

# Wabash Valley Power Association, Inc.

Consolidated Financial Statements as of and for the  
Years Ended December 31, 2018 and 2017 and  
Independent Auditors' Report



**Deloitte & Touche LLP**  
111 Monument Circle  
Suite 4200  
Indianapolis, IN 46204-5105  
USA

Tel: +1 317 464 8600  
Fax: +1 317 464 8500  
[www.deloitte.com](http://www.deloitte.com)

## **INDEPENDENT AUDITORS' REPORT**

To the Board of Directors of  
Wabash Valley Power Association, Inc.  
Indianapolis, Indiana

We have audited the accompanying consolidated financial statements of Wabash Valley Power Association, Inc. and its subsidiary (the "Company"), which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of operations and patronage capital and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### **Management's Responsibility for the Consolidated Financial Statements**

Management is responsible for the preparation and fair presentation of these consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these consolidated 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the consolidated 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 Company'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 consolidated 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Wabash Valley Power Association, Inc. and its subsidiary as of December 31, 2018 and 2017, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*Deloitte & Touche LLP*

March 22, 2019

# WABASH VALLEY POWER ASSOCIATION, INC.

## CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 2018 AND 2017 (In thousands)

	2018	2017
<b>ASSETS</b>		
PLANT:		
In service—at cost	\$ 1,099,612	\$ 1,050,544
Construction work in progress	44,735	35,075
Plant held for future use	225	-
Less accumulated depreciation	<u>(355,464)</u>	<u>(326,044)</u>
	<u>789,108</u>	<u>759,575</u>
CURRENT ASSETS:		
Cash and cash equivalents	84,600	51,539
Short-term investments	20,000	-
Restricted cash	14,554	459
Accounts receivable	78,288	123,134
Fuel stock and material inventory—at average cost	16,573	16,762
Other	<u>4,109</u>	<u>13,340</u>
	<u>218,124</u>	<u>205,234</u>
OTHER ASSETS:		
Investments	15,129	14,034
Deferred charges	<u>162,975</u>	<u>173,420</u>
	<u>178,104</u>	<u>187,454</u>
TOTAL ASSETS	<u>\$ 1,185,336</u>	<u>\$ 1,152,263</u>
<b>CAPITALIZATION AND LIABILITIES</b>		
CAPITALIZATION:		
Patronage capital equity	\$ 223,803	\$ 208,303
Accumulated other comprehensive (loss) income	(1,020)	-
Line of credit borrowings	-	30,000
Capital lease obligations	1,437	1,481
Long-term debt	<u>726,686</u>	<u>684,624</u>
	<u>950,906</u>	<u>924,408</u>
CURRENT LIABILITIES:		
Current portion of long-term debt	43,242	39,240
Accounts payable	50,060	63,216
Accrued interest	6,541	6,363
Accrued taxes other than income	4,311	4,371
Over collected power costs	16,001	798
Other	<u>10,519</u>	<u>14,653</u>
	<u>130,674</u>	<u>128,641</u>
DEFERRED CREDITS	<u>103,756</u>	<u>99,214</u>
TOTAL CAPITALIZATION AND LIABILITIES	<u>\$ 1,185,336</u>	<u>\$ 1,152,263</u>

See notes to consolidated financial statements.

## WABASH VALLEY POWER ASSOCIATION, INC.

### CONSOLIDATED STATEMENTS OF OPERATIONS AND PATRONAGE CAPITAL FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017 (In thousands)

---

	2018	2017
OPERATING REVENUES:		
Member	\$575,857	\$574,107
Other	<u>78,995</u>	<u>128,287</u>
	<u>654,852</u>	<u>702,394</u>
OPERATING EXPENSES:		
Fuel	47,956	39,231
Operation and maintenance	57,490	56,086
Purchased power	420,449	489,655
Administrative and general	18,510	15,930
Other taxes	656	611
Depreciation and amortization	<u>51,207</u>	<u>48,599</u>
	<u>596,268</u>	<u>650,112</u>
OPERATING MARGIN	<u>58,584</u>	<u>52,282</u>
OTHER EXPENSES (INCOME):		
Interest expense—net of amounts capitalized	37,993	38,952
Interest income	(5,659)	(4,533)
Miscellaneous income and deductions—net	<u>2,250</u>	<u>(1,137)</u>
	<u>34,584</u>	<u>33,282</u>
NET MARGIN	24,000	19,000
PATRONAGE CAPITAL—Beginning of year	208,303	197,803
PATRONAGE CAPITAL RETIREMENT	<u>(8,500)</u>	<u>(8,500)</u>
PATRONAGE CAPITAL—End of period	<u>\$223,803</u>	<u>\$208,303</u>

See notes to consolidated financial statements.

# WABASH VALLEY POWER ASSOCIATION, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017 (In thousands)

	2018	2017
OPERATING ACTIVITIES:		
Net margin	\$ 24,000	\$ 19,000
Adjustments to reconcile net margin to net cash provided by operating activities:		
Depreciation and amortization	51,207	48,599
Loss on disposition of assets	2,561	-
Changes in certain assets and liabilities:		
Accounts receivable	44,846	(18,177)
Fuel stock and material inventory	189	828
Over collected/under recovered power costs	15,203	(9,541)
Accounts payable	(11,261)	(5,863)
Other assets	(843)	(1,046)
Other liabilities	(1,105)	(1,783)
Net cash provided by operating activities	<u>124,797</u>	<u>32,017</u>
INVESTING ACTIVITIES:		
Capital expenditures	(77,804)	(70,456)
Restricted assets	(95)	(459)
Proceeds from sale of property, plant and equipment	-	2,400
Proceeds from investments	229	13,403
Purchase of investments	(21,324)	(9,149)
Net cash used in investing activities	<u>(98,994)</u>	<u>(64,261)</u>
FINANCING ACTIVITIES:		
Proceeds from issuance of long-term debt	85,000	35,000
Change in line of credit borrowings	(30,000)	30,000
Patronage capital retirements	(8,500)	(8,500)
Payment on long-term debt	(39,242)	(37,862)
Net cash provided by financing activities	<u>7,258</u>	<u>18,638</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	33,061	(13,606)
CASH AND CASH EQUIVALENTS—Beginning of period	<u>51,539</u>	<u>65,145</u>
CASH AND CASH EQUIVALENTS—End of period	<u>\$ 84,600</u>	<u>\$ 51,539</u>
SUPPLEMENTAL CASH FLOWS INFORMATION:		
Cash paid for interest	\$ 36,914	\$ 38,546
Non-cash investing and operating activities—additions to electric plant included in accounts payable	\$ 1,895	\$ 3,536
Non-cash investing and financing activity—capital lease obligation	\$ -	\$ 1,624

See notes to consolidated financial statements.

# WABASH VALLEY POWER ASSOCIATION, INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2018 AND 2017

---

### 1. ORGANIZATION

**Organization**—Wabash Valley Power Association, Inc. (“Wabash Valley Power” or the “Company”) is a non-profit electric generation and transmission cooperative headquartered in Indianapolis, Indiana. The Company provides wholesale power to 23 rural electric membership corporations (REMCs) located in northern Indiana and parts of Illinois and Missouri.

Each member REMC has signed two All Requirements Contracts (ARCs) that obligate them to purchase all power and energy needed to serve their customers from Wabash Valley Power. The term of the first contract expires in April 2028, and the second contract term is from April 2028 through December 2050.

Membership also includes two non-cooperative organizations, JAron & Company (JAron) and Wabash Valley Energy Marketing, Inc. (Energy Marketing), a wholly owned subsidiary of Wabash Valley Power. JAron currently has contracted purchases from Wabash Valley Power through December 2019.

**Basis of Consolidation**—Due to Wabash Valley Power’s ownership and control over the operations of Energy Marketing, the results of Energy Marketing have been included in the consolidated financial statements and all significant intercompany transactions have been eliminated.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Regulatory Accounting**—Wabash Valley Power is governed by the Federal Energy Regulatory Commission (FERC) under the Federal Power Act and maintains its accounting records in accordance with the Uniform System of Accounts as prescribed by FERC, which conform to accounting principles generally accepted in the United States of America (GAAP) in all material respects. All required adjustments to FERC accounting have been made to make the consolidated financial statements consistent with GAAP.

The rates charged by the Company for power supplied to its members are based on the revenue required by Wabash Valley Power to cover the cost of supplying such power, plus an appropriate margin. As a rate-regulated entity, Wabash Valley Power issues consolidated financial statements that reflect actions of regulators that result in the recognition of revenues and expenses in different periods than enterprises that are not rate-regulated, in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 980—Regulated Operations (ASC 980). As such, regulatory assets are recorded to reflect future revenues associated with costs that are expected to be recovered from customers in future periods. Regulatory liabilities are recorded to reflect future reductions in revenues associated with amounts that are expected to be credited to customers in future periods. For further information, see Note 10—Deferred Charges and Credits.

Revenues and expenses that are deferred are treated as non-cash items in the consolidated statements of cash flows in the year of the deferral.

**Cash and Cash Equivalents**—Cash and cash equivalents include all highly liquid investments with original maturities of three months or less.

**Asset Impairment**—Long-lived assets are reviewed for impairment when events or circumstances change that could impact the recoverability of the asset's carrying amount. There were no impairments recorded during 2018 or 2017.

**Inventories**—Fuel stock and materials and supplies are valued at average cost. The costs of fuel and materials used in production are expensed as consumed and are recovered through rates.

**Revenue Recognition**—Revenue is recognized each period when energy is delivered to Wabash Valley Power's members or other non-member organizations. Member billed revenues reflect estimated power supply costs based on the current year's board-approved operating budget. Per the Formula Rate Tariff, member bills are adjusted in the subsequent year to collect or refund the difference between actual and estimated costs of power supply. Differences are shown as under recovered power costs or over collected power costs on the consolidated balance sheets. The over collected balance at December 31, 2018 and 2017 was \$16.0 million and \$0.8 million, respectively.

**Use of Estimates**—The preparation of consolidated financial statements, in conformity with GAAP, requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and disclosure of contingent assets and liabilities. The estimates and assumptions used in the consolidated financial statements are based on management's evaluation of the relevant facts and circumstances as of the date of the consolidated financial statements. Actual results may differ from those estimates.

**Concentration of Risk**—Approximately 13% of Wabash Valley Power's total revenues for 2018 and 10% of 2017 were derived from sales to Citizens Electric Corporation (Citizens). Accounts receivable balances for Citizens account for 10% of total accounts receivable as of December 31, 2018 and 7% as of December 31, 2017.

**Plant in Service and Maintenance**—Plant in service is stated at original cost, which includes labor, materials, overheads, and interest on borrowed funds used during construction (for major projects only). Maintenance and repairs of plant and replacement of items determined to be less than units of property are charged to maintenance expense as incurred.

When assets other than general plant are retired, sold or otherwise disposed of, the original cost plus the cost of removal, less salvage, is charged to accumulated depreciation and the corresponding gain or loss is amortized over the remaining life of the plant. Losses included in accumulated depreciation that will continue to be amortized are (\$25.7) million and (\$24.8) million at December 31, 2018 and 2017, respectively. As general plant assets are retired, the resulting gain or loss is recognized in the consolidated statements of operations.

Also included in accumulated depreciation are costs of removal for assets that do not have associated legal or contractual retirement obligations. Wabash Valley Power estimates that a regulatory liability related to these removal costs has been recorded in accumulated depreciation on the consolidated balance sheets at December 31, 2018 and 2017 of \$46.2 million and \$42.8 million, respectively.

Wabash Valley Power’s ownership in the Prairie State Energy Group LLC (Prairie State) also includes an interest in coal reserves. The original cost, net of depletion, at December 31, 2018 and 2017 was \$2.9 million and \$3.0 million, respectively.

**Depreciation**—Plant in service is depreciated on a straight-line basis at rates designed to recover the cost of properties over their estimated service lives. The resulting average depreciation rates by plant function at December 31 were as follows:

	<b>2018</b>	<b>2017</b>
Steam production	4.15 %	4.13 %
Other production	3.47 %	3.46 %
Transmission	2.18 %	2.15 %
Distribution	4.16 %	4.03 %
Other utility	3.70 %	3.70 %
General	7.34 %	5.95 %

**Federal Income Taxes**—Wabash Valley Power is exempt from federal income taxes under the provisions of Internal Revenue Code Section 501(c)(12) as long as member gross margins are at least 85% of total gross margins. Member gross margins as a percent of total gross margins for 2018 and 2017 were greater than 85%. As a result, no provision for federal income taxes was made during either year.

The Company has adopted guidance governing uncertain income tax positions that sets forth recognition thresholds and measurement attributes for financial statement recognition. The guidance did not result in the recording of any uncertain tax position liabilities as of December 31, 2018 and 2017. Tax years 2015 through 2018 remain open and could be subject to audit by the IRS.

### **3. RETIREMENT PLANS**

**Multiemployer Plan**-Qualified employees of the Company are members of a pension plan sponsored by the National Rural Electric Cooperative Association (NRECA). The NRECA Retirement Security Plan (RS Plan) is a defined benefit pension plan qualified under Section 401 and is tax-exempt under Section 501(a) of the Internal Revenue Code. It is a multiemployer plan under the accounting standards. The plan sponsor’s Employer Identification Number is 53-0116145 and the Plan Number is 333.

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

Contributions to the RS Plan by Wabash Valley Power in 2018 and 2017 represented less than 5% of the total contributions made to the plan by all participating employers. Wabash Valley Power had no contributions in 2018 and 2017 due to the Company making a prepayment to the RS Plan in 2015.

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% funded at both January 1, 2018 and January 1, 2017 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.

**Retirement Savings Plan**-Employees of the Company may voluntarily participate in the 401(k) savings plan offered through NRECA. Wabash Valley Power makes matching contribution payments to NRECA for the benefit of those employees who participate in the plan. The Company expenses the payments as incurred, and contributions were \$174,000 and \$144,000 for 2018 and 2017, respectively.

**Deferred Compensation Plan**-Wabash Valley Power maintains a nonqualified deferred compensation plan to provide supplemental retirement benefits for certain employees. The following table sets forth the accumulated post-retirement benefit obligation, the change in plan assets, and the components of accumulated post-retirement benefit cost and net periodic benefit cost.

<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
Accumulated benefit obligation - beginning of year	\$ -	\$ -
Plan amendments (new entrants to plan)	1,059	-
Service cost	23	-
Interest cost	11	-
Actuarial gain(loss)	(2)	-
Accumulated benefit obligation - end of year	<u>\$ 1,091</u>	<u>\$ -</u>
Fair value of plan assets - beginning of year	\$ -	\$ -
Company contributions	-	-
Benefits paid	-	-
Fair value of plan assets - end of year	<u>\$ -</u>	<u>\$ -</u>
Funded status - pension liability (deferred credits)	<u>\$ (1,091)</u>	<u>\$ -</u>
Service cost	\$ 23	\$ -
Interest cost	11	-
Amortization of prior service cost	37	-
Net periodic benefit cost	<u>\$ 71</u>	<u>\$ -</u>
Unrecognized actuarial loss (gain)	<u>\$ 1,020</u>	<u>\$ -</u>
Accumulated other comprehensive (income) loss	\$ 1,020	\$ -

#### **4. RECENTLY ISSUED ACCOUNTING STANDARDS**

In May 2014, the FASB issued ASU 2014-09—Revenue from Contracts with Customers. The standard provides guidance on the recognition of revenue from contracts with customers and requires additional disclosures about the nature, amount, timing, and uncertainty of revenue and cash flows from contracts with customers. In August 2015, FASB issued ASU 2015-14 delaying the effective date to January 2019. The new standard can be adopted either retrospectively to each reporting period or as a cumulative-effect

adjustment as of the date of adoption. The Company continues to evaluate the impacts of the standard to determine the overall impact it will have on the consolidated financial statements and related disclosures.

In February 2016, the FASB issued ASU 2016-2—Leases. The standard will increase the transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The standard is effective for Wabash Valley Power beginning January 2020 and is being evaluated to determine the overall impact it will have on the consolidated financial statements and related disclosures.

In August 2016, the FASB issued ASU 2016-15—Statement of Cash Flows: Classification of Certain Cash Receipts and Cash Payments. The standard provides consistency in the reporting of certain cash receipts and payments in the statement of cash flows. The standard is effective for Wabash Valley Power beginning January 2020, with early adoption permitted. The Company is evaluating the changes the standard may have on the statement of cash flows as currently presented.

In November 2016, the FASB issued ASU 2016-18—Statement of Cash Flows: Restricted Cash. The standard clarifies the guidance on the classification and presentation of restricted cash. The standard is effective for Wabash Valley Power beginning January 2019. The Company is evaluating the changes the standard may have on the statement of cash flows as currently presented.

## 5. PLANT IN SERVICE

Plant in service at December 31 consists of the following:

<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
Production	\$ 705,494	\$ 703,237
Transmission	280,001	245,207
Distribution	84,457	72,703
Other utility	12,181	12,003
General	<u>17,479</u>	<u>17,394</u>
Plant in service	<u>\$ 1,099,612</u>	<u>\$ 1,050,544</u>

Wabash Valley Power has an agreement with Duke Energy Indiana, Inc. (Duke Indiana) and Indiana Municipal Power Agency (IMPA) that provides for an undivided 25% ownership interest in the Gibson Unit No. 5 production facility.

Wabash Valley Power has an agreement with Duke Indiana that provides for an undivided 37.5% ownership interest in the Vermillion generating facility.

Wabash Valley Power has an agreement with Hoosier Energy REC (Hoosier) that provides for a one-third ownership interest in the Lawrence generating facility.

Wabash Valley Power and Hoosier jointly own the Holland generating facility. The agreement provides each owner with an undivided 50% ownership in the facility.

Wabash Valley Power has an undivided 5.06% ownership interest in Prairie State, which includes coal reserves and a captive coal mine that serves as the fuel source for the power plant.

Wabash Valley Power jointly owns certain transmission property and local facilities with Duke Indiana and IMPA. These facilities are part of the joint transmission system (JTS) maintained by Duke Indiana.

A substantial portion of Wabash Valley Power's utility plant and related operation and maintenance expenses is included under the terms of the above agreements.

## 6. INVESTMENTS

Investments at December 31, 2018 and 2017 consist of the following:

<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
Capital term certificates—CFC	\$ 4,086	\$ 4,315
Cooperative investment patronage allocation	10,465	9,141
Investment in associated organizations	<u>578</u>	<u>578</u>
Total	<u>\$15,129</u>	<u>\$14,034</u>

The capital term certificates (CTCs) bear interest ranging from 0% to 5.6% and were required in order to borrow from the National Rural Utilities Cooperative Finance Corporation (CFC). All investments with CFC are classified as held-to-maturity investments and are reported at cost.

Wabash Valley Power's cooperative investment patronage allocations are reported at cost, plus allocated equities.

Wabash Valley Power also has authority to make short-term investments. The amounts invested at December 31, 2018 and 2017 were \$20 million and \$0, respectively. As held-to-maturity investments that will mature in less than one year, the notes and commercial paper are carried at cost, which approximates fair value, in short-term investments on the consolidated balance sheets. There were no gains or losses recorded during the year.

## 7. LONG-TERM OBLIGATIONS

**Debt**—Wabash Valley Power’s long-term debt, as of December 31, consists of the following:

<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
First Mortgage Notes (due in quarterly installments):		
Series 1999-B	\$ 469	\$ 1,352
Series 2000-A	2,369	2,511
Series 2000-A	1,154	1,574
Series 2001-A	1,070	1,172
Series 2003-B	3,355	3,896
Series 2004-A	53,205	61,390
Series 2004-B	1,366	4,004
Series 2004-C	5,373	6,230
Series 2004-D	12,658	14,684
Series 2005-A	9,164	10,268
Series 2006-A	15,149	16,509
Series 2007	103,802	110,346
Series 2009-A	90,000	90,000
Series 2009-B	84,047	85,828
Series 2009-C	3,023	4,031
Series 2012	31,250	32,550
Series 2012	20,587	20,587
Series 2015-A	39,200	39,400
Series 2015-B	39,200	39,400
Series 2016-A	48,450	52,250
Series 2016-B	36,975	38,319
Series 2016-C	33,008	34,146
Series 2016-D	17,750	18,750
Series 2018-A	85,000	-
Tax-Exempt Bonds (due in quarterly installments)—		
Series 2010-A	29,000	31,000
Unsecured Notes (due in quarterly installments)—		
Series 2005	<u>5,533</u>	<u>6,202</u>
Total long-term debt	772,157	726,399
Less current maturities	43,242	39,240
Less debt issuance costs	<u>2,229</u>	<u>2,535</u>
Total long-term debt—net of current maturities and debt issuance costs	<u>\$ 726,686</u>	<u>\$ 684,624</u>

(a) Remaining balance due in quarterly installments beginning April 2020

(b) Due in annual installments

- (c) Variable rate on debt with swap to effectively fix the rate at 3.75% (see Note 12—Derivative Instruments)
- (d) Due at maturity
- (e) Variable rate on debt with swap to effectively fix the rate at 3.49% (see Note 12—Derivative Instruments)

Wabash Valley Power issues secured debt under an Indenture of Mortgage, Security Agreement and Financing Statement (Indenture). The Indenture requires the Company to design rates that shall, on an annual basis, yield a minimum times interest earned ratio (TIER) of 1.0 and a debt service coverage (DSC) ratio of 1.10. The TIER and DSC for the year ended December 31, 2018 were 1.64 and 1.48, respectively. Under the Indenture, Wabash Valley Power may retire patronage capital provided members' capital as of the end of the most recent fiscal quarter is not less than 20% of total long-term debt and members' capital (See Note 14—Members' Patronage Capital Equity).

The First Mortgage Notes are collateralized by the Company's generation, transmission, distribution and general plant assets (excluding transportation equipment).

Debt issuance costs are being amortized over the lives of the related debt on a straight-line basis.

Estimated future maturities on long-term obligations as of December 31, 2018 are as follows:

**(In thousands)**

2019	\$ 43,242
2020	44,083
2021	44,586
2022	45,140
2023	45,609
Thereafter	<u>549,497</u>
Total long-term debt	<u>\$772,157</u>

**Credit Facility**—The Company has a \$400 million syndicated revolving credit facility that expires in August 2022. The facility can be used to finance the general operating needs of the Company, provide interim financing of capital projects, and provide letters of credit to power supply counterparties to support purchase and sale obligations. Amounts outstanding under the agreement at December 31, 2018 and 2017 were \$0 million and \$30 million, respectively.

## **8. CAPITAL LEASE OBLIGATIONS**

Wabash Valley Power has three lease agreements for solar generation facilities, with an initial term of fifteen years. At the end of the lease term, Wabash Valley Power can either purchase the facilities or renew the leases for an additional five years. Wabash Valley Power has classified the agreements as capital leases and \$1.6 million is included in plant

in service on the consolidated balance sheets. Future minimum lease payments are as follows:

**(In thousands)**

2019	\$ 115
2020	115
2021	115
2022	115
2023	115
Thereafter	<u>1,443</u>
 Total minimum lease payments	 2,018
 Less amounts representing interest at 3.61%	 <u>(466)</u>
 Present value of minimum lease payments	 1,552
 Less current maturities	 <u>(115)</u>
 Long-term capital lease obligations	 <u>\$ 1,437</u>

Wabash Valley Power has entered into a purchased power agreement for 199 MW of solar generation. The agreement will end 27 years after the facility's commercial operation date, which is expected to be mid-2023. Wabash Valley Power has classified the agreement as a capital lease, however, the Company is not considered the asset owner during construction so no lease obligations have been recorded as of December 31, 2018. Future minimum lease payments are estimated to be \$0 due to the intermittent nature of the resource. Pricing per the contract is considered variable as payments are only required by Wabash Valley Power if there is energy produced from the facility.

**9. FAIR VALUE OF FINANCIAL INSTRUMENTS**

Cash and temporary cash investments, trustee deposits, CTCs, receivables, certain other liabilities and long-term debt are considered to be financial instruments. The carrying value of cash, temporary cash investments, trustee deposits, receivables and certain other liabilities approximate the fair value because of the short maturity of the instruments. The fair value of the CFC CTCs and other investments are not estimable since these instruments are required to be held by Wabash Valley Power as a condition of membership and can only be returned to the investee.

The Company uses observable inputs in the calculation of fair value. ASC 820—Fair Value Measurement and Disclosures (ASC 820) establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The three levels of the hierarchy are described below.

**Level 1**—Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities;

**Level 2**—Quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly;

**Level 3**—Prices or valuations that require inputs that are both significant to the fair value measure and unobservable.

Wabash Valley Power’s gas futures derivatives were valued using Level 1 inputs, which consist of quoted market prices from active exchange markets.

The Company’s power contract derivatives were calculated using broker quotes or appropriate pricing models with primarily externally verifiable model inputs. These valuations are considered Level 2.

The interest rate swap derivatives were valued using yield curves derived from current interest rates and spreads to project and discount swap cash flows to present value. These valuations are considered Level 2.

## 10. DEFERRED CHARGES AND CREDITS

Amounts recorded as deferred charges as of December 31, 2018 and 2017, are as follows:

<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
Regulatory asset—unrealized losses on derivative instruments	\$ 80,956	\$ 85,831
Regulatory asset—contract termination cost	4,595	4,986
Fair value of derivative instruments	56	475
Contributions for transmission upgrades	1,632	1,978
Plant retirement and decommissioning costs	73,253	78,153
Other deferred charges	<u>2,483</u>	<u>1,997</u>
Total deferred charges	<u>\$162,975</u>	<u>\$173,420</u>

Wabash Valley Power has FERC approval to defer all unrealized gains and losses on derivative and hedging contracts. Amounts are recorded as a regulatory asset or liability until the derivative is settled, at which time the gain or loss is recognized in earnings.

A power supply contract with Duke Energy Vermillion LLC (Duke Energy) was terminated in 2004 when the Company acquired an ownership interest in the Vermillion generating facility (see Note 5—Plant in Service). Wabash Valley Power received regulatory approval to defer the termination costs and amortize them over the remaining life of the plant (through September 2030).

The Company has power, gas futures and interest rate contracts that qualify as derivative instruments under FASB ASC 815—Accounting for Derivative Instruments and Hedging Activities (ASC 815), as amended. These contracts are recorded at fair value in the consolidated balance sheets. See Note 12—Derivative Instruments for the recovery period of derivative contracts.

Wabash Valley Power has made contributions to transmission providers to upgrade or install facilities for the sole benefit of Wabash Valley Power’s member systems. The facilities are not owned by Wabash Valley Power and the amounts are billed to the respective Wabash Valley Power customers over a negotiated term, with all amounts to be recovered by April 2048.

Wabash Valley Power had a 50% interest in sgSolutions LLC (sgSolutions) whose assets consisted of a coal gasification plant located in West Terre Haute, Indiana. In 2016, the operations of sgSolutions were discontinued, the assets were sold and the partnership dissolved. Also in 2016, a steam turbine associated with the gasification plant was retired prior to being fully recovered in rates. Wabash Valley Power has FERC approval to defer all costs associated with the retirement and decommissioning of WRU1 and the discontinued operations of sgSolutions. The deferral is being amortized over 14 years, which approximated the remaining lives of the assets, and continues through May 2030.

Amounts recorded as deferred credits as of December 31, 2018 and 2017, are as follows:

<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
Member buy-out payments	\$ 7,311	\$ 8,094
Regulatory liability—unrealized gains on derivative instruments	56	475
Fair value of derivative instruments	80,956	85,831
Asset retirement obligations	3,840	4,236
Collateral from power provider	10,000	-
Other deferred credits	<u>1,593</u>	<u>578</u>
Total deferred credits	<u>\$ 103,756</u>	<u>\$99,214</u>

Midwest Energy Cooperative (Midwest) terminated membership in Wabash Valley Power effective December 31, 2011 and a portion of Midwest's load was being served as a non-member sale via another provider. The member termination fee received from Midwest was deferred and amortized from January 2012 through December 2017. Paulding Putnam REMC's membership terminated at the end of 2014 and Northeastern REMC's (Northeastern) membership terminated on June 30, 2015. The termination fees received were deferred and are being amortized through April 2028 (see Note 14—Members' Patronage Capital Equity).

Under the terms of a long-term solar purchased power agreement, Wabash Valley Power received collateral to cover default by the supplier during the development phase of the project. The funds will be returned to the supplier upon commercial operation of the facility. The collateral can be replaced, at any time, by a letter of credit, at which time the funds would be returned to the supplier.

## **11. ASSET RETIREMENT OBLIGATIONS**

The Company records its ownership share of legal obligations associated with the retirement of waste landfills and ash ponds at the Gibson Unit No. 5 production facility and mine reclamation and closure costs at the Prairie State generating facility. The obligations are recorded at fair value when incurred and capitalized as a cost of the related asset. The liability is accreted to its present value each period and the capitalized cost is depreciated over the useful life of the related asset. When the asset is retired, the entity settles the obligation for its recorded amount or incurs a gain or loss.

The following table represents the details of Wabash Valley Power's asset retirement obligations, which are included on the consolidated balance sheets in deferred credits.

<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
Beginning balance	\$4,236	\$4,121
Liabilities incurred	-	-
Liabilities settled	(614)	(152)
Accretion	156	162
Cash flow revisions	<u>62</u>	<u>105</u>
Ending balance	<u>\$3,840</u>	<u>\$4,236</u>

## **12. DERIVATIVE INSTRUMENTS**

Wabash Valley Power is exposed to various market risks in the normal course of business. Management has established risk management policies to mitigate the potentially adverse effects that these risks may have on member rates. The policies include the use of derivative instruments that generally qualify for the normal purchase and normal sales exception under ASC 815.

Wabash Valley Power enters into power contracts with the primary intent of securing wholesale power requirements for members at the minimum cost, while enhancing the value of Wabash Valley Power's assets and managing the risk associated with volatility in power prices. These contracts generally meet the definition of a derivative as defined in ASC 815. Many of these contracts qualify for the normal purchase and normal sales exception and are not recorded in the consolidated financial statements at fair value. Contracts not meeting the normal purchase and normal sales exception are reflected at fair value on the consolidated balance sheets. Wabash Valley Power values its contracts using market prices from brokers. Notional values of these contracts for 2018 and 2017 were 7.4 million megawatt hours (MWh) and 8.6 million MWh, respectively.

Wabash Valley Power holds gas futures contracts for the primary purpose of mitigating volatility in gas prices related to the operation of its gas-fired plants and as a means to reduce the effect on member rates due to changes in future gas prices. These contracts qualify as derivatives and are recorded at fair value on the consolidated balance sheets. Notional values under these contracts were 13,384,000 MMBtu (million British thermal units) in 2018 and 15,994,000 MMBtu in 2017.

Wabash Valley Power has entered into three interest rate swap agreements with a total notional value of \$60.1 million to mitigate the risk associated with changes in floating interest rates on the issuance of variable-rate long-term debt. The swap agreements convert floating rates into fixed rates on a quarterly basis, so the Company can more accurately predict future interest costs and protect itself against increases in floating rates. These contracts qualify as derivatives and are reflected at fair value on the consolidated balance sheets. See Note 7—Long-term Obligations for additional detail.

See Note 9—Fair Value of Financial Instruments for additional information regarding the fair value of these derivatives.

The following reflects the amounts recorded in assets and liabilities at December 31, 2018 and 2017 for the Company's derivative instruments:

<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
<b>Power contracts:</b>		
Other current assets	\$ 1,503	\$ 296
Deferred charges	6	475
<b>Gas futures:</b>		
Other current assets	11	15
Deferred charges	<u>50</u>	<u>-</u>
Total derivative assets	<u>\$ 1,570</u>	<u>\$ 786</u>
<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
<b>Power contracts:</b>		
Other current liabilities	\$ 262	\$ 9,670
Deferred credits	79,708	85,167
<b>Gas futures:</b>		
Other current liabilities	202	280
Deferred credits	<u>1,248</u>	<u>664</u>
Total derivative liabilities	<u>\$81,420</u>	<u>\$95,781</u>

The changes in the fair value of derivative contracts result in unrealized gains and losses, which are reflected in regulatory assets or liabilities, as appropriate, on the consolidated balance sheets (See Note 10—Deferred Charges and Credits). As the contracts are settled, the derivative assets and liabilities and corresponding regulatory assets and liabilities are relieved and amounts are recognized in fuel expense, purchased power, or interest expense, as appropriate.

Net realized losses (gains) recognized in earnings for the years ended December 31, 2018 and 2017 were as follows:

<b>(In thousands)</b>	<b>2018</b>	<b>2017</b>
Power contracts (purchased power)	\$4,340	\$2,659
Gas futures (fuel expense or purchased power)	(523)	(325)
Interest rate swaps (interest expense)	373	929

The realized portion of derivative gains and losses is reflected in net cash from operating activities on the consolidated statements of cash flows.

All power and gas futures contracts reflected at fair value on the consolidated balance sheets at December 31, 2018 mature on or before December 31, 2025. The interest rate swaps mature in January 2032 and July 2032. Based on the Company's current credit rating, Wabash Valley Power was required to post cash collateral of \$17.5 million under the terms of these agreements as of December 31, 2018.

### 13. RELATED PARTY TRANSACTIONS

Wabash Valley Power is a member of ACES LLC (ACES), which provides wholesale marketing services and efficiencies of combining the marketing of member power resources. The investment in ACES is accounted for using the cost method of accounting. At December 31, 2018 and 2017, Wabash Valley Power's investment in ACES was approximately \$0.5 million.

### 14. MEMBERS' PATRONAGE CAPITAL EQUITY

Revenues in excess of current period costs (net margins) in any year are considered capital furnished by the members and are credited to the members' individual accounts pursuant to the provisions of its by-laws. Net margins are held by Wabash Valley Power until they are retired and returned, without interest, at the discretion of the Board of Directors and subject to certain restrictions under the Indenture (see Note 7—Long-term Obligations). Amounts returned to members in each of the years 2018 and 2017 was \$8.5 million.

Wabash Valley Power's Buyout Policy and Procedure (Buyout Policy) describes the process and obligations for withdrawing from membership. Pursuant to the Buyout Policy, a terminating member continues to be an all-requirements purchaser and member for ten years upon execution of a Supplemental Agreement. During the ten-year period, the terminating member is required to deposit specified amounts into an escrow account, together with accrued interest thereon, which is paid to an Escrow Agent. Upon written notice, the terminating member can elect to cancel the Supplemental Agreement prior to the end of the seventh year, receive all escrow funds and continue its membership in Wabash Valley Power.

### 15. COMMITMENTS, CONTINGENCIES AND PENDING LITIGATION

**Long-Term Supply Agreements**—Wabash Valley Power has several long-term power supply agreements that obligate the Company to purchase power at amounts specified in the agreements without regard to whether it takes delivery of such power. All of these power supply agreements expire on or before December 31, 2035, and the total amount of these future purchase obligations is approximately \$1,320.7 million as of December 31, 2018. The amounts by year are as follows:

(In thousands)

2019	\$107,241
2020	108,309
2021	124,248
2022	123,573
2023	94,104
Thereafter	763,188

Wabash Valley Power also has long-term power supply agreements that are supplier cost-based. The costs are part of a formula rate and vary from year to year. Volumes under these agreements are approximately 305 megawatts (MW) per year and all agreements expire on or before December 31, 2032.

Amounts paid under long-term agreements were \$278.0 million and \$326.1 million in 2018 and 2017, respectively.

**Guarantees**—Wabash Valley Power’s Board of Directors has authorized the following guarantees related to the Company’s 50% ownership of the Holland generating facility.

- Guarantee up to \$10 million of activities related to operations, fuel purchasing, financial and construction activities. A guarantee for \$6.0 million is outstanding as of December 31, 2018.
- Guarantee up to \$0.1 million of MISO activities. A guarantee to MISO for \$0.1 million is outstanding as of December 31, 2018.

As of December 31, 2018 and 2017, Wabash Valley Power has recorded its 50% ownership share of the liabilities of the Holland generating facility.

**Pending Litigation** – On October 1, 2018, Tipmont Rural Electric Membership Corporation (“Tipmont”) filed a Complaint at FERC requesting that the FERC find that Tipmont may terminate service early under its wholesale power supply contracts (“Wholesale Contracts”) with Wabash Valley Power subject to Tipmont’s paying any demonstrated stranded costs that Wabash Valley Power may incur as a result of early termination. Tipmont also requested that FERC initiate an investigation into the justness and reasonableness of certain of the Wholesale Contracts’ rates terms and conditions, including the validity of certain rates, terms and condition of service that Tipmont alleges have never been filed with FERC, specifically, Wabash Valley Power’s Buy Out Policy D-2. On the same date, Tipmont notified Wabash Valley Power that it intends to terminate the purchase of service under the Wholesale Contracts from the Company as of January 1, 2020, and that it is willing to pay fair and appropriate stranded costs approved by FERC.

On November 5, 2018, Wabash Valley Power filed its Answer to Tipmont’s Complaint asking FERC to reject Tipmont’s request to be allowed to terminate service early under the FERC-filed Wholesale Contracts without complying with the ten-year notice and buyout provisions contained in the Wholesale Contracts, reject Tipmont’s request that that FERC determine the level of Tipmont’s buyout costs under an inapplicable stranded cost formula and that FERC reject Tipmont’s invitation to investigate other Wholesale Contract rates, terms and conditions.

Tipmont filed a Response to Wabash Valley Power’s Answer on November 19, 2018 and the Company filed a Reply to Tipmont’s Response on November 30, 2018. Since that date, FERC has taken no action on Tipmont’s Complaint. In the unlikely event that FERC determines that Tipmont may terminate service early, it should not have a material adverse effect on Wabash Valley Power because Tipmont has admitted and agreed that it must pay stranded costs to Wabash Valley Power to make the Company and the other members whole as a result of Tipmont’s early departure and the loss of its load.

**Environmental Matters**—The Environmental Protection Agency (EPA) issued the Cross State Air Pollution Rule (CSAPR) in July 2011 that limits sulfur dioxide (SO<sub>2</sub>) and nitrogen oxide (NO<sub>x</sub>) emissions at generating facilities, which became effective on January 1, 2015 due to delays in litigation. In 2016, the EPA finalized the Cross-State Air Pollution Rule Update for the 2008 Ozone NAAQS (CSAPR II). CSAPR II replaced the NO<sub>x</sub> Ozone Season allowance-trading program established in CSAPR. At this time, the Company’s assets are subjected to the Acid Rain Program, CSAPR SO<sub>2</sub> Group 1, CSAPR Annual NO<sub>x</sub> and CSAPR II Group 2 Ozone Season NO<sub>x</sub> allowance trading programs. The Company purchases allowances needed to comply and the impact to the cost of operations is immaterial.

In late 2013 and mid-2014, the EPA proposed a suite of standards to regulate carbon emissions from new, existing, modified and reconstructed power plants. These standards were finalized in August 2015, but have been stayed by the U.S. Supreme Court. With the advent of the Republican administration, the Clean Power Plan (CPP), which is applicable to existing power plants, is in the process of being undone and proposed to be replaced with the Affordable Clean Energy (ACE) Rule, with promulgation expected by summer 2019. Further, the EPA is proposing revisions to the carbon emissions standards affecting new, modified and reconstructed power plants. Wabash Valley Power has engaged with other utilities and state agencies to minimize the impact of the current rules on its facilities, while developing a strategy to provide meaningful input on the replacement rules. In addition, the EPA tightened the Ozone National Ambient Air Quality Standards (NAAQS) and revised the Steam Electric Effluent Guidelines in 2015. The Company estimates the cost impact to its facilities to be minimal. However, the Company cannot accurately estimate the impact they will have on the costs charged by suppliers under the Company's various power supply agreements.

On April 17, 2015, the EPA published in the Federal Register a rule to regulate the disposal of coal combustion residuals (CCR) from electric utilities as solid waste. The federal regulation, which became effective in October 2015, classifies CCR as nonhazardous waste and allows for beneficial use of CCR with some restrictions. The regulation applies to all new and existing landfills, new and existing surface impoundments receiving CCR and existing surface impoundments that are no longer receiving CCR but contain liquid located at stations currently generating electricity (regardless of fuel source). The rule establishes requirements regarding landfill design, structural integrity design and assessment criteria for surface impoundments, groundwater monitoring and protection procedures and other operational and reporting procedures to ensure the safe disposal and management of CCR. In addition to the requirements of the federal CCR regulation, CCR landfills and surface impoundments will continue to be independently regulated by most states. The Company recorded an asset retirement obligation (ARO) during 2015 because of these new rules. Cost recovery for future expenditures will be pursued through the normal ratemaking process.

The ARO amount recorded on the consolidated balance sheets is based upon estimated closure costs for impacted ash impoundments. The amount recorded represents the discounted cash flows for estimated closure costs based upon closure plans. Actual costs to be incurred will be dependent upon a variety of specific factors. The most significant factors are the method and time frame of closure at the site. The ultimate method and timetable for closure will comply with standards set by federal and state regulations. The ARO amount will be adjusted as additional information is gained through the closure process, including acceptance and approval of compliance approaches that may change management assumptions, and may result in a material change to the balance. Asset retirement costs for operating plants and retired plants are included in Plant in service and the associated AROs are recorded in Deferred Credits (see Note 11—Asset Retirement Obligations).

## **16. SUBSEQUENT EVENTS**

The consolidated financial statements include a review of subsequent events through March 22, 2019, the date the consolidated financial statements were issued.

\* \* \* \* \*