2016

Annual Report

KEPCo

Kansas Electric Power
Cooperative, Inc.

Contents

KEPCo Staff

Marcus Harris................Executive Vice President & Chief Executive Officer

Les Evans...........................Senior Vice President & Chief Operating Officer

Coleen Wells……...............Senior Vice President & Chief Financial Officer

Stephanie Anderson................................Finance & Benefits Analyst 2

Mark Barbee.........Vice President of Engineering, KSI Vice President of Engineering

Chris Davidson....................................Engineer 3

Terry Deutscher........................Manager, SCADA & Meter Maintenance

Mark Doljac...........Director of Rates & Regulation

Carol Gardner.....................Operations Analyst 2

Shawn Geil..........Director of Information Systems

Maurice Hall.......Sr. SCADA/Metering Technician

Robert Hammersmith.........................Sr. SCADA/ Metering Technician

Shari Koch............................Finance & Accounts Payable/Payroll Specialist 2

Elizabeth Lesline............Administrative Assistant/ Receptionist

Mitch Long....................................... Sr. SCADA/ Metering Technician

Matt Ottman......Information System Specialist 2

John Payne...............................Senior Engineer

Rita Petty.............................. Executive Assistant & Manager of Office Services

Kelsey Schrempp........... Administrative Assistant & Benefits Specialist

Paul Stone.................................System Operator

Jill Taggart......Director of Forecasting & Planning

Phil Wages............. Director of Member Services, Government Affairs & Business Development

Organization and Resources

Kansas Electric Power Cooperative, Inc. (KEPCo), headquartered in Topeka, Kansas, was incorporated in 1975 as a not-for-profit generation and transmission cooperative (G&T). It is KEPCo's responsibility to procure an adequate and reliable power supply for its nineteen distribution rural electric cooperative members at a reasonable cost.

Through their combined resources, KEPCo Members support a wide range of other services, such as rural economic development, marketing and diversification opportunities, power requirement and engineering studies, and rate design, among others.

KEPCo is governed by a Board of Trustees representing each of its nineteen Members which collectively serve more than 120,000 electric meters in two-thirds of Kansas. The KEPCo Board of Trustees meets regularly to establish policies and act on issues that often include recommendations from working committees of the Board and KEPCo staff. The Board also elects a seven-person Executive Committee which includes the President, Vice President, Secretary, Treasurer, and three additional Executive Committee members.

KEPCo was granted a limited certificate of convenience and authority by the Kansas Corporation Commission in 1980 to act as a G&T public utility. KEPCo's power supply resources consist of: 70 MW of owned generation from the Wolf Creek Generating Station; 30 MW of owned generation from the Iatan 2 Generating Unit; the 20 MW Sharpe Generating Station located in Coffey County; Prairie Sky Solar, a one-megawatt solar facility in Butler County; hydropower purchases of an equivalent 100 MW from the Southwestern Power Administration; and 13 MW from the Western Area Power Administration; plus partial requirement power purchases from regional utilities.

KEPCo is a Touchstone Energy® Cooperative. Touchstone Energy® is a nationwide alliance of more than 750 cooperatives committed to promoting the core strengths of electric cooperatives - integrity, accountability, innovation, personal service and a legacy of community commitment. The national program is anchored by the motto "The Power of Human Connections".

Kansas Electric
Power Cooperative, Inc.
P.O. Box 4877 Topeka, KS 66604
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(785) 273-7010 www.kepco.org

A Touchstone Energy® Cooperative

2016 Message

from
Kevin Compton
KEPCo President
&
Marcus Harris
Executive Vice President
& Chief Executive Officer

At KEPCo's November Board of Trustees meeting, Mr. Kevin Compton (right) was elected as KEPCo's 12th president. Mr. Compton is Vice-President of the Brown-Atchison Electric Cooperative Association, Inc. Board of Trustees, located in Horton, KS.

As KEPCo completes its 42nd year of operation, our focus remains the same as year one - to provide superior service to our members, while using our mission of providing safe, reliable, and affordable energy as the compass to navigate through challenging times. Each year many strategic decisions are made, often centered around regulatory, political, and energy resource issues. Each decision is made purposefully, with the same end result in mind – for the betterment of our nineteen-member rural electric cooperatives.

"Since 2012, KEPCo's average wholesale rate has decreased by over 5% and has remained relatively constant, averaging 75.6 mills since 2013."

An essential element of providing superior service to the rural communities of Kansas is KEPCo's ability to provide electricity at not only an economical price, but a stable price as well. Since 2012, KEPCo's average wholesale rate has decreased by over 5% and has remained relatively constant, averaging 75.6 mills since 2013. KEPCo has also seen a flattening of demand. In 2011, a record peak demand of 455 megawatts was set. Since 2013, KEPCo's peak demand has averaged 431 megawatts. The decrease in demand is predominantly attributed to four factors: several of KEPCo's member cooperatives have installed diesel-fired generators which are called upon by KEPCo to run during peak times; the accumulative effect of several years of energy efficiency measures, such as the installation of high-efficiency HVAC systems by cooperative members, which is promoted by KEPCo's heat pump rebate program; the decrease in production within the oil and natural gas industries; and the aggressive demand-side response program administered by KEPCo. This year, KEPCo was able to shed approximately 35 megawatts of demand, saving our members approximately $4 million. Reducing peak demand, while retaining energy sales, reduces the wholesale price of power to KEPCo's member cooperatives.

Through careful and deliberate planning, KEPCo has crafted a power supply that is quite diverse, which enables KEPCo to shield its member cooperatives from price fluctuations of a particular generation fuel. This year, KEPCo further augmented its diverse power supply with the addition of a one-megawatt solar facility, designed and engineered by KEPCo Services, Inc. (KSI), a KEPCo-owned subsidiary. The facility was named Prairie Sky Solar, and is anticipated to generate 1,980 megawatt hours of electricity the first year. KEPCo's member cooperatives will have the ability to offer, at the prerogative of the member cooperative, subscribing the generation from the facility in 100 kilowatt hour blocks to the membership of the cooperatives choosing to participate in the subscription program. The facility was financed with low-interest New Clean Renewable Energy Bonds (NCREBs) through National Rural Utilities Cooperative Finance Corporation (CFC). The addition of the solar facility will enable KEPCo to reduce the demand on traditional generation sources in the peak summer months, further reducing demand costs to KEPCo's members.

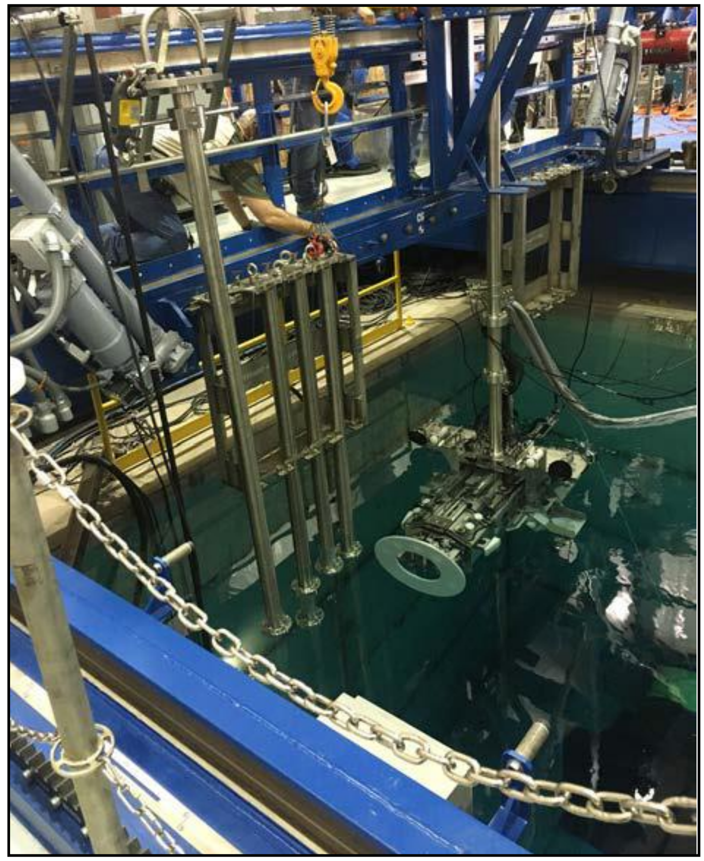

From l to r: Mark Doljac, Director of Rates and Regulation and Mark Barbee, Vice President of Engineering.

"If carbon dioxide regulation remains a national point of emphasis, KEPCo's cost to meet regulatory standards will be substantially lower relative to other utilities as a result of its diverse power supply."

KEPCo had a solid financial performance in 2016. KEPCo ended the year with total revenue of $160.2 million and a consolidated net margin of $1.9 million. KEPCo's total assets, including those of its subsidiary, KSI, were $291 million. The solid financial performance allowed KEPCo to maintain key financial metrics within acceptable levels and enabled KEPCo's equity-to-asset ratio to reach 24.14%, which is a historic high for KEPCo. KEPCo members received $1.93 million in patronage capital and realized cost savings of $11.5 million through the Margin Stabilization Adjustment for 2016. Such notable financial performance is confirmation of KEPCo's commitment of keeping rates affordable and consistent to its members, particularly during periods when upward cost pressures have arisen.

Uncertainty still exists regarding carbon dioxide regulation. This has dissuaded utilities from building new coal-fired power plants, in large part due to the uncertainty of the technology to mitigate emissions and the uncertainty of a permit even being granted for the facility. Even if regulations are relaxed, as anticipated under the new administration, the likelihood of a comprehensive and permanent rollback of emission regulations is most unlikely. Our industry is reliant upon prudent investments in long-lived assets and the industry places value on regulatory certainty, stability, predictability, and gradualism. As such, coal-fired generation will likely continue to be supplanted by renewable energy and natural gas-fired generation. For many utilities, the thought of a carbon-constrained industry is quite troublesome, due to the cost and complexities of regulatory compliance. However, KEPCo is in a more favorable position. With nearly 53% of our energy originating from resources producing zero greenhouse gasses, KEPCo's exposure to generation sources impacted by current and future greenhouse gas emission regulations is far less than utilities with a large exposure to fossil fuels. If carbon dioxide regulation remains a national point of emphasis, KEPCo's cost to meet regulatory standards will be substantially lower relative to other utilities as a result of its diverse power supply.

KEPCo's owned generation assets performed exceptionally well this year. Wolf Creek completed refueling outage 21 this past fall and performed several maintenance procedures during the outage, including one that has never been done before in the United States. Wolf Creek is the first nuclear power plant in the country to use water jet peening, a mechanical process developed in Japan by Mitsubishi Nuclear Energy Services, that works a metal surface to improve its resistance to cracking on its reactor vessel nozzle welds. In the U.S., three plants have had reactor vessel nozzle cracks in the past 15 years and two have had bottom-mounted nozzle cracks. This process is expected to mitigate the risk of stress corrosion cracking for the remaining life of the plant.



Water jet peening of the Wolf Creek reactor vessel.

Iatan 2

Iatan 2, owned in part by KEPCo, is a coal-fired facility in Weston, Missouri, which provided KEPCo's Members with approximately eight percent of their energy requirements for 2016 and continues to be one of the most efficient and lowest greenhouse gas emitting coal plants in the U.S.

In May of 2016, Great Plains Energy (GPE), parent company of Kansas City Power & Light, announced its agreement to purchase Westar Energy in a transaction valued at over $12 billion. The proposed acquisition includes a significant merger premium to be paid by Great Plains and a significant amount of debt to be added to the liabilities of the consolidated company, if the transaction is ultimately approved by regulators. KEPCo has multi-faceted relationships with both GPE and Westar, including generation plant ownership, transmission dependency, and power supply arrangements. KEPCo staff worked throughout the year to protect KEPCo and its members from potential adverse impacts of this transaction on our members. KEPCo played a major role in the regulatory processes at the Federal Energy Regulatory Commission (FERC) and the Kansas Corporation Commission (KCC). The final decisions from the KCC and the FERC are expected in the spring of 2017.

The KEPCo Board of Trustees deserves a special thank you for their hard work and leadership this year. It has also been a challenging year for KEPCo staff, who have done a remarkable job meeting the special demands of 2016 while fulfilling the responsibilities necessary to operate an electric utility. Each year, the Board of Trustees and KEPCo staff demonstrate the expertise and resolve necessary to provide an economical, reliable, and safe supply of energy for our members. It's what we have done for the past four decades and it's our commitment and privilege to do the same for decades to come.

Marcus Harris
KEPCo EVP & CEO

Kevin D. Compton
KEPCo President

KEPCo staff

2016 KEPCo Highlights

KEPCo's Board of Trustees unanimously approved KEPCo's addition of a one-megawatt solar farm to its already diverse resource mix. The solar farm was aptly named Prairie Sky Solar and is located in Andover, Kansas. KEPCo Services, Inc. (KSI) designed and engineered the facility and KEPCo will operate and maintain the facility as well. The facility was put into service on February 22, 2017.


Prairie Sky Solar, a one-megawatt solar facility located in Butler County.

In August, KEPCo filed a Lien Accommodation with Rural Utilities Service to secure New Clean Renewable Energy Bonds (NCREBs) financing through CFC. The NCREBs financing will enable KEPCo to finance the Prairie Sky Solar project at a net effective interest rate of approximately one percent interest per year for 25 years.

Energy and Environmental Economics, Inc. (E3) was retained by KEPCo to provide external perspectives in the development of a strategic plan. At KEPCo's July Board of Trustees meeting, Kush Patel, Senior Managing Consultant at E3, facilitated a discussion with the KEPCo Board of Trustees and KEPCo senior staff that was used as the basis to create a strategic plan for KEPCo to meet its future goals of providing a power supply to its members in a reliable, low-cost, and low-risk manner, while beginning to migrate toward a business model recognizing and capitalizing on trends that are changing the utility industry.


Mr. Kush Patel, E3, discusses the KEPCo Strategic Plan with Scott Whittington, Lyon-Coffey, and Marcus Harris, KEPCo EVP & CEO.

KEPCo staff, completed Load Forecasts for Rolling Hills, Twin Valley, LJEC, Bluestem, Caney Valley, and Sedgwick County. Power Cost Projections were also completed for Radiant, LJEC, DS&O, Bluestem, Heartland, Rolling Hills, Sedgwick, and Caney Valley.

KEPCo Services, Inc. completed 44 engineering projects in 2016. One project of particular note was the Saddlehorn Substation project. KSI provided engineering and project management for the Ninnescah Rural Electric Cooperative Saddlehorn Substation. The new 115 kV to 4.16 kV, 7.5 MVA substation will serve a pump station on the 550 mile Saddlehorn Pipeline from Platteville, Colorado to Cushing, Oklahoma. The pipeline is a joint venture between Magellan Midstream Partners LP, along with Plains All-American Pipeline and Anadarko Petroleum Corp. The substation was put into service on schedule and under budget in early September 2016.

KSI Engineering

Wolf Creek Nuclear Generating Station

The Wolf Creek Nuclear Operating Company successfully completed refueling outage 21 in the fall and the Wolf Creek Nuclear Generating Station has run continuously since the refueling. In December, the plant set an all-time production record of 912,600 megawatt hours. Wolf Creek has made great strides with regulatory and operational performance in recent years.

KEPCo staff participated in the annual Southwest Power Pool (SPP) legislative conference. The conference was a three-day visit to Washington, D.C. to discuss issues with several members of Congress and industry lobbyists, such as federal energy legislation, as well as an update from three of the plaintiff attorneys in the Clean Power Plan lawsuit. KEPCo Staff also continued to work diligently with the KEC and Sunflower on legislative issues in Kansas and Washington, D.C. Staff testified on several bills in 2016 and tracked numerous pieces of legislation.

From l to r: Wayne Penrod and Clare Gustin, Sunflower; Mike Morley, Midwest; and Phil Wages, KEPCo, at the SPP Conference in Washington, D.C.

KEPCo continues to work with its Member cooperatives in an aggressive rural development program that has successfully created rural jobs and wealth retention in Kansas. The USDA Rural Economic Development Loan & Grant (REDLG) program provides zero interest loans to worthy projects.

In August, KEPCo submitted to the Western Area Power Administration (WAPA) an Integrated Resource Plan (IRP). Every five years, KEPCo is required to submit an IRP to WAPA. The IRP includes extensive data, such as; identifying and comparing all practicable energy efficiency and energy supply resources; an action plan with timing established by KEPCo; a description of efforts to minimize adverse environmental efforts of new resource acquisitions; public participation to comment on the IRP; conducting a load forecast; and a measurement strategy for options identified in the IRP to determine whether objectives are being met.

KEPCo's Marcus Harris, Bill Riggins, and Phil Wages, along with a contingent of another 17 Kansas electric cooperative representatives, attended the NRECA Legislative Conference in Washington, D.C. The Kansas contingent, along with 1,500 electric cooperative representatives from across the country conveyed industry issues to their respective congressional leaders.

Kansas electric cooperative representatives at the NRECA Legislative Conference in Washington, D.C.

Safety of our employees is essential to the continued operational success of KEPCo. Appropriate safety meetings are held throughout the year for KEPCo staff. KEPCo is proud to report there were no lost time accidents recorded in 2016.

KEPCo Member Cooperatives
Trustees, Alternates and Managers

Joseph Seiwert

Ark Valley Electric Cooperative Assn., Inc.
PO Box 1246, Hutchinson, KS 67504
620-662-6661
Trustee Rep. -- Joseph Seiwert
Alternate Trustee -- Jackie Holmberg
Manager -- Jackie Holmberg

Jackie Holmberg

Ken Maginley

Bluestem Electric Cooperative, Inc.
PO Box 5, Wamego, KS 66547   785-456-2212
PO Box 513, Clay Center, KS 67432   785-632-3111
Trustee Rep. -- Kenneth J. Maginley
Alternate Trustee -- Robert Ohlde
Manager -- Kenneth J. Maginley

Bob Ohlde

Kevin Compton

Brown-Atchison Electric Cooperative, Assn., Inc.
PO Box 230, Horton, KS 66439   785-486-2117
Trustee Rep. -- Kevin Compton
Alternate Trustee -- James Currie
Manager -- James Currie

Jim Currie

Dale Short

Butler Electric Cooperative Assn., Inc.
PO Box 1242, El Dorado, KS 67402   316-321-9600
Trustee Rep. -- Dale Short
Alternate Trustee -- Riley Walters
Manager -- Dale Short

Riley Walters

Dwane Kessinger

Caney Valley Electric Cooperative Assn., Inc.
PO Box 308, Cedar Vale, KS 67204   620-758-2262
Trustee Rep. -- Dwane Kessinger
Alternate Trustee -- Allen A. Zadorozny
Manager -- Allen A. Zadorozny

Allen Zadorozny


Kirk Thompson

CMS Electric Cooperative, Inc.
PO Box 790, Meade, KS 67864   620-873-2184
Trustee Rep. -- Kirk A. Thompson
Alternate Trustee -- Clifford Friesen
Manager -- Kirk A. Thompson


Cliff Friesen


Dean Allison

DS&O Electric Cooperative, Inc.
PO Box 286, Solomon, KS 67480   785-655-2011
Trustee Rep. -- Dean Allison
Alternate Trustee -- Tim Power
Manager -- Tim Power


Tim Power


Bob Reece

Flint Hills Electric Cooperative Assn., Inc.
PO Box B, Council Grove, KS 66846   620-767-5144
Trustee Rep. -- Robert E. Reece
Alternate Trustee -- Terry Olsen
Manager -- Robert E. Reece


Terry Olsen


Dennis Peckman

Heartland Rural Electric Cooperative, Inc.
PO Box 40, Girard, KS 66743   620-724-8251
Trustee Rep. -- Dennis Peckman
Alternate Trustee -- Dale Coomes
Manager -- Dale Coomes


Dale Coomes


Steven Foss

LJEC
PO Box 70, McLouth, KS 66054   913-796-6111
Trustee Rep. -- Steven O. Foss
Alternate Trustee -- Harlan Hunt
Manager -- Steven O. Foss


Harlan Hunt


Scott Whittington

Lyon-Coffey Electric Cooperative, Inc.
PO Box 229, Burlington, KS 66839   620-364-2116
Trustee Rep. -- Scott Whittington
Alternate Trustee -- Robert Converse
Manager -- Scott Whittington


Robert Converse

KEPCo Member Cooperatives
Trustees, Alternates and Managers


Paul Unruh

Ninnescah Electric Cooperative Assn., Inc.
PO Box 967, Pratt, KS 67124   620-672-5538
Trustee Rep. -- Paul Unruh
Alternate Trustee -- Teresa Miller
Manager -- Teresa Miller


Teresa Miller


Bill Peterson

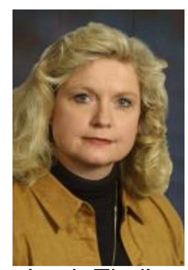
Prairie Land Electric Cooperative, Inc.
PO Box 360, Norton, KS 67654   785-877-3323
District Office, Bird City 785-734-2311
District Office, Concordia 785-243-1750
Trustee Rep. -- Bill Peterson
Alternate Trustee -- Allan J. Miller
Manager -- Allan J. Miller


Allan Miller


Dennis Duft

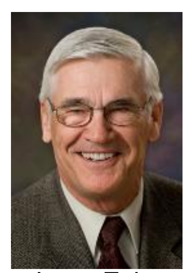
Radiant Electric Cooperative, Inc.
PO Box 390, Fredonia, KS 66736   620-378-2161
Trustee Rep. -- Dennis Duft
Alternate Trustee -- Tom Ayers
Administrative Manager -- Leah Tindle
Operations Manager -- Dennis Duft


Tom Ayers


Leah Tindle


Doug Jackson

Rolling Hills Electric Cooperative, Inc.
PO Box 339, Beloit, KS 67420   785-534-1601
Trustee Rep. -- Douglas J. Jackson
Alternate Trustee -- Leon Eck
Manager -- Douglas J. Jackson


Leon Eck


Donald Metzen

Sedgwick County Electric Cooperative Assn., Inc.
PO Box 220, Cheney, Ks 67025   316-542-3131
Trustee Rep. -- Donald Metzen
Alternate Trustee -- David Childers
Manager -- David Childers


Dave Childers


John Schon

Sumner-Cowley Electric Cooperative, Inc.
PO Box 220, Wellington, KS 67152   620-326-3356
Trustee Rep. -- John Schon
Alternate Trustee -- Cletas Rains
Manager -- Cletas Rains


Cletas Rains


Bryan Coover

Twin Valley Electric Cooperative, Inc.
PO Box 368, Altamont, KS 67330   620-784-5500
Trustee Rep. -- Bryan Coover
Alternate Trustee -- Ron Holsteen
Manager -- Ron Holsteen


Ron Holsteen


Shane Laws

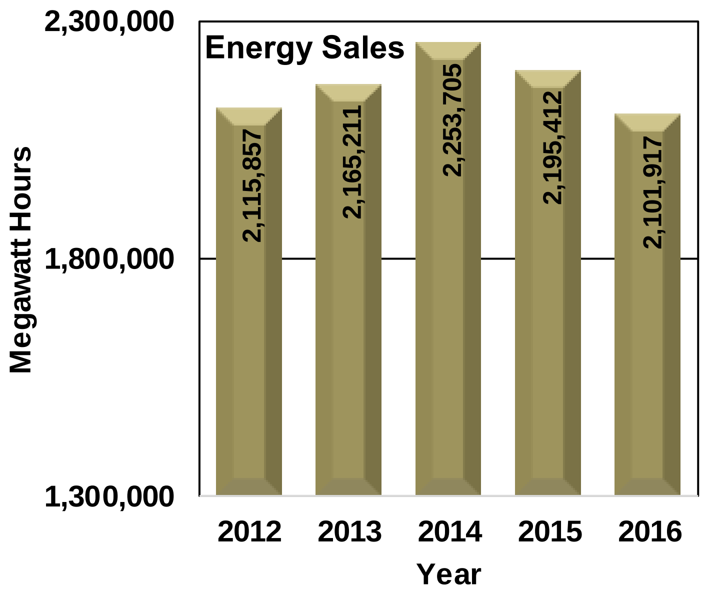
Victory Electric Cooperative Assn., Inc.
PO Box 1335, Dodge City, KS 67801   620-227-2139
Trustee Rep. -- Shane Laws
Alternate Trustee -- Daryl Tieben
Manager -- Shane Laws

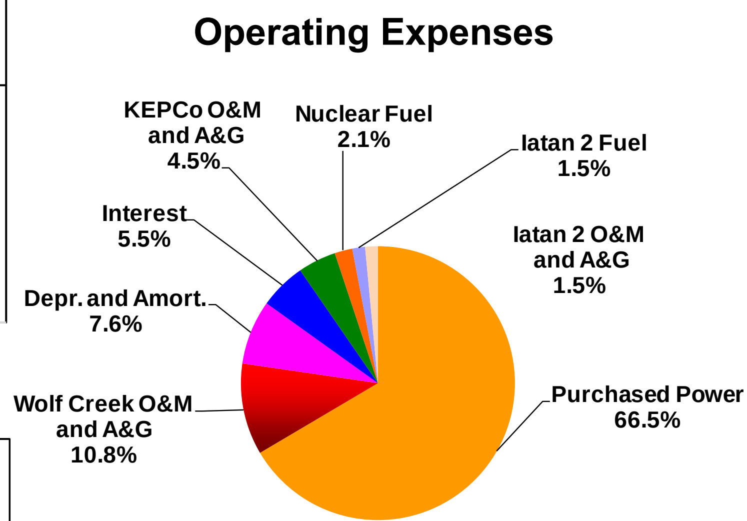

Daryl Tieben

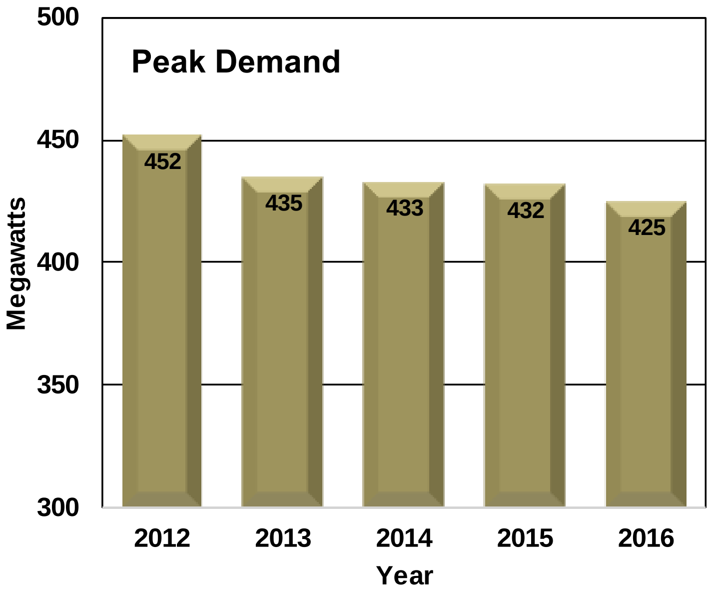
2016 - 2017 KEPCo Executive Committee

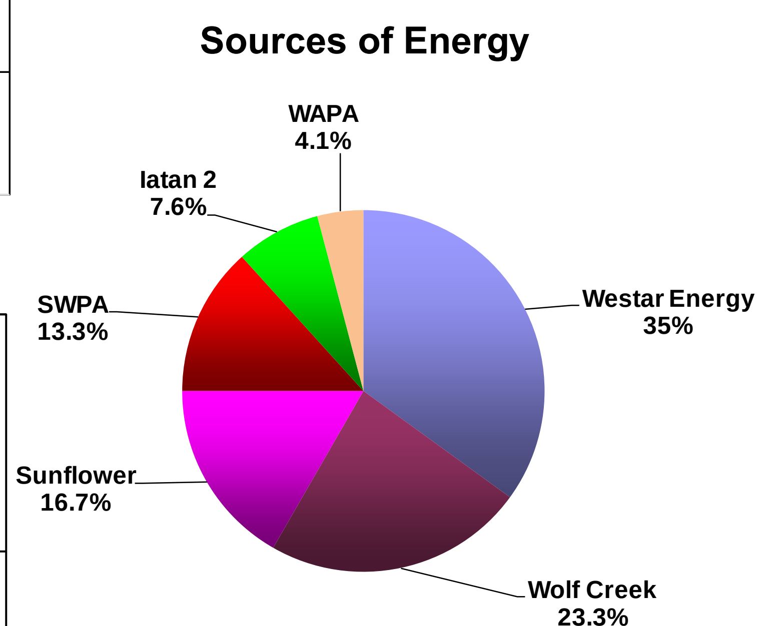
Back row, left to right: Kevin Compton - President; Dale Short - Vice President; Doug Jackson - Secretary; Dean Allison - Treasurer. Front row, left to right: Steve Foss - Executive Committee; Kirk Thompson - Executive Committee; Scott Whittington - Executive Committee.

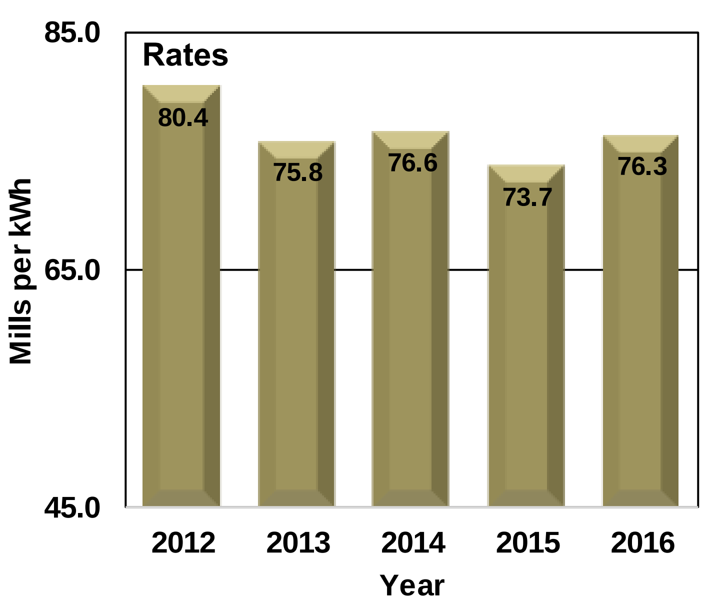
Operating Statistics











INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Kansas Electric Power Cooperative, Inc.
Topeka, Kansas

We have audited the accompanying consolidated financial statements of Kansas Electric Power Cooperative, Inc. and subsidiary ("KEPCo"), which comprise the consolidated balance sheets as of December 31, 2016 and 2015, and the related consolidated statements of margin, patronage capital, 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 consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

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

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

Basis for Qualified Opinion

As more fully described in Note 3 to the financial statements, certain depreciation and amortization methods have been used in the preparation of the 2016 and 2015 consolidated financial statements which, in our opinion, are not in accordance with accounting principles generally accepted in the United States of America. The effects on the consolidated financial statements of the aforementioned departure are explained in Note 3.

Qualified Opinion

In our opinion, except for the effects of using the aforementioned depreciation and amortization methods as discussed in Note 3, the consolidated financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of KEPCo as of December 31, 2016 and 2015, 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.

Changes in Accounting Principle

As described in Note 1 to the financial statements, the Company adopted the provisions of Accounting Standards Updates 2016-01 and 2015-07 in 2016. Our opinion is not modified with respect to these matters.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we also have issued our report dated April 13, 2017, on our consideration of KEPCo's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering KEPCo's internal control over financial reporting and compliance.

Mayer Hoffman McCann P.C.

Mayer Hoffman McCann P.C.
Topeka, Kansas
April 13, 2017

Consolidated Balance Sheets

Assets	December 31, 2016	December 31, 2015
Utility Plant		
In-service	$ 358,299,394	$ 352,889,719
Less allowances for depreciation	(162,033,119)	(155,634,830)
Net in-service	196,266,275	197,254,889
Construction work in progress	13,587,572	9,970,255
Nuclear fuel (less accumulated amortization of $21,184,282 and $23,765,663 for 2016 and 2015, respectively)	7,671,517	8,459,672
Total utility plant	217,525,364	215,684,816
Restricted Assets		
Investments in the National Utilities Cooperative Finance Corporation	11,552,345	11,108,619
Decommissioning fund	21,662,907	19,996,196
Investments in other associated organizations	306,626	282,188
Total restricted assets	33,521,878	31,387,003
Current Assets		
Cash and cash equivalents	13,097,952	6,307,421
Member account receivables	13,584,071	11,993,431
Materials and supplies inventory	6,587,450	6,645,359
Other assets and prepaid expenses	699,538	705,652
Total current assets	33,969,011	25,651,863
Other Long-term Assets		
Deferred charges		
Wolf Creek disallowed costs (less accumulated amortization of $18,692,371 and $17,935,208 for 2016 and 2015, respectively)	7,290,549	8,047,713
Wolf Creek deferred plants costs (less accumulated amortization of $46,948,793 and $43,818,873 for 2016 and 2015, respectively)	-	3,129,920
Wolf Creek decommissioning regulatory asset	(7,017,075)	(6,624,525)
Deferred incremental outage costs	2,421,944	1,968,169
Other deferred charges (less accumulated amortization of $9,782,828 and $9,681,046 for 2016 and 2015, respectively)	6,664	359,142
Unamortized debt issuance costs	8,322	23,713
Other	311,016	270,943
Prepaid Southwest Power Pool	2,320,364	-
Prepaid pension cost	810,468	941,896
Total long-term assets	6,152,252	8,116,971
Total assets	$ 291,168,505	$ 280,840,653

See Notes to the Consolidated Financial Statements

Consolidated Balance Sheets

Patronage Capital and Liabilities	December 31, 2016	December 31, 2015
Patronage Capital		
Memberships	$ 3,200	$ 3,200
Patronage capital	78,731,784	76,798,889
Accumulated other comprehensive loss	(8,440,302)	(7,284,730)
Total patronage capital	70,294,682	69,517,359
Long-term Debt	151,532,880	147,216,732
Other Long-term Liabilities		
Wolf Creek decommissioning liability	19,418,417	18,314,245
Wolf Creek pension and postretirement benefit plans	12,469,376	11,824,521
Wolf Creek deferred compensation	1,319,029	1,249,381
Other deferred credits	9,250	-
Total other long-term liabilities	33,216,072	31,388,147
Current Liabilities		
Current maturities of long-term debt	11,129,805	11,456,396
Accounts payable	14,393,732	13,053,258
Payroll and payroll-related liabilities	233,212	241,353
Deferred revenue	8,704,942	6,104,206
Accrued property taxes	1,157,946	1,312,387
Accrued income taxes	479	(45)
Accrued interest payable	504,755	550,860
Total current liabilities	36,124,871	32,718,415
Total patronage capital and liabilities	$ 291,168,505	$ 280,840,653

See Notes to the Consolidated Financial Statements

Consolidated Statements of Margin

	For the years ending December 31, 2016	2015
Operating Revenues		
Sale of electric energy	$ 160,274,808	$ 161,763,501
Operating Expenses		
Power purchased	106,192,839	105,484,032
Nuclear fuel	3,303,026	3,368,666
Plant operations	15,719,345	17,340,438
Plant maintenance	5,830,421	5,406,848
Administrative and general	7,050,359	6,205,902
Amortization of deferred charges	3,988,865	4,053,051
Depreciation and decommissioning	8,686,169	8,480,727
Total operating expenses	150,771,024	150,339,664
Net operating revenues	9,503,784	11,423,837
Interest and Other Deductions		
Interest on long-term debt	8,558,224	9,090,142
Amortization of debt issuance costs	15,391	56,343
Other deductions	139,195	150,753
Total interest and other deductions	8,712,810	9,297,238
Operating income	790,974	2,126,599
Other Income/(Expense)		
Interest income	860,660	667,857
Other income	285,944	488,538
Income tax	(4,683)	(1,854)
Total other income	1,141,921	1,154,541
Net margin	$ 1,932,895	$ 3,281,140

	2016	2015
Net Margin	$ 1,932,895	$ 3,281,140
Other comprehensive (loss)/income		
Net (loss)/earnings arising during year on pension obligation	(1,716,993)	329,818
Amortization of prior year service costs included in net periodic pension costs	561,421	764,678
Comprehensive income	$ 777,323	$ 4,375,636

See Notes to the Consolidated Financial Statements

Consolidated Statements of Patronage Capital

	Memberships	Patronage Capital	Accumulated Other Comprehensive Income (Loss)	Total
Balance at December 31, 2014	$ 3,200	$ 73,517,749	$ (8,379,226)	$ 65,141,723
Net margin	-	3,281,140	-	3,281,140
Defined benefit pension plans:				
Net earnings arising during year	-	-	329,818	329,818
Amortization of prior year service costs included in net periodic pension costs	-	-	764,678	764,678
Balance at December 31, 2015	3,200	76,798,889	(7,284,730)	69,517,359
Net margin	-	1,932,895	-	1,932,895
Defined benefit pension plans:				
Net loss arising during year	-	-	(1,716,993)	(1,716,993)
Amortization of prior year service costs included in net periodic pension costs	-	-	561,421	561,421
Balance at December 31, 2016	$ 3,200	$ 78,731,784	$ (8,440,302)	$ 70,294,682

See Notes to the Consolidated Financial Statements

Consolidated Statements of Cash Flows

	For the years ending December 31, 2016	For the years ending December 31, 2015
Cash Flows From Operating Activities		
Net margin	$ 1,932,895	$ 3,281,140
Adjustments to reconcile net margin to net cash flows from operating activities		
Depreciation and amortization	8,173,568	7,976,377
Decommissioning	1,496,722	4,400,516
Amortization of nuclear fuel	3,294,777	3,330,466
Amortization of deferred charges	3,898,956	3,901,324
Amortization or deferred incremental outage costs	2,373,725	2,387,697
Amortization of debt issuance costs	15,391	56,342
Changes in		
Member accounts receivable	(1,590,640)	2,048,341
Materials and supplies	57,909	(253,460)
Other assets and prepaid expense	(3,509,895)	1,064,675
Accounts payable	1,340,474	(1,146,640)
Payroll and payroll-related liabilities	(8,141)	(16,170)
Accrued property tax	(154,440)	(59,425)
Accrued interest payable	(46,105)	(38,864)
Accrued income taxes	525	(3,564)
Other long-term liabilities	723,753	(244,940)
Prepaid pension cost	131,427	131,428
Deferred revenue	2,600,736	2,778,884
Net cash flows from operating activities	20,731,637	29,594,127
Cash Flows From Investing Activities		
Additions to electrical plant	(10,825,350)	(13,317,627)
Additions to nuclear fuel	(2,506,622)	(1,980,468)
Reductions in deferred charges	340,606	17,720
Additions to deferred incremental outage costs	(2,827,500)	(3,170,364)
Investments in decommissioning fund assets	(1,666,711)	(617,917)
Proceeds from associated organizations	(468,165)	615,915
Investments in bond reserve assets	-	4,490,786
Proceeds from the sale of property	23,079	39,350
Net cash flows from investing activities	(17,930,663)	(13,922,605)
Cash Flows From Financing Activities		
Principal payments on long-term debt	(11,457,281)	(15,700,763)
Proceeds from issuance of long-term debt	21,229,828	9,887,110
Short term notes payable	-	(1,429,000)
Payments unapplied	(5,782,990)	(3,324,091)
Net cash flows from financing activities	3,989,557	(10,566,744)
Net increase in cash and cash equivalents	6,790,531	5,104,778
Cash and Cash Equivalents, Beginning of Year	6,307,421	1,202,643
Cash and Cash Equivalents, End of Year	$ 13,097,952	$ 6,307,421
Supplemental Disclosure of Cash Flow Information		
Interest paid	$ 8,743,500	$ 9,279,800

See Notes to the Consolidated Financial Statements

Notes to Consolidated Financial Statements

(1) Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations - Kansas Electric Power Cooperative, Inc., and its subsidiary (KEPCo), headquartered in Topeka, Kansas, was incorporated in 1975 as a tax-exempt generation and transmission cooperative (G&T). KEPCo was granted a limited certificate of convenience and authority by the Kansas Corporation Commission (KCC) in 1980 to act as a G&T public utility. It is KEPCo's responsibility to procure an adequate and reliable power supply for its 19 distribution rural electric cooperative members pursuant to all requirements of its power supply contracts. KEPCo is governed by a board of trustees representing each of its 19 members, which collectively serve approximately 120,000 electric meters in rural Kansas.

Recent Accounting Pronouncements - In January 2016, the Financial Accounting Standards Board (FASB) published Accounting Standards Update (ASU) No. 2016-01, which, among other things, changes the presentation and disclosure requirements for non-public entities related to fair value disclosures required for financial instruments not recognized at fair value. Previous GAAP required the disclosure of the fair value of debt if a non-public entity had in excess of $100 million of assets. Under the new standard, non-public entities, regardless of size, no longer need to disclose the fair value of debt. The standard is not fully effective until periods beginning after December 15, 2018; however, early adoption of this specific change is permitted. Management has decided to early adopt this provision, and will, therefore no longer disclose the fair value of financial instruments that are not reported at fair value.

In May 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2015-07, "Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent)." The ASU removes the requirement to categorize within the fair value hierarchy investments for which fair values are estimated using the net asset value per share as a practical expedient provided by FASB Accounting Standards Codification ("ASC") 820 Fair Value Measurement. Disclosures about investments in certain entities that calculate net asset value per share are limited under this ASU to investments for which the entity has elected to estimate the fair value using the net asset value practical expedient. The guidance requires retrospective application and is effective for fiscal years, and interim periods within those years, beginning after December 15, 2016. Early adoption is permitted. Management elected to early adopt the provisions of this new standard. The adoption has been reflected in Note 9 to the financial statements.

System of Accounts - KEPCo maintains its accounting records substantially in accordance with the Rural Utilities Service (RUS) Uniform Systems of Accounts and in accordance with accounting practices prescribed by the KCC.

Rates - Under a 2009 change in Kansas state law, KEPCo has elected to be exempt from KCC regulation for most purposes, including the setting of rates. Rates are set by action of the Board, subject only to statutory review by the KCC if demanded by four or more members. KEPCo's rates were last set by the KCC by an order effective September 1, 2008. KEPCo's rates now include an Energy Cost Adjustment (ECA) mechanism, an annual Demand Cost Adjustment (DCA) mechanism and a Margin Stabilization Adjustment (MSA) mechanism, allowing KEPCo to pass along increases in certain energy and demand costs to its member cooperatives.

Principles of Consolidation - The consolidated financial statements include the accounts of KEPCo and its wholly owned subsidiary, KEPCo Services, Inc. Undivided interests in jointly owned generation facilities are consolidated on a pro rata basis. All material intercompany accounts and transactions have been eliminated in consolidation.

Iatan 2 - Iatan 2 is an 850 MW high efficiency coal-fired power plant utilizing state-of-the-art environmental controls that became commercially operational December 31, 2010. KEPCo owns a 3.53% share of Iatan 2, or 30 MW. Iatan 2, located in Weston, MO, is operated and majority owned by KCP&L. KEPCo's undivided interest in Iatan 2 is consolidated on a pro rata basis. KEPCo is entitled to a proportionate share of the capacity and energy from Iatan 2, which is used to supplement a portion of KEPCo's members' requirements. KEPCo is billed on a daily basis for 3.53% of the operations, maintenance, administrative and general costs, and cost of plant additions related to Iatan 2.

Wolf Creek Nuclear Operating Corporation - KEPCo owns 6% of Wolf Creek Nuclear Operating Corporation (WCNOC), which is located near Burlington, Kansas. The remainder is owned by the Kansas City Power & Light Company (KCPL) 47% and Kansas Gas & Electric Company (KGE) 47%. KGE is a wholly owned subsidiary of Westar Energy, Inc. KCPL is a wholly owned subsidiary of Great Plains Energy, Inc. KEPCo's undivided interest in WCNOC is consolidated on a pro rata basis. KEPCo is entitled to a proportionate share of the capacity and energy from WCNOC, which is used to supplement a portion of KEPCo's members' requirements. KEPCo is billed on a daily basis for 6% of the operations, maintenance, administrative and general costs, and cost of plant additions related to WCNOC.

WCNOC’s operating license expires in 2045. Wolf Creek is regulated by the nuclear Regulatory Commission (NRC), with respect to licensing, operations and safety related requirements.

WCNOC disposes of all classes of its low-level radioactive waste at existing third-party repositories. Should disposal capability become unavailable, WCNOC is able to store its low-level radioactive waste in an on-site facility for up to three years under current regulations.

Estimates - The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Management’s estimates and assumptions include, but are not limited to, estimates of salvage values, estimated useful lives of fixed assets, estimated asset retirement obligations, incremental outage costs and pension and postretirement liability costs. Management’s estimates and assumptions are derived from and are continually evaluated based upon available information, judgment and experience.

Utility Plant and Depreciation - Utility plant is stated at cost. Cost and additions to utility plant include contractual work, direct labor, materials and interest on funds used during construction. No interest has been capitalized in 2016 and 2015. The cost of repairs and minor replacements are charged to operating expenses as appropriate. The original cost of utility plant retired and the cost of removal less salvage are charged to accumulated depreciation.

The composite depreciation rates for electric generation plant for the years ended December 31, 2016 and 2015 are 3.79% and 3.76%, respectively.

The provision for depreciation computed on a straight-line basis for electric and other components of utility plant is as follows:

Transportation and equipment	25-33 years
Office furniture and fixtures	10-20 years
Leasehold improvements	20 years
Transmission equipment (metering, communication and SCADA)	10 years

Nuclear Fuel - The cost of nuclear fuel in the process of refinement, conversion, enrichment and fabrication is recorded as a utility plant asset at original cost and is amortized to nuclear fuel expenses based upon the quantity of heat produced for the generation of electric power.

Nuclear Decommissioning - Nuclear decommissioning is a nuclear industry term for the permanent shutdown of a nuclear power plant and the removal of radioactive components in accordance with Nuclear Regulatory Commission (NRC) requirements. The NRC will terminate a plant's license and release the property for unrestricted use when a company has reduced the residual radioactivity of a nuclear plant to a level mandated by the NRC. The NRC requires companies with nuclear plants to prepare formal financial plans to fund nuclear decommissioning. These plans are designed so that sufficient funds required for nuclear decommissioning will be accumulated prior to the expiration of the license of the related nuclear power plant. Wolf Creek files a nuclear decommissioning site study with the KCC every three years.

The KCC reviews nuclear decommissioning plans in two phases. Phase one is the approval of the revised nuclear decommissioning study including the estimated costs to decommission the plant. Phase two involves the review and approval of a funding schedule prepared by the owner of the plant detailing how it plans to fund the future-year dollar amount of its pro rata share of the decommissioning costs.

In 2014, the nuclear decommissioning study was revised. Based on the study, KEPCo's share of decommissioning costs, including decontamination, dismantling and site restoration, is estimated to be $45.9 million. This amount compares to the prior site study estimate of $37.8 million. The site study cost estimate represents the estimate to decommission Wolf Creek as of the site study year. The actual nuclear decommissioning costs may vary from the estimates because of changes in regulations and technologies as well as changes in costs for labor, materials, and equipment.

KEPCo is allowed to recover nuclear decommissioning costs in its prices over a period equal to the operating license of Wolf Creek, which is through 2045. The NRC requires that funds sufficient to meet nuclear decommissioning obligations be held in a trust. KEPCo believes that the KCC approved funding level will also be sufficient to meet the NRC requirement. The consolidated financial results would be materially affected if KEPCo was not allowed to recover in its prices the full amount of the funding requirement.

KEPCo recovered in its prices and deposited in an external trust fund for nuclear decommissioning approximately $0.5 million in 2016 and $0.5 million in 2015. KEPCo records its investment in the NDT fund at fair value, which approximated $21.7 million and $20.0 million as of December 31, 2016 and 2015, respectively.

Asset retirement obligation - KEPCo recognizes and estimates the legal obligation associated with the cost to decommission Wolf Creek. KEPCo initially recognized an asset retirement obligation at fair value for the estimated cost with a corresponding amount capitalized as part of the cost of the related long-lived asset and depreciated over the useful life.

A reconciliation of the asset retirement obligation for the years ended December 31, 2016 and 2015 is as follows:

	2016	2015
Balance at January 1	$ 18,314,245	$ 13,320,625
2014 decommission study	-	3,952,587
Accretion	1,104,172	1,041,033
Balance at December 31	$ 19,418,417	$ 18,314,245

Any net margin effects are deferred in the Wolf Creek decommissioning regulatory asset and will be collected from members' in future electric rates.

Cash and Cash Equivalents - All highly liquid investments purchased with an original maturity of three months or less are considered to be cash equivalents and are stated at cost, which approximates fair value. Cash equivalents consisted primarily of repurchase agreements, money market accounts and certificates of deposit.

The Federal Deposit Insurance Corporation insures amounts held by each institution in the organization's name up to $250,000. At various times during the fiscal year, the organization's cash in bank balances exceeded the federally insured limits.

KEPCo's repurchase agreements have collateral pledged by a financial institution, which are securities that are backed by the federal government.

Accounts Receivable - Accounts receivable are stated at the amount billed to members and customers. KEPCo provides allowances for doubtful accounts, which is based upon a review of outstanding receivables, historical collection information and existing economic conditions.

Materials and Supplies Inventory - Materials and supplies inventory are valued at average cost.

Unamortized Debt Issuance Costs - Unamortized debt issue costs relate to the issuance of the floating/fixed rate pollution control revenue bonds, mortgage notes payable to the National Rural Utilities Cooperative Finance Corporation (CFC) trusts and fees for repricing the Federal Financing Bank (FFB) debt. These costs are being amortized using the effective interest method over the remaining life of the bonds and notes.

Cash Surrender Value of Life Insurance Contracts - The following amounts related to Wolf Creek Nuclear Operating Corporation (WCNOC) corporate-owned life insurance contracts, primarily with one highly rated major insurance company, are included in other long-term assets on the consolidated balance sheets.

	2016	2015
Cash surrender value of contracts	$ 7,797,588	$ 7,423,520
Borrowings against contracts	(7,528,198)	(7,167,492)
	$ 269,390	$ 256,028

Borrowings against contracts include a prepaid interest charge. KEPCo pays interest on these borrowings at a rate of 5.00% for the years ended December 31, 2016 and 2015.

Revenues - Revenues are recognized during the month the electricity is sold. Revenues from the sale of electricity are recorded based on usage by member cooperatives and customers and on contracts and scheduled power usages as appropriate.

Income Taxes - As a tax-exempt cooperative, KEPCo is exempt from income taxes under Section 501 (c)(12) of the Internal Revenue Code of 1986, as amended. Accordingly, provisions for income taxes have not been reflected in the accompanying consolidated financial statements.

KEPCo Services, Inc., a subsidiary of Kansas Electric Power Cooperative, Inc., is not exempt from income taxes.

Investments – Investments in associated organizations are carried at cost and are classified as held to maturity securities.

Notes to Consolidated Financial Statements

(2) Factors That Could Affect Future Operating Results

KEPCo currently applies accounting standards that recognize the economic effects of rate regulation and, accordingly, has recorded regulatory assets and liabilities related to its generation and transmission operations in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 980, *Regulated Operations.* In the event KEPCo determines that it no longer meets the criteria of ASC 980, the accounting impact could be a noncash charge to operations of an amount that would be material. Criteria that could give rise to the discontinuance of ASC 980 include: 1) increasing competition that restricts KEPCo's ability to establish prices to recover specific costs and 2) a significant change in the manner in which rates are set by regulators from a cost-based regulation to another form of regulation. KEPCo periodically reviews these criteria to ensure the continuing application of ASC 980 is appropriate. Any changes that would require KEPCo to discontinue the application of ASC 980 due to increased competition, regulatory changes or other events may significantly impact the valuation of KEPCo's investment in utility plant, its investment in Wolf Creek and necessitate the write-off of regulatory assets. At this time, the effect of competition and the amount of regulatory assets that could be recovered in such an environment cannot be predicted.

The 1992 Energy Policy Act began the process of restructuring the United States electric utility industry by permitting the Federal Energy Regulatory Commission to order electric utilities to allow third parties to sell electric power to wholesale customers over their transmission systems. KEPCo has elected to deregulate its rate making for sales to its members under recent statutory amendments.

Subject to the possibility of KCC review, KEPCo's member rates are now set by action of the Board. KEPCo's ability to timely recover its costs is enhanced by this change.

(3) Departures From Generally Accepted Accounting Principles

Wolf Creek Disallowed Costs - Effective October 1, 1985, the KCC issued a rate order relating to KEPCo's investment in Wolf Creek, which disallowed $26.0 million of KEPCo's investment in Wolf Creek ($7.3 million and $8.0 million net of accumulated amortization as of December 31, 2016 and 2015, respectively). A subsequent rate order, effective February 1, 1987, allows KEPCo to recover these disallowed costs and other costs related to the disallowed portion (recorded as deferred charges) for the period from September 3, 1985 through January 31, 1987, over a 27.736-year period starting February 1, 1987. Pursuant to a KCC rate order dated December 30, 1998, the disallowed portion's recovery period was extended to a 30-year period. Through December 31, 2001, KEPCo used the present worth (sinking fund) method to recover the disallowed costs, which enabled it to meet the times-interest-earned ratio and debt service requirements in the KCC rate order dated January 30, 1987. The method used by KEPCo through 2001 constituted a phase-in plan that did not meet the requirements of ASC 980- *340, Regulated Operations, Other Assets and Deferred Costs.*

Effective February 1, 2002, the KCC issued an order permitting recovery in rates of the $6.5 million cumulative difference between historical present worth (sinking fund) and straight-line amortization of Wolf Creek disallowed costs over a 15-year period. Such depreciation practice does not constitute a 282 phase-in plan that meets the requirements of ASC 980-340.

If the disallowed costs were recovered using a method in accordance with U.S. generally accepted accounting principles, the costs would have been expensed in their entirety upon implementation of the KCC order, with a corresponding decrease in patronage capital.

Amortization of the Wolf Creek disallowed costs is included in amortization of disallowed charges and amounts to $0.4 million for each of the years ended December 31, 2016, and 2015.

Effective February 1, 1987, the KCC issued an order to KEPCo requiring the use of present worth (sinking fund) depreciation and amortization. Such depreciation and amortization methods constituted phase-in plans that did not meet the requirements of ASC 980-340 *Regulated Operation, Other Assets and Deferred Costs.*

Effective February 1, 2002, the KCC issued an order that extended the depreciable life of Wolf Creek from 40 years to 60 years. This order also permitted recovery in rates of the $53.5 million cumulative difference between historical present worth (sinking fund) depreciation and amortization and straight-line depreciation and amortization of the Wolf Creek generation plant and disallowed costs over a 15-year period. Recovery of these costs in rates is included in operating revenues, and the related amortization expense is included in deferred charges in the consolidated statements of margin.

Amortization of the Wolf Creek deferred plant costs is included in amortization of deferred charges and amounts to $3.6 million for each of the years ended December 31, 2016 and 2015.

If the deferred plant costs were recovered using a method in accordance with accounting principles generally accepted in the United States of America, the costs would have been expensed in their entirety upon implementation of the KCC order, with a corresponding decrease in patronage capital.

The effect of these departures from accounting principles generally accepted in the United States of America is to overstate (understate) the following items in the consolidated financial statements by the following amounts:

	2016	2015
Deferred charges	$ -	$ 3,563,634
Patronage capital	$ -	$ 3,563,634
Net margin	$ (3,563,634)	$ (3,563,634)

(4) <u>Investments in Associated Organizations</u>

At December 31, 2016 and 2015, investments in associated organizations consisted of the following:

	2016	2015
Cooperative Financial Corporation		
Memberships	$ 1,000	$ 1,000
Capital term certificates	395,970	395,970
Patronage capital certificates	1,831,901	1,575,231
Equity term certificates	9,323,474	9,136,418
	11,552,345	11,108,619
Other	306,626	282,188
	$ 11,858,971	$ 11,390,807

Notes to Consolidated Financial Statements

(5) Deferred Charges

Deferred Incremental Outage Costs - In 1991, the KCC issued an order that allowed KEPCo to defer its 6% share of the incremental operating, maintenance and replacement power costs associated with the periodic refueling of Wolf Creek. Such costs are deferred during each refueling outage and are being amortized over the approximate 18-month operating cycle coinciding with the recognition of the related revenues. Additions to the deferred incremental outage costs were $2.8 million and $3.2 million in 2016 and 2015, respectively. The current year amortization of the deferred incremental outage costs was $2.4 million and $2.4 million in 2016 and 2015, respectively.

Other Deferred Charges - KEPCo includes in other deferred charges the early call premium resulting from refinancing. These early call premiums are amortized using the effective interest method over the remaining life of the new agreements.

(6) Prepaid Southwest Power Pool

During 2016, KEPCo was assessed historical charges in the amount of $2,442,488 from Southwest Power Pool related to the Z2 billing issue for generation system upgrades from 2008-2016. The total amount of historical charges was paid in October 2016, and will be amortized over a five year period, ending October 2021. Balance as of December 31, 2016 was $2,320,364.

(7) Line of Credit

As of December 31, 2016, KEPCo has a $20 million line of credit available with the Cooperative Finance Corporation. There were no funds borrowed against the line of credit at December 31, 2016 or 2015. The line of credit requires the Cooperative to pay down the balance to zero annually. Interest rates vary and were 2.50% and 2.90% at December 31, 2016, and 2015, respectively. This line of credit expires in March 03, 2017.

At December 31, 2016, KEPCo has a $10 million line of credit available with CoBank, ACB. There were no funds borrowed against the line of credit at December 31, 2016 or 2015. Interest rate options, as selected by the Company, are a weekly quoted variable rate in which CoBank establishes a rate on the first business day of each week or a LIBOR option at a fixed rate equal to LIBOR plus 1.6%. This line of credit expires May 30, 2017.

(8) Long-Term Debt

Long-term debt consists of mortgage notes payable to the United States of America acting through the Federal Financing Board, the CFC and others. Substantially all of KEPCo's assets are pledged as collateral.

Notes to Consolidated Financial Statements

The terms of the notes as of December 31 are as follows:

	2016	2015
Mortgage notes payable to the FFB at fixed rates varying from .818% to 9.21%, payable in quarterly installments through 2043	$ 65,406,702	$ 59,050,988
Mortgage notes payable to the Grantor Trust Series 1997 at a rate of 7.522%, payable semi-annually, principal payments commencing in 1999 and continuing annually through 2017	3,240,000	7,240,000
Note payable to CoBank at a rate of 3.03%, payable in quarterly installments through 2023	866,802	991,073
Mortgage notes payable, equity certificate loans and member capital security notes to the CFC at fixed rates of 3.25% to 7.50%, payable quarterly through 2045	93,149,181	91,391,067
	162,662,685	158,673,128
Less current maturities	(11,129,805)	(11,456,396)
	$ 151,532,880	$ 147,216,732

Aggregate maturities of long-term debt for the next five years and thereafter are as follows:

2017	$ 11,129,805
2018	7,980,579
2019	8,334,149
2020	8,476,343
2021	7,564,990
Thereafter	119,176,819
	$ 162,662,685

Restrictive covenants related to the CFC debt require KEPCo to design rates that would enable it to maintain a times-interest earned ratio of at least 1.05 and debt-service coverage ratio of at least 1.0, on average, in the two best years out of the three most recent calendar years. The covenants also prohibit distribution of net patronage capital or margins until, after giving effect to any such distribution, total patronage capital equals or exceeds 20% of total assets, unless such distribution is approved by the Rural Utility Service. KEPCo was in compliance with such restrictive covenants as of December 31, 2016 and 2015.

Restriction covenants related to the CoBank debt require KEPCo to design rates that would enable it to maintain a debt-service coverage ratio, as defined by CoBank of at least 1.10. KEPCo was in compliance with the restrictive covenant as of December 31, 2016 and 2015.

In 1997, KEPCo refinanced its mortgage notes payable to the 1988 CFC Grantor Trust through the establishment of a new CFC Grantor Trust Series 1997 (the Series 1997 Trust) by CFC. This refinancing reduced the guaranteed interest rate payable on the mortgage notes to a fixed rate of 7.522%. The mortgage notes payable are pre-payable at any time with no prepayment penalties. The Trust holds certain rights the Cooperative assigned to the Trust under an interest rate swap agreement. The swap agreement was put into place in order to mitigate the interest rate risk inherent in the Trust, which holds a fixed rate asset with a variable rate obligation.

The swap agreement terminates in 2017, but is subject to early termination upon the early redemption of the debt. However, any termination costs relating to the termination of the assigned interest rate swaps is KEPCo's responsibility. At December 31, 2016, the termination obligation associated with the assigned swap agreement to early retire the mortgage notes payable is approximately $186,800.

KEPCo also is exposed to possible credit loss in the event of noncompliance by the counterparty to the swap agreement. However, KEPCo does not anticipate nonperformance by the counterparty.

(9) <u>Benefit Plans</u>

National Rural Electric Cooperative Association (NRECA) Retirement and Security Program
KEPCo participates in the NRECA Retirement and Security Program for its employees. The NRECA is a defined benefit pension plan qualified under Section 401 and tax-exempt under Section 501(a) of the Internal Revenue Code. It is a multiemployer plan under the accounting standards. The plan sponsor's Employer Identification Number is 53-0116145 and the Plan Number is 333.

A unique characteristic of a multiemployer plan compared to a single employer plan is that all plan assets are available to pay benefits of any plan participant. Separate asset accounts are not maintained for participating employers. This means that assets contributed by one employer may be used to provide benefits to employees of other participating employers.

KEPCo's contributions to the RS Plan in 2016 and 2015 represented less than 5 percent of the total contributions made to the plan by all participating employers. KEPCo made contributions to the RS Plan of $470,000, and $410,000, for the years ended December 31, 2016 and 2015, respectively. There have been no significant changes that affect the comparability of 2016 and 2015 contributions.

For the RS Plan, a "zone status" determination is not required, and therefore not determined, under the Pension Protection Act (PPA) of 2006. In addition, the accumulated benefit obligations and plan assets are not determined or allocated separately by individual employer. In total, the RS Plan was over 80 percent funded on January 1, 2016 and over 80 percent funded on January 1, 2015 based on the PPA funding target and PPA actuarial value of assets on those dates.

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

At the December 2012 meeting of the I&FS Committee of the NRECA Board of Directors, the Committee approved an option to allow participating cooperatives in the RS Plan to make a contribution prepayment and reduce future required contributions. The prepayment amount is a cooperative's share, as of January 1, 2013, of future contributions required to fund the RS Plan's unfunded value of benefits earned to date using RS Plan actuarial valuation assumptions. The prepayment amount will typically equal approximately 2.5 times a cooperative's annual RS Plan required contribution as of January 1, 2013. After making the prepayment, for most cooperatives the billing rate is reduced by approximately

25%, retroactive to the January 1st of the year in which the amount is paid to the RS Plan. The 25% differential in billing rates is expected to continue for approximately 15 years from January 1, 2013. However changes in interest rates, asset returns and other plan experience different from expected, plan assumption changes and other factors may have an impact on the differential in billing rates and the 15 year period.

NRECA Savings 401(k) Plan - All employees of KEPCo are eligible to participate in the NRECA Savings 401(k) Plan. Under the plan, KEPCo contributes an amount not to exceed 5%, dependent upon each employee's level of participation and completion of one year of service, of the respective employee's base pay to provide additional retirement benefits. KEPCo contributed approximately $120,000 and $100,000 to the plan for the years ended December 31, 2016 and 2015.

WCNOC Pension and Postretirement Plans - KEPCo has an obligation to the WCNOC retirement, supplemental retirement and postretirement medical plans for its 6% ownership interest in Wolf Creek. The plans provide for benefits upon retirement, normally at age 65. In accordance with the Employee Retirement Income Security Act of 1974, KEPCo has satisfied its minimum funding requirements. Benefits under the plans reflect the employee's compensation, years of service and age at retirement.

Notes to Consolidated Financial Statements

WCNOC uses a measurement date of December 31 for its retirement plan, supplemental retirement plan and postretirement plan (collectively, the Plans). Information about KEPCo's 6% of the Plans' funded status follows:

	Pension Benefits		Postretirement Benefits	
	2016	2015	2016	2015
Change in benefit obligation:				
Benefit obligation beginning of year	$ 26,351,186	$ 26,849,361	$ 994,854	$ 1,051,925
Service cost	861,508	969,547	16,209	17,627
Interest cost	1,232,522	1,150,940	41,529	40,150
Plan participants' contributions	-	-	126,206	119,195
Benefits paid	(890,285)	(793,702)	(195,427)	(207,086)
Actuarial (gains) losses	1,682,308	(1,824,960)	(62,247)	(26,957)
Benefit obligations, end of year	$ 29,237,239	$ 26,351,186	$ 921,124	$ 994,854
Change in plan assets:				
Fair value of plan assets, beginning of year	$ 15,526,150	$ 15,914,004	$ 13,369	$ 762
Actual return on plan assets	1,144,696	(367,512)	(456)	-
Employer contributions	1,891,919	741,046	58,500	100,500
Plan participants' contributions	-	-	126,206	119,195
Benefits paid	(857,971)	(761,388)	(195,427)	(207,088)
Fair value of plan assets, end of year	17,704,794	15,526,150	2,192	13,369
Funded status, end of year	$ (11,532,445)	$ (10,825,036)	$ (918,931)	$ (981,485)

Amounts recognized in the consolidated balance sheets:

	2016	2015
Other long-term liabilities		
Wolf Creek pension and postretirement benefit plans	$ 12,451,376	$ 11,806,521
Wolf Creek provision for injuries	18,000	18,000
Total other long-term liabilities	$ 12,469,376	$ 11,824,521

Notes to Consolidated Financial Statements

Amounts recognized in accumulated other comprehensive income (loss) not yet recognized as components of net periodic benefit cost consist of:

	Pension Benefits		Postretirement Benefits	
	2016	2015	2016	2015
Net (loss) gain	$ (8,466,849)	$ (7,244,265)	$ 83,474	$ 23,533
Prior service cost	(56,927)	(63,998)	-	-
	$ (8,523,776)	$ (7,308,263)	$ 83,474	$ 23,533

Information for the pension plan with an accumulated benefit obligation in excess of plan assets:

	Pension Benefits		Postretirement Benefits	
	2016	2015	2016	2015
Projected benefit obligation	$29,237,239	$26,351,186	$ 921,124	$ 994,854
Accumulated benefit obligation	$25,782,492	$23,070,405	$ -	$ -
Fair value of plan assets	$17,704,794	$15,526,150	$ 2,193	$ 13,370

Weighted average actuarial assumptions used to determine net periodic benefit obligation:

	Pension Benefits		Postretirement Benefits	
	2016	2015	2016	2015
Discount rate	4.26%	4.61%	3.95%	4.27%
Annual salary increase rate	4.00%	4.00%	N/A	N/A

Wolf Creek uses a measurement date of December 31 for its pension and post-retirement benefit plans. The discount rate to determine the current year pension obligation and the following year's pension expense is based on a bond selection-settlement portfolio approach. This approach develops a discount rate by selecting a portfolio of high quality, non-callable corporate bonds that generate a sufficient cash flow to provide for the projected benefit payments of the plan. After the bond portfolio is selected, a single interest rate is determined that equates the present value of the plan's projected benefit payments discounted at this rate with the market value of the bonds selected.

	Pension Benefits		Postretirement Benefits	
	2016	2015	2016	2015
Components of net periodic cost (benefit):				
Service cost	$ 861,508	$ 969,548	$ 16,209	$ 17,628
Interest cost	1,232,522	1,150,940	41,529	40,150
Expected return on plan assets	(1,241,172)	(1,154,587)	-	-
Amortization				
Transition obligation, net	-	-	-	-
Prior service cost	7,071	7,325	-	-
Actuarial loss, net	556,200	757,059	(1,850)	294
Net periodic cost	$ 1,416,129	$ 1,730,285	$ 55,888	$ 58,072

Other changes in plan obligations recognized in other comprehensive income:				
Current year actuarial loss(gain)	$ 1,778,784	$ (302,862)	$ (61,791)	$ (26,957)
Amortization of actuarial loss	(556,200)	(757,059)	1,850	(294)
Amortization of prior service cost	(7,071)	(7,325)	-	-
Amortization of transition obligation	-	-	-	-
Total recognized in other comprehensive income	1,215,513	(1,067,246)	(59,941)	(27,251)
Total recognized in net periodic cost and other comprehensive income	$ 2,631,642	$ 663,040	$ (4,053)	$ 30,821
Weighted average actuarial assumptions used to determine net periodic cost:				
Discount rate	4.61%	4.20%	4.27%	3.89%
Expected long term return on plan assets	7.25%	7.50%	N/A	N/A
Compensation rate increase	4.00%	4.00%	N/A	N/A

KEPCo estimates they will amortize the following amounts from regulatory assets into net periodic cost in 2017:

	Pension Benefits	Postretirement Benefits
Actuarial loss	$ 635,663	$ (6,441)
Prior service cost	7,071	-
Total	$ 642,734	$ (6,441)

The expected long-term rate of return on plan assets is based on historical and projected rates of return for current and planned asset classes in the plans' investment portfolios. Assumed projected rates of return for each asset class were selected after analyzing long-term historical experience and future expectations of the volatility of the various asset classes. Based on target asset allocations for each asset class, the overall expected rate of return for the portfolios was developed, adjusted for historical and expected experience of active portfolio management results compared to benchmark returns and for the effect of expenses paid from plan assets.

For measurement purposes, the assumed annual health care cost growth rates were as follows:

	2016	2015
Health care cost trend rate assumed for next year	6.50%	7.00%
Rate to which the cost trend rate is assumed to decline	5.00%	5.00%
Year that the rate reaches the ultimate trend rate	2020	2020

The health care cost trend rate affects the projected benefit obligation. A 1% change in assumed health care cost growth rates would have effects shown in the following table:

	One percentage point increase	One percentage point decrease
Effect on total service and interest cost	(893)	921
Effect on post-retirement benefit obligation	(16,058)	16,972

In 2012, Wolf Creek changed its investment advisor resulting in the sale of its then existing levels 1, 2 and 3 investments and the purchase of other level 2 and 3 investments. Its pension and post-retirement plan investment strategy is to manage assets in a prudent manner with regard to preserving principal while providing reasonable returns. It has adopted a long-term investment horizon such that the chances and duration of investment losses are carefully weighed against the long-term potential for appreciation of assets. Part of its strategy includes managing interest rate sensitivity of plan assets relative to the associated liabilities. The primary objective of the pension plan is to provide a source of retirement income for its participants and beneficiaries, and the primary financial objective of the plan is to improve its funded status. The primary objective of the post-retirement benefit plan is growth in assets and preservation of principal, while minimizing interim volatility, to meet anticipated claims of plan participants. Wolf Creek delegates the management of its pension and post-retirement benefit plan assets to independent investment advisors who hire and dismiss investment managers based upon various factors. The investment advisors strive to diversify investments across asset classes, sectors and manager styles to minimize the risk of large losses, based upon objectives and risk tolerance specified by Wolf Creek, which include allowable and/or prohibited investment types. It measures and monitors investment risk on an ongoing basis through quarterly investment portfolio reviews and annual liability measurements.

The target allocations for Wolf Creek's pension plan assets are 31% to international equity securities, 25% to domestic equity securities, 25% to debt securities, 10% to real estate securities, 5% to commodity investments and 4% to other investments. The investments in both international and domestic equity include investments in large-, mid- and small-cap companies and investment funds with underlying investments similar to those previously mentioned. The investments in debt include core and high-yield bonds. Core bonds include funds invested in investment grade debt securities of corporate entities, obligations of U.S. and foreign governments and their agencies and private debt securities. High-yield bonds include a fund with underlying investments in non-investment grade debt securities of corporate entities, private placements and bank debt. Real estate securities include funds invested in commercial and residential real estate properties while commodity investments include funds invested in commodity-related instruments.

All of Wolf Creek's pension plan assets are recorded at fair value using daily net asset values as reported by the trustee.

Similar to other assets measured at fair value, GAAP establishes a hierarchal framework for disclosing the transparency of the inputs utilized in measuring pension and post-retirement benefit plan assets at fair value. From time to time, the Wolf Creek pension trust may buy and sell investments resulting in changes within the hierarchy. Where quoted market prices are available in an active market, plan assets are classified within Level 1 of the valuation hierarchy. Level 1 plan assets include cash equivalents, equity and debt investments. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of plan assets with similar characteristics or discounted cash flows. Level 2 investments include cash equivalents, equity, debt and commodity investments. In certain cases where Level 1 or Level 2 inputs are not available, plan assets are classified within Level 3 of the hierarchy and include certain real estate investments. Significant inputs and valuation techniques used in measuring Level 3 fair values include market discount rates, projected cash flows and the estimated value into perpetuity. Investments that do not have a readily determinable fair value are measured at NAV. These investments do not consider the observability of inputs, therefore, they are not included within the fair value hierarchy. We include in this category investments in private equity, real estate and alternative investment funds that do not have a readily determinable fair value. The underlying alternative investments include collateralized debt obligations, mezzanine debt and a variety of other investments.

Notes to Consolidated Financial Statements

The following table provides the fair value of KEPCo's 6% share of Wolf Creek's pension plan assets and the corresponding level of hierarchy as of December 31, 2016 and 2015:

		Fair Value Measurements Using		
December 31, 2016	Fair Value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Cash equivalents	$ 76,575	$ -	$ 76,575	$ -
Equity securities				
U.S.	4,415,136	-	4,415,136	-
International	5,523,744	-	5,523,744	-
Debt securities				
Core bonds	4,474,271	-	4,474,271	-
Alternative investments	1,796,594		1,796,594	-
Total	$ 16,286,320	$ -	$ 16,286,320	$ -
Investments measured at NAV	1,418,474			
Total	$ 17,704,794			

		Fair Value Measurements Using		
December 31, 2015	Fair Value	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Cash equivalents	$ 66,902	$ -	$ 66,902	$ -
Equity securities				
U.S.	3,893,997	-	3,893,997	-
International	4,810,439	-	4,810,439	-
Debt securities	-			
Core bonds	3,866,471	-	3,866,471	-
Commodities	741,858	-	741,858	-
Real estate	781,678	-	781,678	-
Total	$ 14,161,345	$ -	$ 14,161,345	$ -
Investments measured at NAV	1,364,805			
Total	$ 15,526,150			

Estimated future benefit payments as of December 31, 2016, for the Plans, which reflect expected future services, are as follows:

	Pension Benefits		Postretirement Benefits	
	To/from trust	From company assets	To/from trust	From company assets
Expected contributions:				
2017	$ 1,380,000	$ -	$ 72,254	$ -
Expected benefit payments:				
2017	$ 913,684	$ 32,325	$ 250,615	$ -
2018	1,029,583	32,023	287,843	-
2019	1,143,591	32,199	325,899	-
2020	1,256,447	32,205	366,871	-
2021	1,366,180	31,991	407,719	-
2022-2026	8,427,597	165,769	2,573,891	-

(10) Commitments and Contingencies

Current Economic Environment - KEPCo considers the current economic conditions when planning for future power supply and liquidity needs. The current economic climate may also affect the Cooperative's ability to obtain financing.

Given the volatility of the current economic conditions, the values of assets and liabilities recorded in the financial statements could change rapidly, resulting in material future adjustments that could negatively impact the Cooperative's ability to meet debt covenants or maintain sufficient liquidity. Currently under state statutes, the Cooperative's rate making is deregulated and, therefore, expects to be able to recover any economic losses through future rates.

Litigation - The Cooperative is subject to claims and lawsuits that arise primarily in the ordinary course of business. It is the opinion of management that the disposition or ultimate resolution of such claims and lawsuits will not have an adverse effect on the consolidated financial position, results of operations and cash flows of the Cooperative.

There is a provision in the Wolf Creek operating agreement whereby the owners treat certain claims and losses arising out of the operations of Wolf Creek as a cost to be borne by the owners separately (but not jointly) in proportion to their ownership shares. Each of the owners has agreed to indemnify the others in such cases.

Letter of Credit - KEPCo has an open letter of credit with the Cooperative Finance Committee in the amount of $1,500,000 which matures May 23, 2017. The letter of credit is intended to provide financial security to Southwest Power Pool pursuant to its credit policy.

Notes to Consolidated Financial Statements

Nuclear Liability Insurance - Pursuant to the Price-Anderson Act, KEPCo insures against public nuclear liability claims resulting from nuclear incidents to the required limit of public liability, which is approximately $13.4 billion. This limit of liability consists of the maximum available commercial insurance of $375.0 million and the remaining $13.0 billion is provided through mandatory participation in an industry-wide retrospective assessment program. For incidents after January 1, 2017, this commercial insurance limit increased to $450.0 million. Under this retrospective assessment program, the owners of Wolf Creek are jointly and severally subject to an assessment of up to $127.3 million (KEPCo's share is $7.64 million), payable at no more than $19.0 million (KEPCo's share is $1.14 million) per incident per year per reactor for any commercial U.S. nuclear reactor qualifying incident. Both the total and yearly assessment is subject to an inflationary adjustment every five years with the next adjustment in 2018. In addition, Congress could impose additional revenue-raising measures to pay claims.

The owners of Wolf Creek carry decontamination liability, nuclear property damage and premature nuclear decommissioning liability insurance for Wolf Creek totaling approximately $2.8 billion. (KEPCo's share is $168 million) Insurance coverage for non-nuclear property damage accidents total approximately $2.3 billion. In the event of an extraordinary nuclear accident, insurance proceeds must first be used for reactor stabilization and site decontamination in accordance with a plan mandated by the NRC. Our share of any remaining proceeds can be used to pay for property damage or, if certain requirements are met, including decommissioning the plant, toward a shortfall in the NDT fund.

The owners also carry additional insurance with NEIL to help cover costs of replacement power and other extra expenses incurred during a prolonged outage resulting from accidental property damage at Wolf Creek. If significant losses were incurred at any of the nuclear plants insured under the NEIL policies, we may be subject to retrospective assessments under the current policies of approximately $37.5 million (KEPCo's share is $2.25 million).

Although KEPCo maintain various insurance policies to provide coverage for potential losses and liabilities resulting from an accident or an extended outage, KEPCo's insurance coverage may not be adequate to cover the costs that could result from a catastrophic accident or extended outage at Wolf Creek. Any substantial losses not covered by insurance, to the extent not recoverable in KEPCo's prices, would have a material effect on our consolidated financial results.

Decommissioning Insurances - KEPCo carries premature decommissioning insurance that has several restrictions, one of which can only be used if Wolf Creek incurs an accident exceeding $500 million in expenses to safely stabilize the reactor, to decontaminate the reactor and reactor station site in accordance with a plan approved by the Nuclear Regulatory Commission (NRC) and to pay for on-site property damages.

Once the NRC property rule requiring insurance proceeds to be used first for stabilization and decontamination has been complied with, the premature decommissioning coverage could pay for the decommissioning fund shortfall in the event an accident at Wolf Creek exceeds $500 million in covered damages and causes Wolf Creek to be prematurely decommissioned.

Nuclear Fuel Commitments - At December 31, 2016, KEPCo's share of WCNOC's nuclear fuel commitments was approximately $4.2 million for uranium concentrates, $10.8 million for conversion, $10.6 million for enrichment, and $3.8 million for fabrication, all expiring at various times from 2022 through 2045.

Purchase Power Commitments - KEPCo has supply contracts with various utility companies to purchase power to supplement generation in the given service areas. KEPCo has provided the Southwest Power Pool a letter of credit to help insure power is available if needed.

Notes to Consolidated Financial Statements

(11) <u>Fair Value of Assets and Liabilities</u>

ASC Topic 820, *Fair Value Measurements,* defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

ASC Topic 820 also establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

Level 1 Quoted prices in active markets for identical assets or liabilities

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value on a recurring basis and recognized in the accompanying consolidated balance sheets, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy.

Decommissioning Fund - The decommissioning fund consists of various mutual funds where fair value is determined by quoted market prices in an active market and, as such, are classified within Level 1 of the valuation hierarchy.

The following table presents the fair value measurements of assets recognized in the accompanying consolidated balance sheets measured at fair value on a recurring basis and the level within the ASC 820 fair value hierarchy in which the fair value measurements fall at December 31, 2016:

		Fair Value Measurements Using		
	Fair Value	Quoted price in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Decommissioning fund				
Domestic fund	$ 11,909,616	$ 11,909,616	$ -	$ -
International fund	1,468,769	1,468,769	-	-
Domestic bond fund	7,670,901	7,670,901	-	-
Money market	613,621	613,621	-	-
Total	$ 21,662,907	$ 21,662,907	$ -	$ -

The following table presents the fair value measurements of assets recognized in the accompanying consolidated balance sheets measured at fair value on a recurring basis and the level within the ASC 820 fair value hierarchy in which the fair value measurements fall at December 31, 2015:

		Fair Value Measurements Using		
	Fair Value	Quoted price in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Decommissioning fund				
Domestic fund	$ 10,865,536	$ 10,865,536	$ -	$ -
International fund	1,440,767	1,440,767	-	-
Domestic bond fund	7,189,822	7,189,822	-	-
Money market	500,071	500,071	-	-
Total	$ 19,996,196	$ 19,996,196	$ -	$ -

(12) Patronage Capital

In accordance with KEPCo's bylaws, KEPCo's current margins are to be allocated to members. KEPCo's current policy is to allocate to the members based on revenues collected from the members as a percentage of total revenues. If KEPCo's consolidated financial statements were adjusted to reflect accounting principles generally accepted in the United Stated of America, total patronage capital would be substantially less. As noted in the consolidated statements of changes in patronage capital, no patronage capital distributions were made to members in 2016 and 2015.

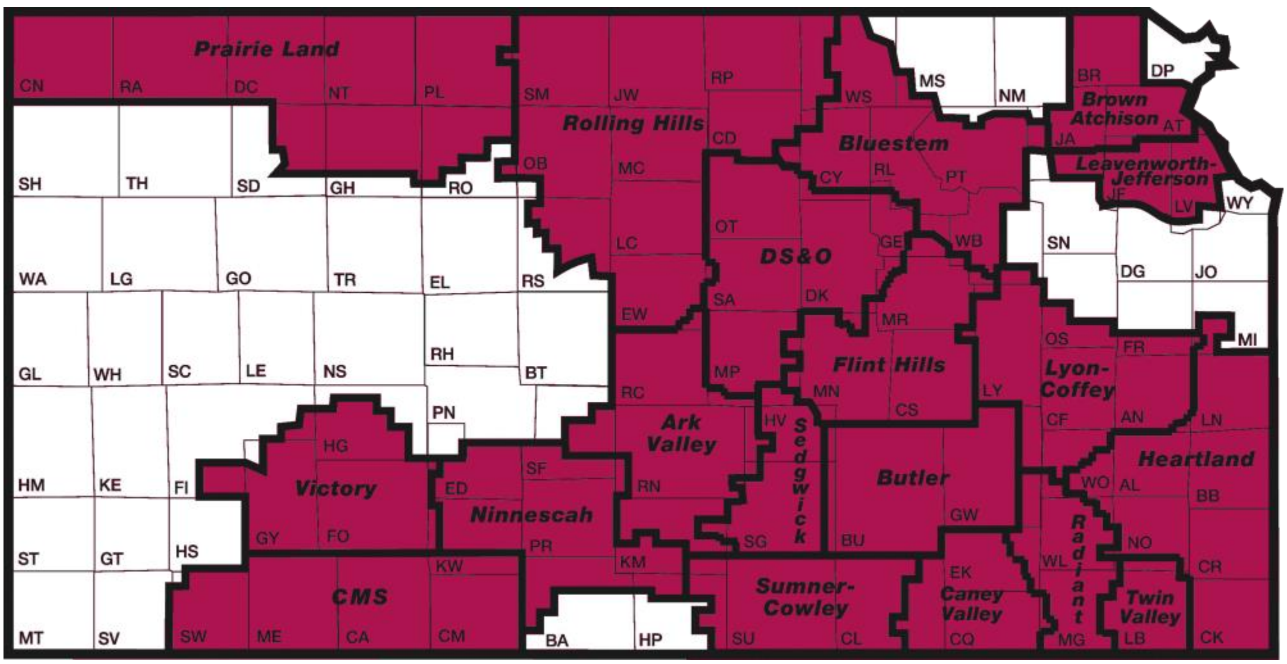
(13) Subsequent Events

The Company has evaluated subsequent events through April 13, 2017, which is the date the financial statements were available to be issued. No events were significant enough to warrant disclosures in the accompanying financial statements or notes.

KEPCo's Mission Statement

KEPCo exists on behalf of its Members to produce, procure, transmit, deliver and maintain a reliable supply of wholesale electricity within financial guidelines and risk tolerances established by the Board.

KEPCo Member System Map



KEPCo's Vision Statement

KEPCo will work to provide Consumer-Members the best possible value in reliable electricity and to play an active role in helping improve the economy and quality of life.

Kansas Electric
Power Cooperative, Inc.

A Touchstone Energy® Cooperative

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