REPORT OF INDEPENDENT AUDITORS AND
CONSOLIDATED FINANCIAL STATEMENTS
WITH SUPPLEMENTARY INFORMATION

MIDWEST ENERGY COOPERATIVE

December 31, 2018 and 2017

MOSSADAMS

Table of Contents

Midwest Energy Cooperative
Board of Directors
December 31, 2018

Clarence A. Barth	Chairman
Ben Russell	Vice Chairman
Ronald Armstrong	Secretary
John Green	Treasurer
Fred Turk	Director
James W. Dickerson	Director
Arell Chapman	Director
Gerry Bundle	Director
Robert Hance	President and CEO

MOSSADAMS

Report of Independent Auditors

The Board of Directors
Midwest Energy Cooperative
Cassopolis, Michigan

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Midwest Energy Cooperative (the Cooperative), which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of operations, equities and margins, and cash flows for the years then ended, and the related notes to the consolidated 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.

Auditor's Responsibility

Our responsibility is to express opinions 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 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 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 audit opinions.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Cooperative as of December 31, 2018 and 2017, 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.

Other Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the Cooperative's consolidated financial statements. The consolidating balance sheets and consolidating statements of operations (collectively, "supplementary information") 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 supplementary information has been subjected to the auditing procedures applied in the audit of the financial statements and certain other 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 supplementary 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 29, 2019, on our consideration of Midwest Energy Cooperative'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 Midwest Energy Cooperative's internal control over financial reporting and compliance.

Moss Adams LLP

Portland, Oregon
March 29, 2019

This page intentionally left blank.

Midwest Energy Cooperative
Consolidated Balance Sheets

ASSETS

	December 31, 2018	December 31, 2017
ELECTRIC PLANT AND EQUIPMENT		
In service – at cost	$ 276,839,575	$ 255,557,752
Construction work in progress	4,407,607	9,314,532
	281,247,182	264,872,284
Less accumulated depreciation	76,832,345	71,393,337
Net electric plant and equipment	204,414,837	193,478,947
OTHER ASSETS AND INVESTMENTS		
Investments in associated organizations	27,997,760	25,348,065
Notes receivable	75,079	161,702
Income taxes receivable	-	16,719
Grant receivable	104,885	119,692
Total other assets and investments	28,177,724	25,646,178
CURRENT ASSETS		
Cash and cash equivalents	18,124,418	7,031,862
Accounts receivable, less allowance for doubtful accounts of $330,000 and $462,000 in 2018 and 2017, respectively	5,423,521	4,921,880
Unbilled revenue	5,339,376	5,206,029
Current portion of notes receivable	60,000	60,000
Materials and supplies	2,537,641	2,256,124
Inventory of subsidiary	334,782	321,999
Other current assets	510,676	453,485
Total current assets	32,330,414	20,251,379
DEFERRED CHARGES	142,300	142,300
Total assets	$ 265,065,275	$ 239,518,804

See accompanying notes.

LIABILITIES, EQUITIES, AND MARGINS

	December 31, 2018	December 31, 2017
EQUITIES AND MARGINS		
Patronage capital and other equities	$ 61,256,303	$ 56,199,354
LONG-TERM DEBT, less current maturities	177,695,800	158,140,643
OTHER LIABILITIES		
Post retirement benefits other than pensions	2,713,721	3,450,816
Accrued pension liability	875,492	1,379,815
Total other liabilities	3,589,213	4,830,631
COMMITMENTS AND CONTINGENCIES (NOTE 7)		
CURRENT LIABILITIES		
Current maturities of long-term debt	6,379,379	4,772,112
Accounts payable		
Purchased power and cooperative payables	6,224,957	7,010,741
Regulatory liabilities – energy optimization	384,081	642,789
Other	357,315	255,809
Power supply cost recovery	1,779,843	455,425
Customer deposits	2,018,797	2,053,020
Income taxes payable	9,848	-
Accrued liabilities	4,539,679	4,615,375
Total current liabilities	21,693,899	19,805,271
DEFERRED TAX LIABILITY	809,292	527,978
DEFERRED CREDITS	20,768	14,927
Total liabilities, equities, and margins	$ 265,065,275	$ 239,518,804

See accompanying notes.

Midwest Energy Cooperative
Consolidated Statements of Operations

	Years Ended December 31, 2018	Years Ended December 31, 2017
OPERATING REVENUES	$ 96,131,000	$ 88,517,038
OPERATING EXPENSES		
Cost of power	49,701,111	47,356,174
Cost of goods sold	3,736,562	2,811,222
Distribution – operations	3,357,710	2,764,651
Distribution – maintenance	7,405,447	9,373,263
Customer accounts	3,000,785	2,363,844
Customer service and information expense	2,551,862	2,503,384
Administrative and general	8,662,758	8,413,160
Depreciation and amortization	9,183,569	7,490,002
Taxes – property	3,493,972	2,635,530
Total operating expenses	91,093,776	85,711,230
OPERATING MARGINS BEFORE FIXED CHARGES	5,037,224	2,805,808
FIXED CHARGES		
Interest on long-term debt	5,170,331	4,180,829
Total fixed charges	5,170,331	4,180,829
OPERATING MARGINS (DEFICITS) AFTER FIXED CHARGES	(133,107)	(1,375,021)
G&T AND OTHER CAPITAL CREDITS	4,327,670	3,594,185
NET OPERATING MARGINS	4,194,563	2,219,164
NON-OPERATING MARGINS		
Interest and dividend income	97,331	143,257
Gain (loss) on sale of assets	40,965	(38,951)
Other income (expense), net	18,044	705,205
Income tax benefit (expense)	(326,310)	16,603
Total non-operating margins (deficits)	(169,970)	826,114
NET MARGINS	4,024,593	3,045,278
COMPREHENSIVE INCOME		
Unrealized gain on pension and post-retirement benefits other than pensions	1,218,400	354,470
COMPREHENSIVE INCOME	$ 5,242,993	$ 3,399,748

See accompanying notes.

Midwest Energy Cooperative
Consolidated Statements of Equities and Margins

	Years Ended December 31,	
	2018	2017
Patronage capital		
Balance at January 1,	$ 60,026,867	$ 58,554,284
Transfer of current year Cooperative net operating margins	2,954,701	1,664,221
Retirement of capital credits, net	(212,282)	(191,638)
Balance at December 31,	62,769,286	60,026,867
Non-operating margins		
Balance at January 1,	3,684,310	2,900,665
Current year Cooperative non-operating margins	132,089	783,645
Balance at December 31,	3,816,399	3,684,310
Undistributed subsidiary earnings		
Balance at January 1,	1,066,411	468,999
Income from subsidiary, excluded from net operating and non-operating margins	937,803	597,412
Balance at December 31,	2,004,214	1,066,411
Other equity		
Balance at January 1,	1,936,739	1,914,138
Additions	26,238	22,601
Balance at December 31,	1,962,977	1,936,739
Accumulated other comprehensive loss		
Balance at January 1,	(10,514,973)	(10,869,443)
Unrealized gain (loss) on pension and post-retirement benefits other than pensions	1,218,400	354,470
Balance at December 31,	(9,296,573)	(10,514,973)
Total equities and margins	$ 61,256,303	$ 56,199,354

See accompanying notes.

Midwest Energy Cooperative
Consolidated Statements of Cash Flows

	December 31, 2018	December 31, 2017
CASH FLOWS FROM OPERATING ACTIVITIES		
Net margins	$ 4,024,593	$ 3,045,278
Adjustments to reconcile net margins to net cash provided by operating activities		
Depreciation and amortization	9,183,569	7,490,002
Capital credits allocated	(4,327,670)	(3,594,185)
Gain (loss) on disposal of assets	(40,965)	38,951
Deferred taxes	281,314	(34,553)
Changes in assets and liabilities		
Customer and other accounts receivable	(501,641)	(359,270)
Unbilled revenue	(133,347)	(729,360)
Inventory of subsidiary	(12,783)	254,035
Power supply cost recovery	1,324,418	526,681
Other current assets and income tax receivable	(30,624)	165,972
Deferred charges	-	-
Accrued pension liability	(199,341)	(405,650)
Post-retirement benefits other than pensions	176,323	225,262
Accounts payable	(684,278)	(2,124,800)
Regulatory liabilities	(258,708)	(187,757)
Customer deposits	(34,223)	(228,088)
Deferred credits	5,841	4,347
Current and accrued liabilities – other	(75,696)	934,995
Net cash provided by operating activities	8,696,782	5,021,860
CASH FLOWS FROM INVESTING ACTIVITIES		
Construction and acquisition of plant, net of retirements	(20,118,979)	(40,902,589)
Net proceeds from sale of plant	40,485	73,462
(Increase) decrease in		
Materials inventory	(281,517)	(127,196)
Notes receivable	86,623	351
Investments – associated organizations	1,677,975	2,040,704
Net cash used in investing activities	(18,595,413)	(38,915,268)

See accompanying notes.

	December 31,	
	2018	2017
CASH FLOWS FROM FINANCING ACTIVITIES		
Advances on long-term debt	$ 26,585,390	$ 56,373,582
Proceeds from line of credit	-	23,000,000
Payments on line of credit	-	(37,500,000)
Cushion of credit payment to RUS	-	390,520
Grant receivable	14,807	14,807
Retirement of patronage capital credits, net	(212,282)	(191,638)
Other equity	26,238	22,601
Payments on long-term debt	(5,422,966)	(3,559,406)
Net cash provided by financing activities	20,991,187	38,550,466
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	11,092,556	4,657,058
CASH AND CASH EQUIVALENTS – beginning	7,031,862	2,374,804
CASH AND CASH EQUIVALENTS – ending	$ 18,124,418	$ 7,031,862
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash paid for interest	$ 5,713,187	$ 3,677,413
Cash paid for property taxes	$ 3,669,285	$ 2,370,833
Cash paid for income taxes	$ 18,429	$ 29,000

See accompanying notes.

Note 1 – Nature of Organization and Operations

Midwest Energy Cooperative (Midwest or Cooperative) is a non-profit organization generally exempt from income tax under Section 501(c)(12) of the United States Internal Revenue Code. The Cooperative is engaged principally in the distribution and sale of electricity in Southwest and Southeast Michigan, Northern Indiana and Northern Ohio.

Midwest Energy, Inc. and Subsidiary, a wholly-owned subsidiary of the Cooperative, is a Michigan corporation, which was incorporated and commenced doing business January 30, 1998. Midwest Energy, Inc. and Subsidiary's principal business activity is providing propane services. The main office is located in Cassopolis, Michigan.

The Cooperative began a project for communication and fiber to the home in 2013. This includes providing phone and high-speed broadband to 8,790 members in their service territory and beyond.

Note 2 – Summary of Significant Accounting Policies

Use of 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Specific estimates include allowance for doubtful accounts, unbilled revenue, depreciation and postretirement benefit obligation. Actual results could differ from those estimates.

Principles of consolidation – The consolidated financial statements for 2018 and 2017 combine the financial results of the Cooperative and its wholly owned subsidiary Midwest Energy, Inc. and subsidiary. The Cooperative has accounted for the investment using the equity method. All significant intercompany transactions and accounts have been eliminated.

Accounting records – The consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as applied to regulated enterprises, which conform to policies prescribed or permitted by the Michigan Public Service Commission (MPSC) and United States Department of Agriculture Rural Utilities Service (RUS). The applicable uniform system of accounts prescribed by these regulatory commissions conform in all material respects with generally accepted accounting principles as applied to rate regulated utilities.

The accounting records of the Cooperative are maintained in accordance with the Uniform System of Accounts as prescribed by the Federal Energy Regulatory Commission (FERC) for Class A and B electric utilities.

Note 2 – Summary of Significant Accounting Policies (continued)

Electric plant and equipment – Additions with a life expectancy of more than one year are recorded at the cost of construction, which includes the cost of contracted services, direct labor and materials, and overhead items, less contributions in aid of construction received from customers. As items are retired or otherwise disposed of, the asset account is credited for the cost and the accumulated depreciation account is charged. The cost of removal, less salvage, is also charged to the accumulated depreciation account.

Cash and cash equivalents – Cash and cash equivalents include cash in bank and all short-term debt securities purchased with a maturity of three months or less to be cash equivalents. The Cooperative places its cash and investments with high credit quality financial institutions. At times, such cash and investments may be in excess of the FDIC insurance limit.

Fair value of financial instruments – Financial instruments include cash, investments and long-term debt. Investments in associated organizations are not considered financial instruments because they represent nontransferable interests in associated organizations.

Investments in associated organizations – The carrying values of investments in associated organizations are stated at cost, adjusted for capital credits earned or retired.

Accounts receivable – Accounts receivable consist primarily of amounts due from members for electric service. An allowance for doubtful accounts has been estimated based on collection history. When a member's account becomes past due and uncollectible, the member's service is terminated. The Board of Directors approve all accounts charged off.

Purchased power billing – Refundable or recoverable power supply cost recovery (PSCR) credit-over collections, as well as under collections of the cost of electricity purchased not recovered or refunded through rates, are deferred and are being refunded or recovered in accordance with procedures approved by the Board.

Materials and supplies – Electrical materials and supplies are valued at lower of average cost or net realizable value.

Inventory of subsidiary – Propane inventory is recorded at the lower of cost or net realizable value using average cost.

Revenue recognition – The Cooperative utilizes cycle billing and records revenue billed to its electric and propane customers primarily when the meters are read (electric) or when propane is delivered (propane).

In addition, the Cooperative records unbilled revenue for electric power and propane delivered but not yet billed at the end of the fiscal year.

The Cooperative bills its fiber customers in advance of services and records unearned revenue for services billed but not yet performed at the end of the fiscal year.

Note 2 – Summary of Significant Accounting Policies (continued)

Recognition of patronage revenue – Patronage revenue of associated organizations is recognized in the year in which the associated organization allocates its earnings to their respective members.

Advertising – The cost of advertising is expensed as incurred.

Regulation and regulatory accounting – The MPSC has jurisdiction over regulated Rural Electric Cooperatives in Michigan. On May 24, 2015, the Board of Directors voted to become member-regulated as of August 24, 2015. On that date, the Cooperative became self-regulated for rates, billing practices, and accounting standards. MPSC regulated the Cooperative's electric utility business operations and rates prior to August 24, 2015. All other aspects of electric service continue to be regulated by MPSC. Due to regulation of its rates by the Board, the Cooperative follows regulatory accounting requirements. Regulatory accounting requirements recognize that the ratemaking process can result in differences in the application of generally accepted accounting principles between regulated and non-regulated businesses. Such differences generally involve the accounting period in which various transactions enter into the determination of net margins. Accordingly, certain costs and income may be capitalized as a regulatory asset or liability that would otherwise be charged to expense or revenues. Regulatory assets and liabilities are recorded when it is probable that future rates will permit recovery and are approved by the Board.

Unclaimed property – Unclaimed property represents refunds to members of deposits, membership fees received and patronage refunds received which have not been claimed. After five years and appropriate notification, such amounts may be credited back to the cooperative as donated capital.

Compensated absences – The Cooperative provides a flexible leave program to meet the needs of their unique employee base. Each regular employee will earn Paid Time Off (PTO) in increments that are based on their length of service on a bi-weekly basis. PTO is added to the employee's PTO bank when the bi-weekly paycheck is issued and subtracted from the employee's bank as used. Each employee may carry over unused hours of PTO, provided they do not exceed the maximum level based on years of service detailed in their accrual schedule. The Cooperative's policy on accumulated extended sick leave is to grant 48 hours annually with any unused hours available to be carried forward to future years up to a maximum of 800 hours. Employees may use extended sick leave hours on their 4th consecutive day of absence due to their own personal illness or injury. It is the Cooperative’s policy to pay one-half of the employee’s accumulated unused sick leave upon normal retirement, provided that their extended sick leave bank is equal to or greater than 520 hours.

The payout is capped at 260 hours and will be reduced by any PTO payouts taken during the employee’s tenure. For the years ended December 31, 2018 and 2017, an accrual has been made for individuals who meet the required qualifications and have attained the age of 60, which has been included in accrued liabilities on the balance sheet.

Note 2 – Summary of Significant Accounting Policies (continued)

Cushion of credit – RUS established a Cushion of Credit Payment Program, whereby borrowers may make advance payments on their RUS and Federal Financing Bank (FFB) notes. These advance payments earn interest at the rate of 5.0% per annum. The advance payments, plus any accrued interest, can only be used for the payment of principal and interest on the notes. The Cooperative's participation in the Cushion of Credit Payment Program totaled $0 and $390,520 at December 31, 2018 and 2017, respectively, and is recorded as a reduction of RUS long-term debt on the balance sheets.

Concentration of credit risk – Financial instruments that are exposed to concentrations of credit risk consist primarily of cash, including temporary investments and receivables. Credit is extended to customers generally without collateral requirements; however, deposits are obtained from certain customers and formal shut-off procedures are in place.

Income taxes – The Cooperative is exempt from federal and state income taxes under Section 501(c)(12) of the Internal Revenue Code. The Cooperative adopted Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 740-10, relating to accounting for uncertain tax positions. As of December 31, 2018 and 2017, the Cooperative does not have any uncertain tax positions. The Cooperative files an exempt organization tax return in the U.S. federal jurisdiction and the state of Michigan.

Midwest Energy, Inc. and Subsidiary is a taxable for-profit corporation for both federal and state tax purposes. Income taxes are provided for in the consolidated financial statements and consist of taxes currently due plus deferred taxes. Deferred taxes are provided on an asset and liability approach whereby deferred tax assets are recognized for deductible temporary differences and operating loss carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion of or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

Patronage capital – Cooperative operating margins are assigned to individual Cooperative members' capital credit accounts based upon their revenue. Amounts are assigned to members within eight months after year end. Non-operating margins are allocated to members at the discretion of the Board of Directors. Capital credits are returned to members in accordance with the Cooperative's bylaws.

Assets pledged – Substantially all assets are pledged as collateral on long-term debt payable to the Rural Utilities Service (RUS) of the United States of America, the National Rural Utilities Cooperative Finance Corporation (CFC), and CoBank Cooperative.

Note 2 – Summary of Significant Accounting Policies (continued)

Recent accounting pronouncements – In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers.* Under the new standard, recognition of revenue occurs when a customer obtains control of promised goods or services in an amount that reflects the consideration to which the entity expects to receive in exchange for those goods or services. In addition, the standard requires disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The new standard was effective for fiscal years beginning after December 15, 2017, with early adoption permitted for fiscal years beginning after December 15, 2016, in certain instances. On July 9, 2015, the FASB affirmed its proposal to defer the effective date of the new revenue standard by one year to annual reporting periods beginning after December 15, 2018. The Cooperative is evaluating the impact of the pending adoption of the new standard on the consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases.* The new standard establishes a right-of-use ("ROU") model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2019, with early adoption permitted. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Cooperative is evaluating the impact of the pending adoption of the new standard on the consolidated financial statements.

Subsequent events – Accounting standards require disclosure of the date through which subsequent events have been evaluated, as well as whether the date is the date the financial statements were issued or the date the financial statements were available to be issued. The Cooperative has evaluated subsequent events through March 29, 2019, the date the financial statements were available to be issued.

Note 3 – Electric Plant and Equipment and Depreciation Rates

Major classes of electric plant and equipment as of December 31, 2018 and 2017, consisted of:

	2018	2017
Cost		
General plant	$ 66,373,783	$ 64,908,055
Transmission plant	6,445,455	6,451,461
Distribution plant	154,035,103	149,764,439
Fiber plant	49,985,234	34,433,797
Construction in progress	4,407,607	9,314,532
Total cost	281,247,182	264,872,284
Accumulated depreciation and amortization	76,832,345	71,393,337
Net electric plant and equipment	$ 204,414,837	$ 193,478,947

Provision has been made for depreciation of the distribution plant at a straight-line composite rate of 3.0 percent per annum, except for ONTs and meters which are being depreciated at the rate of 20.0 percent and 4.6 percent per annum. Depreciation of the subsidiary's assets is computed over the estimated useful life of the assets on a straight-line method for financial reporting and an accelerated method for income tax purposes.

General plant depreciation rates have been applied on a straight-line basis as follows:

Structures and improvements	2.00%
Office furniture, fixtures, data processing, and laboratory equipment	4.80–20.00%
Transportation equipment	10.00–33.30%
Stores, tools, and power operated equipment	6.00%
Communications	8.40%
Miscellaneous	9.60%
Propane tanks	3.33%

Note 4 – Investments in Associated Organizations

Investments in associated organizations consisted of the following at December 31, 2018 and 2017:

	2018	2017
National Rural Utilities Cooperative Finance Corp. (CFC)		
Capital term certificates, 5.00% maturing through 2080	$ 1,049,571	$ 1,049,571
Loan term certificates, 3.00% maturing through 2035	206,000	206,000
Patronage capital		
CFC	422,435	412,807
National Information Solutions Cooperative	313,840	282,336
Wabash Valley Power Association	7,166,180	7,525,455
Buckeye Power, Inc.	1,070,864	987,883
Wolverine Power Supply Cooperative, Inc.	16,034,902	13,395,117
Federated Rural Electric Insurance Cooperative, at cost	290,915	249,101
Buckeye Power, Inc. – membership	98,899	98,889
Resco (WISC)	569,978	567,959
NRTC	213,159	213,486
Other	561,017	359,461
Total	$ 27,997,760	$ 25,348,065

The accounting policies for recognition of patronage revenue are described in Note 2. Investments are pledged to secure long-term debt as described in Note 5.

Note 5 – Long-Term Debt

Long-term debt is composed of mortgage notes payable to the Rural Utilities Service (RUS) of the United States of America, the National Rural Utilities Cooperative Finance Corporation (CFC), the Federal Financing Bank (FFB), and CoBank Cooperative. Several mortgage notes to CFC and RUS will be repriced and the interest rate adjusted accordingly during the next 10 years in accordance with the policy and procedure governing such repricing. The notes are scheduled to be fully repaid at various times from 2019 through 2052. Unadvanced loan funds were available from RUS at December 31, 2018 and 2017, in the amount of $6,557,229 and $32,858,229, respectively.

Midwest Energy, Inc. and Subsidiary long-term debt is composed of mortgage notes payable to National Cooperative Services Corporation (NCSC). These notes are secured by substantially all assets of the organization and guaranteed by the Cooperative.

Note 5 – Long-Term Debt (continued)

Detail of the long-term debt is as follows:

	2018	2017
Cooperative		
Notes payable to CFC in quarterly installments of $259,679, including interest at 4.5%–7.35%, with final maturity ranging from 2019 to 2032. Secured by substantially all assets.	$ 3,136,892	$ 3,376,043
Notes payable to CoBank in monthly installments of $375,861, including interest at 3.49%–3.83%, with final maturity ranging from 2032 to 2037. Secured by substantially all assets.	50,979,568	53,445,737
Notes payable to FFB in quarterly installments of $279,182, including interest at 2.20%–3.94%, with final maturity ranging from 2042 to 2052. Secured by substantially all assets.	129,563,421	105,980,066
RUS advance payments (cushion of credit)	-	(390,520)
Midwest Energy, Inc. and Subsidiary		
Notes payable to NCSC in quarterly installments including interest at 3.70%, per annum, with final maturity in 2023.	395,298	501,429
	184,075,179	162,912,755
Less current maturities	6,379,379	4,772,112
TOTAL LONG-TERM DEBT, less current maturities	$ 177,695,800	$ 158,140,643

Maturities of long-term debt for each of the next five years are as follows:

2019	$ 6,379,379
2020	6,602,402
2021	6,792,774
2022	6,811,126
2023	6,675,487
Thereafter	150,814,011
	$ 184,075,179

Note 6 – Line of Credit

The Cooperative has available a line of credit with CFC in the amount of $10,000,000 for both 2018 and 2017. There was no liability at December 31, 2018 and December 31, 2017.

The Cooperative has available a line of credit with CoBank in the amount of $10,000,000 for 2018 and 2017. The Cooperative has no amounts outstanding as of December 31, 2018 and 2017. Interest at December 31, 2018 and 2017, was 4.86% and 3.97%, respectively.

Midwest Energy, Inc. and Subsidiary had available a $3,750,000, 60 month revolving line of credit with NCSC for 2018 and 2017 with a variable interest rate. The line of credit matures in 2023. Midwest Energy, Inc. and Subsidiary has no amounts outstanding as of December 31, 2018 and 2017. Interest at December 31, 2018, is 4.40%. The agreement provides that Midwest Energy Cooperative unconditionally guarantee all amounts due on the loan.

Note 7 – Commitments and Contingencies

Wholesale power commitment – Under its wholesale power agreement, the Cooperative is committed to purchase most of its electric power and energy requirements from Wolverine Power Supply Cooperative, Inc., until December 31, 2050. The rates paid for such purchases are subject to approval of the Federal Energy Regulatory Commission (FERC).

Propane purchase commitment – Midwest Energy has entered into contracts with Plains Marketing Canada, L.P. and Crestwood Services, LLC to buy propane gas for a specific period, in agreed upon quantities and at agreed upon prices. These transactions lock in the price Midwest Energy will be paying for such gas in the upcoming heating season. Upon entering these contracts, Midwest Energy pays a security deposit for such commitments. This deposit is deducted from each invoice for propane gas upon delivery. As of December 31, 2018, Midwest Energy's related commitment to buy such propane gas from January 1, 2019 through December 31, 2019 totaled 2,956,840 gallons at an average price per gallon of $0.83. As of December 31, 2018, Midwest Energy also other commitments to buy propane gas from January 1, 2019 through March 31, 2020 that totaled 2,088,500 gallons at an average price per gallon of $0.76. In the event that all gallons are not purchased during the agreed upon period, Midwest Energy is obligated to buy such unpurchased propane gas in subsequent months, at escalating prices.

Note 7 – Commitments and Contingencies (continued)

Legal – In the normal course of business, Midwest is a party to claims and matters of litigation. The ultimate outcome of these matters cannot presently be determined; however, in the opinion of management of the Cooperative, the resolution of these matters will not have a material adverse effect on Midwest's financial position, results of operations or liquidity.

Union contracts – The Cooperative has an agreement with two separate unions. One union represents 15 inside staff including the customer service and billing employees. The other union represents 37 outside staff. As of December 31, 2018, 40% of the employees were covered by the two union contracts. The agreement for inside employees expires on July 14, 2019. The agreement with outside employees expires August 31, 2019.

Note 8 – Retirement Plans

The Cooperative has a defined benefit pension plan covering 40 employees. As of January 1, 2007, the plan was closed to all new non-union staff and inside union staff. As of January 1, 2009, the plan was closed to all new outside union staff. Retirement benefits are based on a percentage of compensation, as defined in the plan, and benefits vested after completion of five years of service or age 55. The normal retirement age is 62. The assets of the plan consist primarily of mutual funds. The Cooperative's funding policy is to contribute so as to amortize the unfunded actuarial accrued liabilities over a 30-year period from January 1, 1987.

Note 8 – Retirement Plans (continued)

The following table sets forth the plan's funded status and amounts recognized in the Cooperative's financial statements at December 31, 2018 and 2017:

	2018	2017
Actuarial present value of benefit obligations		
Accumulated benefit obligation, including vested benefits	$ 28,227,542	$ 29,497,900
Change in benefit obligation		
Benefit obligation at beginning of year	$ 33,027,668	$ 28,956,942
Service cost	937,461	919,752
Interest cost	1,199,717	1,209,208
Actuarial loss	(3,435,160)	3,118,007
Benefits paid	(943,035)	(781,491)
Other - freeze highly compensated employees	-	(394,750)
Benefit obligation at end of year	$ 30,786,651	$ 33,027,668
Change in plan assets		
Fair value of plan assets at beginning of year	$ 31,647,853	$ 26,826,638
Actual return on plan assets	(1,656,250)	4,202,706
Employer contributions	1,000,000	1,400,000
Benefits paid	(943,035)	(781,491)
Fair value of plan assets at end of year	$ 30,048,568	$ 31,647,853
Reconciliation of funded status		
Funded status underfunded	$ (738,083)	$ (1,379,815)
Service cost – benefits earned during the period	$ 937,461	$ 919,752
Interest cost on projected benefit obligation	1,199,717	1,209,208
Return on plan assets	(2,073,815)	(1,768,891)
Net amortization and deferral	634,640	683,185
Amortization of prior service cost	(34,872)	-
Net periodic pension cost	$ 663,131	$ 1,043,254
Amounts recognized in accumulated other comprehensive loss – ending	$ (9,787,275)	$ (10,092,257)

Note 8 – Retirement Plans (continued)

The Cooperative expects to contribute $1,050,000 to its pension plan in 2019. Future expected benefit payments are as follows:

2019	$ 1,050,000
2020	1,190,000
2021	1,220,000
2022	1,260,000
2023	1,310,000
2024-2028	7,360,000

The investment strategy is to build an efficient, well-diversified portfolio based on long-term, strategic outlook of the investment markets. The investment market outlook utilizes both historical-based and forward looking return forecasts to establish future return expectations for various asset classes. These return expectations are used to develop a core asset allocation based on the needs of the plan. The core asset allocation utilizes investment portfolios of various asset classes and multiple investment managers in order to help maximize the plans return while providing multiple layers of diversification to help minimize risk.

The plan investments are stated at fair market value. There were no restricted investments as of December 31, 2018 and 2017. The Cooperative has determined that its investments in the pension plan fall into the Level 1 category. Level 1 asset valuations are based on assets at the quoted prices in active markets for identical assets, level 2 asset valuations are based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly and level 3 asset valuations based on inputs that are unobservable and significant to the overall fair value measurement.

Asset allocation for Midwest Energy Cooperative as of December 31 as follows:

	2018	2017
U.S. large cap equity	$ 8,949,345	$ 10,276,601
U.S. small/mid cap equity	1,498,889	1,831,765
International equity	4,832,189	5,111,421
Balanced	607,063	629,157
Fixed income	12,274,998	11,939,056
Other	1,886,085	1,859,853
Total	$ 30,048,569	$ 31,647,853

Weighted-average assumptions used to determine net periodic benefit costs as of December 31 were:

	2018	2017
Discount rate	3.69%	4.25%
Expected long-term return on plan assets	6.50%	6.50%
Rate of compensation increase	3.25%	3.25%

Note 8 – Retirement Plans (continued)

The Cooperative established an unfunded 457(f) deferred compensation plan in 2014 for the purposes of providing benefits for a select group of management or highly compensated employees within the regulations of the Employee Retirement Income Security Act (ERISA). New participants may be added to the plan at the discretion of the Board of Directors.

The plan provides for a deferred compensation benefit equal to the difference between the single lump sum actuarial equivalents of the benefit that the Participant would have accrued under the Cooperative Pension Plan as calculated by the Cooperative without application of the limitations provided in Sections 415 and 401(a)(17) of the Code, and the Participant's accrued benefit under the Cooperative Pension Plan as calculated by the Cooperative after application of those limitations under Code Sections 415 and 401(a)(17). The missed benefit is calculated each year and is recorded to accrued pension liability on the consolidated balance sheet. As of December 31, 2018 and 2017, the related liability for this plan was approximately $0.

Note 9 – Post-Retirement Benefits Other Than Pensions

The Cooperative sponsors a defined benefit post-retirement plan that covers both salaried and non-salaried employees, but none of its subsidiary employees. The plan provides for medical benefits for retirees between the ages of 60 and 65. The Cooperative's funding policy is pay-as-you-go.

The following table sets forth the plan's combined funded status reconciled with the amount shown in the Cooperative's consolidated financial statements at December 31, 2018 and 2017:

	2018	2017
Accrued post-retirement benefit costs, beginning	$ (3,450,816)	$ (3,181,875)
Net periodic post-retirement costs	(307,574)	(325,565)
Contributions made	136,757	100,303
Actuarial adjustment	907,912	(43,679)
Accrued post-retirement benefit cost, end of year	$ (2,713,721)	$ (3,450,816)

Note 9 – Post-Retirement Benefits Other Than Pensions (continued)

Net periodic post-retirement benefit cost includes the following components:

	2018	2017
Service cost-benefits attributed to service during the period	$ 183,560	$ 192,885
Interest cost	124,014	132,680
Net amortization and deferral	-	-
Net periodic post-retirement benefit cost	$ 307,574	$ 325,565
Amounts recognized in accumulated other comprehensive loss:		
Net actuarial gains	$ 490,702	$ (422,716)
Net prior service cost	-	-
Total recognized in other comprehensive income	$ 490,702	$ (422,716)

In 2020, medical costs are expected to increase 6.5% for pre-65 medicals, 6.0% for post-65 medical, and then drop to 4.75% per year in 2028 and after for both categories.

The weighted average discount rate used in determining the accumulated post-retirement benefit obligation is 4.21% and 3.69% for 2018 and 2017, respectively.

Benefit payments of $230,000 are expected for 2019, $200,000 for 2020, $210,000 for 2021, $200,000 for 2022, $180,000 for 2023, and $1,000,000 for 2024-2028.

Note 10 – Income Taxes

The provision for income taxes for Midwest Energy, Inc. consists of the following as of and for the year ended December 31:

	2018	2017
Current	$ 44,996	$ 11,227
Deferred	281,314	207,598
Deferred – Change in federal rate	-	(242,151)
Income tax (benefit) expense	$ 326,310	$ (23,326)

Note 10 – Income Taxes (continued)

The "Tax Reform Act" was enacted December 22, 2017. The law includes significant changes to the U.S. corporate system, including a Federal corporate rate reduction from 35% to 21%. As a result of when the Act was signed into law, the Company's deferred tax assets and liabilities were required to be remeasured using the lower 21% federal rate as of December 31, 2017. This resulted in a one-time favorable charge to tax expense of $242,151.

The net deferred tax liability as of December 31 consists of the following:

	2018	2017
Deferred tax assets (liabilities)		
Allowance for bad debt	$ 16,737	$ 11,020
Tax depreciation greater than book	(911,733)	(771,087)
Net operating losses	51,341	199,430
AMT credits	37,772	37,772
Other	(3,409)	(5,113)
Net deferred tax liability	$ (809,292)	$ (527,978)

As of December 31, 2018, Midwest Energy, Inc. had $37,772 in AMT credits available which do not have an expiration date. At December 31, 2018, Midwest Energy, Inc. had an unused federal net operating loss carryforward of approximately $245,000, which will begin expiring in 2025.

Note 11 – Related Party Transactions

Midwest Energy, Inc. and Subsidiary is a wholly-owned subsidiary of Midwest Energy Cooperative. In addition, Midwest Energy Cooperative has furnished some personnel, office space, and other necessary operating facilities such as computer time for Midwest Energy, Inc. and Subsidiary's operations. During the year, Midwest Energy Cooperative charged Midwest Energy, Inc. and Subsidiary's operations for such services. Midwest Energy, Inc. advanced a note payable to the Cooperative for the fiber activity in the amount of $5,707,134 and $4,539,272 for 2018 and 2017, respectively, bearing an interest rate of 3.50%. There is currently no firm payment plan established on the note payable due to Midwest Energy, Inc. and Subsidiary. These transactions have been eliminated in the consolidated financial statements.

Supplementary Information

This page intentionally left blank.

Midwest Energy Cooperative
Consolidating Balance Sheets
December 31, 2018

	Midwest Energy Cooperative	Midwest Energy Inc. and Subsidiary	Eliminations	Consolidated Total
ASSETS				
ELECTRIC PLANT				
In service – at cost	$ 268,764,742	$ 8,074,833	$ -	$ 276,839,575
Construction work in progress	4,407,607	-	-	4,407,607
	273,172,349	8,074,833	-	281,247,182
Less accumulated depreciation	72,569,386	4,262,959	-	76,832,345
Net electric plant	200,602,963	3,811,874	-	204,414,837
OTHER ASSETS AND INVESTMENTS				
Investments in associated organizations	36,501,076	1,000	(8,504,316)	27,997,760
Notes receivable	75,079	5,707,134	(5,707,134)	75,079
Receivables from subsidiary	85,171	-	(85,171)	-
Grant receivable	104,885	-	-	104,885
Total other assets and investments	36,766,211	5,708,134	(14,296,621)	28,177,724
CURRENT ASSETS				
Cash and cash equivalents	17,984,184	140,234	-	18,124,418
Accounts receivable, less allowance for doubtful accounts of approximately $330,000	4,374,454	1,049,067	-	5,423,521
Accounts receivable, associated organizations	-	61,238	(61,238)	-
Unbilled revenue	5,339,376	-	-	5,339,376
Current portion of notes receivable	60,000	-	-	60,000
Materials and supplies	2,537,641	-	-	2,537,641
Inventory of subsidiary		334,782	-	334,782
Other current assets and accrued assets	149,035	384,041	(22,400)	510,676
Total current assets	30,444,690	1,969,362	(83,638)	32,330,414
DEFERRED CHARGES	142,300	-	-	142,300
Total assets	$ 267,956,164	$ 11,489,370	$ (14,380,259)	$ 265,065,275

See report of independent auditors.

Midwest Energy Cooperative
Consolidating Balance Sheets
December 31, 2018

	Midwest Energy Cooperative	Midwest Energy Inc. and Subsidiary	Eliminations	Consolidated Total
LIABILITIES, EQUITIES, AND MARGINS				
EQUITIES				
Patronage capital and other equities	$ 61,256,303	$ 8,504,316	$ (8,504,316)	$ 61,256,303
LONG-TERM DEBT, NET OF CURRENT MATURITIES	177,382,773	313,027	-	177,695,800
OTHER LIABILITIES				
Post-retirement benefits other than pensions	2,713,721	-	-	2,713,721
Accrued pension liability	875,492	-	-	875,492
Total other liabilities	3,589,213	-	-	3,589,213
COMMITMENTS AND CONTINGENCIES (NOTE 7)				
CURRENT LIABILITIES				
Current maturities of long-term debt	6,297,108	82,271	-	6,379,379
Accounts payable				
Purchased power and cooperative payables	5,994,560	230,397	-	6,224,957
Regulatory Liabilities – energy optimization	384,081	-	-	384,081
Associated organizations	61,240	85,172	(146,412)	-
Other	359,712	-	(2,397)	357,315
Power supply cost recovery	1,779,843	-	-	1,779,843
Customer deposits	682,458	1,336,339	-	2,018,797
Accrued liabilities	4,422,417	117,262	-	4,539,679
Income taxes payable	-	9,848	-	9,848
Note payable to subsidiary	5,707,134	-	(5,707,134)	-
Total current liabilities	25,688,553	1,861,289	(5,855,943)	21,693,899
DEFERRED TAX LIABILITY	-	809,292	-	809,292
DEFERRED CREDITS	39,322	1,446	(20,000)	20,768
Total liabilities, equities, and margins	$ 267,956,164	$ 11,489,370	$ (14,380,259)	$ 265,065,275

Midwest Energy Cooperative
Consolidating Statements of Operations
December 31, 2018

	Midwest Energy Cooperative	Midwest Energy Inc. and Subsidiary	Eliminations	Consolidated Total
OPERATING REVENUES	$ 88,734,597	$ 7,456,523	$ (60,120)	$ 96,131,000
OPERATING EXPENSES				
Cost of power	49,701,111	-	-	49,701,111
Cost of goods sold	-	3,736,562	-	3,736,562
Distribution – operations	3,357,710	-	-	3,357,710
Distribution – maintenance	7,405,447	-	-	7,405,447
Customer accounts	3,000,785	-	-	3,000,785
Customer service and information expense	2,551,862	-	-	2,551,862
Administrative and general	6,491,225	2,231,653	(60,120)	8,662,758
Depreciation and amortization	8,747,804	435,765	-	9,183,569
Taxes – property	3,484,160	9,812	-	3,493,972
Total operating expenses	84,740,104	6,413,792	(60,120)	91,093,776
OPERATING MARGINS BEFORE FIXED CHARGES	3,994,493	1,042,731	-	5,037,224
FIXED CHARGES				
Interest on long-term debt	5,367,462	-	(197,131)	5,170,331
Total fixed charges	5,367,462	-	(197,131)	5,170,331
OPERATING MARGINS (DEFICITS) AFTER FIXED CHARGES	(1,372,969)	1,042,731	197,131	(133,107)
G&T AND OTHER CAPITAL CREDITS	4,327,670	-	-	4,327,670
NET OPERATING MARGINS	2,954,701	1,042,731	197,131	4,194,563
NON-OPERATING MARGINS				
Interest and dividend income	97,331	197,131	(197,131)	97,331
Income from subsidiary	937,803	-	(937,803)	-
Gain on sale of assets	-	40,965	-	40,965
Other income (expense)	34,758	(16,714)	-	18,044
Income tax benefit (expense)	-	(326,310)	-	(326,310)
TOTAL NON-OPERATING MARGINS (DEFICITS)	1,069,892	(104,928)	(1,134,934)	(169,970)
NET MARGINS	4,024,593	937,803	(937,803)	4,024,593
COMPREHENSIVE LOSS				
Unrealized gain on pension and post-retirement benefits other than pensions	1,218,400	-	-	1,218,400
COMPREHENSIVE INCOME	$ 5,242,993	$ 937,803	$ (937,803)	$ 5,242,993

See report of independent auditors.

MOSSADAMS

Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Board of Directors
Midwest Energy Cooperative

We have audited, in accordance with the 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, the consolidated financial statements of Midwest Energy Cooperative (the "Cooperative") as of and for the year ended December 31, 2018, and the related notes to the financial statements, which collectively comprise Midwest Energy Cooperative's consolidated financial statements, and have issued our report thereon dated March 29, 2019.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Midwest Energy Cooperative's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control. Accordingly, we do not express an opinion on the effectiveness of the Cooperative's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Cooperative's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose

Moss Adams LLP

Portland, Oregon
March 29, 2019

MOSSADAMS