas region. The Cooperative records a receivable for electric revenues as billed on a monthly basis. The Cooperative may require a deposit from new members upon connection, which is applied to unpaid bills and fees in the event of default. The deposit accrues interest annually and is returned to residential accounts along with accrued interest after one year of prompt payments. As of December 31, 2019 and 2018, deposits on hand totaled \$5,811,779 and \$6,332,614, respectively.

The Cooperative maintains its cash balances in institutions insured by the Federal Deposit Insurance Corporation (FDIC). The cash balances exceeded applicable insurance coverage at times during 2019 and 2018.

Patronage Capital Certificates

Patronage capital from associated organizations is recorded at the stated amount of the certificate.

Pension Benefit Plans and Other Post-Retirement Benefits

The Cooperative has a defined benefit pension plan for employees meeting eligibility requirements. This plan was amended to close entry to new participants after January 1, 2006. The benefit is based on years of service and the average of the employee's highest 36 months of compensation. The Cooperative also has a defined contribution 401(k) plan for employees eligible to participate.

The Cooperative also sponsors a health care plan for retirees who satisfy eligibility requirements. This plan was amended to close entry to new participants after July 1, 2005 and was amended in 2018 to close entry to new retired participants not currently receiving benefits under the plan. The cost of the Cooperative's obligation is actuarially determined based on certain weighted-average assumptions.

Use of Estimates in the Preparation of Financial Statements

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

Comparative Financial Information

Certain amounts in the prior period financial statements have been reclassified in order to conform to current period presentation.

2. Assets Pledged

Substantially all assets are pledged as security for the long-term debt due to Bank of New York (BONY) and National Rural Utilities Cooperative Finance Corporation (CFC).

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

3. Utility Plant

The major classes of utility plant are as follows:

	December 31,	
	<u>2019</u>	<u>2018</u>
Transmission Plant	\$ 109,540,612	\$ 108,110,511
Distribution Plant	1,545,617,790	1,479,943,124
General Plant	<u>197,530,842</u>	<u>196,104,602</u>
Total Utility Plant in Service	\$ 1,852,689,244	\$ 1,784,158,237
Construction Work in Progress	<u>105,448,674</u>	<u>63,244,834</u>
Total Utility Plant	<u>\$ 1,958,137,918</u>	<u>\$ 1,847,403,071</u>

Provision for depreciation of utility plant is computed using straight-line rates as follows:

	<u>2019</u>	<u>2018</u>
Transmission Plant	1.74% - 2.02%	1.74% - 2.02%
Distribution Plant	1.85% - 20.00%	1.85% - 20.00%
General Plant	2.38% - 20.00%	2.38% - 20.00%

Depreciation for the years ended December 31, 2019 and 2018, was \$57,620,272 and \$56,459,568, respectively, of which \$57,620,272 and \$53,392,308 was charged to depreciation expense and \$0 and \$3,067,260 was allocated to other accounts.

4. Investments in Associated Organizations

Investments in associated organizations consisted of:

	December 31,	
	<u>2019</u>	<u>2018</u>
CFC		
Capital Term Certificates	\$ 4,887,296	\$ 4,887,296
Patronage Capital	6,141,780	5,359,813
Texas Electric Cooperative		
Patronage Capital	3,156,575	2,993,746
Other	<u>667,694</u>	<u>604,250</u>
	<u>\$ 14,853,345</u>	<u>\$ 13,845,105</u>

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

5. Materials and Supplies Inventory

Materials and supplies inventories consist of construction materials and supplies. The ending balances for materials and supplies at December 31, 2019 and 2018 were \$17,921,711 and \$19,443,659, respectively.

6. Deferred Charges and Other Assets

Deferred charges and other assets included the following:

	December 31,	
	2019	2018
Deferred Charge - Defined Benefit Plan	\$ 58,880,411	\$ 60,663,121
Regulatory Asset - LCRA FPCRF (See Note 11)	16,099,689	1,270,911
LCRA Radio Services	167,117	417,793
	<u>\$ 75,147,217</u>	<u>\$ 62,351,825</u>

The Cooperative recognizes a deferred charge for the portion of its pension and other post-retirement benefit plans that has not been recognized as a component of net periodic pension and other post-retirement benefit costs. Accordingly, no amounts have been recorded in other comprehensive income. The unrecognized portion is being amortized into pension and other post-retirement benefit costs over the average future service of current active plan participants expected to receive benefits (see Note 13).

The Cooperative has an agreement in place to utilize LCRA’s trunked radio system in the Junction district. The associated costs were paid upon initiation of the agreement. The costs have been capitalized and are being amortized over the contract term, which ends in August 2020.

7. Patronage Capital and Other Equities

Patronage capital represents the Cooperative’s accumulated retained net margins that have been allocated annually to its members. Distributions to members are made at the discretion of the Board of Directors in accordance with the bylaws, subject to the covenants contained in the long-term debt agreements.

The loan agreements contain provisions that must be met for the Cooperative to make patronage capital retirements. These provisions include maintaining debt service coverage ratios of 1.15 for the BONY bonds and 1.35 for CFC debt. The Cooperative is in compliance with these provisions at December 31, 2019 and 2018.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Under certain circumstances, the Board of Directors may choose to retire patronage capital earlier than the Cooperative's current approximate 30 year retirement schedule. In these instances, the Cooperative retires and pays the net present value of patronage capital to a member or former member before the time the Cooperative anticipates normally retiring and paying patronage capital.

Patronage capital totaling \$12,033,727 and \$11,897,906 was distributed to members during 2019 and 2018, respectively.

Patronage capital assigned and assignable at December 31, 2019 and 2018, is as follows:

	December 31,	
	2019	2018
Assigned to Date	\$ 764,889,011	\$ 705,801,339
Assignable	85,959,457	86,859,651
	<u>\$ 850,848,468</u>	<u>\$ 792,660,990</u>
Less: Retirements to Date	129,824,590	117,790,863
Less: Discounted Patronage Capital to Permanent Equity	253,848,966	215,912,613
	<u>\$ 467,174,912</u>	<u>\$ 458,957,514</u>

The Cooperative's bylaws provide that amounts received by the Cooperative in excess of costs and expenses shall, insofar as permitted by law, (a) be used to offset any losses incurred during the current or any prior fiscal year and, (b) to the extent not needed for that purpose, be allocated to its members on a patronage basis.

Other equities at December 31, 2019 and 2018, are as follows:

	December 31,	
	2019	2018
Discounted Capital Credits	<u>\$ 253,848,966</u>	<u>\$ 215,912,613</u>

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

8. Long-Term Debt

At December 31, 2019 and 2018, long-term debt consisted of the following:

	December 31,	
	<u>2019</u>	<u>2018</u>
First Mortgage Bonds, 2002 Series A; 5.952%; due 2022		
Interest Payable Semi-Annually on May 15 and November 15;	\$ 46,680,000	\$ 60,535,000
First Mortgage Bonds, 2002 Series A; 6.202%; due 2032		
Interest Payable Semi-Annually on May 15 and November 15;		
Principal Payments Begin 2023	239,500,000	239,500,000
CFC Loan; 3.85%; due 2042 and 2043		
Interest and Principal Payable Quarterly		
Principal Payments Begin 2012	196,764,987	202,024,399
CFC Loan; 3.95%; due 2045		
Interest and Principal Payable Quarterly		
Principal Payments Begin 2016	23,211,486	23,714,486
CFC Loan; 2.75%; due 2020		
Interest and Principal Payable Quarterly		
Principal Payments Begin 2016	17,319,818	34,171,091
CFC Loan; 3.80%; due 2046		
Interest and Principal Payable Quarterly		
Principal Payments Begin 2017	75,380,479	76,978,910
CFC Loan; 4.15%; due 2047		
Interest and Principal Payable Quarterly		
Principal Payments Begin 2018	77,190,155	78,624,075
CFC Loan; 3.40%; due 2049		
Interest and Principal Payable Quarterly		
Principal Payments Begin 2019	99,510,930	
Chase Loan; 2.50%; due 2021		
Interest and Principal Payable Quarterly		
Principal Payments Begin 2016	4,500,000	7,500,000
Chase Loan; 3.80%; due 2022		
Interest and Principal Payable Quarterly		
Principal Payments Begin 2017	7,150,000	9,750,000
Less: Bond Issue Costs	<u>(2,188,692)</u>	<u>(2,453,832)</u>
	\$ 785,019,163	\$ 730,344,129
Less: Current Maturities	<u>48,740,433</u>	<u>45,101,040</u>
Total Long-Term Debt	<u>\$ 736,278,730</u>	<u>\$ 685,243,089</u>

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

The Cooperative has \$6,800,000 available on long-term loan commitments from CFC.

The Cooperative has \$100,000,000 available on long-term loan commitments from CoBank.

Annual maturities of long-term debt for the next five years and thereafter are as follows:

2020	\$	48,740,433
2021		31,210,830
2022		30,427,710
2023		30,526,908
2024		32,114,096
Thereafter		614,187,878

9. Short-Term Borrowing

The Cooperative has a perpetual line of credit at a variable interest rate with CFC not to exceed \$100,000,000. At December 31, 2019 and 2018, the Cooperative had \$8,200,000 and \$51,500,000, respectively, outstanding on this line of credit. The line of credit agreement requires the Cooperative to pay down the balance to zero annually and automatically renews unless either party gives a 90 day notice. Pursuant to the Cooperative's utilization of long-term funds to repay these amounts \$8,200,000 and \$51,500,000 is classified as long-term debt on the balance sheet at December 31, 2019 and 2018, respectively.

The Cooperative has a line of credit at a variable interest rate with CoBank not to exceed \$80,000,000. There was no balance outstanding at December 31, 2019 and 2018.

10. Deferred Credits

Deferred credits included the following:

	December 31,	
	2019	2018
Patronage Capital - Pre-Escheat	\$ 7,747,930	\$ 8,177,069
Regulatory Liability - LCRA FPCRFR (See Note 11)	16,099,689	1,270,911
Regulatory Liability - TCOS Over-Recovery	5,995,281	2,449,066
Post-Retirement Medical Benefits Deferred Credit	36,539,821	43,732,808
Other	29,073	
	<u>\$ 66,411,794</u>	<u>\$ 55,629,854</u>

The patronage capital pre-escheat component represents unclaimed patronage capital checks that do not meet escheat criterion. The liability is recorded as unclaimed patronage capital as the checks are voided. As the funds are claimed or reach escheat status, the liability is reduced.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

During 2019 and 2018, the Cooperative realized a gain for post-retirement medical benefits. The Cooperative recognized a deferred credit for the net amount of the unrecognized gain (see Note 14). Accordingly, no amounts have been recorded in other comprehensive income.

The TCOS over-recovery represents the TCOS component of power cost already recovered from customers.

11. LCRA Fuel & Power Cost Recovery Factor (FPCRf)

The LCRA FPCRf represents the amount that the Cooperative will be billed by LCRA in future periods or a reduction in billings by LCRA in future periods for electricity purchased. The offset of this amount will be collected from or due to members in the future through the power cost adjustment (PCA). The FPCRf as of December 31, 2019 represents an over-recovery by LCRA or receivable of \$16,099,689, which is classified as a deferred charge along with the same amount as a deferred credit which is due to members through the PCA. The FPCRf as of December 31, 2018 represents an under-recovery by LCRA or payable of \$1,270,911, which is classified as a deferred credit along with the same amount as a deferred charge which will be collected from members through the PCA.

12. Commitments and Contingencies

Power Supply Contracts

The Cooperative entered into contracts for the purchase and delivery of electric energy to satisfy its electric energy requirements. In 2019 and 2018, the Cooperative purchased energy from the Lower Colorado River Authority (LCRA) and other third party wholesale power suppliers. LCRA was the primary wholesale electric energy supplier, while the other suppliers provided electric energy to serve a portion of the electric energy requirements for the Cooperative's delivery points within LCRA's service territory and the full electric energy requirements for delivery points outside of LCRA's service territory. All of the electric energy purchased by the Cooperative is procured through term contracts of varying durations. As these terms expire, they may or may not be replaced with new agreements.

Transmission Lease Contracts

LCRA leases and operates certain transmission facilities and equipment owned by the Cooperative. Payments for the leased facilities vary from year to year and are based on the original cost of the facilities, adjusted for depreciation, and are updated annually to reflect additions, retirements and depreciation. The terms of the lease are perpetual, but may be terminated by LCRA or the Cooperative upon five years written notice. In 2019, the lease was terminated by both parties. The lease will end in June 2024. The Cooperative's transmission lease revenues totaled \$5,196,223 and \$5,291,822 in 2019 and 2018, respectively.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Litigation

The Cooperative may be involved in various claims and litigation arising in the normal course of business. Although management is unable to predict the outcome of such proceedings, management and the Cooperative's legal counsel do not believe that the resolution of any claims or litigation involving the Cooperative will have a material adverse effect on the Cooperative's results of operations and financial condition.

13. Pension Benefits

The Cooperative has a defined benefit plan covering eligible employees. The cost of the plan is determined by an independent actuary and is funded in amounts sufficient to meet the minimum funding requirements under applicable regulations.

Contributions paid to the defined benefit plan for the years ended December 31, 2019 and 2018, were \$7,037,451 and \$6,277,802, respectively.

The measurement date used for the current valuation is December 31, 2019.

The following weighted-average assumptions were used to develop the accumulated post-retirement benefit obligation for 2019 and 2018:

	<u>2019</u>	<u>2018</u>
Discount Rate	3.25%	4.25%
Rate of Compensation Increase	4.00%	4.00%

The following weighted-average assumptions were used to determine the net benefit cost for 2019 and 2018:

	<u>2019</u>	<u>2018</u>
Discount Rate	4.25%	3.60%
Rate of Compensation Increase	4.00%	4.27%
Expected Long-Term Return on Plan Assets	6.50%	6.50%

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Amounts recognized in the Cooperative's financial statements and funded status of the plan are as follows:

	December 31,	
	2019	2018
I) Net Periodic Benefit Cost		
Service Cost	\$ 4,757,855	\$ 5,575,691
Interest Cost	9,904,325	9,004,454
Amortization	5,332,848	5,508,323
Return on Assets	(11,604,349)	(12,561,466)
	<u>\$ 8,390,679</u>	<u>\$ 7,527,002</u>
II) Projected Benefit Obligation (PBO) Reconciliation:		
PBO Balance at Beginning of Year	\$ 236,828,676	\$ 249,963,880
Actuarial (Gain)/Loss	34,023,378	(19,419,684)
Interest Cost/Service Cost	14,662,180	14,580,145
Benefits Paid	(8,713,566)	(8,295,665)
Projected Benefit Obligation at Year End	<u>\$ 276,800,668</u>	<u>\$ 236,828,676</u>
III) Reconciliation of Funded Status		
Projected Benefit Obligation	\$ 276,800,668	\$ 236,828,676
Fair Value of Assets	<u>223,071,920</u>	<u>182,670,446</u>
Funded Status at Year End	<u>\$ (53,728,748)</u>	<u>\$ (54,158,230)</u>
IV) Deferred Charge		
Actuarial Loss - Beginning of Year	\$ 60,663,121	\$ 61,047,338
Amortization of Loss/Remeasurement	(5,332,848)	(5,508,323)
Actuarial Loss	<u>3,550,138</u>	<u>5,124,106</u>
Deferred Charge at Year End	<u>\$ 58,880,411</u>	<u>\$ 60,663,121</u>

The accumulated benefit obligation for the plan was \$249,547,793 and \$212,033,728 at December 31, 2019 and 2018, respectively.

Plan Asset Information

Information related to fair value hierarchy measurements are disclosed in Note 17. The defined benefit plan asset fair value measurements are substantially Level 1.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Fair value of plan assets at December 31, 2019 and 2018 and asset allocation is as follows:

	December 31,	
	2019	2018
Cash and Cash Equivalents	\$ 959,831	\$ 1,721,743
Government Agencies, Bonds and Notes	104,287,888	89,088,987
Mutual Funds	104,007,990	72,188,478
Other	13,816,211	19,671,238
Total	<u>\$ 223,071,920</u>	<u>\$ 182,670,446</u>

	December 31,	
	2019	2018
Mutual Funds and Equity Securities	47%	40%
Debt Securities	47%	49%
Other	6%	11%
Total	<u>100%</u>	<u>100%</u>

Benefit payments for the next ten years are estimated as follows:

2020	\$ 9,571,113
2021	10,096,841
2022	10,649,851
2023	11,158,627
2024	11,770,817
2025-2029	66,868,788

The estimated 2020 plan year minimum required contribution is \$6,400,000.

The Cooperative has a defined contribution plan (401(k) plan) for employees that are eligible to participate. For employees that are also eligible to participate in the defined benefit plan, the maximum contribution is six percent of the employee's base annual salary. For employees not eligible for the defined benefit plan, the 401(k) plan contribution cost is a maximum of ten percent of the employee's base annual salary. These costs are funded each pay period as accrued. The Cooperative's contributions to the 401(k) plan (net of forfeitures) were \$5,087,827 and \$4,464,994 in 2019 and 2018, respectively.

14. Post-Retirement Benefits Other than Pensions

The Cooperative provides post-retirement medical benefits for eligible employees through a plan with a third-party insurance provider. For purposes of this statement, the written plan in effect is the substantive plan and is considered a defined benefit plan. The Cooperative contributes varying amounts dependent on retirement date, age, and years of service. As of August 2018, the plan is closed to new retired participants not currently receiving benefits under the plan.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Benefits are paid on behalf of retirees and are a function of medical insurance costs and number of retirees. Benefits paid (excluding reimbursements) for the years ended December 31, 2019 and 2018, were \$2,177,390 and \$2,636,137, respectively. The Cooperative's policy for contributions is to contribute the amount of the current benefits in that year.

The measurement date used for the current valuation is December 31, 2019.

The weighted-average discount rate used to develop the accumulated post-retirement benefit obligation for the years ended December 31, 2019 and 2018, were 3.13% and 4.25%, respectively.

Amounts recognized in the Cooperative's financial statements and funded status of the plan are as follows:

	December 31,	
	2019	2018
I) Net Post-Retirement Benefit Cost		
Service Cost	\$	\$ 293,102
Interest Cost	1,379,239	1,780,054
Amortization	(2,330,131)	(139,719)
	\$ (950,892)	\$ 1,933,437
II) Accumulated Post-Retirement Benefit Obligation (APBO) Reconciliation:		
APBO Balance at Beginning of Year	\$ 30,086,542	\$ 65,445,321
Actuarial (Gain)/Loss	4,862,856	(2,028,526)
Plan Amendment		(33,066,762)
Interest Cost / Service Cost	1,379,239	2,073,156
Employer Contributions Net of Participant Amounts	(1,997,063)	(2,336,647)
Net Post-Retirement Benefit Liability at Year End	\$ 34,331,574	\$ 30,086,542
III) Reconciliation of Funded Status		
APBO	\$ 34,331,574	\$ 30,086,542
Accrued Post-Retirement Benefit Cost	\$ 34,331,574	\$ 30,086,542
IV) Deferred Credit		
Actuarial Gain - Beginning of Year	\$ (43,732,808)	\$ (8,777,239)
Amortization	2,330,131	139,719
Plan Amendment		(33,066,762)
Current Year Net (Gain)/Loss	4,862,856	(2,028,526)
Deferred Credit at Year End	\$ (36,539,821)	\$ (43,732,808)

The estimated actuarial amount for the post-retirement medical benefit plan that will be amortized into net post-retirement benefit cost over the next fiscal year is expected to be a gain of \$2,221,780.

The Cooperative has not funded any plan assets as of December 31, 2019 or 2018.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Estimated future benefit payments for the next ten years are as follows:

2020	\$	2,127,758
2021		2,112,246
2022		2,064,416
2023		2,060,922
2024		2,001,971
2025-2029		9,322,681

15. Recently Adopted Accounting Pronouncements

In May 2014, the FASB issued Accounting Standards Update 2014-09, Revenue from Contracts with Customers, Topic 606, which provides a new framework for the recognition of revenue. This standard was effective for nonpublic entities for fiscal years beginning after December 15, 2018. The implementation did not have a material impact on the Cooperative's financial statements, other than increased disclosures regarding revenues related to contracts with customers.

16. Recently Issued Accounting Pronouncements

In February 2016, the FASB issued Accounting Standards Update 2016-02, Leases. The new standard establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements. The new standard is effective for nonpublic entities for fiscal years beginning after December 15, 2020. The Cooperative is evaluating the impact of the new standard on the financial statements.

17. Disclosures About Fair Value of Financial Instruments

Many of the Cooperative's financial instruments lack an available market with similar terms, conditions, and maturities as those reflected in the carrying amount recorded. Accordingly, significant assumptions, estimations, and present value calculations were used for purposes of this disclosure.

Estimated Fair Value has been determined by calculating the present value of financial instruments using the best data available.

Fair Value for some amounts carried on the financial statements has not been calculated for the following reasons:

Patronage Capital from Associated Organizations – The right to receive cash is an inherent component of a financial instrument. The Cooperative holds no right to receive cash since any payments are at the discretion of the governing body for the associated organizations. As such, Patronage Capital from Associated Organizations are not considered financial instruments.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

CFC Capital Term Certificates and Member Capital Securities – It is not practicable to estimate fair value for these financial instruments given the lack of a market and their long holding period. Relevant information with respect to these is as follows:

	<u>AMOUNT</u>	<u>INTEREST RATE</u>	<u>MATURITY</u>
\$	960,968	3.00%	2020-2030
	1,715,690	0.00%	2043
	2,210,638	5.00%	2070-2080

Cash and Short-Term Investments - The recorded book value approximates fair value given the short period to maturity.

Long-Term Debt - Estimated by computing the present value by individual note to maturity, using currently quoted or offered rates for similar issues of debt. The year-end CFC fixed interest rate for long-term debt was used in the calculation for all fixed rate long-term debt. These are the only financial instruments of the Cooperative that have a difference in Fair Value and Carrying Value.

The carrying values of the Cooperative's financial instruments and debt and the estimated fair values are as follows:

	<u>December 31, 2019</u>		<u>December 31, 2018</u>	
	<u>CARRYING VALUE</u>	<u>FAIR VALUE</u>	<u>CARRYING VALUE</u>	<u>FAIR VALUE</u>
Assets:				
Cash and Cash Equivalents	\$ 768,768	\$ 768,768	\$ 2,354,840	\$ 2,354,840
Liabilities:				
Long-Term Debt	\$ 787,207,855	\$ 814,827,315	\$ 732,797,962	\$ 669,942,068

Fair Value Hierarchy

The Fair Value Measurements Topic of the FASB Accounting Standards Codification establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1 - inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Cooperative has the ability to access at the measurement date.

Level 2 - inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 - inputs are unobservable inputs for the asset or liability.

Long-Term Debt valuations are considered Level 2.

PEDERNALES ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

18. Subsequent Events

The Cooperative has evaluated subsequent events through April 6, 2020, the date which the financial statements were available to be issued.

In December 2019, an outbreak of a novel strain of coronavirus (COVID-19) originated in Wuhan, China and has since spread to other countries, including the U.S. On March 11, 2020, the World Health Organization characterized COVID-19 as a pandemic. In addition, multiple jurisdictions in the U.S. have declared states of emergency. It is anticipated that these impacts will continue for some time. There has been no material financial impact to the Cooperative's operations to date. Future potential impacts include disruptions or restrictions on our employees' ability to work, reduced consumer demand for energy, and customers' ability to pay their monthly bills in a timely fashion. Changes to our operating environment may also be impacted. These changes may impact operating costs and net income. The future effects of these issues are unknown.

COMPLIANCE SECTION

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

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**LETTER TO BOARD OF DIRECTORS REGARDING POLICIES
CONCERNING AUDITS OF CFC BORROWERS**

Board of Directors
Pedernales Electric Cooperative, Inc.
Johnson City, Texas

We have audited, in accordance with auditing standards generally accepted in the United States of America, the balance sheets of Pedernales Electric Cooperative, Inc. (the Cooperative) as of December 31, 2019 and 2018, and the related statements of income and patronage capital, and cash flows for the years ended, and have issued our report thereon dated April 6, 2020.

In connection with our audit, nothing came to our attention that caused us to believe that the Cooperative failed to comply with the terms of Article V of the National Rural Utilities Cooperative Finance Corporation Loan Agreement insofar as they relate to accounting matters. However, our audits were not directed primarily toward obtaining knowledge of such incompliance.

This report is intended solely for the information and use of the Boards of Directors and management of Pedernales Electric Cooperative, Inc. and the National Rural Utilities Cooperative Finance Corporation and is not intended to be and should not be used by anyone other than these specified parties.

Bolinger, Segars, Gilbert & Moss L.L.P.

Certified Public Accountants

Lubbock, Texas

April 6, 2020



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