Pioneer Electric Cooperative, Inc.

JUNE 30, 2017

FINANCIAL STATEMENTS

PIONEER ELECTRIC COOPERATIVE, INC.
GREENVILLE, ALABAMA

INDEX

INDEPENDENT AUDITOR'S REPORT

The Board of Trustees
Pioneer Electric Cooperative, Inc.
Greenville, Alabama

Report on the Financial Statements

We have audited the accompanying financial statements of Pioneer Electric Cooperative, Inc., which comprise the balance sheets as of June 30, 2017 and 2016, and the related statements of revenue and patronage capital, and cash flows for the years then ended, and the related notes to 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 Pioneer Electric Cooperative, Inc. as of June 30, 2017 and 2016, 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.

Jackson Thornton & Co. PC

Montgomery, Alabama
September 13, 2017

PIONEER ELECTRIC COOPERATIVE, INC.
GREENVILLE, ALABAMA

BALANCE SHEETS
AT JUNE 30, 2017 AND 2016

ASSETS

	2017	2016
UTILITY PLANT:		
Electric plant in service	$ 72,705,156	$ 71,023,375
Construction work-in-progress	96,212	88,653
	72,801,368	71,112,028
Less: Accumulated provision for depreciation	25,634,083	24,232,223
Net utility plant	47,167,285	46,879,805
OTHER ASSETS AND INVESTMENTS:		
Restricted cash	1,446,175	1,488,270
Investments in associated organizations	13,934,052	13,598,411
Investment in land and buildings	1,033,602	953,909
Notes receivable		76,691
Total other assets and investments	16,413,829	16,117,281
CURRENT ASSETS:		
Cash and cash equivalents	3,366,912	3,160,486
Accounts receivable:		
Customers, less provision for doubtful accounts of $42,180 and $55,204 for 2017 and 2016, respectively	1,089,358	1,283,800
Unbilled revenue	1,418,324	1,418,324
Other	322,613	266,791
Inventories	299,629	329,100
Prepaids	144,280	152,694
Total current assets	6,641,116	6,611,195
DEFERRED ASSETS:		
NRUCFC conversion fees	5,808,524	6,073,422
Prepaid pension	368,670	860,231
Other	380,594	170,313
Total deferred assets	6,557,788	7,103,966
Total assets	$ 76,780,018	$ 76,712,247

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

LIABILITIES AND OTHER CREDITS

	2017	2016
EQUITIES:		
Patronage capital	$ 43,588,072	$ 41,691,429
Retained deficit	(21,965,864)	(21,965,864)
Other equities	404,121	310,665
Total equities	22,026,329	20,036,230
LONG-TERM DEBT:		
Notes payable	45,167,181	46,671,129
Capital lease obligations	150,354	186,175
Less: Current maturities	1,712,191	1,767,554
Total long-term debt	43,605,344	45,089,750
CURRENT LIABILITIES:		
Current maturities on long-term debt	1,712,191	1,767,554
Current portion of NRUCFC conversion fees	260,015	266,504
Current portion of postemployment benefits	22,254	30,946
Accounts payable:		
Purchased power	1,126,184	1,260,678
Trade	206,901	80,022
Customer deposits	1,210,858	1,199,558
Accrued liabilities:		
Taxes	350,579	461,323
Other	456,759	573,709
Total current liabilities	5,345,741	5,640,294
OTHER LONG-TERM LIABILITIES:		
NRUCFC conversion fees, net of current maturities	5,548,509	5,806,918
Postemployment benefits, net of current maturities	254,095	139,055
Total other long-term liabilities	5,802,604	5,945,973
Total liabilities and other credits	$ 76,780,018	$ 76,712,247

PIONEER ELECTRIC COOPERATIVE, INC.

STATEMENTS OF REVENUE AND PATRONAGE CAPITAL
FOR THE YEARS ENDED JUNE 30, 2017 AND 2016

	2017		2016	
OPERATING REVENUES	$ 28,113,922	100.00%	$ 28,188,432	100.00%
OPERATING EXPENSES:				
Cost of power	13,310,347	47.34%	13,478,868	47.82%
Distribution - operations	1,405,813	5.00%	1,377,903	4.89%
Distribution - maintenance	2,871,439	10.21%	2,667,733	9.46%
Consumer accounts	1,272,727	4.53%	1,321,528	4.69%
Energy marketing and communications	333,731	1.19%	264,060	0.94%
Administrative and general	2,343,116	8.33%	2,052,614	7.28%
Depreciation	2,689,503	9.57%	2,657,657	9.43%
Taxes	(51,070)	(0.18%)	191,449	0.67%
Total operating expenses	24,175,606	85.99%	24,011,812	85.17%
OPERATING MARGINS	3,938,316	14.01%	4,176,620	14.82%
G & T AND OTHER CAPITAL CREDITS	462,017	1.64%	656,816	2.32%
NET OPERATING MARGINS	4,400,333	15.65%	4,833,436	17.15%
INTEREST EXPENSE	1,885,865	6.71%	2,043,847	7.25%
NON-OPERATING MARGINS:				
Interest income	29,439	0.10%	44,058	0.16%
Other income	54,823	0.19%	(112,268)	(0.41%)
Total non-operating margins	84,262	0.29%	(68,210)	(0.25%)
NET MARGINS FOR THE YEAR	2,598,730	9.24%	2,721,379	9.65%
PATRONAGE CAPITAL AT BEGINNING OF YEAR	41,691,429		39,507,602	
RETIREMENT OF CAPITAL CREDITS	(702,087)		(709,015)	
UTILITY TAX REFUND			171,463	
PATRONAGE CAPITAL AT END OF YEAR	$ 43,588,072		$ 41,691,429	

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

PIONEER ELECTRIC COOPERATIVE, INC.

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2017 AND 2016
Increase (Decrease) in Cash and Cash Equivalents

	2017	2016
CASH FLOWS FROM (USED FOR) OPERATING ACTIVITIES:		
Net margins	$ 2,598,730	$ 2,721,379
Adjustments to reconcile net margins to net cash provided by operating activities:		
Depreciation and amortization	2,689,503	2,657,657
Amortization of deferred charges	491,561	491,560
Bad debt expense	(21,042)	(36,269)
G & T and other capital credits	(462,017)	(656,816)
Decrease (increase) in operating assets and increase (decrease) in operating liabilities:		
Accounts receivable	158,794	(23,153)
Materials and supplies	29,471	(7,299)
Prepaids	8,414	(14,056)
Other accrued assets	(210,281)	(150,815)
Accounts payable	(7,615)	(132,125)
Consumer deposits	11,300	84,881
Accrued liabilities	(121,346)	(107,930)
Net cash from operating activities	5,165,472	4,827,014
CASH FLOWS FROM (USED FOR) INVESTING ACTIVITIES:		
Purchase of property and equipment, net of salvage and cost of removal	(2,712,085)	(2,711,149)
Principal payments received on other notes receivable	76,691	197,402
Proceeds from investments	46,683	209,428
Net cash used for investing activities	(2,588,711)	(2,304,319)
CASH FLOWS FROM (USED FOR) FINANCING ACTIVITIES:		
Principal payments on notes payable	(1,538,901)	(1,252,396)
Payments on NRUCFC conversion fees	(264,898)	(271,325)
Increase in membership fees and other equity	93,456	264,063
Retirement of capital credits	(702,087)	(709,015)
Net cash used for financing activities	(2,412,430)	(1,968,673)
INCREASE IN CASH AND CASH EQUIVALENTS	164,331	554,022
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	4,648,756	4,094,734
CASH AND CASH EQUIVALENTS AT END OF YEAR	$ 4,813,087	$ 4,648,756
SUPPLEMENTAL CASH FLOWS INFORMATION:		
Restricted cash	$ 1,446,175	$ 1,488,270
Unrestricted cash	3,366,912	3,160,486
Totals	$ 4,813,087	$ 4,648,756
Cash paid for interest	$ 1,946,305	$ 2,119,179
Non-cash capital and related investing activities:		
Net additions of utility plant from capital leases		$ 186,175

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

NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2017 AND 2016

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Nature of business - Pioneer Electric Cooperative, Inc. (the Cooperative) distributes electric power to consumers in rural central Alabama.

Basis of accounting - The accounting records of the Cooperative are maintained in accordance with the Uniform System of Accounts prescribed by the Rural Utilities Service (RUS). As a result, the application of accounting principles generally accepted in the United States of America by the Cooperative differs in certain respects from the application of those principles by non-regulated enterprises. Such differences primarily concern the recognition of gains and losses on the retirement of assets.

Recognition revenue - Electric revenue and the related cost of power purchased are recognized when electricity is used by the ultimate consumer.

Cash equivalents - The Cooperative considers all highly liquid investments with maturity of three months or less when purchased to be cash equivalents.

Taxes - The Cooperative collects gross receipts taxes from its members on behalf of the State of Alabama. Revenue is presented net of taxes collected in the statement of income and patronage capital.

Accounts receivable - The Cooperative extends credit to its customers who are primarily located in central Alabama. Trade receivables are carried at original invoice amount less an estimate made for doubtful receivables based on a review of all outstanding amounts on a monthly basis. Management determines the allowance for doubtful accounts by identifying troubled accounts and by using historical experience applied to an aging of accounts. Trade receivables do not accrue interest. Trade receivables are written-off when deemed uncollectible. Recoveries of trade receivables previously written-off are recorded when received.

Inventories - Electric materials and supplies are priced at average historical cost. Cost is determined by the cumulative average of all costs on a first-in, first-out (FIFO) basis.

Electric plant - The Cooperative's costs associated with electric plant additions and improvements are capitalized based upon the RUS guidelines established in Bulletin 1767B-2. This results in the capitalization of direct costs such as labor and materials expense and also includes capitalization of indirect costs including labor, material charges, taxes, insurance, transportation, depreciation, pensions, and other related expenses. These costs are accumulated in work-in-process accounts and are capitalized to the proper plant accounts at the completion of the construction activity. Certain special equipment additions, as defined by RUS, are capitalized when purchased along with an estimated installation charge. The cost of depreciable property, when retired, is computed at the average unit cost along with removal costs less salvage. The net retirement cost is charged to accumulated depreciation. Maintenance and repairs, including minor items of property, are charged to maintenance expense as incurred.

Income tax status - The Cooperative is exempt from income taxes under Internal Revenue Code Section 501(c)(12).

Management evaluated the Cooperative's tax positions and concluded that the Cooperative had taken no uncertain tax positions that require adjustment to the financial statements.

Investments - Investments in associated organizations represent cooperative capital credits from the Cooperative's suppliers and lenders. Investments in associated organizations are recorded at cost plus allocated equities. Investments in land and buildings are carried at the lower of cost or market value.

Use of estimates - 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 certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Reclassification - Certain prior year amounts have been reclassified to conform to the current year presentation.

NOTE 2 - CASH AND CASH EQUIVALENTS:

The Cooperative maintains cash and cash equivalents in various banks located in Alabama, which at times may exceed federally insured limits. The Cooperative has approximately $8,000 and $35,000 in uninsured cash at multiple financial institutions at June 30, 2017 and 2016. The Cooperative has not experienced any losses in such accounts. The Cooperative believes it is not exposed to any significant credit risk on cash and cash equivalents.

Restricted funds relate to industrial development revolving loan programs. Restricted balances were as follows:

	2017	2016
Intermediary relending program	$ 467,502	$ 509,596
RUS revolving loan fund	388,585	388,585
REDLG	460,993	460,993
RBEG revolving loan fund	129,095	129,096
Total restricted funds	$ 1,446,175	$ 1,488,270

NOTE 3 - UTILITY PLANT AND DEPRECIATION:

Listed below are the major classes of electric plant as of June 30, 2017 and 2016:

	2017 PLANT BALANCES	2016 PLANT BALANCES	ANNUAL DEPRECIATION RATE
Distribution plant	$ 59,919,938	$ 58,420,211	3.20 - 4.00%
General plant:			
Land and rights	243,797	243,797	
Structures and improvements	5,003,304	4,962,807	2.05%
Office furniture and equipment	2,655,209	2,534,237	7.00 - 14.28%
Transportation equipment	1,235,916	1,224,657	17.00%
Power-operated equipment	2,657,669	2,657,725	6.72 - 17.00%
Communication equipment	550,592	541,210	8.00%
Other miscellaneous equipment	438,731	438,731	6.00 - 12.00%
Totals	$ 72,705,156	$ 71,023,375	

Electric plant is depreciated on a straight-line basis.

NOTE 4 - INVESTMENTS IN ASSOCIATED ORGANIZATIONS:

Investments in associated organizations consisted of the following at June 30, 2017 and 2016:

	2017	2016
PowerSouth patronage capital	$ 9,149,080	$ 8,885,701
NRUCFC patronage capital	1,840,479	1,783,611
Investment in NRUCFC capital term certificates	2,215,516	2,215,516
Other investments in associated organizations	728,977	713,583
Totals	$ 13,934,052	$ 13,598,411

NOTE 5 - EQUITIES:
At June 30, 2017 and 2016 equities consisted of:

	2017	2016
Equities at beginning of year	$ 19,725,565	$ 17,541,738
Retirement of capital credits	(702,087)	(709,015)
Utility tax refund		171,463
Net margins	2,598,730	2,721,379
Equities at end of year	$ 21,622,208	$ 19,725,565
Patronage capital	$ 43,588,072	$ 41,691,429
Retained earnings (deficit)	(21,965,864)	(21,965,864)
Equities at end of year	$ 21,622,208	$ 19,725,565
Memberships and other equities:		
Donated capital	$ 22,979	$ 22,979
Retired capital credits - gain	381,142	287,686
Total other equities	$ 404,121	$ 310,665

In 2005, the Cooperative was a lender to a company under common control. The company under common control could not satisfy its debt and was liquidated. Upon dissolution of the company under common control, the Cooperative recognized losses on its investment in that company. The deficit retained earnings are reflective of this loss.

NOTE 6 - NOTES PAYABLE AND LINES OF CREDIT:

DESCRIPTION	2017	2016
Mortgage notes payable - NRUCFC; fixed interest rates from 2.35% to 4.60%; notes due at various times up to December 2040; secured by all assets.	$ 44,711,409	$ 46,177,474
Notes payable - RUS; 1.00% interest; intermediary relending program; principal and interest due in installments until August 2030; secured by related economic development loans.	455,772	493,655
Total long-term notes payable	$ 45,167,181	$ 46,671,129

The Cooperative has covenants with its lenders relating to certain financial ratios.

Estimated maturities on long-term liabilities for the next five years are as follows:

June 30, 2018	$ 1,712,191
June 30, 2019	1,440,018
June 30, 2020	1,487,949
June 30, 2021	1,522,109
June 30, 2022	1,530,086

Lines of credit - The Cooperative has two lines of credit with NRUCFC on which it may borrow up to $12,500,000. One line of credit totals $5,000,000 and may be used only for electric capital or operating needs. The other line of credit totals $7,500,000 and may be used only for expenditures reimbursable by FEMA. As of June 30, 2017 and 2016, there were no outstanding balances outstanding on these lines of credit.

The Cooperative has an available unsecured line of credit with CoBank on which it may borrow up to a total of $5,000,000. The balance outstanding was $-0- at June 30, 2017 and 2016.

The NRUCFC loan conversion fees are payable in quarterly payments, over a period of 30 years. These conversion fees have no carrying cost. The related deferred asset is being amortized over a period of 30 years. Amortization expense related to this deferred asset was $264,898 and $271,325 for 2017 and 2016, respectively.

NOTE 7 - ACCOUNTING FOR PENSIONS:
The Cooperative is a participating employer in the National Rural Electric Cooperative Association (NRECA) Retirement Security Plan (RS Plan), which is a defined benefit pension plan qualified under Section 401 and tax exempt under Section 501(a) of the Internal Revenue Code. It is a multi-employer plan under the accounting standards. The plan sponsor's Employer Identification Number is 53-0116145 and the Plan Number is 333.

A unique characteristic of a multi-employer plan compared to a single employer plan is that all plan assets are available to pay benefits of any plan participant. Separate asset accounts are not maintained for participating employers. This means that assets contributed by one employer may be used to provide benefits to employees of other participating employers.

At the December 2012 meeting of the I&FS Committee of the NRECA Board of Directors, the I&FS Committee approved an option to allow participants in the RS Plan to make a prepayment and reduce future required contributions. In 2013, the Cooperative made a prepayment of $2,457,803 to the RS Plan. The Cooperative is amortizing this amount over five years. Amortization expense was $491,560 in 2017 and 2016.

The prepayment amount was calculated by NRECA as the 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 Cooperative estimates that the prepayment will reduce RS Plan billings by 25% for 15 years from the date of the prepayment. However changes in interest rates, asset returns, and other RS Plan experience differences from expectations, plan assumption changes, and other factors may have an impact on the differential in billings and the 15 year period.

The Cooperative's contributions to the RS Plan in 2017 and in 2016 represented less than 5% of the total contributions made to the plan by all participating employers. The Cooperative made contributions to the plan of $781,217 in 2017 and $758,094 in 2016.

In the RS Plan, a zone status determination is not required, and therefore not determined, under the Pension Protection Act (PPA) of 2006. In addition, the accumulated benefit obligations and plan assets are not determined or allocated separately by individual employer. In total, the Retirement Security Plan was over 80% funded at January 1, 2017 and January 1, 2016 based on the PPA funding target and PPA actuarial value of assets on those dates.

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

The Cooperative has a 401(k) plan for its employees. The total expense related to the 401(k) plan for the Cooperative was $59,435 and $56,790 for 2017 and 2016, respectively.

NOTE 8 - COMMITMENTS:
Under its wholesale power agreement, the Cooperative is committed to purchase its electric power and energy requirements from PowerSouth until December 31, 2055. The rates paid for such purchases are subject to periodic review.

NOTE 9 - CONTINGENCIES:
The Cooperative is a defendant in various lawsuits related to payment of capital credits. The Cooperative is vigorously contesting such lawsuits and denies all liability in these cases. In the opinion of the Cooperative's legal counsel, the likelihood of a favorable or unfavorable outcome to this litigation cannot be determined at this time, and therefore, an estimate of loss associated with such litigation, if any, cannot be determined.

NOTE 10 - SUBSEQUENT EVENTS:
The Cooperative has evaluated subsequent events through September 13, 2017, which is the date these financial statements were available to be issued. All subsequent events requiring recognition as of June 30, 2017, have been incorporated into these financial statements.