Note: There are a few redactions in the audit. All the redactions involve security concerns at federal facilities with which VEA has contracts. The redactions are done at the direction of the U.S. Department of Defense.

VALLEY ELECTRIC ASSOCIATION, INC. AND SUBSIDIARY

PAHRUMP, NEVADA

CONSOLIDATED FINANCIAL STATEMENTS WITH CONSOLIDATING AND ACCOMPANYING INFORMATION

FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS
LUBBOCK, TEXAS

VALLEY ELECTRIC ASSOCIATION, INC. AND SUBSIDIARY

PAHRUMP, NEVADA

CONSOLIDATED FINANCIAL STATEMENTS WITH CONSOLIDATING AND ACCOMPANYING INFORMATION

FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

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REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

VALLEY ELECTRIC ASSOCIATION, INC. AND SUBSIDIARY
PAHRUMP, NEVADA

CONSOLIDATED FINANCIAL STATEMENTS WITH CONSOLIDATING AND ACCOMPANYING INFORMATION
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

TABLE OF CONTENTS

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS
PHONE: (806) 747-3806
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8215 NASHVILLE AVENUE
LUBBOCK, TEXAS 79423-1954

Independent Auditor's Report

Board of Directors
Valley Electric Association, Inc. and Subsidiary
Pahrump, Nevada

We have audited the accompanying consolidated financial statements of Valley Electric Association, Inc. and Subsidiary, which comprise the consolidated balance sheets as of December 31, 2017 and 2016, and the related consolidated statements of income, comprehensive income and patronage capital and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Valley Electric Association, Inc. and Subsidiary as of December 31, 2017 and 2016, and the results of their consolidated operations and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Consolidating and Accompanying Information

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information and schedules of electric plant and other property and equipment, accumulated provision for depreciation, other property and investments, patronage capital, mortgage notes, and five year comparative data are presented for purposes of additional analysis and are not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

Lubbock, Texas

April 9, 2018

CONSOLIDATED FINANCIAL STATEMENTS

VALLEY ELECTRIC ASSOCIATION, INC. AND SUBSIDIARY

Exhibit A

CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2017 AND 2016

ASSETS

	December 31, 2017	December 31, 2016
UTILITY PLANT AT COST		
Electric Plant in Service	$ 275,981,667	$ 258,284,063
Construction Work in Progress	5,961,166	15,462,866
Electric Plant Acquisi ion Adjustment	2,211,617	2,264,656
	$ 284,154,450	$ 276,011,585
Less: Accumulated Provision for Depreciation	69,700,085	65,475,963
	$ 214,454,365	$ 210,535,622
OTHER PROPERTY AND EQUIPMENT		
Nonutility Plant and Equipment - In Service	$ 26,503,557	$ 9,762,134
Construction Work in Progress	15,588,717	12,202,275
	$ 42,092,274	$ 21,964,409
Less: Accumulated Provision for Depreciation	4,246,160	669,897
	$ 37,846,114	$ 21,294,512
OTHER PROPERTY AND INVESTMENTS - AT COST OR STATED VALUE		
Assets Held for Sale	$	$ 82,564,063
Investments in Associated Organizations	6,428,841	5,834,225
Notes Receivable - Long-Term Portion	1,599,138	1,985,612
Other Special Funds	30,012,493	
	$ 38,040,472	$ 90,383,900
CURRENT ASSETS		
Cash and Temporary Cash Investments	$ 64,056,919	$ 1,594,381
Special Deposits	4,072,286	3,023,310
Accounts and Notes Receivable (Less allowance for uncollectibles of $579,297 in 2017 and $274,610 in 2016)	3,931,611	5,285,325
Accrued Unbilled Revenue	2,635,604	2,805,770
Notes Receivable - Current Portion	219,250	244,292
Materials and Supplies	4,132,622	3,491,894
Other Current and Accrued Assets	1,083,082	1,155,764
	$ 80,131,374	$ 17,600,736
DEFERRED DEBITS	$ 30,424,661	$ 31,806,579
TOTAL ASSETS	$ 400,896,986	$ 371,621,349

EQUITIES AND LIABILITIES

	2017	2016
EQUITIES		
Memberships	$ 180,800	$ 178,290
Patronage Capital	99,230,828	55,078,008
Accumulated Other Comprehensive Loss	(1,685,200)	(2,044,100)
Other Equities (Deficits)	(1,107,385)	(9,423,749)
	$ 96,619,043	$ 43,788,449
LONG-TERM DEBT		
CFC Mortgage Notes	$ 160,269,661	$ 234,316,779
CFC Line of Credit - To Be Refinanced With Long-Term Debt	10,500,000	6,250,000
CoBank Mortgage Notes	38,124,083	38,918,078
Capital Leases	9,871,430	5,608,595
Long-Term Debt - [redacted]	17,020,152	16,524,737
	$ 235,785,326	$ 301,618,189
ACCUMULATED PROVISION FOR PENSIONS AND BENEFITS		
Post-Retirement Benefits	$ 2,365,307	$ 2,595,000
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	$ 10,647,820	$ 10,243,698
Current Portion of APBO	278,100	340,300
CoBank Line of Credit	8,500,000	
Accounts Payable	1,835,431	2,428,115
Accounts Payable - Purchased Power	5,722,059	4,344,456
Consumers' Deposits	752,887	643,813
Accrued Compensated Absences	1,836,657	1,684,928
Other Current and Accrued Liabilities	3,175,840	1,014,231
	$ 32,748,794	$ 20,699,541
DEFERRED CREDITS	$ 33,378,516	$ 2,920,170
TOTAL EQUITIES AND LIABILITIES	$ 400,896,986	$ 371,621,349

See accompanying notes to consolidated financial statements.

VALLEY ELECTRIC ASSOCIATION, INC. AND SUBSIDIARY

Exhibit B

CONSOLIDATED STATEMENTS OF INCOME, COMPREHENSIVE INCOME AND PATRONAGE CAPITAL
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	Years Ended December 31,				
	2017		2016		Increase
	Amount	%	Amount	%	(Decrease)
OPERATING REVENUES					
Residential	$ 33,985,908	44.7	$ 35,028,923	46.0	$ (1,043,015)
Irriga ion	3,220,637	4 2	3,343,623	4.4	(122,986)
Commercial and Industrial	21,441,661	28.2	21,709,589	28.5	(267,928)
Public Street and Highway Lighting	40,567	0.1	42,368	0.1	(1,801)
Other Operating Revenues	17,365,969	22.8	16,019,780	21.0	1,346,189
Total Opera ing Revenues	$ 76,054,742	100.0	$ 76,144,283	100.0	$ (89,541)
OPERATING EXPENSES					
Cost of Purchased Power	$ 21,856,144	28.7	$ 22,422,801	29.4	$ (566,657)
Transmission Expense	9,168,478	12.1	9,221,041	12.1	(52,563)
Distribution - Operation	10,047,988	13.2	6,373,184	8.4	3,674,804
Distribution - Maintenance	3,275,140	4.3	2,827,811	3.7	447,329
Consumer Accounts Expense	3,176,180	4.2	2,487,255	3.3	688,925
Customer Service and Information	685,676	0.9	477,456	0.6	208,220
Sales Expense	1,842,016	2.4	1,720,711	2.3	121,305
Administrative and General	12,340,879	16.2	9,410,879	12.4	2,930,000
Depreciation and Amortization	10,855,190	14.3	9,038,233	11.9	1,816,957
Other Interest	4,040	0 0	2,650	0.0	1,390
Other Deductions	216,607	0.3	335,111	0.4	(118,504)
Total Opera ing Expenses	$ 73,468,338	96.6	$ 64,317,132	84.5	$ 9,151,206
OPERATING MARGINS - BEFORE FIXED CHARGES	$ 2,586,404	3.4	$ 11,827,151	15.5	$ (9,240,747)
FIXED CHARGES					
Interest on Long-Term Debt	12,748,053	16.8	12,211,650	16.0	536,403
OPERATING MARGINS (LOSS) - AFTER FIXED CHARGES	$ (10,161,649)	(13.4)	$ (384,499)	(0.5)	$ (9,777,150)
Capital Credits	1,284,726	1.7	1,094,923	1.4	189,803
NET OPERATING MARGINS	$ (8,876,923)	(11.7)	$ 710,424	0.9	$ (9,587,347)
NONOPERATING MARGINS (LOSSES)					
Interest Income	$ 321,287	0.4	$ 26,460	0.0	$ 294,827
Dona ions	(50,000)	(0.1)		0.0	(50,000)
Other Income (Losses)	69,088,523	90.8	(92,388)	(0.1)	69,180,911
	$ 69,359,810	91.1	$ (65,928)	(0.1)	$ 69,425,738
NET MARGINS	$ 60,482,887	79.4	$ 644,496	0.8	$ 59,838,391
OTHER COMPREHENSIVE INCOME (LOSS)					
Post-Retirement Benefits					
Actuarial Gain (Loss)	$ 270,600		$ (175,100)		
Amortization of Loss	88,300		133,900		
	$ 358,900		$ (41,200)		
COMPREHENSIVE INCOME	$ 60,841,787		$ 603,296		
Adjustment for Post-Retirement Benefits	(358,900)		41,200		
PATRONAGE CAPITAL - BEGINNING OF YEAR	55,078,008		54,475,528		
TRANSFER NONOPERATING LOSS TO OTHER EQUITIES			65,928		
TRANSFER TO DONATED CAPITAL	(8,043,857)				
OFFSET PRIOR YEAR LOSSES FROM ELECTRIC OPERATIONS	(12,771,060)				
TRANSFER BROADBAND LOSSES TO OTHER EQUITIES	12,555,971				
PATRONAGE CAPITAL - RETIRED	(8,071,121)		(107,944)		
PATRONAGE CAPITAL - END OF YEAR	$ 99,230,828		$ 55,078,008		

See accompanying notes to consolidated financial statements.

VALLEY ELECTRIC ASSOCIATION, INC. AND SUBSIDIARY

Exhibit C

CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016

	December 31, 2017	December 31, 2016
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margins	$ 60,482,887	$ 644,496
Adjustments to Reconcile Net Margins to Net Cash Provided by (Used in) Operating Activities		
Depreciation	11,614,671	9,649,385
Gain on Disposition of Plant	(115,570,875)	
Capital Credits	(581,069)	(517,194)
Deferred Debits	1,381,918	3,824,035
Deferred Credits	30,458,346	1,348,844
Accounts and Notes Receivable	1,523,880	249,303
Inventories and Other Current Assets	(568,046)	(32,006)
Payables and Accrued Expenses	3,165,965	348,862
Post-Retirement Benefit Obligation	67,007	2,500
Net Cash Provided by (Used in) Operating Activities	$ (8,025,316)	$ 15,518,225
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Utility Plant and Other Property and Equipment	$ (22,410,285)	$ (28,504,786)
Plant Removal More than Salvage and Other Credits	(1,157,683)	(287,987)
Proceeds from Sale of Assets	198,134,938	
Special Deposit	(31,061,469)	(1,468,906)
Other Property and Investments	397,970	270,751
Net Cash Provided by (Used in) Investing Activities	$ 143,903,471	$ (29,990,928)
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances from CFC - Long-Term Debt	$	$ 5,000,000
Payments on Long-Term Debt to CFC	(87,089,007)	(7,714,985)
Advances from CoBank - Long-Term Debt		15,124,375
Payments on Long-Term Debt to CoBank	(476,488)	(209,284)
Advances on [redacted] LTD	1,172,642	
Payments on [redacted] LTD	(635,895)	(604,584)
Payments on Capital Leases	(2,610,189)	(479,706)
Net Advances on CFC Line of Credit	15,734,514	3,400,000
Net Advances on CoBank Line of Credit	8,500,000	
Retirement of Patronage Capital	(8,071,121)	(107,944)
Memberships and Other Equities - Net	59,927	71,888
Net Cash Provided by (Used in) Financing Activities	$ (73,415,617)	$ 14,479,760
CHANGE IN CASH AND CASH EQUIVALENTS	$ 62,462,538	$ 7,057
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	1,594,381	1,587,324
CASH AND CASH EQUIVALENTS - END OF YEAR	$ 64,056,919	$ 1,594,381
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash Paid During the Year for:		
Interest on Long-Term Debt	$ 12,631,236	$ 12,286,472
Income Taxes	$ 0	$ 0

NONCASH INVESTING AND FINANCING ACTIVITIES

The adjustment for post-retirement benefit obligation increased (decreased) the accrued post-retirement benefit liability by ($358,900) and $41,200 and conversely equities by the same amount for the years ended December 31, 2017 and 2016, respectively.

In 2016, the Association refinanced $24,522,179 of CFC debt with new debt issued from CoBank.

During the year ended December 31, 2017 and 2016, the Association converted $11,484,514 and $13,549,000, respectively, of CFC line of credit to CFC long-term debt.

The Association entered into capital lease agreements for the year ended December 31, 2017 and 2016. The leases increased the capital lease obligation by $8,517,048 and $7,428,667, respectively, and increased nonutility plant and equipment in service by the same amount.

During the year ending December 31, 2016, the Association reclassified $92,147,728 of electric plant, $12,027,096 of accumulated depreciation, $1,233,280 of work in progress, and $1,210,351 of deferred debits as assets held for sale. Total net book value of assets held for sale is $82,564,063.

See accompanying notes to consolidated financial statements.

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Valley Electric Association, Inc. (VEA) is a non-profit company organized to provide electric service at the retail level to primarily residential, irrigation, and commercial accounts in a designated service area located in southwestern Nevada and portions of eastern California. Power delivered at retail is purchased wholesale from Macquarie Energy LLC and other suppliers. Any operating revenues earned in excess of costs incurred are allocated to members of VEA and are reflected as patronage capital equity on the balance sheets.

VEA has been involved in power interchange activity with a California utility company for several years. At December 31, 2017 and 2016, the net interchange balance due to the utility company has been calculated at $2,987,037 and $2,700,242, respectively, and is included in Accounts Payable - Purchased Power on the balance sheets.

Valley Electric Transmission Association, L.L.C. (VETA), is a wholly owned subsidiary of VEA and is located in Pahrump, Nevada. VETA was formed in 2011 to construct, maintain and operate the transmission facilities previously included in VEA's records. VEA transferred all transmission plant and work in progress on transmission plant to VETA in 2011 along with long-term debt in the same amount. VETA is currently constructing transmission lines in various areas of Nevada.

Valley Communications Association, L.L.C. (VCA), is a wholly owned subsidiary of VEA and is located in Pahrump, Nevada. VCA was formed in 2016 to provide broadband services to both members and non-members of VEA. VCA is reported as a division of VEA for reporting purposes.

System of Accounts

Although the Association is no longer a RUS borrower, its accounting records are maintained in accordance with the RUS Uniform System of Accounts (USOA) prescribed for RUS electric borrowers.

Principles of Consolidation

The consolidated financial statements include the accounts of VEA and its wholly owned subsidiaries, VETA and VCA. For purposes of this report, VCA and VEA's activity have been combined in the consolidating schedules. All material inter-company transactions have been eliminated.

Electric Plant, Maintenance, and Depreciation

Electric plant is stated at the original cost of construction which includes the cost of contracted services, direct labor, materials, and overhead items. Contributions from others toward the construction of electric plant are credited to the applicable plant accounts.

When property which represents a retirement unit is replaced or removed, the average cost of such property as determined from the continuing property records is credited to electric plant and such cost, together with cost of removal less salvage, is charged to the accumulated provision for depreciation.

Maintenance and repairs, including the renewal of minor items of plant not comprising a retirement unit, are charged to the appropriate maintenance accounts, except that repairs of transportation and service equipment are charged to clearing accounts and redistributed to operating expense and other accounts.

The Association capitalizes interest on its transmission line projects. During 2014, the Association also began capitalizing interest on the construction of a new administration building. The total amount of interest capitalized for the years ending December 31, 2017 and 2016 was $36,172 and $167,475, respectively.

Inventories

Materials and supplies inventories are valued at average cost.

Electric Revenues

VEA records electric revenues as billed to customers on a monthly basis. In addition, VEA has estimated that its unbilled revenue for delivered power usage which has not been billed to consumers at December 31, 2017 and 2016 to be $2,635,604 and $2,805,770, respectively. These amounts have been included in current assets on the balance sheets.

Allowance for Uncollectible Accounts

The Association uses the aging method to allow for uncollectible accounts. During the year management makes an evaluation of past due accounts to determine collectability. The accounts deemed uncollectible are written off upon approval by the Board of Directors.

Group Concentration of Credit Risk

The Association's headquarters facility is located in Pahrump, Nevada. The service area includes members located in an area located in southwestern Nevada and eastern California. VEA will require a deposit from members without a good credit history and who do not elect prepaid metering options. Any deposit will be applied to unpaid bills and fees in the event of default. The deposit accrues interest and is returned periodically. As of December 31, 2017 and 2016, deposits on hand totaled $752,887 and $643,813, respectively.

The cash balances maintained by the Association are on deposit with institutions insured by the Federal Deposit Insurance Corporation. Balances at times exceeded insured amounts.

Patronage Capital Certificates

The Association operates under a patronage capital system. Under this system, operating margins are allocated to members annually based on billings and usage of electricity. Distributions to members are made at the discretion of the Board of Directors in accordance with the bylaws, subject to the restrictions contained in long-term debt agreements.

Patronage capital from associated companies is recorded at the stated amount of the certificate.

Income Tax Status

The Association is exempt from federal income taxes under Section 501(c)(12) of the Internal Revenue Code provided that at least 85% of its revenue and income is derived from members for the sole purpose of meeting losses and expenses. For the year ended December 31, 2016, the Association qualified for exemption and operated as an exempt cooperative. For the year ended December 31, 2017, the Association did not qualify for exemption and operated as a non-exempt or taxable cooperative.

As an exempt cooperative for the 2016 calendar tax year, the Association filed federal Form 990 "Return of Organization Exempt from Income Tax." The Association also engaged in unrelated business income activities, the net income of which is subject to the unrelated business income tax imposed by Section 511 of the Internal Revenue Code. With respect to these unrelated business income activities, which was primarily the provision of Internet services on a non-patronage basis, the Association also filed federal Form 990-T "Exempt Organization Business Income Tax Return."

As a non-exempt cooperative, the Association files Form 1120 "U.S. Corporation Income Tax Return." However, because the Association operates on a patronage basis with respect to its patrons, it is allowed an exclusion from taxable income for the amount of patronage allocated to its patron; provided however, the allocation is made pursuant to a pre-existing obligation, made on a fair and equitable basis, and is from or directly related to the provision of electric service to the patrons. Therefore, the Association is generally only taxed on the net earnings (loss) from non-patronage sources, which is primarily from the provision of Internet Service to both members and non-members on a non-patronage basis. For the year ended December 31, 2017, the Association recognized an overall net loss from non-patronage sources. Therefore, a provision for federal income taxes has not been made.

VETA and VCA are classified as disregarded entities of the Association for federal income tax reporting purposes. Therefore, the operations of these two companies are included in the tax returns filed by the Association and are included in determining whether the Association is taxed as an exempt or non-exempt cooperative. The taxability of VETA and VCA is determined based on how each contributes to the patronage and non-patronage activities of the Association. Current and deferred income taxes, if any, are allocated solely to the Association.

For losses arising in tax years beginning before January 1, 2018, net operating losses (NOLs) may generally be carried back for a period of up to two years to offset prior years' taxable income or carried over to offset future taxable income for a period not to exceed 20 years. At December 31, 2017, the total NOL carryover available to the Association for both its unrelated business and non-patronage activities is $12,064,703 which begins expiring in 2026.

The Association uses the asset and liability method for recoding income taxes. The objective of the asset and liability method is to establish deferred tax assets and liabilities for the temporary differences between the financial reporting basis and the tax basis of the Association's assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized and settled. As changes in the tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes.

Income taxes are provided for tax effects of transactions reported in the financial statements and consist of taxes currently due plus deferred taxes. Deferred income taxes result from transactions which enter into the determination of taxable income in different periods than recorded for financial reporting purposes. These differences represent future tax return consequences (increases and decreases in taxable income) when deferred tax assets and liabilities are recovered, realized, or settled. The principal source of deferred federal income taxes is the NOL carryover. The federal deferred tax asset associated with the NOL carryovers is estimated at $2,533,588. However, until there is sufficient history of net earnings to show that the NOL carryovers will be fully utilized, a valuation allowance has been recorded, resulting in a net deferred tax asset recorded on the books of $0 at December 31, 2017 and 2016.

The Association follows the “uncertain tax positions” provisions of accounting principles generally accepted in the United States of America. The primary tax position of the Association is its filing status as a tax-exempt cooperative in the years it qualifies for exemption. In the years it does not qualify for exemption, the primary tax position of the Association is the exclusion from taxable income for the amount of patronage capital allocated to the patrons. The Association has determined that it is more likely than not that their tax positions will be sustained upon examination by the Internal Revenue Service and that all tax benefits are likely to be realized upon settlement with federal taxing authorities.

The Association, including the operations of VETA and VCA, files its income tax return in the U.S. federal jurisdiction. It is no longer subject to income tax examinations by the applicable federal taxing authority for years before 2014.

The Association recognizes interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. There were no amounts of penalties or interest recognized during the years ended December 31, 2017 and 2016.

Cash and Cash Equivalents

For purposes of the consolidated statements of cash flows, cash and cash equivalents include cash and temporary cash investments.

Use of Estimates in the Preparation of Consolidated Financial Statements

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. Assets Pledged

Substantially all assets are pledged as security for the long-term debt due to and under management of the National Rural Utilities Cooperative Finance Corporation (CFC) and CoBank.

3. Electric Plant

The major classes of electric plant are as follows:

	December 31, 2017	December 31, 2016
VEA		
Intangible Plant	$ 8,993	$ 8,993
Distribution Plant	178,157,725	165,221,000
General Plant	54,785,274	50,568,689
Electric Plant Acquisition Adjustment	2,211,617	2,264,656
Construction Work in Progress	1,460,240	5,436,616
Total Electric Plant in Service - VEA	$ 236,623,849	$ 223,499,954
VETA		
Transmission Plant	$ 43,000,711	$ 42,456,417
General Plant	28,964	28,964
Construction Work in Progress	4,500,926	10,026,250
Total Electric Plant in Service - VETA	$ 47,530,601	$ 52,511,631
Total Plant	$ 284,154,450	$ 276,011,585

During the year ended December 31, 2013, the Association purchased the plant assets on the [redacted]. These assets at the time of the purchase had a book value of $16,143,634 and accumulated depreciation of $1,422,734. In consideration, the Association assumed a long-term note in the amount of $17,213,287 to purchase the assets. The excess consideration over the net book value is reflected as an Electric Plant Acquisition Adjustment of $2,492,387 and is being amortized over the average remaining useful life of the assets.

During the year ended December 31, 2014, the Association purchased additional plant assets on the [redacted]. These assets at the time of the purchase had a net book value of $1,901,740. In consideration, the Association assumed a long-term note in the amount of $1,995,852 to purchase the assets. The excess consideration over the net book value increased the Electric Plant Acquisition Adjustment by $94,112 and is being amortized over the average remaining useful life of the assets.

During the year ended December 31, 2017, the Association purchased additional plant assets on the [redacted]. These assets at the time of the purchase had a net book value of $1,144,849. In consideration, the Association assumed a long-term note in the amount of $1,172,642 to purchase the assets. The excess consideration over the net book value increased the Electric Plant Acquisition Adjustment by $27,793 and is being amortized over the average remaining useful life of the assets.

Provision for depreciation of electric plant is computed using straight-line rates, group composite method, as follows:

Transmission Plant	2.00% - 2.75%
Distribution Plant	2.73%
Structures and Improvements	2.50%
Office Furniture and Fixtures	5.00% - 33.30%
Transportation Equipment	16.60%
Tools, Shop, and Garage Equipment	4.73%
Stores Equipment	4.73%
Communication Equipment	4.36%
Miscellaneous Equipment	2.72%

Depreciation for the years ended December 31, 2017 and 2016, was $8,037,222 and $8,979,488 respectively, of which $7,196,908 and $8,288,407 was charged to depreciation expense, and $840,314 and $691,081 allocated to other accounts. Amortization for the [redacted] acquisition adjustment for the years ended December 31, 2017 and 2016 were $80,833 and $79,929, respectively.

4. Other Property and Equipment

The major classes of other property and equipment are as follows:

	December 31, 2017	December 31, 2016
Broadband Vehicles and Equipment	$ 26,503,557	$ 9,762,134
Construction Work in Progress	15,588,717	12,202,275
Total Other Property and Equipment	$ 42,092,274	$ 21,964,409

Provision for depreciation of nonutility plant and equipment is computed using straight-line rates, group composite method, as follows:

Broadband Vehicles and Equipment	5.00% - 20.00 %

Depreciation for the years ended December 31, 2017 and 2016, was $3,577,449 and $669,897 respectively.

5. Assets Held for Sale

During the year ending December 31, 2016, the Association contracted to sell its 230kV transmission assets. The sale was completed in 2017. The following summary represents the net book value of the assets held for sale as of December 31, 2017 and 2016.

	December 31, 2017	December 31, 2016
Transmission	$	$ 92,147,728
Construction Work in Progress		1,233,280
Preliminary Survey		189,194
Right of Way		946,010
Other Deferred		75,147
	$ 0	$ 94,591,359
Less Accumulated Depreciation		12,027,296
Total Assets Held for Sale	$ 0	$ 82,564,063

6. Investments in Associated Organizations

Investments in associated organizations consisted of the following at December 31, 2017 and 2016:

	December 31, 2017	December 31, 2016
VEA		
CFC		
Capital Term Certificates	$ 1,036,497	$ 1,044,168
Patronage Capital	2,554,696	2,351,033
Federated Rural Insurance	341,689	304,513
Other	381,381	316,786
	$ 4,314,263	$ 4,016,500
VETA		
CFC		
Capital Term Certificates	$ 662,292	$ 670,190
Patronage Capital	1,451,286	1,146,535
Membership	1,000	1,000
	$ 2,114,578	$ 1,817,725
Total Investments in Associated Organizations	$ 6,428,841	$ 5,834,225

7. Notes Receivable

The Association provides loans to its members for the purchase of solar water heaters. The loans may be granted for up to fifteen year periods with zero percent interest. The balance of these loans at December 31, 2017 and 2016 was $1,818,388 and $2,229,904, respectively. The current portion of these loans at December 31, 2017 and 2016 was $219,250 and $244,292, respectively, and is included in current assets on the balance sheet.

8. Other Special Funds

Other Special Funds consisted of the following:

	December 31, 2017	December 31, 2016
CFC Daily Fund	$ 30,012,493	$

During the year ended December 31, 2017, the Association deferred revenue of $30,000,000 and deposited the funds at CFC.

9. Materials and Supplies

Materials and supplies consisted of the following:

	December 31, 2017	December 31, 2016
Construction Materials and Supplies	$ 2,966,644	$ 2,529,115
Transportation and Other Materials	198,548	228,787
Solar Water Heaters	243,077	265,217
Valley Communications Association	724,353	468,775
	$ 4,132,622	$ 3,491,894

10. Deferred Debits

Deferred debits included the following:

	December 31, 2017	December 31, 2016
VEA		
J.P. Morgan Termination Charge	$ 24,201,305	$ 26,401,423
Skylar Energy Contract	4,326,667	4,720,000
[redacted] Contract Costs	305,234	316,402
Community Solar Project	1,418,917	
Other Charges	172,538	258,752
	$ 30,424,661	$ 31,696,577
VETA		
Work Plan and Engineering Charges	$	$ 78,015
Other Charges		31,987
	$ 0	$ 110,002
Total Deferred Debits	$ 30,424,661	$ 31,806,579

The work plan and engineering charges are cleared based on the life of the construction work plan.

On December 26, 2013, VEA signed a termination agreement with J.P. Morgan Ventures Energy Corporation to terminate its power contract effective January 1, 2014. In consideration for this termination VEA was required to pay $33,000,000 to J.P. Morgan. This amount will be amortized over the life of the purchased power contract VEA has signed with Skylar Energy, L.P. and discussed below.

On January 7, 2014, VEA entered into a Master Power and Sale Agreement with Skylar Energy, L.P. (Skylar). The contract commenced on February 1, 2014 and will expire on January 31, 2029. In order to obtain discounted pricing, VEA was required to pay $5,900,000 into an escrow account. This amount will be amortized over the life of the contract beginning in February, 2014.

The [redacted] contract costs represent cost to obtain the contract to purchase the assets of the [redacted] assets. This amount will be amortized over the life of the [redacted] contract of 32 years.

The community solar project deferred debit is related to environmental impact study costs that will be amortized over the power purchase agreement for solar energy.

11. Return of Capital

The mortgage with CFC contains provisions that must be met for VEA to make patronage capital retirements. These provisions include minimum equity and debt service ratios. Net patronage capital totaling $8,071,121 and $107,944 was retired during the years ended December 31, 2017 and 2016, respectively.

12. Patronage Capital

	December 31, 2017	December 31, 2016
Assigned	$ 76,560,936	$ 71,942,160
Assignable	78,365,743	712,534
Assignable - Deferred Revenue	(30,000,000)	
	$ 124,926,679	$ 72,654,694
Less: Retired	25,695,851	17,576,686
	$ 99,230,828	$ 55,078,008

13. Other Equities (Deficits)

	December 31, 2017	December 31, 2016
Donated Capital	$ 11,448,586	$ 3,347,310
Operating Deficits	(12,555,971)	(12,771,059)
	$ (1,107,385)	$ (9,423,749)

As of December 31, 2017, the operating deficits are related to the accumulated losses from the broadband division. Future net margins from the broadband division will be used to offset the accumulated losses. Prior year operating deficits in the amount of $12,771,059 from electric operations were offset by the gain on the transmission sale that occurred in 2017.

14. Long-Term Debt – CFC

Following is a summary of long-term mortgage notes due CFC and those under CFC Management but owned by Farmer Mac, with scheduled maturities at various times through 2052:

	December 31, 2017	December 31, 2016
VEA		
3.75% - 4.90% Fixed Rate Notes	$ 71,086,699	$ 81,981,319
Variable Rate Notes (2.75%)	38,506,961	26,899,284
Variable Rate Loans Under Management (2.661%)	7,655,040	8,683,511
	$ 117,248,700	$ 117,564,114
Less: Current Maturities	5,338,075	5,244,384
	$ 111,910,625	$ 112,319,730
VETA		
3.20% - 5.55% Fixed Rate Notes	$ 33,500,221	$ 115,003,063
Variable Rate Notes (2.75%)	15,742,504	9,528,742
	$ 49,242,725	$ 124,531,805
Less: Current Maturities	883,689	2,534,756
	$ 48,359,036	$ 121,997,049
	$ 160,269,661	$ 234,316,779

Principal and interest installments on the notes are due quarterly. As of December 31, 2017, scheduled annual maturities of amounts due CFC for the next five years is as follows:

	VEA	VETA	Total
2018	$ 5,338,075	$ 883,689	$ 6,221,764
2019	5,537,672	920,095	6,457,767
2020	5,745,832	958,114	6,703,946
2021	5,962,950	997,822	6,960,772
2022	6,175,204	1,039,297	7,214,501

Interest for the years ended December 31, 2017 and 2016, was $10,079,104 and $11,351,515, respectively, of which $10,042,932 and $11,184,040 was charged to interest and $36,172 and $167,475 was capitalized.

VEA had unadvanced funds available from CFC in the amount of $5,070,000. VETA had unadvanced funds available from CFC in the amount of $23,802,486.

15. Long-Term Debt – CoBank

Following is a summary of long-term mortgage notes due CoBank, with scheduled maturities at various times through 2046:

	December 31, 2017	December 31, 2016
VEA		
3.06% Fixed Rate Notes	$ 38,919,416	$ 39,437,270
Less: Current Maturities	795,333	519,192
	$ 38,124,083	$ 38,918,078

Principal and interest installments on the notes are due monthly. As of December 31, 2017, scheduled annual maturities of amounts due CoBank for the next five years is as follows:

2018	$ 795,333
2019	1,194,403
2020	1,228,112
2021	1,269,124
2022	1,308,269

16. Mortgage Notes – Other Long-Term Debt

Following is a summary of the debt that is being financed for the purchase of [redacted]:

	December 31, 2017	December 31, 2016
Variable Rate Note (2.58%)	$ 17,666,484	$ 17,129,737
Less: Current Maturities	646,332	605,000
	$ 17,020,152	$ 16,524,737

Principal and interest installments on the notes are due monthly. As of December 31, 2017, scheduled annual maturities for the next five years is as follows:

2018	$ 646,332
2019	646,332
2020	646,332
2021	646,332
2022	646,332

17. Short-Term Borrowing

VEA has a $20,000,000 perpetual line of credit with CFC. At December 31, 2017 and 2016, $10,500,000 and $3,000,000 was outstanding on the perpetual line of credit, respectively. This line of credit is expected to be refinanced by advancing long-term debt funds available from CFC, therefore they have been included as long-term debt on the balance sheet.

VETA has a $5,000,000 perpetual line of credit with CFC. At December 31, 2017 and 2016, $0 and $3,250,000 was outstanding on this line of credit, respectively. This line of credit is expected to be refinanced by advancing long-term debt funds available from CFC, therefore they have been included as long-term debt on the balance sheet.

During 2017, VEA opened a $15,000,000 perpetual line of credit with CoBank with a 3.72% interest rate and maturity date of September 30, 2018. At December 31, 2017 $8,500,000 was outstanding on this line of credit.

18. Capital Lease Obligation

In 2016 and 2017, Valley Communications Association entered into five year leases with Crestmark Equipment Finance for the purchase of broadband equipment. These leases expire at various times in 2021 and 2022. The economic substance of the capital leases is that the Association is financing the acquisition of the assets through the leases over their terms, and accordingly, they are reflected in the Association's non-utility plant assets and long-term liabilities. Interest expense for the years ended December 31, 2017 and 2016, totaled $921,150 and $174,925, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following is an analysis of the book value of the leased assets included in non-utility plant at December 31, 2017 and 2016:

	December 31, 2017	December 31, 2016
Cost	$ 15,945,715	$ 7,428,667
Accumulated Depreciation	(3,093,655)	(500,097)
	$ 12,852,060	$ 6,928,570

Following is a summary of the capital lease obligation due to Crestmark Equipment Finance with scheduled maturities:

	December 31, 2017	December 31, 2016
Crestmark Equipment Finance	$ 12,855,820	$ 6,948,961
Less: Current Maturities	(2,984,390)	(1,340,366)
	$ 9,871,430	$ 5,608,595

The entire lease obligation to Crestmark Equipment Finance calls for payments totaling $14,723,120 over the remaining term of the leases. Below is a schedule by years of the future minimum payments required under the leases, with their present value at December 31, 2017:

	Crestmark
2018	$ 3,779,819
2019	3,779,819
2020	3,779,819
2021	3,131,868
2022	251,795
Total Minimum Lease Payments	$ 14,723,120
Amount Representing Interest	1,867,300
	$ 12,855,820

19. Deferred Credits

Deferred credits included the following:

	December 31, 2017	December 31, 2016
VEA		
Customer Advances for Construction	$ 102,864	$ 98,563
[redacted]	802,980	556,082
Deferred Revenue	30,000,000	
Other	112,902	112,902
Valley Communications Association	791,367	907,304
	$ 31,810,113	$ 1,674,851
VETA		
Congestion Rights Revenue	$ 1,568,403	$ 1,245,319
	$ 33,378,516	$ 2,920,170

The congestion rights revenue represents the rights for the following year. This amount will be recorded as revenue in the following year as the rights expire.

During the year ended December 31, 2017, the Association adopted a resolution to defer $30,000,000 from the transmission sale and deposit the funds at CFC. The Association plans to use these funds, over the next three to five years, (1) to maintain the current electric rates and lessen the need for a rate increase and (2) to meet equity and debt covenants with CFC.

20. Pension Benefits

The National Rural Electric Cooperative Association (NRECA) Retirement Security Plan (RS Plan) is a defined benefit pension plan qualified under Section 401 and tax-exempt under Section 501(a) of the Internal Revenue Code. It is a multi-employer plan under the accounting standards. The RS Plan sponsor's Employer Identification Number is 53-0116145 and the RS 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 Association contributions to the RS Plan in 2017 and in 2016 represented less than five percent of the total contributions made to the RS Plan by all participating employers. The Association made contributions to the RS Plan of $5,323,490 in 2017 and $3,927,550 in 2016.

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

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

The employees also participate in a 401(k) plan, a defined contribution plan provided through National Rural Electric Cooperative Association. The Association makes monthly contributions to the plan. The cost to the Association under this plan for the years ended December 31, 2017 and 2016, were $349,339 and $262,120, respectively.

21. Post-Retirement Benefits and Deferred Compensation

The Association provides post-retirement medical and life benefits for eligible employees. For purposes of this statement, the written plan in effect is the substantive plan and is considered a defined benefit plan. The Association contributes varying amounts dependent on retirement date, age, and years of service based on a plan amendment adopted in 2007 and revised in 2009.

Accounting principles generally accepted in the United States of America requires an employer that sponsors a defined benefit post-retirement plan to report the current economic status (the overfunded or underfunded status) of the plan in its balance sheet, to measure the plan assets and plan obligations as of the consolidated balance sheet date, and to include enhanced disclosures about the plan.

Benefits paid for the year ended December 31, 2017 were $281,800.

The Association's policy for contributions is to contribute annually as deemed necessary.

The measurement date used for the current valuation is December 31, 2017.

The weighted-average discount rate used to develop the accumulated post-retirement benefit obligation was 4.28%. The assumed health care cost trend rate for 2017 is 7.0% declining to an ultimate level of 5.0% in 2025.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Amounts recognized in the Association's consolidated financial statements and funded status of the plan is as follows:

	December 31, 2017	December 31, 2016
I) Net Post-Retirement Benefit Cost		
Service Cost	$ 125,907	$ 63,100
Interest Cost	147,300	168,700
Expected Return on Plan Assets	(12,700)	(12,700)
Amortization	88,300	133,900
	$ 348,807	$ 353,000
II) Accumulated Post-Retirement Benefit Obligation (APBO) Reconciliation:		
APBO Balance at Beginning of Year	$ (4,041,323)	$ (3,997,503)
Expected Return	10,685	12,580
Actuarial Gain (Loss)	270,600	(175,100)
Interest Cost / Service Cost	(273,207)	(231,800)
Benefits Paid	281,800	350,500
Net Post-Retirement Benefit Liability at Year End	$ (3,751,445)	$ (4,041,323)
III) Reconciliation of Funded Status		
APBO	$ (3,751,445)	$ (4,041,323)
Assets Funded	1,108,038	1,106,023
Accrued Post-Retirement Benefit Cost	$ (2,643,407)	$ (2,935,300)
IV) Amounts Recognized in the Balance Sheet		
Current Liability	$ (278,100)	$ (340,300)
Noncurrent Liability	(2,365,307)	(2,595,000)
	$ (2,643,407)	$ (2,935,300)
V) Accumulated Other Comprehensive Loss		
Actuarial Loss - Beginning of Year	$ 2,044,100	$ 2,002,900
Amortization of Loss	(88,300)	(133,900)
Actuarial Gain (Loss)	(270,600)	175,100
Other Comprehensive Loss	$ 1,685,200	$ 2,044,100
VI) Plan Assets		
Change in Plan Assets		
Fair Value of Plans Assets at Beginning of Year	$ 1,106,023	$ 1,105,903
Return on Plan Assets	2,015	120
	$ 1,108,038	$ 1,106,023

The Association's post-retirement benefit plans asset allocations are as follows:

	December 31, 2017	December 31, 2016
NRECA Homestead Funds Money Market Fund	$ 1,108,038	$ 1,106,023

The asset rate of return was 1.15%.

The estimated actuarial loss for the post-retirement medical benefit plan that will be amortized from accumulated other comprehensive income into net post-retirement benefit cost over the next fiscal year is expected to be $87,300.

Estimated future benefit payments for the next five years and the total payments for the sixth through tenth years are as follows:

2018	$ 278,100
2019	255,900
2020	299,700
2021	311,200
2022	281,400
2023-2027	1,242,100

22. Litigation, Commitments, and Subsequent Events

There is no pending or threatened litigation against VEA, VETA or VCA, which would materially affect its financial position.

The Association has evaluated subsequent events through April 9, 2018, the date which the financial statements were available to be issued.

23. Disclosures about Fair Value of Financial Instruments

Many of the Association's financial instruments lack an available market with similar terms, conditions, and maturities as those reflected in the carrying amount recorded. Accordingly, significant assumptions, estimations, and present value calculations were used for purposes of this disclosure.

Estimated fair value has been determined by calculating the present value of financial instruments using the best available data.

Fair value for amounts carried on the consolidated financial statements has not been reflected for the following reasons:

Patronage Capital from Associated Organizations – The right to receive cash is an inherent component of a financial instrument. The Association holds no right to receive cash since any payments are at the discretion of the governing body for the associated organizations. As such, patronage capital from associated organizations is not considered financial instruments.

CFC Variable Interest Notes – As of December 31, 2017, the Association has $61,904,505 of CFC variable interest rate notes outstanding. The carrying amount is not materially different from the fair value.

CFC and CoBank Fixed Long-Term Debt – The fair value of VEA's and VETA's CFC and CoBank fixed long-term debt is calculated by computing the present value of the individual notes to maturity. The discount rate used is the currently available CFC fixed interest rate available for long-term debt re-pricing every seven years. These debt valuations are considered Level 2 as described below.

	Carrying Value	Fair Value
As of December 31, 2017	$ 143,506,337	$ 135,040,619

Fair Value Hierarchy

The Fair Value Measurements Topic of the FASB Accounting Standards Codification establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to measurements involving significant unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are as follows:

Level 1 - Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the Association has the ability to access at the measurement date.

Level 2 - Inputs are inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3 - Inputs are unobservable inputs for the asset or liability.

24. Related Party Transactions

VEA and VETA have executed an operating agreement for VEA to manage the operations of VETA. No management fees were charged to VETA from VEA during 2017 or 2016.