



# Third Quarter Report

As of and for the three and nine months ended July 31, 2014

## ORGANIZATION

Arkansas Electric Cooperative Corporation (AECC) is a generation and transmission cooperative incorporated under the laws of the state of Arkansas, headquartered in Little Rock. AECC is the wholesale power supplier for 17 electric distribution cooperatives (members) in Arkansas. Generation resources immediately available to AECC provide 3,916 MW of capacity. The mission of AECC is to assist each of its member cooperatives in improving the quality of life in the areas they serve through the delivery of reliable electric power and other related services, which address essential consumer needs. This is to be done at the lowest possible cost consistent with sound business practices.

## RESULTS OF OPERATIONS

AECC has two components of revenue: 1) a demand charge, based on each member's peak demand for energy during the four summer months, which recovers a portion of AECC's fixed costs; and 2) an energy charge, based on total members' usage, which recovers certain variable and a portion of AECC's fixed costs. AECC is also able to recover the actual cost of fuel and purchased power through a fuel adjustment clause approved by the Arkansas Public Service Commission (APSC), along with additional expenses related to the entering energy markets of separate Regional Transmission Organizations (RTO).

"Operating revenues" for the nine months ended July 31, 2014, increased approximately \$32.6 million compared to the same period in 2013. Operating revenue experienced an increase in energy revenue of \$27.6 million. There are two reasons for the increase in energy revenue: 1) an increase in fuel and purchased power costs during the nine months ended July 31, 2014, in the amount of \$15.7 million, which was passed on to members through the fuel adjustment clause; and 2) a 3.7% increase in member megawatt hour consumption, which resulted in an increase of \$11.9 million in energy revenue. Member megawatt billing demand, which is set during the four summer months of June - September, declined by 4.8% or \$7.9 million during the nine months ended July 31, 2014, as compared to the same period in 2013, due to the unusually cool summer. Effective April 1, 2014, AECC received APSC approval to include in rates a Transmission Rider (TO/RTO Rider) to collect transmission expenses incurred in excess of an approximate base of \$5.0 million per month. The TO/RTO Rider earned in fiscal year 2014 was \$6.3 million. In addition, hourly energy sales in excess of hourly loads settled in the RTO markets increased by \$6.6 million during that same period.

Beginning December 19, 2013, AECC began participating in Midcontinent Independent System Operator, Inc.'s (MISO) RTO, which included MISO's day-ahead and real-time energy markets. MISO covers the Entergy Arkansas, Inc. footprint, which represents the eastern two-thirds of Arkansas. In addition, AECC began operating in the Integrated Marketplace launched by Southwestern Power Pool's (SPP) RTO effective March 1, 2014. SPP covers the western one-third of Arkansas, for the American Electric Power/Southwestern Electric Power Company (AEP/SWEPCO), Oklahoma Gas and Electric

Company and The Empire District Electric Company footprints. MISO and SPP coordinate, control and monitor the electricity transmission grid within AECC's respective load and generation areas. Both RTO markets use Locational Marginal Pricing (LMP) which is the method used to price energy purchases and sales on a nodal basis. LMPs reflect the value of energy at a specific location at the time it is delivered.

Because they are so interrelated to the services AECC provides to members, "Operation and maintenance, generation" and "power purchased" are categories that are combined for comparative purposes. "Operation and maintenance, generation" and "power purchased" increased during the nine months ended July 31, 2014, by \$22.1 million, compared to the same period in 2013. The total cost of energy as a percentage of operating revenue was 72.2% for the nine months ended July 31, 2014, compared to 72.4% for the nine months ended July 31, 2013. The main contributor of the increase is due to the increase in megawatt hour sales to members and the RTO markets.

"Operation and maintenance, transmission" increased by \$13.9 million during the nine months ended July 31, 2014, compared to same period in 2013. The main driver of this increase is related to AECC entering the RTO markets.

"Depreciation" expense decreased by \$6.0 million during the nine months ended July 31, 2014 compared to the same period in 2013. Along with co-owner AEP/SWEPCO, AECC received regulatory approval to install environmental upgrades to the Flint Creek Power Plant (Flint Creek) coal-fired power plant, which will extend the life of that plant. AECC engaged an outside consulting firm to prepare a depreciation study related to three of its co-owned coal fired plants that were put into production in the late 1970s and early 1980s. Effective January 1, 2014, AECC decreased the composite depreciation rate of these coal fired plants based on the preliminary study results, subject to regulatory approval by Rural Utilities Service (RUS). The depreciation rate reduction resulted in a decrease of approximately \$10.8 million in depreciation expense for the period from January 2014 to July 2014. The decrease was offset by depreciation related to the John W. Turk, Jr. Plant (Turk), which became operational in December 2012.

"Interest" expense increased by \$1.9 million compared to the nine months ended July 31, 2013. This increase was primarily due to AECC's Magnet Cove power plant acquisition in September 2012, which was fully funded by RUS long-term debt in February 2013. The increase was also due to the Turk power plant being placed into commercial operation in December 2012. The interest on long-term financing that was previously capitalized during Turk construction is now expensed.

## LIQUIDITY AND CAPITAL RESOURCES

As detailed in the "Interim Statements of Cash Flows" for the nine months ended July 31, 2014, net cash and cash equivalents decreased \$29.3 million. The major components of this decrease were deposits in the RUS Cushion of Credit program of \$40.0 million, \$62.3 million

of capital expenditures, \$22.1 million in principal payments on long term debt, along with reductions of \$39.3 million in the amount of funds held under the member line of credit funds. These decreases were offset by funds received related to AECC's commercial paper program in the amount of \$39.9 million, \$50.2 million in proceeds from the Federal Financing Bank (FFB) S8 note related to the environmental upgrade equipment at Flint Creek, along with cash provided by operating activities of \$43.4 million.

For the calendar year 2014, AECC has budgeted \$159.5 million for capital expenditures. This amount includes \$109.9 million to be incurred for generation and \$49.6 million for transmission and other miscellaneous general capital expenditures. The budgeted generation capital expenditures for 2014 include \$71.0 million for environmental controls at Flint Creek.

AECC has a \$75.0 million perpetual line of credit with the National Rural Utilities Cooperative Finance Corporation and a \$10.0 million committed line of credit with Regions Bank, which matures on August 15, 2016. AECC uses advances from the member line of credit program to support daily cash needs.

On April 28, 2011, AECC entered into a three year \$250 million senior unsecured revolving credit facility. On June 13, 2013, this agreement was extended through June 12, 2016. This \$250 million credit facility will be used to support AECC's commercial paper program, for general purposes and for the issuance of letters of credit. On July 31, 2014, AECC had \$50.0 million of outstanding commercial paper.

Moody's Investors Service (Moody's) has assigned an A1 senior secured rating to AECC's First Mortgage Obligation Series 2011 A & B private placement. AECC has also been assigned an issuer credit rating of AA by Standard and Poor's (S&P) and A+ by Fitch Ratings (Fitch). AECC's short-term debt ratings are, A1+, Prime-1and F-1 from S&P, Moody's and Fitch respectively.

## OTHER FINANCIAL INFORMATION

The interim financial statements for July 31, 2014, and 2013 are unaudited. In the opinion of AECC management, the accompanying unaudited financial information furnished herewith reflects all adjustments (consisting primarily of normal recurring accruals) necessary for a fair statement of its financial position and its results of operations for the interim periods presented; however, the business of AECC is subject to rate changes, seasonal fluctuations in sales and other factors. Accordingly, the results for the interim periods presented should not be used as a basis for estimating results of operations for a full year.

It is suggested that these interim financial statements be read in conjunction with financial statements and notes thereto included in AECC's October 31, 2013 Annual Report.

Duane Highley, President/CEO  
Michael Henderson, Executive Vice President/CFO  
Arkansas Electric Cooperative Corporation

## Arkansas Electric Cooperative Corporation BALANCE SHEETS

As of July 31, 2014 (Unaudited) and October 31, 2013

	July 31, 2014 (Unaudited) (In Thousands)	October 31, 2013 (In Thousands)		July 31, 2014 (Unaudited) (In Thousands)	October 31, 2013 (In Thousands)
<b>ASSETS</b>			<b>EQUITIES AND LIABILITIES</b>		
<b>UTILITY PLANT:</b>			<b>MEMBERS' EQUITIES:</b>		
Electric plant in service, at cost	\$ 2,163,346	\$ 2,159,776	Membership fees	\$ 2	\$ 2
Construction work in progress	140,185	66,968	Patronage capital	378,458	388,699
	2,303,531	2,226,744	Accumulated margins	19,140	8,857
Less accumulated depreciation	1,093,451	1,058,368	Other equities	118,140	118,140
Net utility plant	1,210,080	1,168,376	Total members' equities	515,740	515,698
<b>LONG-TERM INVESTMENTS:</b>			<b>LONG-TERM DEBT:</b>		
Marketable securities	-	10,000	Rural Utilities Service	61	90
Gas reserves	14,848	15,366	Federal Financing Bank	524,613	489,725
Deposit with RUS - restricted investment	85,381	42,845	CoBank	62,037	71,157
Other	22,016	20,967	CoBank, Unsecured	11,666	12,676
Total long-term investments	122,245	89,178	First Mortgage Obligation Series 2011 A & B	193,000	195,500
<b>CURRENT ASSETS:</b>			Other long-term debt	-	13
Cash and cash equivalents	77,918	107,187	Total long-term debt	791,377	769,161
Accounts receivable, members	61,410	58,450	<b>CURRENT LIABILITIES:</b>		
Fuel inventories and prepaid fuel supply	24,121	36,210	Notes payable, members	124,998	164,298
Material and supply inventories	21,694	21,939	Notes payable, related parties	30,000	30,000
Prepaid warranty agreement	489	144	Notes payable, others	49,978	9,995
Deposit with RUS - restricted investment	38	60	Current maturities of long-term debt	35,524	29,664
Other current assets	12,717	6,407	Accounts payable and other accrued liabilities	68,285	63,591
Total current assets	198,387	230,397	Accrued property taxes	8,409	6,302
			Accrued interest	3,029	5,502
			Total current liabilities	320,223	309,352
<b>DEFERRED CHARGES</b>	110,782	120,744	<b>COMMITMENTS AND CONTINGENCIES</b>		
<b>DEFERRED CREDITS</b>					
Total assets	\$ 1,641,494	\$ 1,608,695	Total members' equities and liabilities	\$ 1,641,494	\$ 1,608,695



**ARKANSAS ELECTRIC COOPERATIVE CORPORATION  
INTERIM STATEMENTS OF OPERATIONS**

For the three and nine months ended July 31, 2014 and 2013 (Unaudited)

	Three Months Ended		Nine Months Ended	
	2014	2013	2014	2013
	(In Thousands)		(In Thousands)	
<b>OPERATING REVENUES</b>	\$ 186,642	\$ 189,885	\$ 575,287	\$ 542,671
<b>OPERATING EXPENSES:</b>				
Operation and maintenance, generation	95,892	95,621	269,994	291,793
Power purchased	33,518	41,763	145,170	101,237
Operation and maintenance, transmission	21,831	18,382	65,370	51,500
Administrative and general	6,456	7,214	18,396	18,694
Depreciation	10,887	14,449	35,687	41,692
Taxes, other than income taxes	39	40	115	122
Interest	11,476	11,840	34,630	32,750
Total operating expenses	180,099	189,309	569,362	537,788
<b>MARGIN FROM OPERATIONS</b>	6,543	576	5,925	4,883
<b>INTEREST INCOME</b>	1,252	702	3,047	2,126
<b>OTHER INCOME (LOSS)</b>	773	(26)	1,156	(97)
<b>ALLOWANCE FOR FUNDS USED DURING CONSTRUCTION</b>	33	-	155	235
<b>NET MARGIN</b>	\$ 8,601	\$ 1,252	\$ 10,283	\$ 7,147

**ARKANSAS ELECTRIC COOPERATIVE CORPORATION  
INTERIM STATEMENTS OF CASH FLOWS**

For the three and nine months ended July 31, 2014 and 2013 (Unaudited)

	Three Months Ended		Nine Months Ended	
	2014	2013	2014	2013
	(In Thousands)		(In Thousands)	
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>				
Net Margin	\$ 8,601	\$ 1,252	\$ 10,283	\$ 7,147
Adjustments to reconcile net margin to net cash provided by operating activities-				
Depreciation	10,887	14,449	35,687	41,692
Amortization of gas reserves	228	268	518	625
Allowance for funds used during construction	(33)	-	(155)	(235)
Allocation of patronage from associated organizations	(7)	(11)	(1,266)	(1,275)
Gain on sale of oil inventory	(967)	-	(967)	-
Interest earned on deposit into cushion of credit	(1,063)	(528)	(2,567)	(1,781)
Changes in operating assets and liabilities-				
Accounts receivable	(4,011)	(12,634)	(2,960)	(14,345)
Fuel inventories and prepaid fuel supply	9,434	7,028	13,056	9,710
Other current assets	(356)	354	(6,310)	3,501
Material and supply inventories	(36)	(314)	245	(2,028)
Deferred charges	3,281	2,016	9,962	(7,031)
Accounts payable and accrued liabilities	4,010	2,350	(10,946)	(4,641)
Other deferred credits	(236)	(384)	(1,175)	(1,330)
Net cash provided by operating activities	29,732	13,846	43,405	30,009
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>				
Sales of marketable securities	-	-	10,000	-
Net sales of other investments	-	150	1,063	1,202
Deposit with RUS - restricted investment	-	-	(40,000)	-
Withdrawals from RUS - restricted investments	10	80	53	17,126
Capital expenditures	(29,733)	(14,812)	(62,307)	(48,215)
Net cash used in investing activities	(29,723)	(14,582)	(91,191)	(29,887)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>				
Net (payments) borrowings on notes payable	(9,596)	16,221	(39,300)	(21,012)
(Payments) borrowings on notes payable, other	(134,990)	(159,986)	39,983	(239,875)
Principal payments on long-term debt	(6,384)	(6,825)	(22,110)	(24,186)
Redemption of patronage capital	-	-	(10,242)	(9,908)
Proceeds from long-term debt	28,351	-	50,186	254,751
Net cash (used in) provided by financing activities	(122,619)	(150,590)	18,517	(40,230)
Net decrease in cash and cash equivalents	(122,610)	(151,326)	(29,269)	(40,108)
<b>CASH AND CASH EQUIVALENTS, beginning of period</b>	200,528	201,679	107,187	90,461
<b>CASH AND CASH EQUIVALENTS, end of period</b>	\$ 77,918	\$ 50,353	\$ 77,918	\$ 50,353

**MEMBER SYSTEMS AND BOARD OF DIRECTORS**

Mel Coleman, Chairman  
Jerry Pahal, Vice-Chairman  
Bill Conine, Secretary-Treasurer

**Arkansas Valley Electric**  
Ozark  
John Pendergrass  
Bill Peters

**Carroll Electric**  
Berryville  
Alan Hunnicutt  
Rob Boaz

**Farmers Electric**  
Newport  
Sam Houston  
Larry Bright

**North Arkansas Electric**  
Salem  
Mark Montgomery  
Mel Coleman

**Petit Jean Electric**  
Clinton  
Carroll Bradford  
Bill Conine

**Southwest Arkansas Electric**  
Texarkana  
Don Stemple  
Wayne Whitaker

**Ashley-Chicot Electric**  
Hamburg  
Jerry Pahal  
Rodney Chapman

**Clay County Electric**  
Corning  
John Dalton  
David Smith

**First Electric**  
Jacksonville  
Robert Hill  
Don Crabbe

**Ouachita Electric**  
Camden  
Corbet Lamkin  
Mark Cayce

**Rich Mountain Electric**  
Mena  
Mark Robbins  
Leon Philpot

**Woodruff Electric**  
Forrest City  
J. A. Wampler  
Billy Martin

**C & L Electric**  
Star City  
Bubba Hudson  
W. H. Frizzell

**Craighead Electric**  
Jonesboro  
Tom Sloan  
Brian Duncan

**Mississippi County Electric**  
Blytheville  
Robert E. Davis  
Brad Harrison

**Ozarks Electric**  
Fayetteville  
Jerry Bolinger  
Mitchell Johnson

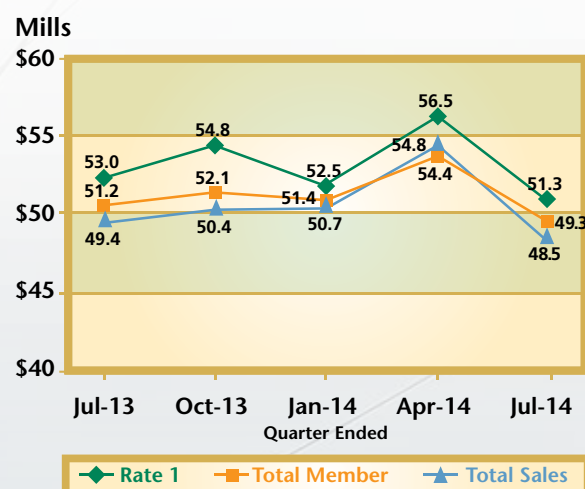
**South Central Arkansas Electric**  
Arkadelphia  
Francis Nelson  
Kevin Brownlee

**Selected Financial Highlights**

As of July 31, 2014 and October 31, 2013

	July 31, 2014	October 31, 2013
Equity as a Percent of Assets	31.42%	32.06%
Debt/Equity Ratio	1.60	1.55
Current Ratio	0.62	0.74
Margins for Interest Ratio	1.41	1.43
Debt Service Coverage Ratio	1.50	1.62
Average Cost of Long-term Debt	4.165%	4.243%

**Revenue Per MWH Sold**



**Management Team**

President/CEO

**Duane Highley**

Executive VP and General Counsel

**Robert M. Lyford**

Executive VP/CFO

**Michael Henderson**

VP Planning, Rates and Dispatching

**Ricky Bittle**

VP/CIO

**Robert McClanahan**

VP Power Production

**Jonathan Oliver**

VP Public Affairs and Member Services

**Sandra Byrd**

VP Human Resources

**Maria Smedley**



**Arkansas Electric  
Cooperative Corporation**

We Are Arkansas

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