

**NORTHERN MUNICIPAL POWER AGENCY
THIEF RIVER FALLS, MINNESOTA**

AUDITED FINANCIAL STATEMENTS

FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014

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**NORTHERN MUNICIPAL POWER AGENCY
ROSTER OF BOARD OFFICIALS
FOR THE YEAR ENDED DECEMBER 31, 2015**

Participants

Bagley, Minnesota
Baudette, Minnesota
Fosston, Minnesota
Grafton, North Dakota
Halstad, Minnesota
Hawley, Minnesota
Park River, North Dakota
Roseau, Minnesota
Stephen, Minnesota
Thief River Falls, Minnesota
Warren, Minnesota
Warroad, Minnesota

Representatives

Mike Jensen
Roger Schotl
David Larson
Chris West
Lucas Spaeth
Jerald Pederson
Dennis Larson
Todd Peterson
Leonard Bazey
Barry Froiland
Shannon Mortenson
Ron Kleinschmidt

President
Vice-President
Secretary-Treasurer
General Manager

Jerald Pederson
Lucas Spaeth
Dalene Monsebroten
Darryl Tveitbakk



CERTIFIED PUBLIC ACCOUNTANTS
AND CONSULTANTS

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
Northern Municipal Power Agency
Thief River Falls, Minnesota

Report on the Financial Statements

We have audited the accompanying financial statements of Northern Municipal Power Agency, which comprise the statements of net position as of December 31, 2015 and 2014, and the related statements of revenues and costs, and cash flows for the years then ended, and the related notes to the 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 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 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 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 includes performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's 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 net position of Northern 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 accounting principles generally accepted in the United States of America.

Emphasis of Matter

Adoption of New Accounting Standard

As described in Note 10 to the financial statements, the Agency adopted the provisions of Governmental Accounting Standards Board Statement No. 68, *Accounting and Financial Reporting for Pensions* and Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*. As discussed in Note 10 to the financial statements, the Agency has accounted for the provisions of the statements entirely in 2015. Our opinions are not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, schedule of Agency's contributions to the PERA retirement fund, and schedule of Agency's share of the net pension liability as listed in the table of contents 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 management's 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.



**BRADY, MARTZ & ASSOCIATES, P.C.
GRAND FORKS, NORTH DAKOTA**

February 24, 2016

NORTHERN MUNICIPAL POWER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS
FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014

FINANCIAL STATEMENT OVERVIEW

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

The basic financial statements are prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America. Northern's basic financial statements include the statements of net position, the statements of revenues and costs, and the statements of cash flows.

The statements of net position provide information about the nature and amount of assets and obligations (liabilities) of Northern as of the end of the year. The statements of revenues and costs report revenues and expenses for the current year. 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

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

Condensed Statements of Net Position

	2015	2014	2013	2015 vs 2014	
				Dollar Change	Percent Change
Net Utility Plant	\$ 144,158,888	\$ 160,521,964	\$ 178,311,778	\$ (16,363,076)	(10.2)
Current Assets	74,443,255	80,335,696	80,699,320	(5,892,441)	(7.3)
Total Assets	<u>218,602,143</u>	<u>240,857,660</u>	<u>259,011,098</u>	<u>(22,255,517)</u>	<u>(9.2)</u>
Deferred Outflows of Resources	<u>22,466</u>	<u>-</u>	<u>-</u>	<u>22,466</u>	<u>100.0</u>
Current Liabilities	30,490,282	32,112,660	29,251,098	(1,622,378)	(5.1)
Long-term Liabilities	188,115,658	208,745,000	229,760,000	(20,629,342)	(9.9)
Total Liabilities	<u>218,605,940</u>	<u>240,857,660</u>	<u>259,011,098</u>	<u>(22,251,720)</u>	<u>(9.2)</u>
Deferred Inflows of Resources	<u>18,669</u>	<u>-</u>	<u>-</u>	<u>18,669</u>	<u>100.0</u>
Net Investment in Capital Assets	(64,586,112)	(69,238,036)	(70,528,222)	4,651,924	6.7
Restricted by Bond Agreements	60,095,964	64,307,988	63,091,472	(4,212,024)	(6.5)
Unrestricted	4,490,148	4,930,048	7,436,750	(439,900)	(8.9)
Total Net Position	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>-</u>

NORTHERN MUNICIPAL POWER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014

Condensed statements of net position highlights are as follows:

- Net utility plant decreased by approximately \$16.4 million. Net utility plant includes Northern's 30% share of the Coyote generating station and Northern's approximate load-ratio share of the related transmission system. The \$16.4 million decrease in net utility plant is mainly due to an additional year's depreciation offset by property additions.
- Current assets decreased by approximately \$5.9 million. Current assets include cash, investments and accounts receivable. The decrease is primarily related to the use of construction funds to finance Coyote plant and transmission property additions.
- Current liabilities decreased by approximately \$1.6 million primarily due to a decrease in the accounts payable to Minnkota Power Cooperative, Inc. (Minnkota). This decrease was related to a decrease from the prior year in joint system transmission property additions along with more Coyote construction costs reimbursed to Minnkota throughout 2015.
- Revenue bonds, net of current maturities, decreased by approximately \$20.8 million. The decrease is due to scheduled bond principal payments made in 2015.
- The net pension liability, deferred outflows of resources, and deferred inflows of resources were due to the implementation of GASB 68, which required the Agency to record its share of the PERA net pension liability.

The following table summarizes the changes in financial position of Northern for the years ended December 31, 2015, 2014 and 2013:

Condensed Statements of Revenues and Costs

	<u>2015</u>	<u>2014</u>	<u>2013</u>	<u>2015 vs 2014</u>	
				<u>Dollar Change</u>	<u>Percent Change</u>
Revenues	\$ 54,746,684	\$ 57,777,997	\$ 54,986,308	\$ (3,031,313)	(5.2)
Operating Costs	\$ 44,343,163	\$ 46,285,212	\$ 43,739,157	\$ (1,942,049)	(4.2)
Interest	10,403,521	11,492,785	11,247,151	(1,089,264)	(9.5)
Total Costs	\$ 54,746,684	\$ 57,777,997	\$ 54,986,308	\$ (3,031,313)	(5.2)

Condensed statements of revenues and costs highlights are as follows:

- Total revenues decreased by \$3.0 million. A decrease in Revenues from Exempt Sales to Public Authorities and Other Income of \$9.5 million was partially offset by an increase in Revenues from Participants of \$0.3 million and an increase in Revenues from Minnkota of \$6.2 million. Revenues from Exempt Sales to Public Authorities and Other Income decreased primarily due to lower surplus sales from the Coyote Plant related to boiler feed pump issues in 2015. The increase in Revenues from Participants is due to a 5% rate increase on April 1, 2015 offset by a 3.5% decrease in energy kWh sales. Revenues from Minnkota were up primarily due to there being more Coyote plant costs in 2015 for Minnkota to cover under the Power Supply Coordination Agreement. Per this Agreement, Minnkota purchases all capacity and energy in excess of Northern's requirements at a cost to satisfy Northern's revenue requirements.

NORTHERN MUNICIPAL POWER AGENCY
MANAGEMENT'S DISCUSSION AND ANALYSIS - CONTINUED
FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014

- Total operating costs decreased by \$1.9 million. Total operating costs include fuel and operating & maintenance expenses for Northern's 30% share of the Coyote generating plant, transmission operating expenses, administrative expenses, and depreciation. Depreciation is provided for on a sinking fund method with depreciation equivalent to the principal payments required to pay the outstanding bonds. Depreciation expense decreased \$0.2 million due to lower bond principal payments. Operation and maintenance expense increased by \$1.7 million due in part to pension and post-retirement medical benefit adjustments for Coyote employees. Fuel decreased by \$2.9 million mainly due to the Coyote plant operating at a reduced load for most of the year resulting from the boiler feed pump issues previously mentioned.

- Interest expense decreased by \$1.1 million in 2015.

DEBT ADMINISTRATION

As of December 31, 2015, Northern had debt outstanding of approximately \$208.7 million, a decrease of approximately \$21.0 million from December 31, 2014. Northern made scheduled bond principal payments of \$21.0 million on January 2, 2015. Northern bonds have an "A-" rating from Standard & Poor's and an "A3" rating from Moody's.

FACTORS BEARING ON NORTHERN'S FUTURE

Northern is subject to various federal, state and local laws, rules and regulations relating to air and water quality, hazardous and solid waste disposal, reporting of toxic releases and air emissions, and other environmental matters. These laws, rules and regulations often require Northern to undertake considerable efforts and substantial costs to obtain licenses, permits and approvals from various federal, state and local agencies. Northern cannot predict at this time whether any additional legislation or rules will be enacted which will affect its operations, and if such laws or rules are enacted, what the future cost to Northern might be because of such action.

NORTHERN MUNICIPAL POWER AGENCY
STATEMENTS OF NET POSITION
AS OF DECEMBER 31, 2015 AND 2014

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES

	2015	2014
UTILITY PLANT		
Plant in Service	\$ 355,828,341	\$ 352,334,517
Transmission System	49,260,677	48,327,577
Total	405,089,018	400,662,094
Accumulated Depreciation	(260,930,130)	(240,140,130)
Net Utility Plant	144,158,888	160,521,964
 CURRENT ASSETS		
Cash	644,653	275,900
Investments - Unrestricted	5,439,354	6,919,440
Investments - Restricted	65,297,725	70,044,038
Accounts Receivable		
Participants	3,061,523	3,096,318
Total Current Assets	74,443,255	80,335,696
 TOTAL ASSETS	 218,602,143	 240,857,660
 DEFERRED OUTFLOWS OF RESOURCES		
Cost Sharing Defined Benefit Pension Plan	22,466	-

LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION

LONG TERM LIABILITIES		
Revenue Bonds, Net of Current Maturities	187,955,000	208,745,000
Net Pension Liability	160,658	-
Total Long Term Liabilities	188,115,658	208,745,000
 CURRENT LIABILITIES		
Accounts Payable		
Participants	644,653	275,900
Minnkota Power Cooperative, Inc.	3,853,868	5,085,710
Accrued Interest	5,201,761	5,736,050
Current Maturities of Revenue Bonds	20,790,000	21,015,000
Total Current Liabilities	30,490,282	32,112,660
 TOTAL LIABILITIES	 218,605,940	 240,857,660
 DEFERRED INFLOWS OF RESOURCES		
Cost Sharing Defined Benefit Pension Plan	18,669	-
 NET POSITION		
Net Investment in Capital Assets	(64,586,112)	(69,238,036)
Restricted by Bond Agreements	60,095,964	64,307,988
Unrestricted	4,490,148	4,930,048
Total Net Position	\$ -	\$ -

See Notes to Financial Statements

NORTHERN MUNICIPAL POWER AGENCY
STATEMENTS OF REVENUES AND COSTS
FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014

	2015	2014
REVENUES:		
Participants	\$ 33,834,095	\$ 33,538,804
Minnkota Power Cooperative, Inc.	16,128,278	9,950,302
Exempt Sales to Public Authorities and Other Income	4,784,311	14,288,891
Total	\$ 54,746,684	\$ 57,777,997
 COSTS:		
Plant Operations		
Fuel	\$ 11,099,808	\$ 14,005,157
Operation and Maintenance	10,097,949	8,382,716
Transmission Operations	1,886,127	2,433,317
Administrative Expense	469,279	449,022
Depreciation	20,790,000	21,015,000
Total	44,343,163	46,285,212
 Interest	 10,403,521	 11,492,785
Total	\$ 54,746,684	\$ 57,777,997

See Notes to Financial Statements

NORTHERN MUNICIPAL POWER AGENCY
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014

	2015	2014
CASH FLOWS FROM OPERATING ACTIVITIES:		
Receipts from Participants	\$ 33,983,096	\$ 34,847,650
Receipts from Minnkota Power Cooperative, Inc.	13,645,040	9,122,167
Receipts from Other Public Authorities	4,958,173	13,566,026
Receipts from Others	317,671	278,911
Receipt of Interest	343,409	90,555
Payments for Fuel	(11,099,808)	(14,005,157)
Payments for Operating and Maintenance	(10,097,949)	(8,382,716)
Payments for Transmission Operations	(1,886,127)	(2,433,317)
Payments for Interest	(10,937,810)	(11,457,154)
Payments for Administrative Expense	(100,526)	(447,042)
Net Cash Provided (Used) by Operating Activities	19,125,169	21,179,923
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:		
Principal Paid on Debt	(21,015,000)	(19,080,000)
Addition to Utility Plant	(3,967,815)	(1,272,999)
Net Cash Provided (Used) by Capital and Related Financing Activities	(24,982,815)	(20,352,999)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from Sale of Investments	136,443,391	119,847,456
Purchase of Investments	(130,216,992)	(120,672,401)
Net Cash Provided (Used) By Investing Activities	6,226,399	(824,945)
INCREASE IN CASH	368,753	1,979
CASH AT BEGINNING OF YEAR	275,900	273,921
CASH AT END OF YEAR	\$ 644,653	\$ 275,900
CASH FLOWS FROM OPERATING ACTIVITIES:		
Depreciation	\$ 20,790,000	\$ 21,015,000
Deferred Charges	(302,248)	(1,952,187)
Change in Current Assets and Liabilities:		
Accounts Receivable	34,795	1,190,548
Accounts Payable	(863,089)	890,929
Accrued Interest	(534,289)	35,633
Net Cash Provided (Used) by Operating Activities	\$ 19,125,169	\$ 21,179,923

See Notes to Financial Statements

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS
AS OF DECEMBER 31, 2015 AND 2014

NOTE 1 ORGANIZATION

Northern Municipal Power Agency (Northern) is a municipal corporation and a political subdivision of the State of Minnesota. Its membership consists of ten Minnesota and two North Dakota municipalities each of which owns and operates a municipal electric utility distribution system.

Northern was incorporated on December 14, 1976, for the purpose of providing a means for its members to secure an adequate, economical and reliable long-term supply of electric energy.

In April 1981, Northern purchased a 30% interest in the Coyote Station plant near Beulah, North Dakota and related transmission facilities from Minnkota Power Cooperative, Inc. As of December 31, 2015, the participants in Coyote No. 1 are as follows:

<u>Name</u>	<u>Ownership</u>
Otter Tail Power Company	35%
Northern Municipal Power Agency	30%
Montana Dakota Utilities	25%
Northwestern Corporation	<u>10%</u>
Total	<u>100%</u>

Otter Tail Power Company is the operating agent for the Coyote Station plant.

NOTE 2 ACCOUNTING POLICIES

Basis of Accounting

Northern maintains accounting records on an accrual basis in conformity with accounting principles generally accepted in the United States of America, as applicable to governmental entities, including the application of the Government 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 deferral of revenues and expenses to future periods in which the revenues are earned or the expenses are recovered through the rate-making process.

Deposits and Investments

Deposits and investments include cash and money market funds. Investments are reported on fair value based on quoted market prices.

Restricted Investments

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

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS - CONTINUED
AS OF DECEMBER 31, 2015 AND 2014

Revenue

Revenues as defined by the Electric System Revenue Bond Resolution are established at amounts sufficient to cover operating costs (excluding depreciation) and debt service on revenue bonds, less capitalized interest. Revenues are computed and billed so that no equity is accumulated for Northern.

Utility Plant

Utility plant includes all direct acquisition costs and other costs related to the acquisition of a 30% interest in the Coyote Station plant and the related transmission facilities, along with Northern's approximate load-ratio share of Minnkota Power Cooperative's transmission system. Bond expenses, including premiums and discounts, and interest expense (less interest earned on investment securities) are included in the cost of the utility plant.

Depreciation is provided for on a sinking fund method with depreciation equivalent to the principal payments required to pay the outstanding bonds.

Cash Flows

For purposes of the Statements of Cash Flows, Northern considers cash to be demand deposits.

Income Taxes

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

Net Position

Northern has implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position.* This statement provides guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in accordance with Concepts Statement No. 4, *Elements of Financial Statements.*

Pensions

For purposes of measuring the net pension liability, deferred outflows/inflows of resources, and pension expense, information about the fiduciary net position of the Public Employees Retirement Association (PERA) and additions to/deductions from PERA's fiduciary net position have been determined on the same basis as they are reported by PERA except that PERA's fiscal year end is June 30. For this purpose, plan contributions are recognized as of employer payroll paid dates and benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Reclassifications

Certain 2014 amounts have been reclassified to conform to the 2015 presentation.

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS - CONTINUED
AS OF DECEMBER 31, 2015 AND 2014

NOTE 3 POWER SUPPLY COORDINATION AGREEMENT

On March 1, 1981, Northern entered into a Power Supply Coordination Agreement with Minnkota. This agreement is effective until the later of December 31, 2031, or the date on which the Coyote Plant is retired from service. The agreement provides for Minnkota to purchase all capacity and energy in excess of Northern's requirements. Minnkota is the operating agent for Northern.

NOTE 4 CASH AND INVESTMENTS

The bond resolution under which the revenue bonds were issued provides for the creation and maintenance of certain funds and accounts as follows:

	December 31 2015	December 31 2014
Unrestricted:		
Working Fund	\$ 644,653	\$ 275,900
Operating Fund	3,180,254	3,044,085
General Reserve Fund	683,975	2,300,230
Reserve and Contingency Fund	<u>1,575,125</u>	<u>1,575,125</u>
Total Unrestricted	<u>6,084,007</u>	<u>7,195,340</u>
Restricted:		
Bond Fund Debt Service Reserve Account	15,827,630	15,751,017
Rate Stabilization Fund	4,631,675	4,631,212
Cost of Issuance Fund	4,635	4,635
2013 Plant Additions Fund	17,037,209	22,841,054
Bond Fund Interest Account	4,023,647	4,622,061
Bond Fund Principal Account	<u>23,772,929</u>	<u>22,194,059</u>
Total Restricted	<u>65,297,725</u>	<u>70,044,038</u>
Total Cash and Investments	<u>\$ 71,381,732</u>	<u>\$ 77,239,378</u>

The funds consist of \$70,737,079 of investment securities and \$644,653 of cash deposits at December 31, 2015, and \$76,963,478 of investment securities and \$275,900 of cash deposits at December 31, 2014.

As of December 31, 2015 and 2014, the agency had the following investments:

Investment Type	2015 Fair Value	2014 Fair Value
Treasury Money Market	\$ 50,689,136	\$ 54,138,120
US Treasury	-	4,462,000
FHL Bank Discount Note	5,237,127	6,302,761
FHLMC Discount Note	1,751,000	-
Abbey National Na LLC C P	-	4,277,795
FNMA	<u>13,059,816</u>	<u>7,782,802</u>
Total Investments	<u>\$ 70,737,079</u>	<u>\$ 76,963,478</u>

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS - CONTINUED
AS OF DECEMBER 31, 2015 AND 2014

Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of the failure of the counter party, the agency will not be able to recover the value of the investments or collateral securities that are in the possession of an outside party. The agency's investments are held by the investments counter party, in the agency's name.

Credit Risk

Northern is authorized to invest in:

- (a) Direct obligations of the U.S. Government, its agencies or instrumentalities.
- (b) New Housing Authority Bonds or Project Notes issued by public agencies or municipalities.
- (c) Direct and general obligations of any state or municipalities, which are rated "Aa".
- (d) Certificates of Deposit.
- (e) Bankers Acceptances.
- (f) Repurchase Agreements.

Interest Rate Risk

Northern has a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Northern entered into a Forward Purchase Agreement with Barclays Bank PLC on May 30, 2014 for investing funds in the bond fund principal and bond fund interest accounts. The agreement establishes a guaranteed rate of return on the investments held in the bond fund principal and bond fund interest accounts at 1.405%. The agreement expires on January 1, 2021.

NOTE 5 UTILITY PLANT

Utility plant activity was as follows:

	Beginning Balance	Additions	Adjustments	Ending Balance
Utility Plant as of 12/31/15				
Plant in Service	\$ 352,334,517	\$ 3,034,715	\$ 459,109	\$ 355,828,341
Transmission System	48,327,577	933,100	-	49,260,677
Total Utility Plant	400,662,094	3,967,815	459,109	405,089,018
Less Accumulated Deprec.	(240,140,130)	(20,790,000)	-	(260,930,130)
Net Utility Plant	<u>\$ 160,521,964</u>	<u>\$ (16,822,185)</u>	<u>\$ 459,109</u>	<u>\$ 144,158,888</u>
Utility Plant as of 12/31/14				
Plant in Service	\$ 350,174,331	\$ 207,999	\$ 1,952,187	\$ 352,334,517
Transmission System	47,262,577	1,065,000	-	48,327,577
Total Utility Plant	397,436,908	1,272,999	1,952,187	400,662,094
Less Accumulated Deprec.	(219,125,130)	(21,015,000)	-	(240,140,130)
Net Utility Plant	<u>\$ 178,311,778</u>	<u>\$ (19,742,001)</u>	<u>\$ 1,952,187</u>	<u>\$ 160,521,964</u>

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS - CONTINUED
AS OF DECEMBER 31, 2015 AND 2014

The Electric System Revenue Bond Resolution requires that revenues equal costs. At December 31, 2015 and 2014, \$2,845,334 and \$2,053,047, respectively were deferred against plant in service.

NOTE 6 REVENUE BONDS

Revenue bonds payable at December 31, 2015 and 2014 are summarized below:

	December 31 2015	December 31 2014
Electric System Revenue Bonds, Series 2007A, Interest 4.125% to 5.00%, due Annually In Varying Amounts from January 1, 2016 through January 1, 2031	\$ 28,060,000	\$ 28,485,000
Electric System Revenue bonds, Series 2008A, Interest 5.00%, Due Annually in varying amounts from January 1, 2016 thru January 1, 2021	62,275,000	62,275,000
Electric System Revenue Bonds, Series 2008, Interest 5.82% Due January 1, 2017	19,610,000	21,955,000
Electric System Revenue Bonds, Series 2009A, Interest 5.00%, Due Annually in Varying Amounts through January 1, 2016	15,715,000	33,820,000
Electric System Revenue Bonds, Series 2010A-1, Interest 2.50% to 5.00%, Due Annually in Varying Amounts from January 1, 2016 through January 1, 2020	46,080,000	46,220,000
Electric System Revenue Bonds, Series 2010A-2, Interest 5.00%, Due Annually in Varying Amounts from January 1, 2022 through January 1, 2024	6,785,000	6,785,000
Electric System Revenue Bonds, Series 2010B, Interest 2.734%, Due January 1, 2016	1,770,000	1,770,000
Electric System Revenue Bonds, Series 2013A, Interest 4.13% to 5.00%, Due Annually in Varying Amounts from January 1, 2023 through January 1, 2031	26,155,000	26,155,000
Electric System Revenue Bonds, Series 2013B, Interest 4.35%, Due January 1, 2022	2,295,000	2,295,000
Totals	\$ 208,745,000	\$ 229,760,000

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS - CONTINUED
AS OF DECEMBER 31, 2015 AND 2014

Revenue bond debt service requirements to maturity are as follows:

	Principal	Interest	Total
2016	\$ 20,790,000	\$ 10,403,520	\$ 31,193,520
2017	24,150,000	9,383,629	33,533,629
2018	24,325,000	8,035,826	32,360,826
2019	24,980,000	6,823,820	31,803,820
2020	26,215,000	5,578,608	31,793,608
2021-2025	53,200,000	13,812,446	67,012,446
2026-2030	28,565,000	5,568,999	34,133,999
2031	6,520,000	310,725	6,830,725
	<u>\$ 208,745,000</u>	<u>\$ 59,917,573</u>	<u>\$ 268,662,573</u>

The principal and interest on the bonds are payable solely from and secured solely by a pledge of (1) the proceeds of the sale of the bonds to the extent held in special funds established by the Bond Resolution, (2) the revenues of Northern subject to prior payments therefrom of operating expenses and (3) all funds and accounts established by the Bond Resolution permitting the application thereof for the purpose and on the terms and conditions set forth in the Bond Resolution.

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

	Beginning Balance	Net Additions	Net Reductions	Ending Balance
Long-term liabilities, 12/31/15				
Revenue bonds	\$ 229,760,000	\$ -	\$ (21,015,000)	\$ 208,745,000
Long-term liabilities, 12/31/14				
Revenue bonds	\$ 248,840,000	\$ -	\$ (19,080,000)	\$ 229,760,000

NOTE 7 DEFINED BENEFIT PENSION PLAN

Public Employees Retirement Association

Plan Description

The Agency participates in the following defined benefit pension plans administered by the Public Employees Retirement Association of Minnesota (PERA). PERA's defined benefit pension plans are established and administered in accordance with Minnesota Statutes, Chapters 353 and 356. PERA's defined benefit pension plans are tax qualified plans under Section 401 (a) of the Internal Revenue Code.

1. General Employees Retirement Fund (GERF)

All full-time and certain part-time employees of the Agency are covered by the General Employees Retirement Fund (GERF). GERF members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security and Basic Plan members are not. The Basic Plan was closed to new members in 1967. All new members must participate in the Coordinated Plan.

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS - CONTINUED
AS OF DECEMBER 31, 2015 AND 2014

Benefits Provided

PERA provides retirement, disability, and death benefits. Benefit provisions are established by state statute and can only be modified by the state legislature.

Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan. Members in plans that are at least 90% funded for two consecutive years are given 2.5% increases. Members in plans that have not exceeded 90% funded, or have fallen below 80%, are given 1% increases.

The benefit provisions stated in the following paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not receiving them yet are bound by the provisions in effect at the time they last terminated their public service.

1. GERF Benefits

Benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service. Two methods are used to compute benefits for PERA's Coordinated and Basic Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate for a Basic Plan member is 2.2% of average salary for each of the first ten years of service and 2.7% for each remaining year. The annuity accrual rate for a Coordinated Plan member is 1.2% of average salary for each of the first ten years and 1.7% for each remaining year. Under Method 2, the annuity accrual rate is 2.7% of average salary for Basic Plan members and 1.7% for Coordinated Plan members for each year of service. For members hired prior to July 1, 1989, a full annuity is available when age plus years of service equal 90 and normal retirement age is 65. For members hired on or after July 1, 1989, normal retirement age is the age for unreduced Social Security benefits capped at 66.

Contributions

Minnesota Statutes Chapter 353 sets the rates for employer and employee contributions. Contribution rates can only be modified by the state legislature.

1. GERF Contributions

Basic plan members and Coordinated Plan members were required to contribute 9.1% and 6.50%, respectively, of their annual covered salary in calendar year 2015. The Agency was required to contribute 11.78% of pay for Basic Plan members and 7.50% for Coordinated Plan members in calendar year 2015. The Agency's contributions to the GERF for the year ended December 31, 2015, were \$14,232. The Agency's contributions were equal to the required contributions as set by state statute.

GERF Pension Costs

At December 31, 2015, the Agency reported a liability of \$160,658 for its proportionate share of the GERF's net pension liability. The net pension liability was measured as of June 30, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Agency's proportion of the net pension liability was based on the Agency's contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2014, through June 30, 2015, relative to the total

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS - CONTINUED
AS OF DECEMBER 31, 2015 AND 2014

employer contributions received from all of PERA's participating employers. At June 30, 2015 the Agency's proportion share was 0.0031%.

For the year ended December 31, 2015, the Agency recognized pension expense of \$17,892 for its proportionate share of GERF's pension expense.

At December 31, 2015, the Agency reported its proportionate share of GERF's deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual economic experience	\$ -	\$ 8,100
Changes in actuarial assumptions	-	-
Difference between projected and actual investment earnings	15,209	-
Changes in proportion	-	10,569
Contributions paid to PERA subsequent to the measurement date	7,257	-
Total	\$ 22,466	\$ 18,669

\$7,257 reported as deferred outflows of resources related to pensions resulting from Agency contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending December 31, 2016. Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

Year Ending December 31:	Pension Expense Amount
2016	\$ (2,421)
2017	(2,421)
2018	(2,421)
2019	3,802
2020	-
Thereafter	-

Actuarial Assumptions

The total pension liability in the June 30, 2015, actuarial valuation was determined using the following actuarial assumptions:

Inflation	2.75% per year
Active Member Payroll Growth	3.50% per year
Investment Rate of Return	7.90%

Salary increases were based on a service-related table. Mortality rates for active members, retirees, survivors and disabilitants were based on RP-2000 tables for males or females, as appropriate, with slight adjustments. Cost of living benefit increases for retirees are assumed to be: 1% effective every January 1st until 2034, then 2.5% for GERF.

Actuarial assumptions used in the June 30, 2015, valuation were based on the results of actuarial experience studies. The experience study in the GERF was for the period July 1, 2004, through June 30, 2008, with an update of economic assumptions in 2014. Experience studies have not been prepared for PERA's other plans, but assumptions are reviewed annually.

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS - CONTINUED
AS OF DECEMBER 31, 2015 AND 2014

There were no changes in actuarial assumptions in 2015.

The long-term expected rate of return on pension plan investments is 7.9%. The State Board of Investment, which manages the investments of PERA, prepares an analysis of the reasonableness of the long-term expected rate of return on a regular basis using a building-block method in which best-estimate ranges of expected future rates of return are developed for each major asset class. These ranges are combined to produce an expected long-term rate of return by weighting the expected future rates of return by the target asset allocation percentages. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Domestic Stocks	45%	5.50%
International Stocks	15%	6.00%
Bonds	18%	1.45%
Alternative Assets	20%	6.40%
Cash	2%	0.50%

Discount Rate

The discount rate used to measure the total pension liability was 7.9%. The projection of cash flows used to determine the discount rate assumed that employee and employer contributions will be made at the rate specified in statute. Based on that assumption, each of the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Pension Liability Sensitivity

The following presents the Agency's proportionate share of the net pension liability for all plans it participates in, calculated using the discount rate disclosed in the preceding paragraph, as well as what the Agency's proportionate share of the net pension liability would be if it were calculated using a discount rate 1 percentage point lower or 1 percentage point higher than the current discount rate:

	1% Decrease in Discount Rate (6.9%)	Discount Rate (7.9%)	1% Increase in Discount Rate (8.9%)
Agency's proportionate share of the GERS net pension liability:	\$ 252,612	\$ 160,658	\$ 84,719

Pension Plan Fiduciary Net Position

Detailed information about each defined benefit pension plan's fiduciary net position is available in a separately issued PERA financial report that includes financial statements and required supplementary information. That report may be obtained on the Internet at www.mnpera.org.

NORTHERN MUNICIPAL POWER AGENCY
NOTES TO FINANCIAL STATEMENTS - CONTINUED
AS OF DECEMBER 31, 2015 AND 2014

For the year ended December 31, 2014:

Minnesota Statutes Chapter 353 sets the rates for employer and employee contributions. These statutes are established and amended by the state legislature. Northern makes annual contributions to the pension plans equal to the amount required by state statutes. GERF Coordinated Plan members were required to contribute 6.25% of their annual covered salary in 2014. In 2014, Northern was required to contribute 7.25% of annual covered payroll for Coordinated Plan members. Northern's contributions to the Public Employees Retirement Fund for the years ended December 31, 2014, 2013 and 2012 were \$12,967, \$12,683, and \$12,434, respectively. Northern's contributions were equal to the contractually required contributions for each year as set by state statute.

NOTE 8 RISK MANAGEMENT

Northern is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees and others; and natural disasters. The Reserve and Contingency Fund was established to fund uninsured risks of loss. At December 31, 2015 and 2014, Reserve and Contingency Fund assets were \$1,575,125. There were no outstanding or unpaid claims as of December 31, 2015 and 2014. Northern continues to carry commercial insurance for other risks of loss, including workers' compensation, property and liability, and employee health and accident. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

NOTE 9 COMMITMENTS AND CONTINGENCIES

The United States Environmental Protection Agency has provided Otter Tail Power Company (the operator of the Coyote Station at Beulah, North Dakota) with a Request to Provide Information Pursuant to the Clean Air Act concerning Coyote and other plants owned or operated by Otter Tail Power Company. The Environmental Protection Agency is requesting the information to determine whether the emission source is complying with the Clean Air Act. Potential penalties could be authorized by the Clean Air Act if violations were noted but since the request is in preliminary stages, it is not possible to predict if any violations and subsequent penalties would be enforced. Northern believes the Coyote Station has been operating in accordance with the Clean Air Act and expects no violations to be found.

NOTE 10 CHANGE IN ACCOUNTING PRINCIPLE

The Agency implemented GASB Statement No. 68 *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27* and GASB Statement No. 71 *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68*. As a result, the following table indicates the balances that would have related to the prior year that the Agency has chosen to include in 2015.

Prior year balance for pension accounting:	
Net Pension Liability	\$ (159,715)
Pension related Deferred Outflows of Resources	<u>6,484</u>
Effect on current year statements from prior year balances	<u>\$ (153,231)</u>

NORTHERN MUNICIPAL POWER AGENCY
SCHEDULE OF AGENCY'S CONTRIBUTIONS TO MN PERA RETIREMENT PLAN
LAST 10 YEARS

<u>Year Ended</u> <u>December 31</u>	<u>Pension Plan</u>	<u>Statutorily</u> <u>Required</u> <u>Contribution</u>	<u>Contributions in</u> <u>Relation to the</u> <u>Statutorily Required</u> <u>Contributions</u>	<u>Contribution</u> <u>Deficiency (Excess)</u>	<u>Agency's Covered-</u> <u>Employee Payroll</u>	<u>Contributions as a</u> <u>Percentage of Covered-</u> <u>Employee Payroll</u>
2015	PERA	\$ 14,232	\$ 14,232	\$ -	\$ 189,767	7.50%

The Agency implemented GASB Statement No. 68 for its fiscal year ended December 31, 2015. Information for the prior years is not available.

NORTHERN MUNICIPAL POWER AGENCY
SCHEDULE OF AGENCY'S SHARE OF THE NET PENSION LIABILITY
LAST 10 YEARS

<u>For the Year Ended December 31</u>	<u>Agency's Proportion of the Net Pension Liability (Asset)</u>	<u>Agency's Proportionate Share of the Net Pension Liability (Asset) (a)</u>	<u>State of Minnesota's Proportionate Share of the Net Pension Liability (if Applicable) (b)</u>	<u>Proportionate Share of the Net Pension Liability and State of Minnesota's Share of the Net Pension Liability (if Applicable) (a+b)</u>	<u>Agency's Covered-Employee Payroll</u>	<u>Agency's Proportionate Share of the Net Pension Liability (Asset) as a Percentage of its Covered-Employee Payroll</u>	<u>Plan Fiduciary Net Position as a Percentage of the Total Pension Liability</u>
2015 PERA	0.0031%	\$ 160,658	-	\$ 160,658	\$ 189,767	84.66%	78.20%

The amounts presented for each fiscal year were determined as of the measurement date of the collective net pension liability which is June 30, 2015.

The Agency implemented GASB Statement No. 68 for its fiscal year ended December 31, 2015. Information for the prior years is not available.