Southside Electric Cooperative, Inc.
Financial Statements
December 31, 2019 and 2018

Contents

Financial Statements

Supplemental Matters Required by the Rural Utilities Service

ADAMS, JENKINS AND CHEATHAM
CERTIFIED PUBLIC ACCOUNTANTS AND BUSINESS CONSULTANTS

Independent Auditor's Report

The Board of Directors
Southside Electric Cooperative, Inc.
Crewe, Virginia

Report on the Financial Statements

We have audited the accompanying financial statements of Southside Electric Cooperative, Inc. (the "Cooperative") which comprise the balance sheets as of December 31, 2019 and 2018 and the related statements of operations, equities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the 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 Cooperative's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Southside Electric Cooperative, Inc. as of December 31, 2019 and 2018, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 11, 2020 on our consideration of Southside Electric Cooperative, Inc'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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Cooperative's internal control over financial reporting and compliance.

Adams, Jenkins & Cheatham

Richmond, Virginia
March 11, 2020

Balance Sheets

Southside Electric Cooperative, Inc.

	December 31, 2019	December 31, 2018
Assets		
Electric plant		
Electric plant	$ 376,894,354	$ 371,651,896
Less accumulated provision for depreciation	127,325,661	117,950,347
	249,568,693	253,701,549
Other property and investments		
Investments in associated organizations	52,509,794	51,360,316
Other investments	708,019	705,108
	53,217,813	52,065,424
Current assets		
Cash and cash equivalents	4,268,397	10,910,082
Accounts receivable, net	23,554,173	22,281,193
Materials and supplies	1,866,665	2,251,701
Notes receivable	26,655	33,740
Other current assets	193,231	153,166
	29,909,121	35,629,882
Deferred charges and regulatory assets	2,685,059	3,472,409
	$ 335,380,686	$ 344,869,264

See Independent Auditor's Report and Notes to Financial Statements

	December 31, 2019	December 31, 2018
Equities and Liabilities		
Equities		
Patronage capital	$ 106,468,111	$ 105,918,046
Other equities	2,082,493	1,449,672
Memberships	234,805	233,235
	108,785,409	107,600,953
Noncurrent liabilities		
Long-term debt	202,847,865	212,238,216
Other	60,355	48,357
	202,908,220	212,286,573
Current liabilities		
Accounts payable	9,118,016	9,542,194
Current maturities of long-term debt	9,394,080	9,082,224
Consumer deposits	2,307,501	2,202,571
Other current and accrued liabilities	1,867,512	2,193,986
	22,687,109	23,020,975
Deferred credits and regulatory liabilities	999,948	1,960,763
	$ 335,380,686	$ 344,869,264

Statements of Operations

Southside Electric Cooperative, Inc.

	Year Ended December 31, 2019	Year Ended December 31, 2018
Operating revenues	$ 125,797,672	$ 121,430,186
Operating expenses		
Cost of power	76,302,062	69,080,662
Transmission	120,919	138,807
Distribution - operation	5,822,515	5,139,736
Distribution - maintenance	10,448,719	13,276,676
Consumer accounts	2,348,536	2,146,320
Customer service and informational	2,913,550	2,652,035
Administrative and general	6,283,025	6,314,546
Depreciation and amortization	11,704,584	11,724,397
Taxes	123,394	1,086
Interest on long-term debt	7,179,605	6,918,208
Other	983,907	93,430
	124,230,816	117,485,903
Operating Margins Before Patronage Allocations	1,566,856	3,944,283
Patronage allocations		
Generation and transmission	1,365,087	1,083,667
Other	622,012	702,843
	1,987,099	1,786,510
Net Operating Margins	3,553,955	5,730,793
Nonoperating income (expense)		
Investment income, net	133,881	128,058
Other	(20,490)	(17,414)
Gain (Loss) on disposition of property	(2,569)	238,289
	110,822	348,933
Net Margins	$ 3,664,777	$ 6,079,726

See Independent Auditor's Report and Notes to Financial Statements

Statements of Equities

Southside Electric Cooperative, Inc.

Years Ended December 31, 2019 and 2018

	Patronage Capital	Other Equities	Memberships	Total
Balance, December 31, 2017	$ 103,363,475	$ 1,242,468	$ 232,490	$ 104,838,433
Net margins	6,079,726			6,079,726
Retirement of capital credits	(3,709,907)	391,956		(3,317,951)
Reallocated gains	184,752	(184,752)		
Net change in memberships			745	745
Balance, December 31, 2018	105,918,046	1,449,672	233,235	107,600,953
Net margins	3,664,777			3,664,777
Retirement of capital credits	(3,299,289)	817,398		(2,481,891)
Reallocated gains	184,577	(184,577)		
Net change in memberships			1,570	1,570
Balance, December 31, 2019	$ 106,468,111	$ 2,082,493	$ 234,805	$ 108,785,409

Statements of Cash Flows

Southside Electric Cooperative, Inc.

	Year Ended December 31, 2019	2018
Cash Flows from Operating Activities		
Cash received from members	$ 128,268,226	$ 122,069,127
Cash paid to suppliers and employees	(108,030,388)	(99,618,061)
Interest received	133,881	128,058
Interest paid	(7,223,408)	(6,942,017)
Net Cash Provided by Operating Activities	13,148,311	15,637,107
Cash Flows from Investing Activities		
Extension and replacement of plant	(9,754,791)	(10,523,690)
Plant removal costs	(1,240,736)	(1,322,987)
Contributions in aid of construction	2,070,702	722,436
Proceeds from retirement of investments in CTC's	19,642	18,383
Proceeds from the sale of plant	57,155	395,171
Net Cash Used by Investing Activities	(8,848,028)	(10,710,687)
Cash Flows from Financing Activities		
Principal payments of long-term debt	(9,078,494)	(9,035,662)
Capital credits paid to members, net	(2,307,588)	(2,752,136)
Proceeds from capital credits and other investments	337,614	2,000,358
Net change in member deposits	104,930	9,878
Net change in memberships	1,570	745
Payments on line of credit		(21,500,000)
Proceeds from long-term debt		32,900,000
Net Cash Provided (Used) by Financing Activities	(10,941,968)	1,623,183
Net Increase (Decrease) in Cash and Cash Equivalents	(6,641,685)	6,549,603
Cash and cash equivalents - beginning of year	10,910,082	4,360,479
Cash and Cash Equivalents - End of Year	$ 4,268,397	$ 10,910,082

See Independent Auditor's Report and Notes to Financial Statements

	Year Ended December 31,	
	2019	2018
Net margins	$ 3,664,777	$ 6,079,726
Adjustments to reconcile net margins to net cash provided by operating activities:		
Depreciation and amortization	11,704,584	11,724,397
Net change in life insurance benefit	(2,911)	(7,920)
(Gain) loss on disposition of plant		(238,289)
Noncash capital credits received	(1,506,734)	(1,786,510)
(Increase) decrease in:		
Accounts receivable	214,928	(1,748,780)
Other current assets	21,150	2,847,376
Deferred charges	787,350	907,600
Increase (decrease) in:		
Accounts payable	(459,542)	907,535
Other current and accrued liabilities	(326,474)	385,111
Other noncurrent liabilities	11,998	(66,699)
Deferred credits and regulatory liabilities	(960,815)	(3,366,440)
Net Cash Provided by Operating Activities	$ 13,148,311	$ 15,637,107

Notes to Financial Statements

Southside Electric Cooperative, Inc.

December 31, 2019 and 2018

Note A - Significant Accounting Policies

Nature of Operations

Southside Electric Cooperative, Inc. (the "Cooperative") is a member owned, nonprofit Cooperative organized to provide electric service to its members residing in eighteen counties, five towns and one city in the Commonwealth of Virginia. The Cooperative's main office is located in Crewe, Virginia.

Basis of Presentation

These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), including GAAP for regulated operations. The system of accounts of the Cooperative are maintained in accordance with the Uniform System of Accounts as prescribed by the Federal Energy Regulatory Commission (FERC) for Class A and B electric utilities modified for electric borrowers of the Rural Utilities Service (RUS).

Accounting Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Cash and Cash Equivalents

The Cooperative considers all highly liquid investments with a maturity of three months or less to be cash equivalents.

Income Taxes

The Cooperative has been granted exemption from income tax under Internal Revenue Service Code Section 501(c)(12) of the Internal Revenue Code. The Cooperative evaluates the components of the annual test for compliance to maintain its filing status as a tax-exempt entity. In accordance with Accounting Standards Codification ("ASC") Topic 740 for "uncertain tax positions", the Cooperative had determined that it is more likely than not that their tax positions will be sustained upon examination by the Internal Revenue Service.

Notes to Financial Statements

Southside Electric Cooperative, Inc.

December 31, 2019 and 2018

Note A - Significant Accounting Policies - Continued

Electric Plant

Electric plant is stated at the original cost of construction, which includes the cost of contracted services, direct labor, materials and overhead items. 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 expenses and other accounts.

Depreciation

Provision for depreciation has been made by application of the straight-line method to the original cost, by groups of depreciable properties in service. Current depreciation rates, which are estimated to amortize the cost of plant over the service lives, were as follows at December 31, 2019 and 2018:

Transmission plant	2.75%
Distribution plant	2.70 - 5.30%
Load management equipment	11.00%
General plant	3.00 - 25.00%

Materials and supplies

Inventories are generally used for construction, operation and maintenance work, and are not for resale. They are valued at the lower of moving average unit cost or market.

Accounts Receivable

Accounts receivable from customers are recorded at the billed amount and do not bear interest. The Cooperative maintains an allowance based on the expected collectability of accounts receivable. The allowance is determined based on historical experience and other circumstances which may affect the ability of customers to meet their obligations. The Cooperative reviews its allowance for doubtful accounts on a monthly basis. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote.

Note A - Significant Accounting Policies - Continued

Regulatory Assets and Liabilities

The Cooperative currently complies with accounting guidance set forth by the ASC Topic 980 regarding accounting for the effect of certain types of regulation. This guidance allows a regulated cooperative to record certain costs or credits that have been or are expected to be allowed in the ratemaking process in a period different from the period in which the costs would be charged to expense or income by a non-regulated enterprise. Accordingly, the Cooperative records certain assets and liabilities that result from the regulated ratemaking process that would not be recorded under GAAP for non-regulated entities.

Advertising Costs

Advertising costs were expensed as incurred.

Subsequent Events

Subsequent events have been evaluated through March 11, 2020, which is the date the financial statements were available to be issued.

Revenue Recognition

The Cooperative recognizes revenue when earned, that is, when electricity is used by customers on a monthly basis. The Cooperative's billing system bills customers on a cycle billing basis as opposed to a calendar month; therefore, the Cooperative estimates unbilled revenue on a monthly basis for power delivered but not billed to customers. See Note F for unbilled revenue recorded as of December 31, 2019 and 2018.

The Cooperative has analyzed the provisions of ASC Topic 606, *Revenue from Contracts with Customers,* and has concluded that no changes are necessary to conform to the new standard. Revenue from electricity is recorded when it is consumed, which complies with the requirements of ASC Topic 606. The Cooperative recognizes revenue from consumed electricity in the appropriate reporting period through its estimate of unbilled revenue.

Recently Issued Accounting Standards

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, Revenue from Contracts with Customers (Topic 606), which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The ASU replaced most existing revenue recognition guidance in U.S. GAAP. In August 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers (Topic 606)* - *Deferral of the Effective Date,* which deferred the effective date of ASU 2014-09 to January 1, 2019. The Cooperative has elected to apply the new standard using the modified retrospective method. The new standard does not have a material impact on the financial statements.

Note B - Assets Pledged

All assets are pledged as security for the long-term debt to National Rural Utilities Cooperative Finance Corporation (CFC), Federal Financing Bank (FFB) and CoBank.

Note C - Electric Plant

Listed below are the major classes of electric plant:

	December 31, 2019	December 31, 2018
Distribution plant	$ 306,509,098	$ 302,117,914
General plant	44,819,109	44,398,530
Transmission plant	19,931,704	18,471,197
Electric plant in service	371,259,911	364,987,641
Construction work in progress	5,634,443	6,664,255
	$ 376,894,354	$ 371,651,896

In accordance with the guidance for asset retirement obligations, as set forth in the ASC Topic 410 – Asset Retirement and Environmental Obligations, and FERC Order 631 as adopted by the RUS, the Cooperative has determined that it had no legal asset retirement obligations as of December 31, 2019 and 2018. Regarding non-legal retirement costs, the Cooperative follows the regulatory principle of inter-generational cost allocation by including net salvage (gross salvage less cost of removal) as a component of depreciation rates. For the years ended December 31, 2019 and 2018, the Cooperative followed the RUS prescribed rates for depreciation and therefore, collections for net salvage and differences in timing of recognition of period costs associated with non-legal retirement obligations had not been specifically identified.

Note D - Concentrations of Credit Risk

The Cooperative places its cash on deposit with financial institutions located in the United States of America, which are insured by the Federal Deposit Insurance Corporation (FDIC). The FDIC provides insurance coverage for up to $250,000 of cash held by the Cooperative in each separate FDIC insured bank and savings institution. From time to time, the Cooperative may have amounts on deposit in excess of the insured limits. As of December 31, 2019, the Cooperative had approximately $898,000 of deposits that exceed the insured limits.

Note E - Investments in Associated Organizations

Investments in associated organizations consisted of the following:

	December 31,	
	2019	2018
Patronage capital:		
Old Dominion Electric Cooperative (ODEC)	$ 46,134,561	$ 45,249,837
CFC	2,060,834	1,967,667
Tarheel Electric Membership Corp. (TEMA)	740,947	670,964
Federated Rural Electric Insurance Corp.	455,097	427,570
Other	171,295	157,248
	49,562,734	48,473,286
Capital Term Certificates (CTC):		
Subscriptions (SCTC's)	1,552,277	1,552,277
Loan (LCTC's)	367,050	367,050
Loan (ZCTC's)	195,805	215,447
	2,115,132	2,134,774
Other:		
TEC Trading, Inc.	622,500	622,500
Membership fees	154,319	76,574
Other	55,109	53,182
	831,928	752,256
	$ 52,509,794	$ 51,360,316

The capital term certificates invested in CFC are unsecured and subordinated. The SCTC’s bear interest at an annual rate of 5% payable semiannually and the LCTC’s bear interest at an annual rate of 3% payable semiannually. The ZCTC’s are non-interest bearing.

The investment in TEC Trading, Inc. represents an unconsolidated joint venture with other members of ODEC. The Cooperative has a non-controlling ownership interest that has been accounted for under the cost method.

Note F - Accounts Receivable

Accounts receivable consisted of the following:

	December 31, 2019	December 31, 2018
Consumer accounts receivable	$ 8,474,306	$ 8,833,452
Unbilled revenue	7,614,309	8,069,089
Other accounts receivable	7,545,987	5,464,388
	23,634,602	22,366,929
Less provision for uncollectible accounts	80,429	85,736
	$ 23,554,173	$ 22,281,193

Note G - Deferred Charges and Regulatory Assets

Deferred charges and regulatory assets consisted of the following:

	December 31, 2019	December 31, 2018
Regulatory asset:		
NRECA prepayment (Note K)	$ 2,600,865	$ 3,467,820
Survey and Investigation - preliminary	84,194	4,589
	$ 2,685,059	$ 3,472,409

Note H - Patronage Capital

Patronage capital consisted of the following:

	December 31, 2019	December 31, 2018
Assigned	$ 102,803,334	$ 99,838,320
Assignable	3,664,777	6,079,726
	$ 106,468,111	$ 105,918,046

Note H - Patronage Capital - Continued

Under provisions of the long-term debt agreements and Title 7 of the Code of Federal Regulations (Part 1717.617), the Cooperative may refund capital to patrons without limitation if total equity is equal to or greater than 30% of total assets and there are no instances of default. If equities are between 20% and 30% of total assets, general refunds are limited to 25% (adjusted for returns to estates, which are not limited) of patronage capital or margins received in the next preceding year. Total equities and margins amounted to approximately 32% and 31% of total assets for 2019 and 2018, respectively.

Note I - Long-Term Debt

Long-term debt consisted of the following:

	December 31,	
	2019	2018
FFB		
Mortgage notes, fixed	$ 145,448,386	$ 149,187,411
CFC		
Mortgage notes, fixed	52,970,668	57,365,370
CoBank		
Mortgage note, fixed	13,822,891	14,767,659
	212,241,945	221,320,440
Less current maturities	9,394,080	9,082,224
	$ 202,847,865	$ 212,238,216

The long-term debt payable to CoBank is represented by a mortgage note with an interest rate of 3.79%. The note matures in December 2031. Principal and interest installments were due monthly in the amount of approximately $115,000.

Long-term debt payable to CFC is represented by mortgage notes with rates ranging from 2.85% to 6.80%. The notes generally have 35-year maturity periods and are payable on an installment basis. The notes mature at various dates between March 2020 and December 2047. Principal and interest installments were due quarterly in the amount of approximately $1,750,000. The Cooperative had no unadvanced loan funds from CFC at December 31, 2019.

Note I - Long-Term Debt - Continued

The long-term debt payable to FFB is represented by mortgage notes with interest rates ranging from 1.69% to 5.86%. The notes mature at various dates between March 2020 and December 2052. Principal and interest installments were due quarterly in the amount of approximately $1,892,000. The Cooperative had unadvanced loan funds from FFB of $27,700,000 at December 31, 2019.

Approximate future maturities of long-term debt were estimated as follows:

	Total
2020	$ 9,394,080
2021	10,202,769
2022	10,304,995
2023	9,321,398
2024	9,057,344
2025 and thereafter	163,961,359
	$ 212,241,945

Under the terms of the loan agreements with RUS and CFC, there are certain restrictions, which include requirements to maintain a TIER (times interest earned ratio) of 1.25 and DSC (debt service coverage) of 1.25. There were also restrictions on the return of capital to patrons as discussed in (Note H). As of December 31, 2019 and 2018, the Cooperative was in compliance with all restrictions.

The Cooperative had a $15,000,000 line of credit with CFC at a variable interest rate (2.85% at December 31, 2019), there were no funds outstanding on the line at December 31, 2019 and 2018. The line of credit is secured by substantially all of the Cooperative’s assets and renews annually.

The Cooperative had a $8,000,000 line of credit with First Citizens Bank at a variable interest rate (3.70% at December 31, 2019), of which there was no balance outstanding at December 31, 2019 and 2018, respectively. The line of credit is unsecured and will expire in June 2020.

The Cooperative has a $5,000,000 line of credit with CoBank at variable rates (3.89% at December 31, 2019), of which there were no funds outstanding on the line at December 31, 2019 and 2018. The line of credit is unsecured and will expire in September 2020.

Note J - Deferred Credits and Regulatory Liabilities

Deferred credits and regulatory liabilities consisted of the following:

	December 31,	
	2019	2018
Regulatory liabilities:		
Deferred power costs	$ 966,094	$ 1,938,515
Other	33,854	22,248
	$ 999,948	$ 1,960,763

Note K - Retirement Plans

Pension Plan

The Retirement Security Plan (RS Plan), sponsored by the National Rural Electric Cooperative Association (NRECA) is a defined benefit pension plan qualified under Section 401 and tax-exempt under Section 501(a) of the Internal Revenue Code. It is considered 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 2019 and in 2018 represented less than 5 percent of the total contributions made to the RS Plan by all participating employers. The Cooperative made contributions to the RS Plan of approximately $3,164,000 in 2019 and $3,070,000 in 2018.

For 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 at January 1, 2019 and over 80 percent funded on January 1, 2018 based on the PPA funding target and PPA actuarial value of assets on those dates.

Because the provisions of the PPA do not apply to the 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.

Note K - Retirement Plans - Continued

At its December 2012 meeting, the I&FS Committee of the NRECA Board of Directors approved an option to allow participating cooperatives in the RS Plan to make a contribution prepayment and reduce future required contributions. The prepayment amount is a cooperative's share, as of January 1, 2013, of future contributions required to fund the RS Plan's unfunded value of benefits earned to date using RS Plan actuarial valuation assumptions. The prepayment amount will typically equal approximately 2.5 times a cooperative's annual RS Plan required contribution as of January 1, 2013. After making the prepayment, the billing rate for most co-ops is reduced by approximately 25%, retroactive to the January 1 of the year in which the amount is paid to the RS Plan. The 25% differential in billing rates is expected to continue for approximately 15 years from January 1, 2013. However, unexpected changes in interest rates, asset returns and other plan experience, plan assumption changes and other factors may have an impact on the differential in billing rates and the 15-year period.

On April 29, 2013 the Cooperative made a prepayment of $8,669,550 to the NRECA RS Plan. The Cooperative elected to finance the prepayment through a 10 year term loan with a fixed interest rate of 2.85%. The Cooperative is amortizing the prepayment to expense over 10 years with the balance represented as a part of deferred charges.

Deferred Income Plan

In addition to the NRECA RS Plan, substantially all employees of the Cooperative are eligible to participate in the NRECA SelectRE pension plan (the "Plan"), a defined contribution multi-employer deferred income plan qualified under Section 401(k) of the Internal Revenue Code. The Cooperative's required contribution to the Plan and its net pension cost was approximately $423,000 and $431,000 for the years ended December 31, 2019 and 2018, respectively.

Note L - Financial Instruments Carried at Cost

The Cooperative has recorded all financial instruments based on the carrying amount (book value) in the financial statements in accordance with ASC Topic 825. According to this guidance, the Cooperative is required to disclose the fair value of those financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using discounted cash flow analysis. This technique involves subjective judgment and is significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. As a result, the derived fair value estimates cannot be substantiated by comparison to independent markets, and in many cases, could not be realized in immediate settlement of the instrument. Accordingly, the following methods and assumptions were used to estimate the fair value of each class of financial instruments for which it was practicable to estimate that value.

Cash and Cash Equivalents

The carrying amount of cash and cash equivalents approximates fair value due to the short maturity of these instruments.

Note L - Financial Instruments Carried at Cost - Continued

Accounts Receivable

The carrying amount of accounts receivable approximates fair value due to the short period of time amounts are outstanding.

Investments in Associated Organizations

Investments in associated organizations are primarily composed of patronage capital assigned from associated organizations. These investments are recorded at costs plus allocated equities.

Fair value of capital term certificates was determined by computing the present value of estimated future cash flows, discounted at the long-term treasury rate of 2.39% and 3.02% for the years ended December 31, 2019 and 2018, respectively. The fair value of patronage capital is not determinable since no legal obligation exists to retire capital credits. The fair value of the cost method investment is not estimated since there are no identified events or changes in circumstances that may have a significant adverse effect on the fair value and it is not practicable to estimate fair value. The carrying value of memberships approximates fair value.

Accounts Payable

The carrying amount of accounts payable approximates fair value due to the short period of time amounts are outstanding.

Long-Term Debt

The carrying amount of the Cooperative's fixed long-term debt includes certain interest rates that are below quoted market prices for the same or similar issues. Therefore, the fair value of fixed long-term debt is estimated based on current market prices for the same or similar issues offered for debt of the same and remaining maturities which was 4.19% and 5.90% for the years ended December 31, 2019 and 2018, respectively.

The carrying amount of lines of credit approximates fair value due to the short maturity of the instruments.

Consumer Deposits

The carrying amount approximates fair value due to the relatively short maturity of the deposits.

Note L - Financial Instruments Carried at Cost - Continued

The estimated fair value of the Cooperative's financial instruments were as follows:

	December 31,			
	2019		2018	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Assets:				
Capital term certificates	$ 2,115,132	$ 3,400,000	$ 2,134,774	$ 2,990,000
Liabilities:				
Long-term debt, including mortgage notes	$ 212,241,945	$ 184,860,000	$ 221,320,440	$ 177,470,000

Note M - Commitments and Contingencies

Purchased Power

The Cooperative, as a member of ODEC, an organization composed of electric cooperatives in Virginia, Maryland and Delaware, has entered into a long-term contract with ODEC for the acquisition of wholesale power through ODEC as have other members of the organization. The cost of wholesale power purchases through ODEC may increase or decrease based upon rates established by the Board of Directors of ODEC.

Other

From time to time, the Cooperative becomes involved in litigation in the ordinary course of business. In management's opinion, the ultimate resolution of these matters will not have a material adverse effect on the Cooperative's financial position, results of operations or cash flows.

Note N - Related Party Transactions

The Cooperative is a member of the following organizations and conducted business transactions during the current and prior years as set forth below:

The Cooperative is a member of CFC (Notes E and I), a national financing organization, and had investment assets and mortgage notes payable at various interest rates and maturities.

The Cooperative, as a member of the ODEC, has entered into a contract for the acquisition of wholesale power.

The Cooperative is a shareholder of Federated Rural Electric Insurance Corporation (Note E), and purchases its general property and liability coverage from this organization.

The Cooperative, as a member of TEMA (Note E), purchased materials and supplies for construction and maintenance of the utility assets.

Supplemental Matters Required by the

Rural Utilities Service

Independent Auditor's 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
Southside Electric Cooperative, Inc.
Crewe, Virginia

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 Southside Electric Cooperative, Inc. (the "Cooperative"), which comprise the balance sheets as of December 31, 2019 and 2018, and the related statements of operations, equities and cash flows for the years then ended, and the related notes to the financial statements, and have issued our report thereon dated March 11, 2020.

Internal Control Over Financial Reporting

In planning and performing our audits 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 on the effectiveness of the Cooperative's internal control. Accordingly, we do not express an opinion on the effectiveness of the Cooperative's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or 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 internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audits we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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Compliance and Other Matters

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

We noted certain matters that we reported to management of Southside Electric Cooperative, Inc. in a separate letter dated March 11, 2020.

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 *Governmental Auditing Standards* in considering the Cooperative's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Adams, Jenkins & Cheatham

Richmond, Virginia
March 11, 2020

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

The Board of Directors
Southside Electric Cooperative, Inc.
Crewe, Virginia

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 Southside Electric Cooperative, Inc. (the "Cooperative"), which comprise the balance sheet as of December 31, 2019, and the related statements of operations, equities, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 11, 2020. In accordance with *Government Auditing Standards*, we have also issued a report dated March 11, 2020 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. No reports other than the reports referred to above 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*, §1773.33 and clarified in the 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 related 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 for accumulating and recording labor, material, and overhead costs, and the distribution of these costs to construction, retirement, and maintenance or other expense accounts;
- Reconcile continuing property records to the controlling general ledger plant accounts;
- Clear construction accounts and accrue depreciation on completed construction;
- Record and properly price the retirement of plant;
- Seek approval of the sale, lease or transfer of capital assets and disposition of proceeds for the sale or lease of plant, material, or scrap;

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- 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, operations, 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.

Adams, Jenkins & Cheatham

Richmond, Virginia
March 11, 2020