

FINANCIAL STATEMENTS
AND
INDEPENDENT AUDITOR'S REPORT



December 31, 2022 and 2021

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

CONTENTS

	PAGE
INDEPENDENT AUDITOR'S REPORT	1-2
FINANCIAL STATEMENTS	
BALANCE SHEETS	3-4
STATEMENTS OF REVENUES AND MARGINS	5
STATEMENTS OF CHANGES IN EQUITIES AND MARGINS	6
STATEMENTS OF CASH FLOWS	7-8
NOTES TO FINANCIAL STATEMENTS	9-19
RUS AND GOVERNMENT AUDITING STANDARDS REPORTS	20-24
INDEPENDENT AUDITOR'S CERTIFICATION OF CFC LOAN PROCEEDS	25

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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, 2022 and 2021, 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, 2022 and 2021, 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 are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users made on the basis of these 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 February 22, 2023, 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
February 22, 2023

Inside Passage Electric Cooperative, Inc.

BALANCE SHEETS

December 31, 2022 and 2021

ASSETS

	<u>2022</u>	<u>2021</u>
UTILITY PLANT - AT COST (notes 1, 2 and 11)		
Electric plant in service - at cost	\$ 25,151,406	\$ 25,427,469
Construction work in progress	1,079,346	29,025
	<u>26,230,752</u>	25,456,494
Less accumulated depreciation and amortization	14,322,946	14,217,840
Net electric plant	<u>11,907,806</u>	11,238,654
INVESTMENTS IN ASSOCIATED ORGANIZATIONS AND RESTRICTED CASH (notes 1 and 4)		
Investments in associated organizations	1,559,511	1,635,956
Restricted cash:		
Consumer deposits	83,579	73,633
State of Alaska performance guarantees	13,600	13,600
	<u>1,656,690</u>	1,723,189
CURRENT ASSETS (notes 1, 3 and 11)		
Cash and cash equivalents	856,245	1,844,501
Accounts receivable, less provision for doubtful accounts of \$35,461 in 2022 and \$35,587 in 2021	517,149	456,759
Grants receivable	94,734	41,399
Other receivables	469,259	670,393
Unbilled revenue	342,543	299,168
Materials and supplies	330,209	252,583
Fuel inventory	301,393	297,646
Prepaid expenses	70,697	85,486
Total current assets	<u>2,982,229</u>	3,947,935
DEFERRED CHARGES (notes 1 and 5)	<u>-</u>	13,693
	<u><u>\$ 16,546,725</u></u>	<u><u>\$ 16,923,471</u></u>

The accompanying notes are an integral part of these statements.

EQUITIES, MARGINS AND LIABILITIES

	<u>2022</u>	<u>2021</u>
EQUITIES AND MARGINS (note 1)		
Patronage capital	\$ 2,029,318	\$ 1,770,479
Other equities	<u>5,928,008</u>	<u>5,932,141</u>
	7,957,326	7,702,620
LONG-TERM DEBT, less current maturities (note 6)	7,119,065	7,560,219
COMMITMENTS AND CONTINGENCIES (notes 7 and 9)	-	-
CURRENT LIABILITIES (notes 1, 3, and 6)		
Accounts payable	719,619	880,773
Consumer deposits	83,579	73,633
Accrued payroll and related liabilities	100,591	103,279
Accrued taxes	7,979	7,654
Current maturities of long-term debt	<u>440,993</u>	<u>427,204</u>
Total current liabilities	1,352,761	1,492,543
DEFERRED CREDITS (notes 1 and 8)	<u>117,573</u>	<u>168,089</u>
	<u>\$ 16,546,725</u>	<u>\$ 16,923,471</u>

Inside Passage Electric Cooperative, Inc.

STATEMENTS OF REVENUES AND MARGINS

Years ended December 31, 2022 and 2021

	<u>2022</u>	<u>2021</u>
Operating revenues (note 1)	\$ 6,753,943	\$ 5,831,809
Operating expenses (notes 10 and 11)		
Purchased power	215,882	307,223
Power production - operation	3,432,841	2,406,208
Power production - maintenance	380,171	400,327
Distribution - operation	200,815	198,793
Distribution - maintenance	97,698	122,815
Consumer accounts	197,860	200,773
Consumer service and information	40,355	21,490
Sales expense	31,681	29,202
Administrative and general	1,070,473	1,077,118
Depreciation and amortization	540,931	580,467
Taxes	5,245	5,331
Total operating expenses	<u>6,213,952</u>	<u>5,349,747</u>
Net operating margins before fixed charges	539,991	482,062
Fixed charges		
Interest on long-term debt	278,449	244,353
Donations to member communities	2,703	900
	<u>281,152</u>	<u>245,253</u>
Net operating margin	258,839	236,809
Non-operating (losses) margins		
Patronage (losses) capital allocated	(55,395)	100,624
Interest income	11,363	867
Other non-operating income	39,899	1,630
	<u>(4,133)</u>	<u>103,121</u>
NET MARGINS	<u>\$ 254,706</u>	<u>\$ 339,930</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, 2022 and 2021

	<u>Patronage Capital</u>	<u>Other Equities</u>		
	<u>Inside Passage Operating Margins</u>	<u>Inside Passage Non-Operating Margins (losses)</u>	<u>THREA Donated Capital</u>	<u>Total</u>
Balance at December 31, 2020	\$ 1,533,670	\$ 1,942,843	\$ 3,886,177	\$ 7,362,690
Net margins	<u>236,809</u>	<u>103,121</u>	<u>-</u>	<u>339,930</u>
Balance at December 31, 2021	<u>\$ 1,770,479</u>	<u>\$ 2,045,964</u>	<u>\$ 3,886,177</u>	<u>\$ 7,702,620</u>
Net margins (losses)	<u>258,839</u>	<u>(4,133)</u>	<u>-</u>	<u>254,706</u>
Balance at December 31, 2022	<u><u>\$ 2,029,318</u></u>	<u><u>\$ 2,041,831</u></u>	<u><u>\$ 3,886,177</u></u>	<u><u>\$ 7,957,326</u></u>

The accompanying notes are an integral part of these statements.

Inside Passage Electric Cooperative, Inc.

STATEMENTS OF CASH FLOWS

Years ended December 31, 2022 and 2021

	<u>2022</u>	<u>2021</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net margins	\$ 254,706	\$ 339,930
Adjustments to reconcile net margins to net cash provided by operating activities:		
Depreciation and amortization	540,931	580,467
Net operating changes in:		
Accounts receivable	(60,390)	(83,885)
Other receivables	279,146	(660,646)
Unbilled revenue	(43,375)	(62,228)
Materials and supplies	(77,626)	5,047
Fuel inventory	(3,747)	(97,796)
Prepaid expenses	14,789	(51,876)
Accounts payable	(161,154)	558,806
Consumer deposits	9,946	(4,559)
Accrued payroll and related liabilities	(2,363)	11,985
Deferred credits	(50,516)	48,623
	<u>700,347</u>	<u>583,868</u>
NET CASH PROVIDED BY OPERATING ACTIVITIES		
CASH FLOWS FROM INVESTING ACTIVITIES		
Net additions to utility plant	(905,605)	(648,961)
Book value of property dispositions and plant removal - net of retirements	(422,132)	(5,337)
Net decrease (increase) in investments in associated organizations	76,445	(43,988)
	<u>(1,251,292)</u>	<u>(698,286)</u>
NET CASH USED IN INVESTING ACTIVITIES		

The accompanying notes are an integral part of these statements.

	<u>2022</u>	<u>2021</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on long-term debt	\$ (427,365)	\$ (359,989)
Proceeds from borrowings of long-term debt	-	3,200,000
Payments on line of credit	-	(1,500,000)
Proceeds from borrowings on line of credit	-	500,000
	<u> </u>	<u> </u>
NET CASH (USED IN) PROVIDED BY FINANCING ACTIVITIES	<u>(427,365)</u>	<u>1,840,011</u>
Net (decrease) increase in cash	(978,310)	1,725,593
Cash and cash equivalents at beginning of year	<u>1,931,734</u>	<u>206,141</u>
Cash and cash equivalents at end of year	<u><u>\$ 953,424</u></u>	<u><u>\$ 1,931,734</u></u>

Cash paid for interest during the years December 31, 2022 and 2021 amounted to \$278,449 and \$244,353, respectively.

Reconciliation of Cash and Cash Equivalents to Balance Sheet:

Cash and cash equivalents	\$ 856,245	\$ 1,844,501
Restricted cash:		
Consumer deposits	83,579	73,633
State of Alaska performance guarantees	13,600	13,600
	<u>97,179</u>	<u>87,233</u>
	<u><u>\$ 953,424</u></u>	<u><u>\$ 1,931,734</u></u>

NOTES TO FINANCIAL STATEMENTS

December 31, 2022 and 2021

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 receivables 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, 2022 and 2021

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

d. Grants receivable

Grants receivable represents the amount due to the Cooperative for reimbursable expenses from the Alaska Energy Authority (AEA) for two grants related to hydroelectric dam projects. 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>2022</u>	<u>2021</u>
Energy sales	\$ 6,642,568	\$ 5,752,746
Waste heat project	76,353	44,833
Pole rentals	12,936	12,936
Late payment fees	11,308	11,436
Other revenue	10,778	9,858
	<u>\$ 6,753,943</u>	<u>\$ 5,831,809</u>

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2022 and 2021

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, 2022 and 2021 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, 2022 and 2021

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. No interest was capitalized for the years ended December 31, 2022 and 2021.

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 exempt organization tax returns in the U.S. federal jurisdiction. The tax returns remain open for possible examination for a period of three years after the date on which those returns are filed.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2022 and 2021

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, 2022 and 2021, 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, 2022 and 2021

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 February 22, 2023, 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>2022</u>	<u>2021</u>
Production	\$ 8,413,230	\$ 8,338,560
Distribution	13,650,136	14,064,185
General plant	<u>3,088,040</u>	<u>3,024,724</u>
	<u>\$ 25,151,406</u>	<u>\$ 25,427,469</u>

Construction work in progress at December 31, 2022 includes \$1,015,781 for a system-wide meter upgrade that is expected to be completed in 2023.

NOTE 3 - ACCOUNTS, GRANTS, AND OTHER RECEIVABLES

Accounts receivable consisted of the following at December 31:

	<u>2022</u>	<u>2021</u>
Consumer accounts	\$ 371,013	\$ 355,983
Power cost equalization (PCE)	<u>181,597</u>	<u>136,363</u>
Total accounts receivable	552,610	492,346
Allowance for doubtful accounts	<u>(35,461)</u>	<u>(35,587)</u>
	<u>\$ 517,149</u>	<u>\$ 456,759</u>

Inside Passage Electric Cooperative, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2022 and 2021

NOTE 3 - ACCOUNTS, GRANTS, AND OTHER RECEIVABLES - Continued

Other receivables consisted of the following at December 31:

	<u>2022</u>	<u>2021</u>
Outside non-electric receivables	\$ 468,080	\$ 669,214
Interest receivable on CFC investments	1,179	1,179
	<u>\$ 469,259</u>	<u>\$ 670,393</u>

Outside non-electric receivables at December 31, 2022 and 2021 included receivables of \$443,514 and \$521,526, respectively, from the Alaska Department of Transportation related to a project to relocate a portion of the highway in Haines. Similar amounts are also included in accounts payable for the respective periods. Also included in outside non-electric receivables at December 31, 2021 was an insurance claim of \$138,147 submitted to ARECA Insurance Exchange from a failed penstock at a hydroelectric dam. The remaining outside non-electric receivables at December 31, 2022 and 2021 totaled \$24,566 and \$9,541, respectively.

The grants receivable at December 31, 2022 are the result of grants of \$461,474 and \$62,368 obtained from the Alaska Energy Authority (AEA). The grant projects are to design a hydroelectric dam at Water Supply Creek near Hoonah and to perform a reconnaissance study for a hydroelectric dam proposed at Jenny Creek near Kake. The receivables relate to submission of expenses under the grant agreements. The Cooperative anticipates it will have a cost of \$85,000 on these projects 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>2022</u>	<u>2021</u>
Alaska Rural Electric Cooperative Association (ARECA) Insurance Exchange patronage capital credits	\$ 1,405,142	\$ 1,488,964
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	40,971	33,340
National Information Solutions Cooperative (NISC) patronage capital	<u>18,855</u>	<u>19,109</u>
	<u>\$ 1,559,511</u>	<u>\$ 1,635,956</u>

Inside Passage Electric Cooperative, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2022 and 2021

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, 2022 and 2021 was \$13,693 and \$13,693, respectively.

NOTE 6 - LONG-TERM DEBT

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

	<u>2022</u>	<u>2021</u>
Mortgages payable to the United States of America (Rural Utilities Service), payable in monthly installments of \$28,783, including interest at either 2% or 5%, maturing between May 2028 and July 2029	\$ 1,776,436	\$ 2,063,192
Mortgages payable to the National Rural Utilities Cooperative Finance Corporation (CFC), payable in quarterly installments of \$90,120, including interest between 3.46% and 4.65%, maturing between December 2045 and June 2048	<u>5,783,622</u>	<u>5,924,231</u>
	<u>7,560,058</u>	<u>7,987,423</u>
Less current maturities	<u>(440,993)</u>	<u>(427,204)</u>
	<u><u>\$ 7,119,065</u></u>	<u><u>\$ 7,560,219</u></u>

The aggregate long-term debt maturing over the next five years is approximately as follows: 2023 - \$440,993; 2024 - \$455,292; 2025 - \$470,126; 2026 - \$485,518; 2027 - \$501,492; and succeeding years of \$5,206,637. 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. Approximately \$1,000,000 of these funds have been utilized on a system-wide meter upgrade during 2022 (note 2).

Inside Passage Electric Cooperative, Inc.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2022 and 2021

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 5.55% at December 31, 2022. At December 31, 2022 and 2021, the outstanding balance due on the line of credit was \$0 and \$0, respectively.

NOTE 8 - DEFERRED CREDITS

Deferred credits consisted of the following at December 31:

	<u>2022</u>	<u>2021</u>
Cost of power adjustment	\$ 103,571	\$ 118,907
Customer advances for construction	14,002	15,582
Special equipment costs (note 11)	<u>-</u>	<u>33,600</u>
	<u>\$ 117,573</u>	<u>\$ 168,089</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, 2022.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2022 and 2021

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 2022 and in 2021 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 \$410,420 in 2022 and \$384,373 in 2021. There have been no significant changes that affect the comparability of 2022 and 2021 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, 2022 and over 80 percent funded at January 1, 2021 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 2022 and 2021 were \$34,826 and \$33,293, respectively.

NOTES TO FINANCIAL STATEMENTS - CONTINUED

December 31, 2022 and 2021

NOTE 11 - CHANGE IN SPECIAL EQUIPMENT ACCOUNTING

The Cooperative has historically followed Rural Utility Services (RUS) guidance with regards to special equipment accounting. Special equipment are materials such as meters, transformers, switches, or similar that are continually being moved from one location to another. These types of materials are capitalized, including estimated installation costs, as part of utility plant in service when they are purchased.

Due to issues caused by following the RUS guidance for special equipment accounting, the Cooperative is electing to change its accounting for special equipment from special equipment accounting (as prescribed by 7 CFR Part 1767) to inventory accounting (as outlined in an RUS memorandum dated November 14, 2000). During the year ended December 31, 2022, the cost of special equipment, primarily including transformers, still in inventory (that is, not in service as part of the utility system) that had already been capitalized with installation costs were transferred to materials and supplies. The associated installation costs (capitalized labor) of these items were charged to operating expense. Going forward, any such items purchased will be included in materials and supplies and then classified as utility plant in service once the item is installed. The cost of assets transferred from utility plant in service to materials and supplies was \$33,513 and the cost of capitalized labor charged to operating expense was \$19,900.

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, 2022 and 2021, 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 February 22, 2023. In accordance with *Government Auditing Standards*, we have also issued our report dated February 22, 2023, 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 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 and Grantees*, §1773.33, 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, Mickelsen & Adamson, P.S.

Kennewick, Washington
February 22, 2023

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, 2022, 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 February 22, 2023.

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

February 22, 2023

BLODGETT, MICKELSEN & ADAMSON, P.S.

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INDEPENDENT AUDITOR'S CERTIFICATION OF CFC LOAN PROCEEDS
YEAR ENDED DECEMBER 31, 2022

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, 2022 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 February 22, 2023.

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, 2022, the Cooperative received \$0 in long-term loan fund advances and \$0 of draws on the line of credit from CFC loans and line of credit controlled by the Loan and Line of Credit Agreements.

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
February 22, 2023