

ANNUAL REPORT



2016 annual meeting

Thursday, June 16, 2016
Linton High School, Linton



KEM
Electric Cooperative, Inc.



Your Touchstone Energy® Cooperative

OFFICIAL NOTICE OF THE ANNUAL MEETING OF MEMBERS

The annual meeting of the members of KEM Electric Cooperative Inc. will be held in the Linton High School auditorium, Linton, N.D., at 7 p.m. on Thursday, June 16, 2016, to take action on the following matters:

1. Election of two directors

In connection with the election of two directors scheduled to be held at this meeting, the following members have been nominated for director by petition, which is in accordance with the bylaws of the cooperative:

District 3

Mark Dohn, Ventura
Neil Meidinger, Zeeland
Allen Wolf, Zeeland

District At Large

Dean Hummel, Hague

2. Report of officers and directors and for the transaction of such other and further business that may come before the meeting or any adjournment or adjournments thereof.

Dated: May 9, 2016

/s/ Carter Vander Wal, secretary

KEM Electric Cooperative Inc. 2016 annual meeting

Thursday, June 16, 2016

Linton High School auditorium
Linton, N.D.

5:30-7 p.m. – Registration

- Member gifts
- Health fair by Emmons County Public Health
- Electric technologies booth by Basin Electric Power Cooperative will be on display throughout the evening.

5:30-7 p.m. – Meal compliments of KEM

7 p.m. – Business meeting

- Election of directors
- Report of officers
- Innovative Energy Alliance report

- Door prizes
- Grand prize and \$400 cash membership prize will be drawn. (All members' names will be entered for the cash prize. Must be present to win.)

7 p.m. – Children's Fun Night

- Activities for children ages 3-10
- All children will receive a door prize

If you need assistance because of a disability or physical handicap, please contact KEM Electric at 701-254-4666 or 800-472-2673

KEM ELECTRIC COOPERATIVE EMPLOYEES

CO-GENERAL MANAGERS/CEO'S

Chris Baumgartner
Don Franklund

STAFF

Gary Hulm, line superintendent
Alex Craigmile, business manager

OFFICE EMPLOYEES

Dawn Schiele, executive assistant
Kirk Praus, member support technician
Marcy Sanders, service dispatcher
Gerald and Ramona Birdsell, custodians

LINE DEPARTMENT

Linton office
Jeff Gefre, area foreman
Tim Dockter, area foreman
Dave Twardoski, journeyman lineworker
Dale Nagel, journeyman lineworker
Kevin Horner, journeyman lineworker
Austin Ohlhauser, journeyman lineworker
Jeff Werner, warehouseman/purchasing clerk

Steele outpost

Paul Hewitt, area foreman
Jake Zink, journeyman lineworker
Martin Messer, journeyman lineworker



Dewald

Chairman's report **KEM Electric Cooperative faces challenges**

BY DEAN DEWALD

Greetings to the members, friends and employees of KEM Electric Cooperative from the board of directors. Our weather this past year was very similar to the prior year. We have had a mild winter, with little snow, but much-needed moisture in April.

KEM Electric had a good year again, although sales are down due to the mild weather. The cooperative had very little storm damage this past year.

With this being an election year, it is very disappointing how the current administration is attacking the coal industry. Coal has been the backbone of our industry since its beginning. I wonder what will happen if the price of natural gas skyrockets again or if the subsidies are not maintained for the wind generation. It is sad how the politicians have the answers in election years, but get very little done the rest of the time. The message when I became a director was that rural co-ops are going to live and die in politics. This has become more true now than ever.

At this annual meeting, Milton Brandner has decided not to run for re-election. I would like to personally thank Milton for his years of service and dedication. Milton and former director Adolph Feyereisen have been committed to the co-op family. They have both been very good mentors to me and to many others. Thank you to both!

I would like to thank the members and the board for the support they have given me this past year. The board and management team are doing all they can to control costs and plan for the future.

Please plan to attend your annual meeting in Linton June 16. We hope to see you there! ■



KEM Electric Cooperative

BOARD OF DIRECTORS



District 1
John Beck
Director
Linton



District 2
**Carter Vander
Wal**
Secretary-
treasurer
Pollock, S.D.



District 3
**Milton
Brandner**
Director
Zeeland



District 4
Victor J. Wald
Vice chairman
Napoleon



District 5
Dean Dewald
Chairman
Steele



At-Large director
Dean Hummel
Hague



*At-Large
director*
Carmen Essig
Lehr

**Baumgartner****Franklund**

Managers' report

Reliability – regulations – resources Ready to serve you

BY CHRIS BAUMGARTNER AND DON FRANKLUND, CO-GENERAL MANAGERS

What a difference a year makes. As we at KEM Electric Cooperative reflect on the work plans and activities that happened across our service area over the past year, we can honestly say nothing – and everything – has changed.

Last year, we talked about KEM's culture of safety, and how we focus on working safely every day, all day. Safety continues to be our priority, and we assure you this will never change. Before they do a job, our lineworkers meet as a group to assess what needs to be done and how they are going to do it as a team.

While working outdoors, our employees wear brightly colored clothing that makes them highly visible, and our lineworkers wear personal protective gear in the field, including the relatively new fall-restraint system while climbing. Indoors, our employees do what

they need to do to minimize slips, trips and falls. We are required to follow the rules set forth by the Occupational Safety and Health Administration, but our employees choose to work safely so they can go home to their families every night. Together as a team, we continue our culture of safety.

Our commitment to safety is one of few things that did not change in 2015, which proved to be an eventful year for KEM. While your cooperative remained steeped in its grassroots foundation, KEM and its membership began to see some of the effects of the evolving electric generation and transmission environment.

As we have reported in our *North Dakota Living* local pages, KEM's power suppliers, Basin Electric Power Cooperative and the Western Area Power Administration, have joined the Southwest Power Pool, a

regional transmission organization (RTO). The ultimate benefit of participating in an RTO is that our power providers can more economically purchase power from other regional utilities in time of need and sell power in time of excess. While this is a complicated and philosophical change, the KEM board of directors and management believe this move is the right one.

As KEM was realizing this change, an environmental regulation on the federal level came into play. Last year, the Environmental Protection Agency (EPA) enacted the Clean Power Plan – an environmental regulation that calls for the reduction of carbon dioxide emissions from existing fossil fuel power plants.

With a heavy focus on the Midwest, each state was given a target level of reduction. North Dakota was handed one of the highest reductions at 45 percent.

INDEPENDENT AUDITOR'S REPORT

Report on the financial statements

We have audited the accompanying financial statements of KEM Electric Cooperative Inc. (a nonprofit cooperative), which are comprised of the balance sheets as of Dec. 31, 2015 and 2014, and the related statements of revenue and expenses, patronage capital and other equities, 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 and the standards applicable to financial audits contained in Government Auditing Standards, issued by the comptroller general of the United States. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain

audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the 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.

Electric cooperatives here and across the nation are faced with serious questions about compliance options, concerns about reliability, and the impact the plan could have on electric rates. Basin Electric, with support from its member-cooperatives including KEM, chose to litigate this rule.

Currently the issue is scheduled to be heard by the Washington, D.C. Circuit Court in September of this year. However, any decision that is rendered is expected to be appealed to the United States Supreme Court and as a result we do not anticipate a final decision on this issue until late 2017 or 2018. Rest assured, we will keep the membership informed as this issue progresses through the legal system.

How will the landscape of the electric generation and transmission environment evolve in the coming years? With the help of key tax breaks, new wind energy impacted electric generation across the country in 2015 more than any other power source. Texas accounted for most of the additions, followed by Oklahoma, Kansas, Iowa and then North Dakota. We remain vigilant as federal and state regulatory plans unfold, but we also remain true to our cooperative roots.

Like those before us, the resourcefulness of our employees and their dedication to you, the member-owner, runs deep. Line crews worked hard to reduce outages, bumps and blinks. In the past year, KEM has replaced several miles of three-phase overhead line with three-phase underground line, along with creating a tie-line between the Midway and Danzig substations, to improve system reliability. System reliability and safety are essential to the success of KEM, and we are mindful of the delicate balance between affordability and reliability, as we strategically plan to meet the electrical needs of our members.

Innovative Energy Alliance (IEA) LLC, our shared group of employees, continues to help with that balance by providing a way to pool resources and employees among KEM, Mor-Gran-Sou, Roughrider and Slope electric cooperatives, in addition to 3C Construction LLC and West Dakota Utility Services. This year, the alliance added a transmission and substation maintenance manager to provide oversight on our transmission line and substations, and assist staff with regulations set forth by the North American Electric Reliability Council and the Federal Energy Regulatory Commission.

In existence since 2008, the alliance allows us to stay current with technology, regulations, members' needs and more, which otherwise would be hard to do as individual entities. This relationship provides significant savings to the memberships and allows us to be prudent with the revenue provided by you, the member-owners. As the topic of power generation and transmission persists in the headlines, please know your cooperative's interest and resources remain with you, our member. While we are not immune to decisions made on the federal level and how future rates may impact us all, you remain our top priority.

As a Touchstone Energy® Cooperative, KEM's board, management and employees are committed to providing safe, dependable and reliable electric service that will fulfill the needs of today's and tomorrow's members.

We look forward to visiting with you at the annual meeting on June 16 at Linton Public School, and thank you for supporting KEM Electric Cooperative Inc. ■

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of KEM Electric Cooperative Inc., as of December 31, 2015 and 2014, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other information

Our audit was conducted for the purpose of forming an opinion on the financial statements as a whole. The detailed schedule of deferred debits and deferred credits, and the detailed schedule of investments on the equity basis are presented for purposes of additional analysis and are not a required

part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Other reporting required by Government Auditing Standards

In accordance with Government Auditing

Standards, we have also issued our report dated March 20, 2016, on our consideration of KEM Electric Cooperative Inc.'s internal control over financial reporting and on 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 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 KEM Electric Cooperative Inc.'s internal control over financial reporting and compliance.

BRADY, MARTZ & ASSOCIATES P.C.

Bismarck
March 20, 2016

Meet the candidates

This year, three candidates are seeking the seat of retiring director Milton Brandner in District 3. At-large incumbent director, Dean Hummel, is running unopposed. Here, KEM Electric Cooperative provides a statement from each candidates:

District At Large

Dean Hummel

I will be running for re-election as a District At-Large director. I have been farming for 37 years on a farmstead three miles north of Hague. I am married with four children and six grandchildren. Also, I am a graduate of North Dakota State College of Science.

I've been a director for 12 years at KEM Electric. During this time, I've completed all the courses to become a certified director, which involved a lot of classroom and home courses.

I've been honored to serve the membership for the last 12 years and hope to continue to work for the members and the employees for the next three years. Your appearance and vote at the KEM Electric annual meeting on Thursday, June 16, at Linton High School would be greatly appreciated.

District 3

Mark Dohm

I would appreciate your vote for director of District 3. I live on a farm six miles southeast of Venturia and have been farming and ranching for more than 40 years with my wife, Pauletta. We have three grown children: Alicia, Todd and Andrew.

I completed college at Northern State University in Aberdeen, S.D. Our farm has been served by KEM Electric for more than 60 years. I would consider it an honor to

serve on the KEM Electric board of directors.

Neil Meidinger

I am asking for your vote as the next District 3 KEM Electric Cooperative board member. As a lifelong resident of McIntosh County, and an elected official for many years, I feel I am uniquely qualified to fill the position that has been vacated by Milton Brandner's retirement.

I live 10 miles north of Zeeland on the farm that I own and operate with my wife of 10 years, Rebecca, and our 7-year-old son, Jacob. Rebecca is a special education teacher in the Napoleon School District. I also haul cattle and grain with my trucking business, Meidinger Trucking.

I am a nationally registered EMT with the Wishek Ambulance and have worked with the ambulance for 24 years. I am currently serving my 14th year as a McIntosh County commissioner and have been a member of the Zeeland School Board for the past 18 years. I am also a Tri-County Fair director.

Being a leader in the community

has always been important to me. I will work hard for the cooperative and do my best to continue the great work that the board has done. I am a quick learner and I am excited to study everything that this position has to offer.

I greatly appreciate your support and thank you for your vote.

Allen Wolf

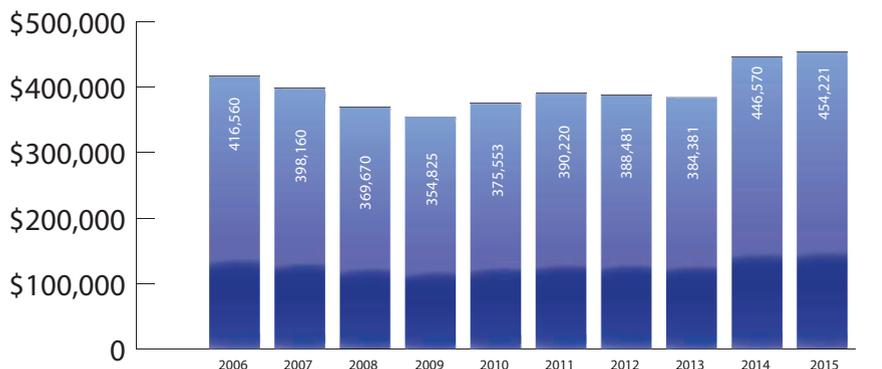
I live on the farm where I was raised. I graduated from Zeeland High School and attended Bismarck State College before taking over the family farm. I have also been doing construction work the last two years.

In Zeeland, I have been a member of the volunteer fire department, serving as the board president for the last several years. I am also a longtime member of the Zeeland Lions Club, holding the office of club president three times.

My hobbies include hunting, fishing and camping.

I am married to Trudy Fraase Wolf, who is the principal and music teacher at Zeeland Public School. Trudy and I have three children. ■

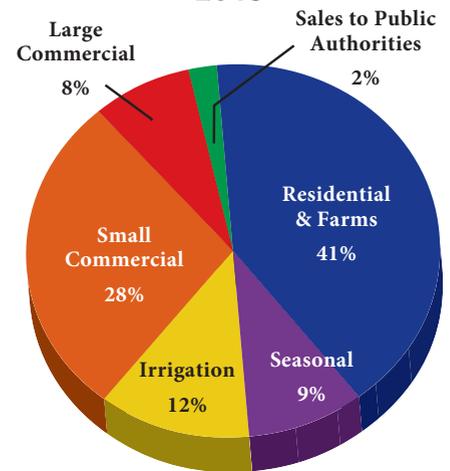
Capital Credit Retirements



2015 Comparative Income Statement

	<u>2015</u>	<u>2014</u>
Operating Revenue	\$8,483,659	\$9,121,108
Cost of wholesale electric power	3,961,020	4,567,433
Transmission line and substation expense	25,146	18,819
Distribution expense-operations and maintenance	1,092,601	1,089,962
Consumer accounts and customer service expense	171,430	132,101
General and administrative expense	1,006,635	1,048,284
Depreciation	1,134,281	1,030,288
Tax expense	52,396	77,822
Interest	685,692	656,159
Other deductions	12,835	22,228
Total cost of electric service	<u>\$8,142,036</u>	<u>\$8,643,096</u>
Patronage capital and operating margins	341,623	478,012
Other operating margins (associated cooperatives)	220,827	237,194
Non-Operating margins	132,285	51,757
Total Margins and Patronage Capital	<u>\$694,735</u>	<u>\$766,963</u>

WHERE YOUR DOLLAR CAME FROM 2015

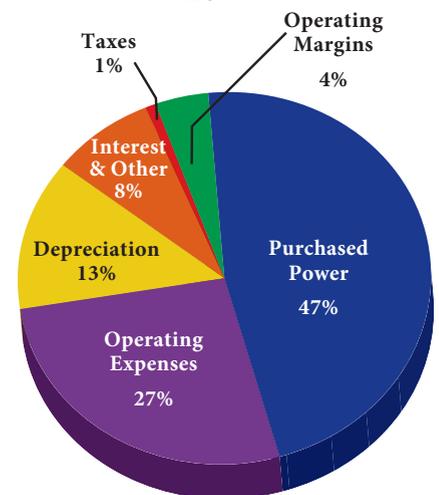


Balance Sheet

December 31, 2015 and 2014

	<u>2015</u>	<u>2014</u>
Assets		
Electric Plant	\$43,690,587	\$41,568,130
Less Depreciation	19,765,744	19,768,360
Net Electric Plant	<u>\$23,924,843</u>	<u>\$21,799,770</u>
Cash - General Fund	\$649,176	\$460,226
Temporary Cash Investment	0	0
Investments in Associated Organizations	5,314,096	4,951,185
Accounts Receivable (Net)	852,381	908,051
Materials and Supplies	184,804	793,422
Other	341,841	379,769
Total Assets	<u>\$31,267,141</u>	<u>\$29,292,423</u>
Liabilities		
Long-Term Debt (Net)	\$16,783,956	\$15,009,346
Consumer Prepayments	51,194	72,337
Accounts Payable	990,773	1,287,525
Other Current and Accrued Liabilities	253,598	287,589
Power Cost Refund Deferred	1,300,000	1,000,000
Total Liabilities	<u>\$19,379,521</u>	<u>\$17,656,797</u>
Net Worth		
Patronage Capital	\$8,859,957	\$8,751,728
Donated Capital	261,590	250,111
Non-Operating Margins	2,766,072	2,633,787
Total Net Worth	<u>\$11,887,619</u>	<u>\$11,635,626</u>
Total Liabilities and Net Worth	<u>\$31,267,141</u>	<u>\$29,292,423</u>

WHERE YOUR DOLLAR WENT 2014



Minutes of the annual meeting

KEM Electric Cooperative Inc.

June 18, 2015

The 71st annual meeting of KEM Electric Cooperative Inc. was called to order at 7 p.m., June 18, 2015, in the Linton Public School auditorium, Linton, N.D., with Chairman Dean Dewald presiding. The meeting commenced following an evening meal.

Fr. Jason Signalness, the pastor of St. Peter & Paul Catholic Church in Strasburg and St. Mary's Catholic Church in Hague, gave the invocation.

Brady Weber sang the national anthem.

Sharon Jangula, the city of Linton administrator, gave the welcome address.

Chairman Dewald announced the order of business for the meeting. Cooperative Attorney Tom Bair was introduced.

Chairman Dewald reviewed the contents of the packets members received during registration and directed children to the location for the Children's Fun Night activities.

Secretary Carter Vander Wal reported the cooperative's membership as of June 18, 2015, consisted of 2,135 members and there were 168 members present at the time the meeting was called to order. This number represented a quorum. Chairman Dewald declared the meeting officially opened.

Secretary Vander Wal moved to dispense with reading of the notice of the annual meeting since it was mailed to the membership. The motion was seconded and carried. Chairman Dewald directed the secretary to attach a copy of the notice of the meeting and proof of mailing to all members to the 2014 annual meeting minutes.

Chairman Dewald called for reading of the minutes of the June 19, 2014, annual meeting. Secretary Vander Wal moved to dispense with reading of the minutes and approve the minutes as published in the

2014 annual report. The motion was seconded and carried.

Chairman Dewald informed the members there would be time later in the meeting for members to address the meeting.

The early bird prize was awarded.

Chairman Dewald introduced guests in attendance and acknowledged the receipt of letters from public officials.

Chairman Dewald introduced the members of the board of directors as well as the employees of KEM Electric as well as the Innovative Energy Alliance employees.

Chairman Dean Dewald announced the next order of business to be the election of two directors and introduced the following election tellers: Neil Meidinger, Zealand; Gordon Knoll, Ventura; Linda Rudolph, Dawson; Bill Becker, Wishek; Kris Stoh, Tappen; Linda Rudolph, Dawson; Dan Schuler, Wishek; and Jack Horner, Wishek. Chairman Dean Dewald stated the director seats up for election are in District 1 and District 2 at this annual meeting.

Dean Dewald, chairman, introduced John Beck, Linton, nominee for the District 1 position having been nominated by petition. Prior to calling for nominations from the floor, Mr. Dewald reviewed the requirements for nominations. Mr. Dewald asked for additional nominations. Hearing none, a motion was made from the floor to cast a unanimous ballot for John Beck. Motion carried.

Dean Dewald, Chairman, introduced Carter Vander Wal, Pollock, nominee for the District 2 position having been nominated by petition. Prior to calling for nominations from the floor, Mr. Dewald reviewed the requirements for nominations. Mr. Dewald asked for additional nominations. Hearing none, a motion was made from the

floor to cast a unanimous ballot for Carter Vander Wal. Motion carried.

Chairman Dewald introduced Tony Schaffner, chairman of KEM Electric Operation Round Up. Mr. Schaffner reported on activities and introduced the Operation Round Up board members.

Co-Alliance Managers Don Franklund and Chris Baumgartner, and Chief Financial Officer Travis Kupper, from the Innovative Energy Alliance gave reports on the 2014 KEM Electric activities.

A motion was made and seconded to approve the chairman's and treasurer's reports as mailed. The motion carried.

Prizes were awarded.

Vice Chairman Victor J. Wald announced Grace Schuler as the recipient of the Basin \$1,000 scholarship and Casandra Rutschke as the \$500 KEM Electric scholarship.

Vice Chairman Victor J. Wald introduced Morgan Gallagher who was the winner of the 2015 Rural Electric Youth Tour Essay Contest.

Prizes were awarded.

A brief question-and-answer period was held.

A motion was made for the board to change the bylaws to vote by mail. The motion failed.

Chairman Dewald called for any further business. Chairman Dewald assured the membership that all questions and comments from the membership are welcome.

Prizes were awarded.

Chairman Dewald thanked the employees and everyone that helped make the annual meeting possible.

The grand prize drawings were held. The winner of the \$300 progressive door prize was not present. At the 2016 annual meeting, the drawing will be \$400.

It was moved and seconded the meeting be adjourned. The motion carried. ■