

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITOR'S REPORT



December 31, 2021 and 2020

BLODGETT, MICKELSEN & ADAMSON, P.S.
CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Inside Passage Electric Cooperative, Inc.
Auke Bay, Alaska

Opinion

We have audited the accompanying financial statements of Inside Passage Electric Cooperative, Inc. which comprise the balance sheets as of December 31, 2021 and 2020, and the related statements of revenues and margins, changes in equities and margins, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Inside Passage Electric Cooperative, Inc. as of December 31, 2021 and 2020, 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.

Basis for Opinion

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

Responsibilities of Management for the Financial Statements

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

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

Auditor's Responsibilities for the Audit of the Financial Statements

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

In performing an audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Inside Passage Electric Cooperative, Inc.'s internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Inside Passage Electric Cooperative, Inc.'s ability to continue as a going concern for a reasonable period of time.

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

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 2, 2022, on our consideration of Inside Passage Electric Cooperative, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Inside Passage Electric Cooperative, Inc.'s 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 Inside Passage Electric Cooperative, Inc.'s internal control over financial reporting and compliance.

Blodgett, Mickelsen & Adamson, P.S.

Kennewick, Washington
March 2, 2022

Inside Passage Electric Cooperative, Inc.

BALANCE SHEETS

December 31, 2021 and 2020

ASSETS

	<u>2021</u>	<u>2020</u>
UTILITY PLANT - AT COST (notes 1, 2 and 11)		
Electric plant in service - at cost	\$ 25,427,469	\$ 24,842,613
Construction work in progress	29,025	6,319
	<u>25,456,494</u>	<u>24,848,932</u>
Less accumulated depreciation and amortization	14,217,840	13,656,404
Net electric plant	<u>11,238,654</u>	<u>11,192,528</u>
INVESTMENTS IN ASSOCIATED ORGANIZATIONS AND RESTRICTED CASH (notes 1 and 4)		
Investments in associated organizations	1,635,956	1,591,968
Restricted cash:		
Consumer deposits	73,633	78,192
State of Alaska performance guarantees	13,600	13,600
	<u>1,723,189</u>	<u>1,683,760</u>
CURRENT ASSETS (notes 1 and 3)		
Cash and cash equivalents	1,844,501	114,349
Accounts receivable, less provision for doubtful accounts of \$35,587 in 2021 and \$24,256 in 2020	456,759	372,874
Grant receivable	41,399	-
Other receivables	670,393	9,747
Unbilled revenue	299,168	236,940
Materials and supplies	252,583	257,630
Fuel inventory	297,646	199,850
Prepaid expenses	85,486	33,610
Total current assets	<u>3,947,935</u>	<u>1,225,000</u>
DEFERRED CHARGES (notes 1 and 5)	<u>13,693</u>	<u>27,387</u>
	<u>\$ 16,923,471</u>	<u>\$ 14,128,675</u>

The accompanying notes are an integral part of these statements.

EQUITIES, MARGINS AND LIABILITIES

	2021	2020
EQUITIES AND MARGINS (note 1)		
Patronage capital	\$ 1,770,479	\$ 1,533,670
Other equities	5,932,141	5,829,020
	7,702,620	7,362,690
LONG-TERM DEBT, less current maturities (notes 6 and 11)	7,560,219	4,805,730
COMMITMENTS AND CONTINGENCIES (note 9)	-	-
CURRENT LIABILITIES (notes 1, 6, 7 and 11)		
Accounts payable	880,773	321,967
Consumer deposits	73,633	78,192
Accrued payroll and related liabilities	103,279	91,923
Accrued taxes	7,654	7,025
Line of credit	-	1,000,000
Current maturities of long-term debt	427,204	341,682
Total current liabilities	1,492,543	1,840,789
DEFERRED CREDITS (notes 1 and 8)	168,089	119,466
	\$ 16,923,471	\$ 14,128,675

The accompanying notes are an integral part of these statements.

Inside Passage Electric Cooperative, Inc.

STATEMENTS OF REVENUES AND MARGINS

Years ended December 31, 2021 and 2020

	<u>2021</u>	<u>2020</u>
Operating revenues (note 1)	\$ 5,831,809	\$ 4,966,551
Operating expenses		
Purchased power	307,223	199,798
Power production - operation	2,406,208	1,981,622
Power production - maintenance	400,327	426,627
Distribution - operation	198,793	161,296
Distribution - maintenance	122,815	102,066
Consumer accounts	200,773	190,090
Consumer service and information	21,490	8,782
Sales expense	29,202	27,408
Administrative and general	1,077,118	1,069,497
Depreciation and amortization	580,467	467,363
Taxes	5,331	4,612
Total operating expenses	<u>5,349,747</u>	<u>4,639,161</u>
Net operating margins before fixed charges	482,062	327,390
Fixed charges		
Interest on long-term debt	244,353	158,549
Donations to member communities	900	1,285
	<u>245,253</u>	<u>159,834</u>
Net operating margin	236,809	167,556
Non-operating margins		
Patronage capital	100,624	66,100
Interest income	867	1,221
Rental income, net of rental expenses	-	21,145
Other non-operating income	1,630	781
	<u>103,121</u>	<u>89,247</u>
NET MARGINS	<u><u>\$ 339,930</u></u>	<u><u>\$ 256,803</u></u>

The accompanying notes are an integral part of these statements.

Inside Passage Electric Cooperative, Inc.

STATEMENTS OF CHANGES IN EQUITIES AND MARGINS

Years ended December 31, 2021 and 2020

	Patronage Capital	Other Equities		Total
	Inside Passage Operating Margins	Inside Passage Non-Operating Margins	THREA Donated Capital	
Balance at December 31, 2019	\$ 1,366,114	\$ 1,853,596	\$ 3,886,177	\$ 7,105,887
Net margins	167,556	89,247	-	256,803
Balance at December 31, 2020	\$ 1,533,670	\$ 1,942,843	\$ 3,886,177	\$ 7,362,690
Net margins	236,809	103,121	-	339,930
Balance at December 31, 2021	\$ 1,770,479	\$ 2,045,964	\$ 3,886,177	\$ 7,702,620

Inside Passage Electric Cooperative, Inc.

STATEMENTS OF CASH FLOWS

Years ended December 31, 2021 and 2020

	<u>2021</u>	<u>2020</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net margins	\$ 339,930	\$ 256,803
Adjustments to reconcile net margins to net cash provided by operating activities:		
Depreciation and amortization	580,467	467,363
Net operating changes in:		
Accounts receivable	(83,885)	124,380
Grant receivable	(41,399)	439,955
Other receivables	(660,646)	22,531
Unbilled revenue	(62,228)	7,148
Materials and supplies	5,047	(5,545)
Fuel inventory	(97,796)	58,816
Prepaid expenses	(51,876)	24,430
Deferred charges	13,694	22,347
Accounts payable	558,806	45,226
Consumer deposits	(4,559)	22,364
Accrued payroll and related liabilities	11,985	27,969
Deferred credits	48,623	(20,791)
	<u>556,163</u>	<u>1,492,996</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES		
CASH FLOWS FROM INVESTING ACTIVITIES		
Net additions to utility plant	(607,562)	(1,549,153)
Book value of property dispositions and plant removal - net of retirements	(19,031)	(108,329)
Net increase in investments in associated organizations	(43,988)	(42,927)
	<u>(670,581)</u>	<u>(1,700,409)</u>
NET CASH USED IN INVESTING ACTIVITIES		

The accompanying notes are an integral part of these statements.

	<u>2021</u>	<u>2020</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on long-term debt	\$ (359,989)	\$ (331,312)
Proceeds from borrowings of long-term debt	3,200,000	-
Payments on line of credit	(1,500,000)	(993,500)
Proceeds from borrowings on line of credit	500,000	1,142,000
	<hr/>	<hr/>
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	1,840,011	(182,812)
	<hr/>	<hr/>
Net increase (decrease) in cash	1,725,593	(390,225)
Cash and cash equivalents at beginning of year	206,141	596,366
	<hr/>	<hr/>
Cash and cash equivalents at end of year	\$ 1,931,734	\$ 206,141
	<hr/> <hr/>	<hr/> <hr/>

Cash paid for interest during the years December 31, 2021 and 2020 amounted to \$244,353 and \$212,019, respectively.

Reconciliation of Cash and Cash Equivalents to Balance Sheet:

Cash and cash equivalents	\$ 1,844,501	\$ 114,349
Restricted cash:		
Consumer deposits	73,633	78,192
State of Alaska performance guarantees	13,600	13,600
	<hr/>	<hr/>
	87,233	91,792
	<hr/>	<hr/>
	\$ 1,931,734	\$ 206,141
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NOTES TO FINANCIAL STATEMENTS

December 31, 2021 and 2020

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Inside Passage Electric Cooperative, Inc. (IPEC or the Cooperative) operates an electric utility from offices in Auke Bay, Alaska, which provides services to the southeast Alaska communities of Angoon, Hoonah, Kake, Klukwan and Chilkat Valley. IPEC operates on a not-for-profit basis and, accordingly, seeks only to generate revenues sufficient to pay operating and maintenance costs, capital expenditures, depreciation, and interest on indebtedness and to provide for the establishment of reasonable margins and reserves.

The accounting records of IPEC conform to the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission as modified for electric borrowers of the Rural Utility Service (RUS). A summary of the Cooperative's significant accounting policies consistently applied in the preparation of the accompanying financial statements follows:

a. Cash and cash equivalents

For purposes of the statement of cash flows, the Cooperative considers all cash on hand, cash in banks and highly liquid instruments that are readily convertible to known amounts of cash and that present an insignificant risk of change in value due to changes in interest rates or other factors to be cash equivalents.

b. Investments in associated organizations

Because fair value is not readily determinable, the Cooperative's investments in associated organizations are carried at cost, which approximates fair value, plus patronage capital credits allocated and not retired. Investments are reduced by distributions received. Capital credits from associated organizations are not valued until allocated.

Investments in associated organizations were not evaluated for impairment because (a) it is not practicable to estimate their fair values due to insufficient information available and (b) management did not identify any events or changes in circumstances that might have a significant adverse effect on the fair value of those investments.

c. Accounts and other receivables

Accounts and other receivable are recorded when invoices are issued and are written off as a charge to the allowance for doubtful accounts when they are determined to be uncollectible. The allowance for doubtful accounts is estimated considering the Cooperative's historical losses, review of specific problem accounts, existing economic conditions and the financial stability of its customers. Generally, IPEC considers accounts receivable past due after 25 days.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

d. Grant receivable

Grant receivable represents the amount due to the Cooperative for reimbursable expenses from the Alaska Energy Authority (AEA) for a grant related to the design of a hydroelectric dam project. As the Cooperative incurred expenses that were reimbursable under the grants, the expenses were billed to AEA and recorded as grant receivable until the reimbursement was received. See note 3 for further details.

e. Revenue recognition and unbilled revenue

The majority of the Cooperative’s revenue is from energy sales to the Cooperative’s members. Energy sales are recognized upon delivery of electricity to the member’s meter based on billing rates set by the Cooperative’s Board of Trustees. These rates include base charges which are fixed fees based on the type of meter and variable charges which depend on the member’s usage of electricity on a per kilowatt (kWh) basis during the billing period. The Cooperative utilizes cycle billing and records revenue billed based upon monthly meter readings. In addition, the Cooperative recognizes unbilled revenue, revenue from electric power delivered but not yet billed. The Cooperative’s energy rates follow the Cooperative Principles, which include operating at cost and allocating any surplus margins back to the membership. The majority of the Cooperative’s contracts do not contain variable consideration and contract modifications are typically minimal.

For non-electric revenue, revenue is recognized at a single point in time when ownership, risk and rewards transfer. Any revenue recognized over time consists of performance obligations that are typically one year or less. Sales and other taxes the Cooperative collects concurrent with revenue-producing activities are excluded from revenue. There are no shipping and handling fees charged to customers or incurred by the Cooperative. Incidental items that are immaterial in the context of any contracts are recognized as expense.

Operating revenues consist of the following for the years ended December 31:

	<u>2021</u>	<u>2020</u>
Energy sales	\$ 5,752,746	\$ 4,894,476
Waste heat project	44,833	34,801
Pole rentals	12,936	12,936
Late payment fees	11,436	12,470
Other revenue	9,858	11,868
	<u>\$ 5,831,809</u>	<u>\$ 4,966,551</u>

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

f. Fair value of financial instruments

The fair value of current assets and current liabilities approximates carrying value because of the short-term nature of these items.

g. Materials and supplies and fuel inventory

The inventory of materials and supplies is recorded at the lower of average cost or market. Fuel inventory is recorded at the cost the fuel is purchased at during the year based on the volume on hand at year end.

h. Utility plant

Utility plant is stated substantially at original cost. Cost of utility plant includes labor, materials, payments to contractors, transportation and construction equipment use and indirect costs, such as employee benefits and general and administrative expenses, less customers' contributions. The Cooperative requires customers to pay for a majority of the costs associated with extending service to them. The Cooperative's utility plant is understated by the amount of these required customer contributions.

The Cooperative has received more than \$33 million of grant funding since being founded in 2004. The grants were primarily to fund significant long-term assets that are included in the Cooperative's utility plant accounts. The funding was received from both Federal programs and the State of Alaska. The Cooperative's utility plant is understated by the amount of the grant funds received and used for these assets. These assets include hydro projects in Haines, Hoonah, and Kake; primary line extensions in Angoon, Hoonah, and Klukwan; LED streetlights in Kake and Klukwan; and power plant buildings and generation equipment in Angoon, Hoonah and Kake. Many of these assets were completed at zero cost to the Cooperative's membership and the value of these assets at December 31, 2021 and 2020 are recorded net of the grants received. This funding has therefore provided a significant number of assets to Cooperative members at significantly lower cost to them. This in turn has reduced the depreciation expense for each year and therefore allows the Cooperative to provide power to their members at lower rates.

The cost of maintenance and repairs, including replacement of minor items of property, is charged to operating expense. The cost for replacement of depreciable property units, as distinguished from minor items, is charged to utility plant. The cost of units of property replaced or retired, including cost of removal less salvage value from the transmission or distribution plants, is charged to accumulated depreciation as prescribed by standard industry practice.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

i. Depreciation

Depreciation rates have been applied on a straight-line basis using the following annual rates which are taken from a depreciation study performed for the year ended December 31, 2017 (see note 5):

Production plant	0.72% to 9.03%
Distribution plant	1.26% to 6.06%
General plant	1.98% to 25.00%

j. Recoverability of long-lived assets

The Cooperative reviews its long-lived assets whenever events or changes in circumstances indicate the carrying amount of the assets may not be recoverable and determines whether an impairment loss should be recognized. No impairment losses have been identified in the financial statements.

k. Asset retirement obligation

Professional accounting standards require entities to record the fair value of a liability for legal obligations associated with an asset retirement in the period in which obligations are incurred. The Cooperative has determined it does not have a material legal obligation to remove long-lived assets, and accordingly has not recognized any asset retirement obligation costs in its financial statements.

l. Capitalization of interest

The Cooperative follows the policy of capitalizing interest as a component of the cost of significant property, plant and equipment constructed for its own use. In 2021, total interest incurred was \$244,353 of which \$0 was capitalized. In 2020, total interest incurred was \$212,019 of which \$53,470 was capitalized.

m. Income taxes

The Cooperative is exempt from federal income taxes under section 501(c)(12) of the Internal Revenue Code while functioning for the benefit of its members. The Cooperative had no unrelated business income. The Cooperative adopted Accounting Standards Codification (ASC) 740-10, relating to accounting for uncertain tax positions. The Cooperative does not have any uncertain tax positions. The Cooperative files an exempt organization tax return in the U.S. federal jurisdiction and is no longer subject to examination by taxing authorities before 2018.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

n. Credit risk

Financial instruments which could potentially subject the Cooperative to concentrations of credit risk consist principally of temporary cash investments and trade receivables. The Cooperative maintains its cash and cash equivalents with First National Bank Alaska.

The balances are insured by the Federal Deposit Insurance Corporation up to \$250,000. At December 31, 2021 and 2020, there were uninsured balances of \$0 and \$0, respectively. Concentrations of credit risk with respect to trade receivables are limited due to the number of customers comprising the Cooperative's customer base. However, there is a risk that adverse economic conditions in the Cooperative's service area could impact the Cooperative's ability to collect amounts due from customers.

o. Other equities

Other equities consists of the equity balances of Tlingit-Haida Regional Electrical Authority (THREA) which transferred at the formation of IPEC and the collective non-operating margins of the Cooperative since the Cooperative was founded.

p. Deferred charges and credits

Due to regulation of its rates by its Board, the Cooperative is subject to the accounting requirements of the Accounting Standards Codification (ASC) 980, *Regulated Operations*. Accordingly, certain costs and income may be capitalized as a regulatory asset or liability that would otherwise be charged to expense or revenues. Regulatory assets and liabilities are recorded when it is probable that future rates will permit recovery.

q. Regulation

Since its formation, IPEC has been subject to economic regulation by the Regulatory Commission of Alaska (RCA). In September 2018, a deregulation election was held which made IPEC no longer subject to certain regulations. The Cooperative is still required to make quarterly cost of power adjustment (COPA) filings in order to participate in the power cost equalization program which is a State subsidy to individual customers and community facilities in rural Alaska locations. Management anticipates recognizing significant cost savings as a result of being deregulated.

r. Use of estimates

In preparing financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions that affect certain reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Inside Passage Electric Cooperative, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

s. **Reclassifications**

Certain prior year balances have been reclassified to conform with the current year's presentation. The reclassifications had no effect on net margins or equity for either period.

t. **Subsequent events**

The Cooperative has evaluated subsequent events through March 2, 2022, the date the financial statements were available to be issued. Management is not aware of any material subsequent events.

NOTE 2 – ELECTRIC PLANT IN SERVICE

Electric plant in service consisted of the following at December 31:

	<u>2021</u>	<u>2020</u>
Production	\$ 8,338,560	\$ 8,283,459
Distribution	14,064,185	13,873,381
General plant	<u>3,024,724</u>	<u>2,685,773</u>
	<u>\$ 25,427,469</u>	<u>\$ 24,842,613</u>

NOTE 3 – ACCOUNTS, GRANT, AND OTHER RECEIVABLES

Accounts receivable consisted of the following at December 31:

	<u>2021</u>	<u>2020</u>
Consumer accounts	\$ 355,983	\$ 289,632
Power cost equalization (PCE)	<u>136,363</u>	<u>107,498</u>
Total accounts receivable	492,346	397,130
Allowance for doubtful accounts	<u>(35,587)</u>	<u>(24,256)</u>
	<u>\$ 456,759</u>	<u>\$ 372,874</u>

Other receivables consisted of the following at December 31:

	<u>2021</u>	<u>2020</u>
Outside non-electric receivables	\$ 669,214	\$ 2,599
NRECA receivable	-	5,969
Interest receivable on CFC investments	<u>1,179</u>	<u>1,179</u>
	<u>\$ 670,393</u>	<u>\$ 9,747</u>

Inside Passage Electric Cooperative, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 3 – ACCOUNTS, GRANT, AND OTHER RECEIVABLES - Continued

Outside non-electric receivables at December 31, 2021 included \$521,526 receivable from the Alaska Department of Transportation related to a project to relocate a portion of the highway in Haines. The amount was collected on January 6, 2022. Also included in the outside non-electric receivables was an insurance claim of \$138,147 submitted to ARECA Insurance Exchange and collected on January 13, 2022. The claim is the result of a failed penstock at a hydroelectric dam. The remaining outside non-electric receivables at December 31, 2021 total \$9,541.

The grant receivable at December 31, 2021 is the result of a \$461,474 grant obtained from the Alaska Energy Authority (AEA) during 2021. The grant project is to design a hydroelectric dam at Water Supply Creek near Hoonah. The receivable is related to the initial submission of expenses under the grant agreement. The Cooperative anticipates it will have a cost of \$75,000 on this project that will not be reimbursed by AEA.

NOTE 4 – INVESTMENTS IN ASSOCIATED ORGANIZATIONS

Investments in associated organizations consisted of the following as of December 31:

	<u>2021</u>	<u>2020</u>
Alaska Rural Electric Cooperative Association (ARECA) Insurance Exchange patronage capital credits	\$ 1,488,964	\$ 1,450,406
National Rural Utilities Cooperative Finance Corporation (CFC):		
Membership	1,000	1,000
Capital term certificates, interest bearing, 3 to 5 percent	93,543	93,543
Patronage capital certificates	33,340	29,404
National Information Solutions Cooperative (NISC) patronage capital	19,109	17,615
	<u>\$ 1,635,956</u>	<u>\$ 1,591,968</u>

Inside Passage Electric Cooperative, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 5 – DEFERRED CHARGES

Deferred charges consisted of costs relating to a depreciation study for the year ended December 31, 2017. The study was completed in October 2018 and was approved by the Rural Utility Service (RUS) in April 2019. The Cooperative began amortizing the cost of the study during 2019 and it is being amortized over a four-year period. Total amortization expense for the years ended December 31, 2021 and 2020 was \$13,693 and \$22,348, respectively.

NOTE 6 – LONG-TERM DEBT

Long-term debt consisted of the following at December 31:

	2021	2020
Mortgages payable to the United States of America (Rural Utilities Service), payable in monthly installments of \$23,416, including interest at either 2% or 5%, maturing between May 2028 and July 2029	\$ 2,063,192	\$ 2,341,817
Mortgages payable to the National Rural Utilities Cooperative Finance Corporation (CFC), payable in quarterly installments of \$90,077, including interest between 3.46% and 4.65%, maturing between December 2045 and June 2048	<u>5,924,231</u>	<u>2,805,595</u>
	<u>7,987,423</u>	<u>5,147,412</u>
Less current maturities	<u>(427,204)</u>	<u>(341,682)</u>
	<u>\$ 7,560,219</u>	<u>\$ 4,805,730</u>

The aggregate long-term debt maturing over the next five years is approximately as follows: 2022 - \$427,204; 2023 - \$440,987; 2024 - \$455,285; 2025 - \$470,119; 2026 - \$485,511; and succeeding years of \$5,708,317. The mortgage notes are subject to various covenants and requirements detailed in the loan documents. All assets of the Cooperative are pledged as collateral on these notes. In August 2021, the Cooperative obtained a \$3,200,000 loan from CFC and used \$1,500,000 to repay the outstanding line of credit (note 7) and deposited the remaining \$1,700,000.

Inside Passage Electric Cooperative, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 7 – LINE OF CREDIT

The Cooperative has a \$3,000,000 perpetual line of credit with National Rural Utilities Cooperative Finance Corporation (CFC). Provisions on the line of credit require repayment in full within 360 days of the advance. Interest is accrued and payable quarterly. The interest rate is determined and set by CFC each month and was 2.25% at December 31, 2021. At December 31, 2021 and 2020, the outstanding balance due on the line of credit was \$0 and \$1,000,000, respectively. Proceeds on the line of credit were used to fund work on the Gunnuk Creek hydroelectric dam project in Kake (see note 11). Accordingly, interest on the line of credit was capitalized to that project through October 2020 when the project was completed. The Cooperative borrowed an additional \$500,000 during 2021 and repaid the balance of \$1,500,000 in August 2021 using proceeds from a new loan with CFC. See note 6.

NOTE 8 – DEFERRED CREDITS

Deferred credits consisted of the following at December 31:

	<u>2021</u>	<u>2020</u>
Cost of power adjustment	\$ 118,907	\$ 82,008
Special equipment costs	33,600	26,050
Customer advances for construction	<u>15,582</u>	<u>11,408</u>
	<u>\$ 168,089</u>	<u>\$ 119,466</u>

NOTE 9 – COMMITMENTS AND CONTINGENCIES

The Cooperative is party to various claims, for and against its interest, which are either covered by insurance or which management believes will not have a material effect to its financial position. See note 3 for details of a significant insurance claim made during 2021. There are no pending or threatened claims against the Cooperative as of December 31, 2021.

On July 19, 2021 the Cooperative, along with other utilities and organizations in the State of Alaska, filed a lawsuit against Governor Mike Dunleavy's administration over the Power Cost Equalization (PCE) fund. On August 11, 2021 a Superior Court judge ruled in favor of the Cooperative and other organizations and directed the state to keep funding for the PCE program.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 10 – EMPLOYEE BENEFIT PLANS

Retirement Security 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 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.

The Cooperative's contributions to the RS Plan in 2021 and in 2020 represented less than 5 percent of the total contributions made to the plan by all participating employers. The Cooperative made contributions to the plan of \$384,373 in 2021 and \$316,333 in 2020. There have been no significant changes that affect the comparability of 2021 and 2020 contributions.

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 Retirement Security Plan was over 80 percent funded on January 1, 2021 and over 80 percent funded at January 1, 2020 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.

401(k) Plan

The Cooperative also participates in a 401(k) plan that is available to all employees. Employees may contribute to the plan on a payroll deduction basis. The Cooperative matches 100% of the first 3% of employee contributions and up to an additional 50% of the next 2% of employee contributions. Contributions made during 2021 and 2020 were \$33,293 and \$31,372, respectively.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2021 and 2020

NOTE 11 – GUNNUK CREEK HYDROELECTRIC DAM PROJECT

During 2018 the Cooperative was awarded a \$3,920,000 grant by the Alaska Energy Authority (AEA) from the Alaska Renewable Energy Fund. An additional \$3,000,000 was awarded by the Rural Utility Service (RUS) under its High Energy Costs Grant program. These funds were used to construct a 500kW Run of River hydro project on Gunnuk Creek in Kake which is expected to produce approximately 50-55% of Kake's annual energy needs. Start up and commissioning of the project took place in October 2020.

Through December 31, 2020 the Cooperative had received all grant funding related to this project. The Cooperative has invested over \$2,900,000 of its own funds into the project through December 31, 2020. These funds were obtained by using the CFC line of credit and on August 16, 2019 the Cooperative converted \$1,000,000 of the line of credit into a long-term loan with interest at 3.76% and maturing on June 30, 2046. This conversion is recorded as a non-cash transaction on the statement of cash flows. See notes 6 and 7. The project was capitalized as part of production plant in October 2020 at a final cost of \$2,904,976 and had been recorded in construction work in progress at \$1,383,498 as of December 31, 2019. These balances reflect project costs being reduced by total grant funding of \$7,000,000.

NOTE 12 – NOVEL CORONAVIRUS OUTBREAK

On March 13, 2020, President Trump declared a national emergency over the novel coronavirus or COVID-19. Alaska Governor Mike Dunleavy issued a public health disaster emergency declaration on March 11, 2020 and has taken a number of steps to restrict social contact since that time. Many other state and local governments have imposed other restrictions. At this point, the Cooperative has maintained its normal hours of operation and at times certain staff have been asked to work remotely or on a rotating basis. It is unclear at this time how the outbreak will impact the operations of the Cooperative going forward as the length and severity of the situation remains unknown.

RUS AND GOVERNMENT AUDITING STANDARDS REPORTS

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH ASPECTS OF CONTRACTUAL AGREEMENTS AND REGULATORY REQUIREMENTS FOR ELECTRIC BORROWERS

Board of Directors
Inside Passage Electric Cooperative, Inc.
Auke Bay, Alaska

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 Inside Passage Electric Cooperative, Inc. (the Cooperative), which comprise the balance sheets as of December 31, 2021 and 2020, and the related statements of revenue and margins, changes in equities and margins, and cash flows for the years then ended, and the related notes to the financial statements, and have issued our report thereon dated March 2, 2022. In accordance with *Government Auditing Standards*, we have also issued our report dated March 2, 2022, on our consideration of the effectiveness of the Cooperative's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. No reports other than the reports referred to above and our certification of CFC loan proceeds and our schedule of findings and recommendations and related to our audit have been furnished to management.

In connection with our audit, nothing came to our attention that caused us to believe that the Cooperative failed to comply with the terms, covenants, provisions, or conditions of their loan, grant, and security instruments as set forth in 7 CFR Part 1773, *Policy on Audits of Rural Utilities Service Borrowers*, §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 relate to accounting matters. In connection with our audit, we noted no matters regarding the Cooperative's accounting and records to indicate that the Cooperative did not:

- Maintain adequate and effective accounting procedures;
- Utilize adequate and fair methods 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;
- Maintain adequate control over materials and supplies;
- Prepare accurate and timely financial and operating reports;
- Obtain written RUS approval to enter into any contract for the management, operation, or maintenance of the borrower's system if the contract covers all or substantially all of the electric system;
- Disclose material related party transactions in the financial statements, in accordance with requirements for related parties in generally accepted accounting principles;
- Record depreciation in accordance with RUS requirements (See RUS Bulletin 183-1, Depreciation Rates and Procedures);
- Comply with the requirements for the detailed schedule of deferred debits and deferred credits; and
- Comply with the requirements for the detailed schedule of investments.

This report is solely to communicate, in connection with the audit of the financial statements, on compliance with aspects of contractual agreements and the regulatory requirements for electric borrowers based on the requirements of 7 CFR Part 1773, *Policy on Audits of Rural Utilities Service Borrowers and Grantees*. Accordingly, this report is not suitable for any other purpose.

Blodgett, Mickelson & Adamson, P.S.

Kennewick, Washington

March 2, 2022

BLODGETT, MICKELSEN & ADAMSON, P.S.

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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**

Board of Directors
Inside Passage Electric Cooperative, Inc.
Auke Bay, Alaska

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Inside Passage Electric Cooperative, Inc. (a nonprofit organization) (the Cooperative), which comprise the balance sheet as of December 31, 2021, and the related statements of revenues and margins, changes in equities and margins, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 2, 2022.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Inside Passage Electric Cooperative, Inc.'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 a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the Cooperative'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 preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Inside Passage Electric Cooperative, Inc.'s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants 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 audit, 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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Cooperative's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Cooperative's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Blodgett, Mickelsen & Adamson, P.S.

Kennewick, Washington

March 2, 2022

BLODGETT, MICKELSEN & ADAMSON, P.S.

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INDEPENDENT AUDITOR'S CERTIFICATION OF CFC LOAN PROCEEDS

Board of Directors
Inside Passage Electric Cooperative, Inc.
Auke Bay, Alaska

We have audited, in accordance with U.S. generally accepted auditing standards and *Government Auditing Standards*, the balance sheet of Inside Passage Electric Cooperative, Inc. as of December 31, 2021 and the related statements of revenues and margins, changes in equities and margins, and cash flows for the year then ended, and have issued our report thereon dated March 2, 2022.

In conducting our audit, nothing came to our attention that caused us to believe that the Cooperative was not in compliance with the provisions of the Loan Agreement with National Rural Utilities Cooperative Finance Corporation (CFC) insofar as it relates to accounting matters. During the year ended December 31, 2021, the Cooperative received \$3,200,000 in long-term loan fund advances and \$500,000 of draws on the line of credit from CFC loans and line of credit controlled by the Loan and Line of Credit Agreements. The long-term loan fund advances and draws on the line of credit in the year ended December 31, 2021 were used for purposes contemplated in the agreement for such proceeds. \$1,500,000 of the long-term loan fund advances were used to repay the line of credit balance during the year.

It should be noted, however, that our audit was not directed primarily toward obtaining knowledge of such noncompliance.

This report is intended solely for the information and use of the Board of Trustees, management and CFC and is not intended to be and should not be used by anyone other than these specified parties.

Blodgett, Mickelsen & Adamson, P.S.

Kennewick, Washington
March 2, 2022