KPMG

MINNESOTA MUNICIPAL POWER AGENCY

Financial Statements

December 31, 2015 and 2014

(With Independent Auditors' Report Thereon)

MINNESOTA MUNICIPAL POWER AGENCY

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KPMG LLP
4200 Wells Fargo Center
90 South Seventh Street
Minneapolis, MN 55402

Independent Auditors' Report

The Board of Directors
Minnesota Municipal Power Agency:

Report on Financial Statements

We have audited the accompanying financial statements of Minnesota Municipal Power Agency (the Agency), which comprise the statements of net position as of December 31, 2015 and 2014, and the related statements of revenues, expenses, and changes in net position and cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the Agency's basic financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes 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.

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the 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 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 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 financial statements referred to above present fairly, in all material respects, the financial position of Minnesota Municipal Power Agency as of December 31, 2015 and 2014, and the results of its operations and its cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.

Other Matter

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 3 through 9 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with managements' responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

KPMG LLP

Minneapolis, Minnesota
April 22, 2016

Financial Statements Overview

This discussion and analysis of Minnesota Municipal Power Agency's (the Agency) financial performance provides an overview of the Agency's activities for the fiscal years ended December 31, 2015 and 2014. The information presented should be read in conjunction with the financial statements and the accompanying notes to the financial statements.

The Agency follows the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission. The basic financial statements are prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles. The Agency's basic financial statements include the statements of net position, the statements of revenues, expenses, and changes in net position, the statements of cash flows, and notes to the financial statements.

The statements of net position provide information about the nature and amount of assets and obligations (liabilities) of the Agency as of the end of each year reported. The statements of revenues, expenses, and changes in net position report revenues and expenses. The statements of cash flows report cash receipts, cash payments, and net changes in cash resulting from operating, capital and related financing activities, and investing activities.

Financial Highlights

Comparison of 2015 with 2014

The following table summarizes the financial position of the Agency as of December 31:

Condensed Statements of Net Position

	2015	2014	Dollar change	Percentage change
Capital assets, net	$ 277,474,999	279,273,679	(1,798,680)	(0.6)%
Current assets	40,613,347	59,252,913	(18,639,566)	(31.5)
Other noncurrent assets	58,857,018	57,814,783	1,042,235	1.8
Total assets	376,945,364	396,341,375	(19,396,011)	(4.9)
Deferred outflows of resources	2,359,009	1,788,969	570,040	31.9
Total assets and deferred outflows	$ 379,304,373	398,130,344	(18,825,971)	(4.7)
Current liabilities	$ 20,526,018	24,422,643	(3,896,625)	(16.0)
Long-term liabilities	262,673,538	287,433,515	(24,759,977)	(8.6)
Total liabilities	283,199,556	311,856,158	(28,656,602)	(9.2)
Deferred inflows of resources	37,995,438	37,629,591	365,847	1.0
Total liabilities and deferred inflows	321,194,994	349,485,749	(28,290,755)	(8.1)

(Continued)

Condensed Statements of Net Position

	2015	2014	Dollar change	Percentage change
Net position:				
Net investment in capital assets	$ 32,099,907	9,508,833	22,591,074	237.6
Restricted	5,363,890	6,298,873	(934,983)	(14.8)
Unrestricted	20,645,582	32,836,889	(12,191,307)	(37.1)
Total net position	58,109,379	48,644,595	9,464,784	19.5
Total liabilities, deferred inflows, and net position	$ 379,304,373	398,130,344	(18,825,971)	(4.7)

Condensed statements of net position highlights are as follows:

- The assets of the Agency exceeded its liabilities at the close of 2015 by approximately $58.1 million (net position) as compared with $48.6 million at the end of 2014. Net position provides necessary liquidity to the Agency and supports its investment-grade credit rating.
- Capital assets, net decreased by approximately $1.8 million during 2015 primarily the result of an increase in construction and land acquisition costs in relation to the distributed generation project located in Shakopee, Minnesota. These costs were offset by additional depreciation on capital assets in service.
- Current assets decreased by $18.6 million from 2014 to 2015. Cash and cash equivalents decreased by $17.8 million, primarily the result of redeeming the Agency's unrefunded Series 2005 bonds and making capital expenditures on a generation project that have not yet been funded by long-term debt. Short-term investments decreased by $2 million. Other receivables decreased by $0.2 million and power sales receivables decreased $0.4 million. Prepaid expenses increased from 2014 to 2015 by $0.5 million.
- Other noncurrent assets, which include restricted cash and cash equivalents, noncurrent investments, restricted investments, prepaid expenses, and deferred costs, increased by approximately $1.0 million from 2014 to 2015, primarily the result of a $4.6 million increase in future recoverable costs related to the levelization of depreciation, bond interest, and costs associated with the Agency's generating resources. Noncurrent investments decreased by $1.0 million from 2014 to 2015 and restricted investments decreased by $2.4 million.
- Deferred outflows of resources increased by $0.6 million from 2014 to 2015 primarily as a result of the Agency's hedging activities.
- Current liabilities decreased by approximately $3.9 million from 2014 to 2015 primarily the result of a $4.6 million decrease of accounts payable and accrued liabilities, and a $0.3 million decrease of retainage payable. This was partially offset by an increase in derivative instruments – futures of $0.7 million, and a $0.4 million increase in accrued interest payable.

- Long-term liabilities decreased by approximately $24.8 million from 2014 to 2015, primarily the result of principal payments on Agency debt and the Agency's redemption of the remaining unrefunded Series 2005 bonds.
- Deferred inflows of resources increased by $0.4 million, primarily the result of the Agency's redemption of the remaining unrefunded Series 2005 bonds.

Comparison of 2014 with 2013

The following table summarizes the financial position of the Agency as of December 31:

Condensed Statements of Net Position

	2014	2013	Dollar change	Percentage change
Capital assets, net	$ 279,273,679	281,014,770	(1,741,091)	(0.6)%
Current assets	59,252,913	60,403,201	(1,150,288)	(1.9)
Other noncurrent assets	57,814,783	53,373,491	4,441,292	8.3
Total assets	396,341,375	394,791,462	1,549,913	0.4
Deferred outflows of resources	1,788,969	—	1,788,969	N/A
Total assets and deferred outflows	$ 398,130,344	394,791,462	3,338,882	0.8
Current liabilities	$ 24,422,643	27,390,664	(2,968,021)	(10.8)
Long-term liabilities	287,433,515	290,974,213	(3,540,698)	(1.2)
Total liabilities	311,856,158	318,364,877	(6,508,719)	(2.0)
Deferred inflows of resources	37,629,591	35,215,990	2,413,601	6.9
Total liabilities and deferred inflows	349,485,749	353,580,867	(4,095,118)	(1.2)
Net position:				
Net investment in capital assets	9,508,833	9,719,015	(210,182)	(2.2)
Restricted	6,298,873	5,733,585	565,288	9.9
Unrestricted	32,836,889	25,757,995	7,078,894	27.5
Total net position	48,644,595	41,210,595	7,434,000	18.0
Total liabilities, deferred inflows, and net position	$ 398,130,344	394,791,462	3,338,882	0.8

Condensed statements of net position highlights are as follows:

- The assets of the Agency exceeded its liabilities at the close of 2014 by approximately $48.6 million (net position) as compared with $41.2 million at the end of 2013. Net position provides necessary liquidity to the Agency and supports its investment-grade credit rating.
- Capital assets, net decreased by approximately $1.7 million during 2014 primarily the result of a decrease in electric plant in service associated with a grant received by Hometown BioEnergy, LLC that reduced the cost basis of the Hometown BioEnergy project and by depreciation on capital assets. This was partially offset by the Agency investing in a transmission line in Anoka, Minnesota.
- Current assets decreased by $1.2 million from 2013 to 2014. Cash and cash equivalents decreased by $1.9 million while short-term investments increased by $3.0 million. Other receivables decreased by $1.6 million. Power sales receivables increased $0.2 million from 2013 to 2014.
- Other noncurrent assets, which include restricted cash and cash equivalents, noncurrent investments, restricted investments, prepaid expenses, and deferred costs, increased by approximately $4.4 million from 2013 to 2014, primarily the result of a $2.2 million increase in future recoverable costs related to the levelization of depreciation, bond interest, and costs associated with the Agency's capital lease. Noncurrent investments increased by $2.0 million from 2013 to 2014.
- Deferred outflows of resources increased by $1.8 million from 2013 to 2014 as a result of the Agency current refunding its Electric Revenue Bonds, Series 2004A, and advance refunding a portion of its Electric Revenue Bonds, Series 2005.
- Current liabilities decreased by approximately $3.0 million from 2013 to 2014 primarily the result of a $2.0 million decrease of accounts payable and accrued liabilities and a $1.0 million decrease in accrued interest payable.
- Long-term liabilities decreased by approximately $3.5 million from 2013 to 2014, primarily the result of principal payments on Agency debt. This was partially offset by the issuance of the Agency's Series 2014 bonds.
- Deferred inflows of resources increased by $2.4 million, primarily the result of the Agency making contributions to its rate stabilization account and other rate-related accruals in 2014.

The following table summarizes the changes in financial position of the Agency for the years ended December 31, 2015 and 2014:

Condensed Statements of Revenues, Expenses, and Changes in Net Position

	2015	2014	Dollar change	Percentage change
Operating revenues, power sales	$ 105,383,587	104,878,860	504,727	0.5%
Other nonoperating revenues	1,100,465	3,081,874	(1,981,409)	(64.3)
Total revenues	106,484,052	107,960,734	(1,476,682)	(1.4)
Operating expenses	89,024,188	88,696,787	327,401	0.4
Other nonoperating expenses	12,621,245	14,097,285	(1,476,040)	(10.5)
Total expenses	101,645,433	102,794,072	(1,148,639)	(1.1)
Future recoverable costs	4,626,165	2,267,338	2,358,827	104.0
Change in net position	9,464,784	7,434,000	2,030,784	27.3
Beginning net position	48,644,595	41,210,595	7,434,000	18.0
Ending net position	$ 58,109,379	48,644,595	9,464,784	19.5

Condensed statements of revenues, expenses, and changes in net position highlights are as follows:

- Operating revenues – power sales increased by approximately $0.5 million between 2015 and 2014 primarily the result of higher transmission revenue received in 2015. Operating revenues – power sales consist primarily of member power sales revenue, power sales to nonmembers, and transmission revenue. Operating expenses did not materially change between 2015 and 2014.
- Other nonoperating revenues decreased by approximately $2.0 million between 2015 and 2014 primarily related to a decrease in fair value of investments, partially offset by an increase in investment income and a $0.4 million gain on extinguishment of debt.
- Operating expenses increased by approximately $0.3 million between 2015 and 2014 primarily the result of an increase in transmission, other operating expenses, and depreciation, partially offset by a decrease in power acquisition expense.
- Other nonoperating expenses decreased by approximately $1.5 million between 2015 and 2014 primarily related to a decrease in interest expense, partially offset by an increase in amortization of premium on long-term debt.
- Future recoverable costs increased by approximately $2.4 million between 2015 and 2014 primarily the result of the application of the Agency's policy regarding the levelization of costs for generating assets financed by debt and the application of the Agency's policy of not recognizing the change in value of investments for ratemaking purposes.

The following table summarizes the changes in financial position of the Agency for the years ended December 31, 2014 and 2013:

Condensed Statements of Revenues, Expenses, and Changes in Net Position

	2014	2013	Dollar change	Percentage change
Operating revenues, power sales	$ 104,878,860	106,103,819	(1,224,959)	(1.2)%
Other nonoperating revenues	3,081,874	949,652	2,132,222	224.5
Total revenues	107,960,734	107,053,471	907,263	0.8
Operating expenses	88,696,787	88,963,438	(266,651)	(0.3)
Other nonoperating expenses	14,097,285	16,615,086	(2,517,801)	(15.2)
Total expenses	102,794,072	105,578,524	(2,784,452)	(2.6)
Future recoverable costs	2,267,338	4,587,328	(2,319,990)	(50.6)
Change in net position	7,434,000	6,062,275	1,371,725	22.6
Beginning net position	41,210,595	35,148,320	6,062,275	17.2
Ending net position	$ 48,644,595	41,210,595	7,434,000	18.0

Condensed statements of revenues, expenses, and changes in net position highlights are as follows:

- Operating revenues – power sales decreased by approximately $1.2 million between 2014 and 2013 primarily the result of the expiration of a term sale to a nonmember customer. Operating revenues – power sales consist primarily of member power sales revenue, power sales to nonmembers, and other transmission revenue. Operating expenses decreased by approximately $0.3 million between 2014 and 2013, primarily as a result of decreased power acquisition expense, partially offset by increased other operating expenses and depreciation.
- Other nonoperating revenues increased by approximately $2.1 million between 2014 and 2013 primarily related to an increase in fair value of investments.
- Other nonoperating expenses decreased by approximately $2.5 million between 2014 and 2013 as there was no loss on the disposition of property in 2014, whereas 2013 had a $2.6 million loss on the disposition of property related to the Agency discontinuing development efforts on a wind project.
- Future recoverable costs decreased by approximately $2.3 million between 2014 and 2013 primarily the result of the application of the Agency's policy regarding the levelization of costs for generating assets financed by debt and the application of the Agency's policy of not recognizing the change in value of investments for ratemaking purposes.

Debt Administration

As of December 31, 2015, the Agency had long-term debt outstanding of approximately $238.6 million.

On September 18, 2013, the Agency issued Electric Revenue Bonds Series 2013 in the amount of $17.9 million. The bonds were issued for the purpose of constructing a bioenergy facility.

On September 24, 2014, the Agency issued Electric Revenue Bonds Series 2014 in the amount of $46.4 million. The bonds were issued for the purpose of refunding the Agency's outstanding Electric Revenue Bonds Series 2004A and constructing a transmission line in Anoka, Minnesota.

On December 17, 2014, the Agency issued Electric Revenue Refunding Bonds Series 2014A in the amount of $75.3 million. The bonds were issued for the purpose of advance refunding a portion of the Agency's outstanding Electric Revenue Bonds Series 2005.

On October 1, 2015, the Agency redeemed the remaining unrefunded Series 2005 bonds in the amount of $14.0 million.

Moody's upgraded the Agency's rating from A3 to A2 in 2014. The Agency continued to hold an A2 rating from Moody's in 2015. The Agency continued to hold an A rating from Fitch in 2015.

MINNESOTA MUNICIPAL POWER AGENCY

Statements of Net Position

December 31, 2015 and 2014

Assets		**2015**	**2014**
Current assets:			
Cash and cash equivalents	$	21,329,356	39,090,296
Restricted cash and cash equivalents		5,363,890	4,299,485
Short-term investments		1,000,000	2,999,556
Accrued interest receivable		169,253	68,420
Power sales receivables		8,104,945	8,519,502
Other receivable		304,177	458,169
Fuel inventory		1,354,777	1,501,063
Plant inventory – spares		1,981,104	1,843,544
Prepaid expenses		1,005,845	472,878
Total current assets		40,613,347	59,252,913
Noncurrent assets:			
Capital assets:			
Equipment		1,192,857	962,290
Capital lease asset		29,080,531	29,080,531
Land		6,116,062	4,222,351
Electric plant		311,946,139	310,305,095
Rotable combustion turbine parts		9,844,205	9,844,205
Less accumulated depreciation		(87,446,358)	(75,612,012)
Property and equipment, net		270,733,436	278,802,460
Construction in progress		6,741,563	471,219
Total capital assets, net		277,474,999	279,273,679
Investments		1,000,000	2,000,000
Restricted cash and cash equivalents		269,341	441,405
Restricted investments		19,814,495	22,206,743
Prepaid expenses		530,538	561,243
Future recoverable costs		37,242,644	32,605,392
Total noncurrent assets		336,332,017	337,088,462
Total assets		376,945,364	396,341,375
Deferred Outflows			
Deferred outflows of resources		2,359,009	1,788,969
Total assets and deferred outflows of resources	$	379,304,373	398,130,344
Liabilities			
Liabilities:			
Current liabilities:			
Accounts payable and accrued liabilities	$	7,389,957	11,985,661
Retainage payable		—	338,934
Accrued interest payable		2,815,077	2,386,016
Long-term debt due within one year		8,713,333	8,813,334
Capital lease liability due within one year		865,561	816,798
Derivative instruments – futures		742,090	81,900
Total current liabilities		20,526,018	24,422,643
Long-term debt, net		242,763,042	266,657,458
Capital lease liability		19,910,496	20,776,057
Total noncurrent liabilities		262,673,538	287,433,515
Total liabilities		283,199,556	311,856,158
Deferred Inflows			
Deferred inflows of resources – rate stabilization		30,450,000	30,450,000
Deferred inflows of resources – other		7,545,438	7,179,591
Total liabilities and deferred inflows of resources		321,194,994	349,485,749
Net Position			
Net position:			
Net investment in capital assets		32,099,907	9,508,833
Restricted for debt service		5,363,890	6,298,873
Unrestricted		20,645,582	32,836,889
Total net position		58,109,379	48,644,595
Total liabilities and deferred inflows of resources and net position	$	379,304,373	398,130,344

See accompanying notes to financial statements.

MINNESOTA MUNICIPAL POWER AGENCY

Statements of Revenues, Expenses, and Changes in Net Position

Years ended December 31, 2015 and 2014

	2015	2014
Operating revenues:		
Power sales to members	$ 104,806,467	104,722,737
Power sales to nonmembers	577,120	156,123
Total operating revenues	105,383,587	104,878,860
Operating expenses:		
Power acquisition expense	42,466,770	44,839,029
Transmission	11,125,853	10,444,101
Other operating expenses	23,597,219	21,836,740
Depreciation	11,834,346	11,576,917
Total operating expenses	89,024,188	88,696,787
Operating income	16,359,399	16,182,073
Nonoperating revenues (expenses):		
Amortization of premium on long-term debt, net	782,146	324,833
Interest expense	(13,403,391)	(14,422,118)
Investment income	1,402,545	980,363
Net (decrease) increase in fair value of investments	(680,102)	1,999,388
Gain on extinguishment of debt	378,022	—
Gain on sale of investments	—	102,123
Total nonoperating revenues (expenses), net	(11,520,780)	(11,015,411)
Change in net position before future recoverable costs	4,838,619	5,166,662
Future recoverable costs	4,626,165	2,267,338
Change in net position	9,464,784	7,434,000
Total net position, beginning of year	48,644,595	41,210,595
Total net position, end of year	$ 58,109,379	48,644,595

See accompanying notes to financial statements.

MINNESOTA MUNICIPAL POWER AGENCY

Statements of Cash Flows

Years ended December 31, 2015 and 2014

		2015	2014
Cash flows from operating activities:			
Receipts from power sales	$	105,798,144	105,836,604
Payments for power acquisition/production and operating expenses		(81,428,973)	(76,957,681)
Net cash provided by operating activities		24,369,171	28,878,923
Cash flows from capital and related financing activities:			
Construction of capital assets		(10,704,870)	(18,859,890)
Payments received from grant for capital asset construction		—	8,215,319
Proceeds from issuance of long-term debt		—	134,081,722
Principal payments on electric revenue bonds		(8,813,334)	(53,558,333)
Other financing use – payment to refunded bond escrow agent		(13,985,000)	(84,187,854)
Principal payments on capital lease		(816,798)	(770,782)
Payment of interest		(12,974,330)	(14,772,518)
Payment of debt issuance costs		(47,000)	(243,257)
Net cash used in capital and related financing activities		(47,341,332)	(30,095,593)
Cash flows from investing activities:			
Proceeds from sales of investments		18,145,302	17,012,761
Purchase of investments		(13,343,452)	(20,044,789)
Interest received		1,301,712	1,128,084
Net cash provided by (used in) investing activities		6,103,562	(1,903,944)
Net change in cash and cash equivalents		(16,868,599)	(3,120,614)
Cash and cash equivalents, beginning of year		43,831,186	46,951,800
Cash and cash equivalents, end of year	$	26,962,587	43,831,186
Cash components:			
Cash and cash equivalents	$	21,329,356	39,090,296
Restricted cash and cash equivalents		5,633,231	4,740,890
Cash and cash equivalents, end of year	$	26,962,587	43,831,186
Cash flows from operating activities:			
Operating income	$	16,359,399	16,182,073
Adjustments to reconcile operating income to net cash provided by operating activities:			
Depreciation		11,834,346	11,576,917
Changes in current assets and liabilities:			
Power sales receivables		414,557	(192,256)
Other receivables		153,992	1,623,380
Fuel inventory		146,286	(566,046)
Plant inventory – spares		(137,560)	(233,264)
Prepaid expenses		(502,262)	122,151
Accounts payable and accrued liabilities		(4,265,434)	(2,047,633)
Deferred revenue – rate stabilization		—	1,150,000
Deferred revenue – other		365,847	1,263,601
Total adjustments		8,009,772	12,696,850
Net cash provided by operating activities	$	24,369,171	28,878,923
Supplemental cash flow information and noncash capital and related financing activities:			
Amortization of premium on electric revenue bonds	$	782,146	324,833
Capital assets in retainage payable		—	338,934
Capital assets in accounts payable		360,160	690,430

See accompanying notes to financial statements.

(1) Organization and Significant Accounting Policies

(a) Organization and Operation

Minnesota Municipal Power Agency (the Agency) was created as a municipal corporation and a political subdivision of the State of Minnesota by an agency agreement recorded with the Secretary of the State of Minnesota on May 11, 1992. The Agency's purpose is to secure an adequate, economical, and reliable supply of electric energy for its member municipalities. As of December 31, 2015, the Agency comprises 12 Minnesota municipalities. In 2013, the City of Elk River, by and through the Elk River Utilities Commission, joined the Agency, becoming its 12th member. Elk River will begin purchasing all of its power and energy needs from the Agency on October 1, 2018.

The accompanying financial statements present the Agency and its component units, entities for which the Agency is considered to be financially accountable. Blended component units, although legally separate entities, are, in substance, part of the Agency's operations.

Blended Component Units: The Agency owns 100% of Minnesota Renewable Energy, LLC. Minnesota Renewable Energy, LLC owns 100% of Oak Glen Wind Farm, LLC and 100% of Hometown BioEnergy, LLC. Oak Glen Wind Farm, LLC is responsible for the operation of Oak Glen Wind Farm, a 44 megawatt (MW) wind project located in Steele County, Minnesota. Hometown BioEnergy, LLC is responsible for the operation of the Hometown BioEnergy project, an 8 MW renewable energy project located in Le Sueur, Minnesota. The Agency owns 100% of Hometown GeoPower, LLC. Hometown GeoPower, LLC provides services to residents of the Agency's member municipalities. The Agency owns 100% of MMPA Transmission LLC. MMPA Transmission LLC holds the Agency's transmission-related assets. Complete financial statements for each of the individual component units may be obtained from the Agency.

The Agency sells power to its members under long-term power sales contracts. Ten of the Agency's power sales contracts with members have a term that expires December 31, 2050. Two of the Agency's power sales contracts with members have a term that expires October 31, 2040. Under the terms of these contracts, the Agency is obligated to furnish, and each member is obligated to take and pay for, the total power and energy required by each member.

The Agency has entered into agreements with various providers to purchase accredited power and energy during 2015. The power capacity charge for 2015 is approximately $1.7 million. Capacity commitments and charges include 41 MW of capacity purchased pursuant to an agreement with the City of Chaska, a member of the Agency. Under the terms of that agreement and its amendment, the Agency has agreed to make certain payments to the City of Chaska in exchange for the peaking power capacity provided by specified generation facilities owned by the City of Chaska in an amount at least sufficient, together with certain available interest income, to pay the principal of and interest on the bonded indebtedness issued by the City of Chaska for the construction of the generation facility. Energy rates assessed by the Agency vary based on contract terms and production costs.

Minimum commitments under the terms of the power sales agreements to purchase power capacity for the next five years are as follows:

	Megawatts
Year ending December 31:	
2016	96
2017	41
2018	41
2019	41
2020	41

The Agency has an agreement with Xcel Energy Corporation (Xcel Energy) to provide transmission services through December 31, 2015. The Agency is obligated to pay for these services at rates established by the Federal Energy Regulatory Commission (FERC), $36.50 per kilowatt per year at December 31, 2015, plus ancillary charges.

The Agency has an agreement with Rochester Public Utilities (RPU) to purchase 25 MW of capacity and energy from November 1, 2010 through May 31, 2015.

The Agency enters into contracts in connection with the purchase, generation, and sale of electric power to or from its member cities, the Midcontinent Independent System Operator (MISO), and other wholesale market participants. A substantial portion of these contracts are for the purchase of natural gas at power plants owned and operated by the Agency and for the physical delivery of power to designated interconnection points on the electric grid as a normal course of business. Substantially all of the Agency's power purchases and sales are with MISO. The Agency also enters into futures or forward contracts to manage exposure to unfavorable trends in the prices of fuel (natural gas) and electric power, which are directly related to the business of the Agency. Open positions at the end of the year are carried at fair value in the Agency's financial statements with an offsetting deferral amount to reflect the effectiveness of the hedge.

Additionally, the Agency has agreements for dispatching, billing, maintenance services, and other general administration. The Agency has a contract with Avant Energy, Inc. to manage the Agency, which terminates on December 31, 2023.

(b) Basis of Accounting

The Agency follows the FERC's Uniform System of Accounts and maintains accounting records on an accrual basis in conformity with U.S. generally accepted accounting principles, including the application of Governmental Accounting Standards Board (GASB) Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, as the guidance relates to Regulated Operations. The guidance allows for the deferral of revenues and expenses to future periods in which the revenues are earned or the expenses are recovered through the rate-making process.

(c) Capital Assets

Capital assets are recorded at cost, including capitalized interest on borrowed funds during construction. The capitalized interest is recorded as part of the asset to which it relates and is amortized over the asset's estimated useful life.

The Agency follows a preventative and predictive approach to its maintenance of the Faribault Energy Park (FEP) facility. In doing so, it inspects the combustion turbine and steam turbine and performs major maintenance at intervals suggested by the turbine manufacturers. Periodically, one set of combustion parts is removed from the turbine and a replacement set is rotated into the turbine. The parts that have been removed are refurbished and are then ready to be rotated back into the turbine at the next major maintenance cycle. The Agency is depreciating the cost of the combustion turbine spare parts over the remaining life of the FEP asset. The amount on the statements of net position is the gross acquisition cost, with depreciation associated with the parts included in accumulated depreciation.

Equipment is recorded at cost and consists of telecommunication equipment, transportation equipment, and certain maintenance/testing equipment. Depreciation is provided over the estimated useful lives of the property and equipment by use of the straight-line method. Generally, the estimated useful life is 30 years for electric plant, 40 years for transmission assets, and 5 years for telecommunications equipment and transportation equipment. Other specialized equipment may differ.

(d) Restricted Cash and Cash Equivalents

The Agency's bond resolution requires the segregation of bond proceeds and prescribes the application of the Agency's revenues. Amounts classified as restricted cash and cash equivalents on the statements of net position represent cash and cash equivalents whose use is restricted by the bond resolution. It is the Agency's policy to use restricted resources first for debt service, and then unrestricted resources as they are needed.

(e) Investments and Short-Term Investments

Investments are reported at fair value based on quoted market prices. Short-term investments comprise certificates of deposit having an initial maturity of less than one year when purchased and banker's acceptances having an initial maturity of less than one year when purchased.

(f) Deferred Costs to Be Recovered in Future Periods

Rates charged to members include amounts sufficient to pay levelized principal and interest payments on long-term debt. For financial reporting purposes, the Agency recognizes depreciation and amortization pertaining to capital assets and other assets financed by long-term debt in addition to interest paid on such debt. As permitted by the application of the provisions of GASB 62, the Agency defers the current depreciation, amortization, and interest costs in excess of levelized principal and interest costs on long-term debt for assets placed into service prior to September 24, 2013 and after December 15, 2015. These costs will be recovered through rates charged to members in future periods when the levelized costs of principal and interest on long-term debt exceed the then current depreciation and interest costs related to such issues.

(g) Unamortized Debt Premium/Discount

Debt premium/discount is amortized over the repayment period of the related issues using the straight-line method, which approximates the effective-interest method.

(h) Cash Flows

For purposes of the statements of cash flows, cash equivalents are cash and equivalents and investments having an initial maturity of three months or less when purchased.

(i) Power Sales Receivables

Power sales receivables represent power sales for the period between the last billing date and the end of the period that are accrued in the period earned.

(j) Fuel Inventory and Plant Inventory – Spares

Fuel inventory and plant inventory – spares are valued on a cost basis, using the first-in, first-out (FIFO) method, which does not exceed market.

(k) Rates

Rates and charges for providing wholesale power supply are reviewed and adopted by the Agency's board of directors. Power supply services provided by the Agency are not subject to state or federal rate regulation.

(l) Revenue Recognition

The Agency recognizes revenue on sales when the electricity is provided to and used by the customers. The Agency reports only the net amount of operating revenues – power sales and power purchases expense resulting from its transactions with MISO as revenue.

(m) Operating Revenues and Expenses

Operating revenues result from exchange transactions associated with the principal activity of the Agency, the sale of electricity. Reported operating revenues are affected by contributions to or distributions from the rate stabilization account. Operating expenses are defined as expenses directly related to, or incurred in support of, the production and transmission of electricity to the participating members. All other expenses are classified as nonoperating expenses.

(n) Income Taxes

The Agency is exempt from federal and state income taxes as it is a political subdivision of the State of Minnesota.

(o) Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(2) Cash, Cash Equivalents, and Investments

The agency agreement that established the Agency and the bond resolution, under which the Electric Revenue Bonds were issued, provides for the creation and maintenance of certain funds and accounts. The funds and accounts consist principally of deposits and investments in accordance with the agency agreement, bond resolution, and applicable state law. Funds and accounts are reported in the financial statements as follows:

	December 31	
	2015	**2014**
Current assets:		
Cash and cash equivalents	$ 21,329,356	39,090,296
Restricted cash and cash equivalents	5,363,890	4,299,485
Short-term investments	1,000,000	2,999,556
Subtotal	27,693,246	46,389,337
Noncurrent assets:		
Restricted cash and cash equivalents	269,341	441,405
Investments	1,000,000	2,000,000
Restricted investments	19,814,495	22,206,743
Subtotal	21,083,836	24,648,148
Total	$ 48,777,082	71,037,485

At December 31, 2015, all deposits for the Agency were insured or collateralized by securities held by the Agency's agent in the Agency's name.

In accordance with its investment policy, the Agency invests in the following types of investments, subject to the limitations and requirements of Minnesota statutes:

- Interest bearing checking accounts
- U.S. Treasury bills, bonds, and notes
- U.S. government agencies and instrumentalities securities
- State and local securities
- Minnesota Joint Powers Investment Trusts

- Certificates of deposit
- Banker's acceptances of U.S. banks eligible for purchase by the Federal Reserve System
- Commercial paper issued by U.S. corporations or their Canadian subsidiaries, of the highest quality and maturing within 270 days
- Money market mutual funds – open-end, no-load
- Guaranteed investment contracts
- Repurchase agreements fully (100%) collateralized by U.S. securities

(a) Interest Rate Risk

Interest rate risk is the risk that the fair value of investments will be adversely affected by a change in interest rates.

The Agency had the following investments and maturities as of December 31, 2015 and 2014:

	December 31, 2015 Investment maturities (in years)			December 31, 2014 Investment maturities (in years)		
	Less than one year	**Greater than one year**	**No maturity**	**Less than one year**	**Greater than one year**	**No maturity**
Investment type:						
U.S. government agencies	$ 5,938,888	10,151,758	—	7,681,310	10,708,707	—
U.S. Treasuries	—	—	—	—	—	—
Commercial paper	9,042,489	—	—	15,013,742	—	—
Banker's acceptances	—	—	—	1,999,556	—	—
Certificates of deposit	1,000,000	1,291,000	—	1,000,000	2,291,000	—
State and local bonds	—	3,432,849	—	—	3,525,726	—
Money market accounts	—	—	5,633,231	—	—	4,589,025
Cash and cash equivalents	—	—	12,286,867	—	—	24,228,419
Total	$ 15,981,377	14,875,607	17,920,098	25,694,608	16,525,433	28,817,444

(b) Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Credit risk is measured using credit quality ratings of investments in debt securities as described by nationally recognized rating agencies such as Standard & Poor's and Moody's. The certificates of deposit are FDIC insured. The money market accounts and cash and cash equivalents are invested in short-term U.S. government securities and commercial paper.

The following tables list the credit quality ratings per Standard & Poor's and/or Moody's of the Agency's investments as of December 31, 2015 and 2014:

		December 31, 2015				
			Quality ratings			
		Amount reported	AA	AAA	P-1/A-1+	Unrated
Investment type:						
U.S. government agencies	$	16,090,646	16,090,646	—	—	—
Certificates of deposit		2,291,000	—	—	—	2,291,000
Commercial paper		9,042,489	—	—	9,042,489	—
Bankers' acceptances		—	—	—	—	—
State and local bonds		3,432,849	3,432,849	—	—	—
Money market accounts		5,633,231	—	5,633,231	—	—
Cash and cash equivalents		12,286,867	—	—	—	12,286,867
Total	$	48,777,082	19,523,495	5,633,231	9,042,489	14,577,867

		December 31, 2014				
			Quality ratings			
		Amount reported	AA	AAA	P-1/A-1+	Unrated
Investment type:						
U.S. government agencies	$	18,390,017	18,390,017	—	—	—
Certificates of deposit		3,291,000	—	—	—	3,291,000
Commercial paper		15,013,742	—	—	15,013,742	—
Bankers' acceptances		1,999,556		—	—	1,999,556
State and local bonds		3,525,726	3,525,726	—	—	—
Money market accounts		4,589,025	—	4,589,025	—	—
Cash and cash equivalents		24,228,419	—	—	—	24,228,419
Total	$	71,037,485	21,915,743	4,589,025	15,013,742	29,518,975

(c) Custodial Credit Risk

Custodial credit risk is the risk that, in the event of the failure of a counterparty, the Agency will not be able to recover the value of the investments, collateral securities, or deposits that are in the possession of the counterparty. The Agency's adopted and revised investment policy addresses, among other things, custodial credit risk. At December 31, 2015 and 2014, all of the Agency's investments are insured and registered and are held by the counterparty's trust department or agent in the Agency's name.

(d) Concentration of Credit Risk

The Agency does not have an investment policy related to investing 5% or more of the Agency's portfolio in the securities of a single issue.

(3) Capital Assets

Capital assets activity was as follows:

	2015			
	Beginning balance	Additions	Retirements/ Transfers	Ending balance
Nondepreciable capital assets:				
Construction work in progress	$ 471,219	8,681,298	(2,410,954)	6,741,563
Land	4,222,351	1,893,711	—	6,116,062
Depreciable capital assets:				
Telemetering and telecommunication	962,290	230,567	—	1,192,857
Capital lease asset	29,080,531	—	—	29,080,531
Electric plant	310,305,095	1,641,044	—	311,946,139
Rotable combustion turbine parts	9,844,205	—	—	9,844,205
Less accumulated depreciation for assets in service	(75,612,012)	(11,834,346)	—	(87,446,358)
Capital assets, net	$ 279,273,679	612,274	(2,410,954)	277,474,999

	2014			
	Beginning balance	Additions	Retirements/ Transfers	Ending balance
Nondepreciable capital assets:				
Construction work in progress	$ 4,598,781	16,426,382	(20,553,944)	471,219
Land	1,132,083	3,090,268	—	4,222,351
Depreciable capital assets:				
Telemetering and telecommunication	765,116	197,174	—	962,290
Capital lease asset	29,080,531	—	—	29,080,531
Electric plant	303,409,822	15,110,592	(8,215,319)	310,305,095
Rotable combustion turbine parts	6,063,531	3,780,674	—	9,844,205
Less accumulated depreciation for assets in service	(64,035,094)	(11,576,918)	—	(75,612,012)
Capital assets, net	$ 281,014,770	27,028,172	(28,769,263)	279,273,679

(Continued)

(4) Long-Term Debt

The Agency has issued the following Electric Revenue Bonds to finance its construction activities:

		2015	2014
Series 2005, 3.50%–5.25%, due October 1, 2007 to 2035	$	—	16,745,000
Series 2007, 4.00%–5.25%, due October 1, 2007 to 2037		22,785,000	23,355,000
Series 2009A, 1.40%, due October 1, 2009 to 2023		2,666,667	3,000,000
Series 2010A, 3.00%–5.25%, due October 1, 2011 to 2035		77,955,000	80,200,000
Series 2013, 3.00%–5.00%, due October 1, 2014 to 2023		14,955,000	16,470,000
Series 2014, 2.00%–5.00%, due October 1, 2015 to 2044		45,005,000	46,395,000
Series 2014A, 3.50%–5.00%, due October 1, 2016 to 2035		75,250,000	75,250,000
Total bonds outstanding		238,616,667	261,415,000
Less current maturities		(8,713,333)	(8,813,334)
Add unamortized premium		12,859,708	14,055,792
	$	242,763,042	266,657,458

On September 24, 2014, the Agency issued Electric Revenue Bonds Series 2014 in the amount of $50.8 million, including net premium on the bonds. $6.6 million of the bonds were issued for the purpose of constructing a transmission line in Anoka, Minnesota. $44.2 million of the bonds were issued for the purpose of current refunding the Agency's outstanding Electric Revenue Bonds Series 2004A. The net proceeds of $43.9 million (after payment of $0.3 million in underwriter's discount and issuance costs) plus an additional $2.8 million of Agency funds were deposited with the Agency's bond trustee and used to pay the principal and interest on the Agency's Series 2004A bonds when due on October 1, 2014, and to redeem all remaining outstanding Series 2004A bonds.

The current refunding resulted in a difference between the reacquisition price and net carrying amount of the old debt of $0.4 million. This difference, reported on the Agency's statement of net position as a deferred outflow of resources, is being charged to interest expense through the year 2034 using the straight-line method, which approximates the effective-interest method. The Agency completed the current refunding to reduce its total debt service payments over the next 20 years by $15.6 million and to obtain an economic gain (difference between the present values of the old and new debt service payments) of $10.1 million.

On December 17, 2014, the Agency issued Electric Revenue Refunding Bonds Series 2014A in the amount of $83.8 million, including net premium on the bonds. The bonds were issued for the purpose of advance refunding a portion of the Agency's outstanding Electric Revenue Bonds Series 2005. The net proceeds of $83.4 million (after payment of $0.4 million in underwriter's discount and issuance costs) plus an additional $0.8 million of Agency funds were deposited in an irrevocable trust with an escrow agent to provide for all future debt service payments on the Series 2005 bonds that were advance refunded. As of December 31, 2015, all of the Series 2005 bonds were either refunded or redeemed.

The advance refunding resulted in a difference between the reacquisition price and net carrying amount of the old debt of $1.3 million. This difference, reported on the Agency's statements of net position as a deferred outflow of resources, is being charged to interest expense through the year 2033 using the straight-line method, which approximates the effective-interest method. The Agency completed the current refunding to reduce its total debt service payments over the next 21 years by $6.8 million and to obtain an economic gain (difference between the present values of the old and new debt service payments) of $7.5 million. Electric Revenue Bonds are the major source of financing for the Agency's construction activities. These bonds are secured by a pledge of the net revenues derived from the operation of the system and a grant of a security interest in certain other property and contract rights of the Agency.

On October 1, 2015, the Agency redeemed the remaining unrefunded Series 2005 bonds. The redemption resulted in a difference between the redemption price and net carrying amount of the redeemed bonds of $0.4 million. This difference is reported on the Agency's statements of net position as a gain on extinguishment of debt.

Debt service requirements on the outstanding bonds are as follows:

Year		Principal	Interest	Total
2016	$	8,713,333	11,260,302	19,973,635
2017		9,113,333	10,857,335	19,970,668
2018		9,523,333	10,444,094	19,967,427
2019		9,968,333	9,995,715	19,964,048
2020		10,368,334	9,585,610	19,953,944
2021–2025		54,070,001	40,390,669	94,460,670
2026–2030		59,245,000	27,313,856	86,558,856
2031–2035		71,650,000	11,829,156	83,479,156
2036–2040		4,620,000	685,550	5,305,550
2041–2045		1,345,000	137,200	1,482,200
	$	238,616,667	132,499,487	371,116,154

The Agency has an agreement with the City of Chaska to purchase capacity, described more fully in note 1. A portion of the payments under this agreement are accounted for as a capital lease. Future minimum payments under the agreement are as follows:

Year		Principal	Interest	Executory costs	Payment
2016	$	865,561	1,184,815	435,808	2,486,184
2017		917,235	1,133,141	435,808	2,486,184
2018		971,994	1,078,382	435,808	2,486,184
2019		1,030,022	1,020,354	435,808	2,486,184
2020		1,091,514	958,861	435,808	2,486,183
2021–2025		6,516,395	3,735,482	2,179,042	12,430,919
2026–2030		8,708,074	1,543,804	2,179,042	12,430,920
2031–2032		675,262	8,197	196,897	880,356
	$	20,776,057	10,663,036	6,734,021	38,173,114

Long-term liability activity for the years ended December 31, 2015 and 2014 was as follows:

Long-term liabilities as of December 31, 2015		Beginning balance	Additions	Reductions	Ending balance
Long-term bonds	$	261,415,000	—	(22,798,333)	238,616,667
Less current maturities		(8,813,334)	(8,713,333)	8,813,334	(8,713,333)
Add unamortized premium, net		14,055,792	—	(1,196,084)	12,859,708
Long-term bonds, net	$	266,657,458	(8,713,333)	(15,181,083)	242,763,042
Capital lease liability	$	21,592,855	—	(816,798)	20,776,057

Long-term liabilities as of December 31, 2014		Beginning balance	Additions	Reductions	Ending balance
Long-term bonds	$	273,643,333	121,645,000	(133,873,333)	261,415,000
Less current maturities		(8,058,333)	(8,813,334)	8,058,333	(8,813,334)
Add unamortized premium, net		3,796,358	12,436,723	(2,177,289)	14,055,792
Long-term bonds, net	$	269,381,358	125,268,389	(127,992,289)	266,657,458
Capital lease liability	$	22,363,637	—	(770,782)	21,592,855

(5) Power Acquisition Expense

Power acquisition expense consists primarily of power purchases, production fuel, and related expenses. The Agency sells substantially all of the power and energy produced by its generating facilities into the MISO market and purchases substantially all of its power and energy needs for sales to members and others from the MISO market. The Agency reports its purchases from and sales to MISO on a net basis. The components of power acquisition expense are as follows:

		2015	2014
Power purchases	$	31,176,098	31,084,259
Production fuel		11,290,672	13,754,770
Total power acquisition expense	$	42,466,770	44,839,029

(6) Credit Facilities

The Agency entered into a $5.0 million credit facility October 1, 2008. This facility was renewed in September 2011 and again in June 2013. The commitment fee is 0.45% per annum; interest on outstanding balances is tied to the prime rate. The facility expires on June 30, 2016. There were no amounts outstanding as of December 31, 2015 or 2014.

(7) Risk Management

The Agency is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters.

The Agency participates in a public entity risk pool related to public officials' liability. The Agency has a $60,000 deductible per occurrence, with a $200,000 annual maximum deductible for its liability coverage. The Agency also purchases municipal automobile coverage from the same public entity risk pool with a $1,000 deductible per occurrence.

The public entity risk pool has purchased a reinsurance policy to guard against excessive losses.

The Agency also carries commercial insurance for its risks of property loss, business interruption, and general liability. The Agency's property loss has varying deductibles based on the equipment insured that range from $250,000 to $1,500,000. The Agency's business interruption insurance has a 60-day deductible.

The Agency also has an umbrella policy related to its municipal automobile insurance and general liability insurance.

Settled claims have not exceeded insurance coverage in any of the past three years for any of the Agency's insurance policies.

(8) Contingencies

The Agency is a party to various contracts for the sale, purchase, and transmission of power. In the ordinary course of business, contractual disputes sometimes occur between the Agency and its counterparties. The Agency does not expect the outcome of any existing dispute resolution proceedings to have a material adverse impact on financial position, results of operations, or cash flows.

The Agency is a market participant in the MISO "Day 2" electricity markets. MISO does not provide final settlement results for a trading day until 105 days after a trading day. The financial statements reflect the Agency's best estimates of final settlement results since the commencement of "Day 2" electricity markets on April 1, 2005.