HEARTLAND

ADDING VALUE

2017 Annual Report

Celebrating 40 years

HEARTLAND CONSUMERS POWER DISTRICT

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KEY PROFESSIONAL RESOURCES

AUDITORS

BKD, LLP

BOND COUNSEL

Katten Muchin Rosenman

TRUSTEE

First National Bank in Sioux Falls, SD

PAYING AGENT

Bank of New York

POWER SUPPLY

Burns & McDonnell

Energy Mix

53%
Coal-Fired

19%
Wind

0%
Peaking

28%
Market Purchase

2017 Energy

73.5 MW
Customer Peak

425,050 MWH
Demand & Energy Sales

2017 Finance

$57.7 M
Total Operating Revenue

$54.3 M
Total Operating Expenses

Adding Value

At Heartland Consumers Power District, we strive to be more than just a power provider, but rather a partner—players on the same side sharing common goals.

Each and every day we work to ensure we fulfill our vision of being a trusted leader and partner of choice in the delivery of competitively priced electricity while adding value to the communities we serve.

Opposite page: Heartland has been serving Miller, South Dakota (population 1,430) since 2005. Main Street staple Miller Rexall Drug was honored in 2015 by the South Dakota Retailers Association as South Dakota Retailer of the Year.


MILLER
Rexall
DRUGS
THE CLOTHES GARDEN
ACCESSORIES

Introduction

To be involved in a partnership means you and another party have a joint interest, a common goal you are working together to accomplish.

The year 2017 marked 40 years since Heartland began supplying electrical power to our customers. That's 40 years of partnerships that have only strengthened with time.

Our customers are the lifeblood of our organization and we work hard every day to bring value to the communities we serve. We strive to be not only a trusted power supplier, but also a valued partner in the betterment of each community we serve.

Adding Value

Hosting educational events, providing incentives for energy efficiency improvements, assisting with filing necessary reports and simply making visits are just a few of the ways Heartland serves as a community partner.

Throughout 2017, Heartland's economic development incentives saw great success as we helped facilitate a sizable amount of growth from within our customer communities.

Our Energy ONE Incentive continued to gain traction with two businesses signing on to take advantage of the special, fixed energy only pricing. Only large users of electricity are eligible to take advantage of this special rate and since its launch in 2013, only one other business had qualified.

We also had several businesses make use of our low-interest financing tool, the HELP Fund, which utilizes money from USDA's Intermediary Relending Program. We also invested in business growth by providing over $75,000 in growth incentives in 2017, which will generate an additional 1,681 megawatt-hours of energy consumed.

We look forward to much of the same in 2018 as we are already working with several businesses who are looking to take advantage of our rebates, incentives and special pricing to build or expand in the communities we serve.

Customers First

At the end of 2016, voters in the Heartland customer cities of Arlington, Howard, Miller and Plankinton elected for those municipalities to be annexed into the Heartland Consumers Power District.

The Heartland board voted to accept the annexation and placed each city in the subdivision they had requested – Plankinton into the existing Subdivision 7 and Miller, Arlington and Howard into a newly created Subdivision 11.

In early 2017, Vern Hill of Plankinton was appointed to represent Subdivision 7, filling a vacancy created by the retirement of long-time director and board president Merlin Van Walleghen. Bill Lewellen of Miller was appointed to represent Subdivision 11.

The addition of these cities to the district helped fulfill a long-held desire by customers to have more representation on Heartland's board. The original Heartland district consisted of nine subdivisions including virtually all rural areas of the 36 counties in eastern South Dakota. These subdivisions were established and board members appointed before Heartland had signed any contracts with customers. The cities of Madison, Volga and Groton eventually elected to be annexed into the district and Subdivision 10 was created.

We are glad to have these new board members who both possess extensive, first-hand knowledge of municipal utilities as well as bring the customer perspective to our board.

The board also saw one other change in 2017 as Mark Joffer was elected to serve as board president after Van Walleghen's retirement and Lisa Rave was elected to serve as vice president.

"We've always tried to keep the rates as low as possible, and made decisions with the best possible knowledge we had at the time. I have great confidence the board will keep moving in the right direction."

- Merlin VanWalleghen

Career farmer and longtime Heartland board member Merlin Van Walleghen retired in 2017 after 24 years of dedicated service. His tenure included six years as vice president and four years as president, representing Aurora, Brule, Charles Mix, Davison, Miner and Sanborn counties in South Dakota.

Heartland has served Hecla, South Dakota, (population 229) since 1976. Pictured, from left to right, are Hecla First Utility Assistant Dennis Shelton and Superintendent Brandon Casey.

Survey provides enlightenment

Heartland conducted a customer survey in 2017 so we could better understand the ultimate recipients of the electricity we provide and how they interact with their local utility. One of the first things we learned was that we have a lot of room for improvement in touting the public power story. Thirty-eight percent of respondents didn't know they were served by a public power utility.

Public power is uniquely structured and offers many advantages such as local control, funding of essential services and reliable, affordable power. We often talk about these benefits, but the survey reminded us we need to take a step back and first make sure people know who they are receiving their electricity from, before we remind them of the benefits we have to offer.

Another takeaway from the survey was the overwhelming desire by end-users for their utility to be concerned about cybersecurity. This affirmed that

Heartland's partnership with SBS Cybersecurity is an essential one. All our customers have the option to utilize a five-phase program with SBS to ensure sensitive information is protected and reduce the risk of a cyber attack.

A strong future

We were happy to announce the addition of a new customer in 2017 as the city of Valentine, Nebraska voted in April to select Heartland as their new wholesale electric power provider beginning in 2019. Valentine is Heartland's first customer in the state of Nebraska and with a winter peak of approximately 13 megawatts, one of our largest.

We at Heartland, just like our customers, know the value of careful planning and the importance of being prepared. We continually look to the future, set goals and make decisions with the best interests of our customers in mind.

Over the past three years, customers withstood incremental rate increases to meet financial projections, increase our credit rating and ensure a stable financial future for our customers.

Because our customers believed in our plan, we were happy to announce steady rates for 2018.

We look forward to another successful year and will continue looking forward, analyzing scenarios and making decisions in the best interest of our customers.

Heartland continues to look for new ways to ensure our future is bright. We are never happy with the status quo, but rather will leave no stone unturned in the quest for not just a stable outlook, but a prosperous one.

Heartland Board President Mark Joffer, left, and CEO Russell Olson

Partner and Power Provider

For the past 40 years, Heartland has been supplying electric energy to our customers throughout the Midwest.

Heartland has served Groton, South Dakota, (population 1,509) since 1976. Pictured, from left to right, are Groton Metering Technician Paul Kosel, Assistant Finance Officer April Abeln and Finance Officer Hope Block.

Heartland believes in the *power of forward thinking* — making decisions today for a sound and stable future. Heartland is dedicated to providing reliable, affordable power to our customers while ensuring open communication, excellent customer service and sound decision making for a brighter tomorrow.

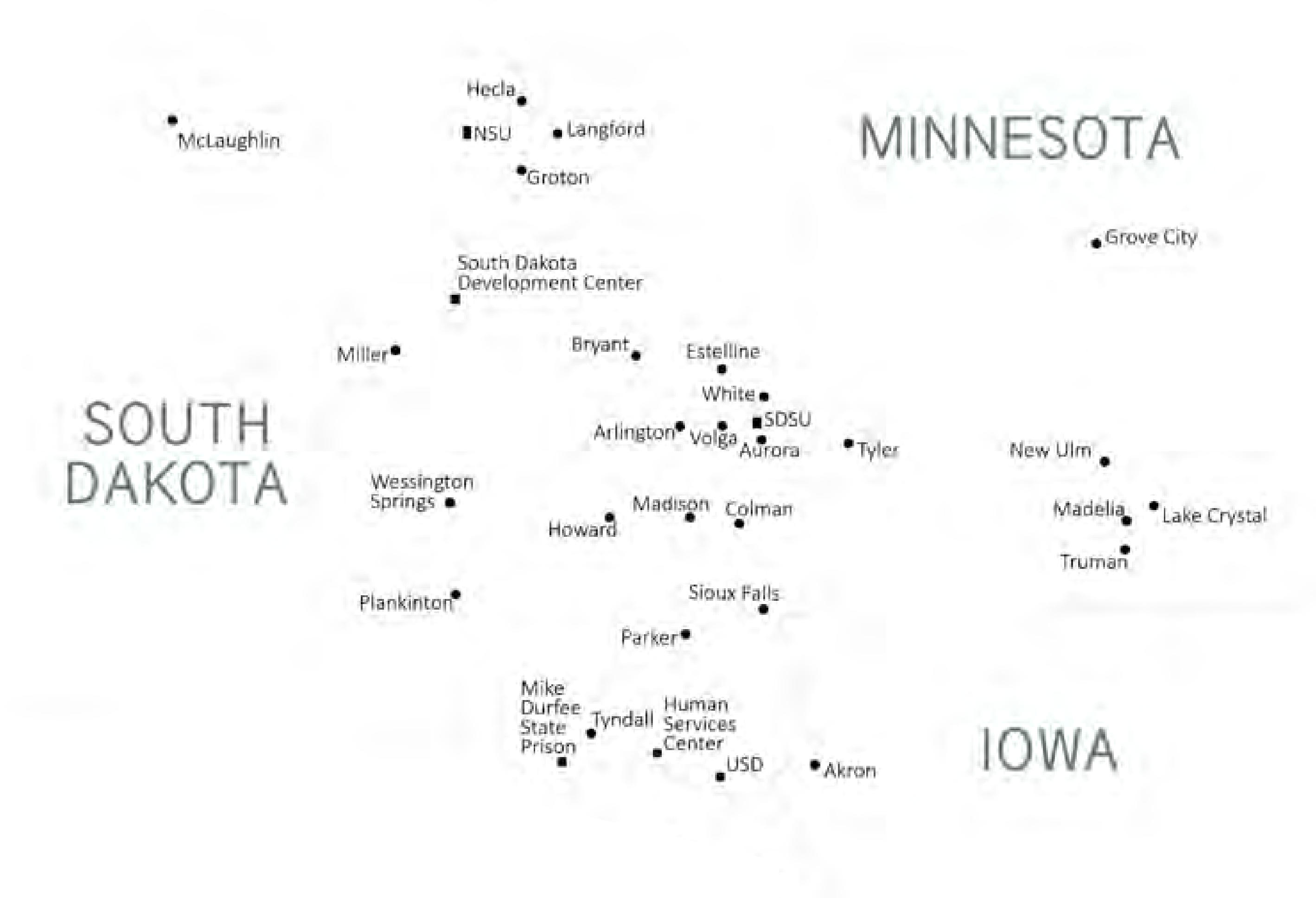
Who we serve

Heartland provides wholesale electric energy to 26 municipal electric systems in South Dakota, Minnesota and Iowa. Most of these communities are rural, with populations less than 3,000. We also provide energy solutions to six public institutions in South Dakota and have short-term or unit-contingent contract requirements with Basin Electric Power Cooperative and North Iowa Municipal Electric Cooperative Association, as well as the cities of Stanhope and Auburn, Iowa, and Garden City, Kansas.

Heartland's Customer Connections Committee was formed in 2011 to further strengthen the relationship between Heartland and our customers. Consisting of up to nine elected members, each representing a different customer, the CCC provides customers the opportunity to share feedback with Heartland staff and board members and further engage in Heartland operations.

The CCC meets regularly to discuss issues important to their individual communities as well as the entire customer base. Members bring new ideas to Heartland staff as well as collaborate with each

Heartland has been the hometown power provider of Madison, South Dakota, (population 7,425) since 1976. Pictured, left to right, are Madison Electric Utility Linemen Roy Brown and Skyler Sutten.



other to seek out solutions to problems their utilities may be facing or explore new ideas in hopes of providing the best services possible.

The CCC welcomed five new members in 2017 and includes finance officers, electric superintendents, city administrators, a state energy manager and more. Municipalities both large and small are represented with members hailing from Minnesota and South Dakota.

Power supply

Heartland provides supplemental, partial or full-requirements power supply, depending on the needs of each of our customers. Heartland's generation resources and customer loads are spread across the Midcontinent Independent System Operator and the Southwest Power Pool, both Regional Transmission Organizations managing the grid in the upper Midwest. Membership in an RTO ensures reliable power supplies, adequate transmission infrastructure and competitive wholesale electricity prices.

Heartland's coal-fired resources include a 51 MW share in Laramie River Station located in Wheatland, Wyoming as well as an 80 MW share in Whelan Energy Center Unit 2 in Hastings, Nebraska. Heartland also purchases the entire output of the Wessington Springs Wind Energy Center in South Dakota. To fulfill its power supply needs, Heartland acquires peaking capacity from its customers and other utilities.

Services and programs

Customers are at the core of our operations, and we strive to be a trusted partner to those we serve. We provide a variety of services to help foster growth and expansion in their communities as well as promote the more efficient use of electricity and improve operations.

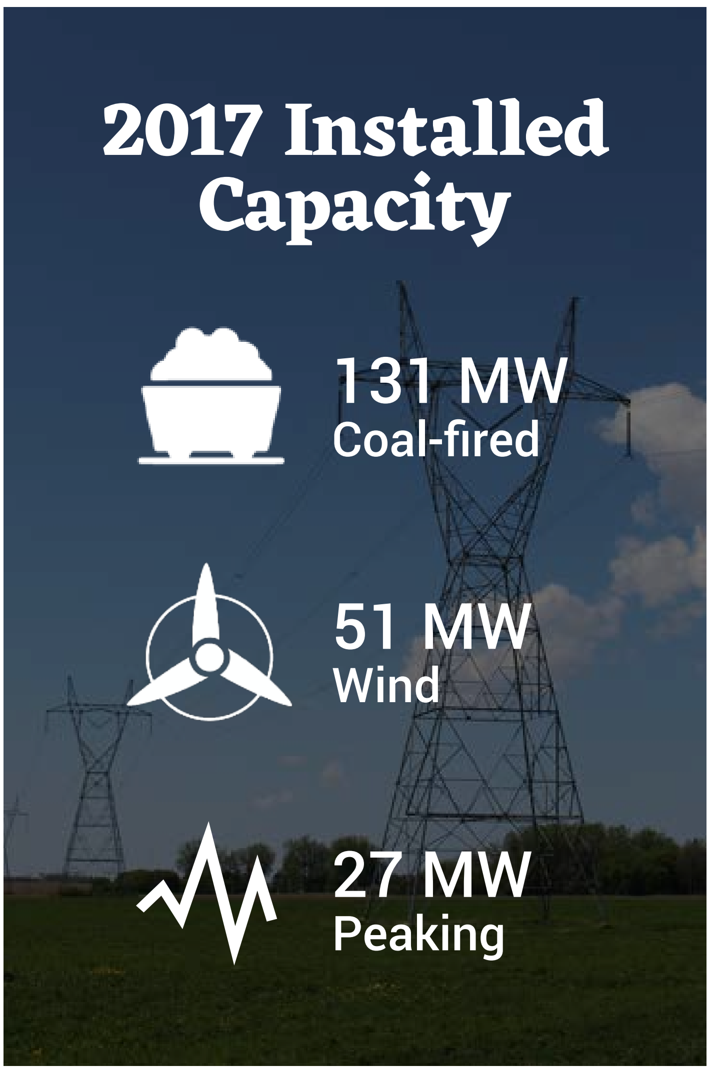
Our progressive economic development program includes grants, a revolving loan fund, growth incentives and a large-load incentive program–all of which help create economic stability while maintaining a superior quality of life.

Our comprehensive energy efficiency program, Power Forward, provides customers with valuable tools, such as incentives for residential and commercial consumers as well as grants to help with projects that optimize electric energy use at city facilities.

Through a partnership with SBS CyberSecurity, our cybersecurity program helps utilities ensure appropriate security controls are in place to prevent a crippling cyber attack. Our five-phase program helps customers establish and maintain a cybersecurity program to continually monitor and protect sensitive information.

We also host a variety of educational meetings and conferences to provide customers with the tools to succeed in this evolving environment. Each event provides insight on issues related to specific assets of electric utility operations: finance, safety, load management, economic development and more. These forums provide details on the latest technologies, techniques and obstacles while helping customers network and learn from each other and the experts.

Heartland's goal is to continually exceed our customers' expectations and provide value to each community we serve.



Heartland's annual Summer Conference combines work and play. Considered our premier customer event for twelve years and running, the Summer Conference consists of informative meetings in the morning, with speakers providing insight on effective methods to grow and develop rural communities. The afternoon allows for attendees to get to know each other while playing a round of golf or participating in alternative activities provided.

Heartland Customer Events

Annual Meeting
Since 2012

Updates customers on current activities at Heartland plus latest news, events and information relevant to the electric industry

Summer Conference
Since 2005

Connects customers with legislators and economic development officials while discussing tools and programs designed to help communities grow and thrive

Budget Meetings
Since 1995

Consists of a series of meetings in various customer communities in which the budget for the upcoming fiscal year is discussed in detail

Winter Conference
Since 2013

Offers insight on topics related to utility operations, such as safety, key accounts or load management

We are Public Power

Knowledge is power. The more knowledge people have about their utility, the more likely they are to be supportive.

Having a clear understanding of how the utility works and how decisions are made can give people a sense of ownership and pride in their utility and community.

In 2017, Heartland took steps to provide clarity on the benefits of public power and improve the customer experience.

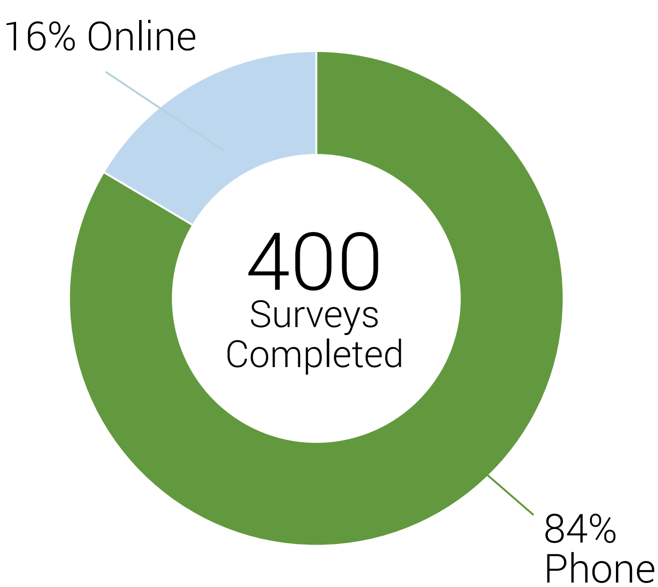
Long-time water/wastewater operator Dan Rolfes, pictured, took over as city administrator in Akron, Iowa in January of 2017. In his new role, he hopes to boost the local business district by enriching relationships with existing business owners as well as finding ways to create opportunities for new ventures on Main Street and beyond.

The best way to improve customer service is to better understand the customers. In order to get a better idea of what people value and how Heartland can better support our customer utilities we performed a customer survey in 2017.

We partnered with SDS Research to learn more about the residents in our customer communities and the expectations they have of their electricity provider. We hoped for insight to ensure we are providing services that are beneficial to the residents of each community we serve.

SDS randomly selected residents in Heartland customer communities and asked questions about customer service, social media, energy efficiency and other topics. The survey was also available online.

In all, four hundred surveys were completed and we received a lot of valuable feedback which will allow us to adjust our actions according to their wants, needs and values.



Public power story falling short

We often talk about the benefits of public power, weaving it into our newsletter stories and press releases, social media messages and other marketing material. However, according to our survey, only about half of end-use customers know they're served by a public power utility, which tells us we have to do a better job getting our message out.

Public power utilities are owned by local governments for the benefit of the citizens they serve. Municipal governments who own their power systems have more revenue available to help with essential services throughout the city.

One of the most important benefits of public power is the public has a voice in the operation of the utility. Decisions are made at the local level by those elected to represent the interests of all citizens.

If we do a better job promoting these benefits to end-users, we'll likely find more trust and stronger relationships between customers and power providers.

Stories spark a connection between residents and utilities

Timing is everything, and our survey results were released just as we were about to prepare our marketing campaign for the annual Public Power Week celebration in October. It was the perfect opportunity to start improving awareness in our customer communities.

2017 End-User Survey

SDS Research received a total of 400 returned surveys, including 335 by phone and 65 online. The margin of error is ±4.73% from a database of 5,731.

47%

Unaware their utility is public power

74%

Find value in local provider vs non-local

Overall Utility Satisfaction

1-5 Rating Scale (5 = most positive)

54% Rating 5

28% Rating 4

18% Rating 3, 2, 1

Desired Focus Areas

Reliability 43%

Value 33%

Customer Service 12%

5 out of 6

Believe their utility should be concerned about cybersecurity

Public power is great news, and we need to do a better job of shouting it from the rooftops.

We partnered with customer utilities to craft narratives highlighting each individual hometown power provider—sharing the benefits of public power with supporting information specific to that utility.

If a city was working on a project that would improve system reliability or customer service, we made sure to include that information. If a utility was staffed by a number of long-time employees, we called attention to their dedication, knowledge and years of top-quality service.

Accompanying the stories, which were submitted to all local papers to run during Public Power Week, were print advertisements featuring images of local utility staff as well as elected officials.

Our aim was to not only emphasize the value of the local utility, but also put faces with the names behind public power. We wanted to spark a connection between residents and their utility.

Expanding our reach

Building on the momentum of our Public Power Week campaign, we used other avenues to keep the public power message in the forefront.

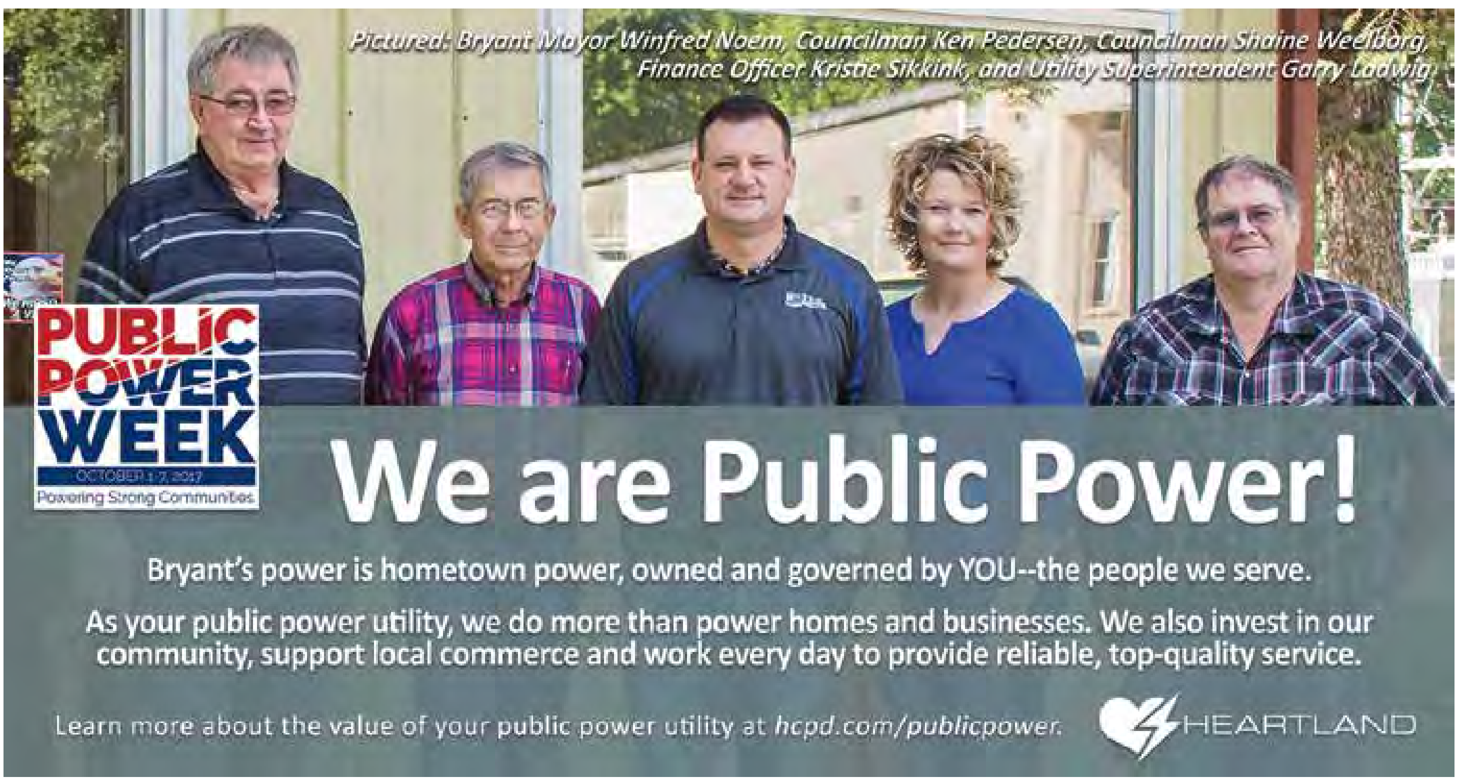
We created a new page on our website dedicated solely to the public power story. We developed and distributed marketing material for use by our customers touting the benefits of public power.

We consistently share success stories from our customer communities and the role public power plays in that success. From new businesses on Main Street to lighting upgrades at local ball fields to utility system improvements, we fill our newsletter and social media accounts with narratives emphasizing the role public power plays in community advancement. Social media affords us a further reach through interactive hashtags such as #publicpower, and allows us to collaborate with other organizations to spread and share our message.

The way we tell stories and how we share them is increasingly important in today's world of abundant and easily accessible information. We have to find ways to stand out, curating content that directs people to our customers and utilizing methods to reach more people.

We should all be proud of our public power status, and remind others every chance we get of all the assets it provides our communities.

3. We are Public Power



Heartland ran advertisements leading up to and during Public Power Week featuring local utility employees and elected officials.

Winning Over the Heart City

Heartland was excited to announce the addition of our newest customer in 2017—Valentine, Nebraska.

While many utilities experience a summer peak, the lack of natural gas supply in the city makes Valentine peak in the winter months.

The Valentine, Nebraska city council voted unanimously at their April 2017 meeting to select Heartland as their new wholesale power provider beginning in 2019.

Valentine is a unique community with progressive leadership and Heartland looks forward to serving as a valuable partner.

City will transition from Nebraska Public Power District

The council voted to move forward with Heartland based on terms submitted in response to the city's request for power supply.

Heartland will begin supplying supplemental power to the city on January 1, 2019 until their contract with Nebraska Public Power District expires at the end of 2021. After a three year step out from NPPD, Heartland will become Valentine's full-requirements supplier.

Valentine City Manager Shane Siewert noted an appreciation for Heartland's economic development programs and exceptional customer service when making the selection.

One of Heartland's largest customers

Dubbed "The Heart City," Valentine is home to roughly 2,700 people. Situated near the winding Niobara River within Nebraska's famous Sand Hills region, Valentine is Heartland's first customer in the state.

Although located in new territory, Valentine's size and location make the city a great addition to our customer mix.

As a public power community, Valentine provides electric, water and sewer services to its residents. The city's electric department provides service to approximately 1,875 electric customers and has a winter peak of approximately 13 megawatts, making it one of Heartland's largest customers in terms of energy and capacity.

A positive partnership

Heartland's suite of economic development programs was especially enticing to Valentine. The city is poised for growth and Heartland will help facilitate that growth any way we can.

Under the initial contract, Heartland will provide electric service to the city for eight years with the option to extend.

Building From Within

For many, economic development means new businesses and new jobs. But it also means improved economic well-being and quality of life, increased utility sales, an expanded tax base and added infrastructure.

For Heartland customers, it means all the above, plus just a little more.

One of the nation's leading manufacturers of specialized snowmobile parts now makes its home in Madison, South Dakota. SlyDog, Inc. specializes in the manufacture of highly engineered, compression-molded after-market snowmobile skis. Occupancy in an affordable spec building coupled with low-interest financing from Heartland have helped this start-up focus on innovative design and high-performance parts.

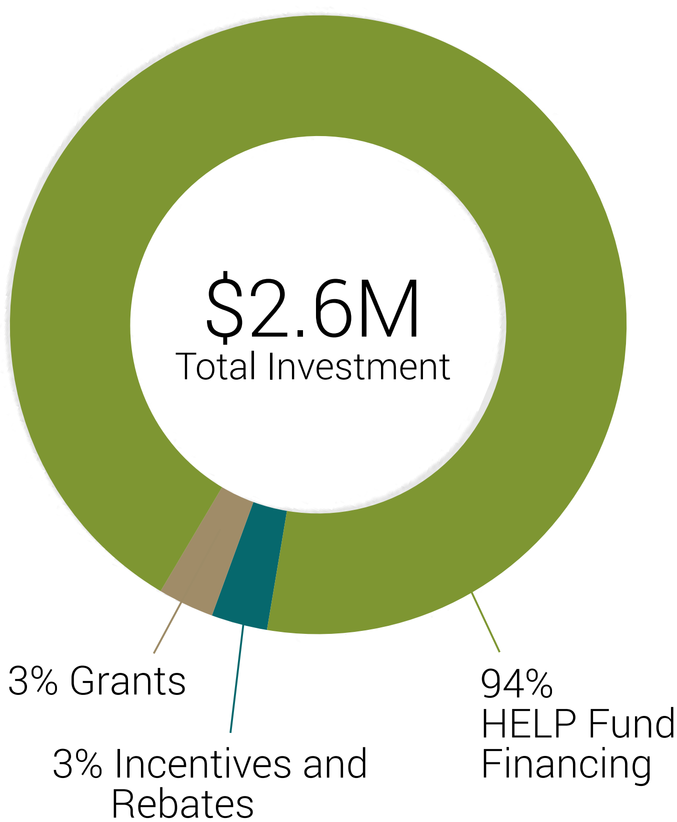
SlyDog, Inc. is a family-owned and run business. Owner Dan Palli, pictured far right, is proud to work with his three sons, from left to right, Matt, Mikael and Marcus.

Incentives, rebates, grants and loans help build healthy, self-sufficient economies. Healthy economies mean healthy communities, and for Heartland customers, a more stable power district.

Heartland's economic development program marked fifteen years of helping ensure healthy communities in 2017. Although individual components have evolved over the years, the program's goal remains the same: strengthening our customer base by promoting and rewarding growth.

Heartland invested $2.6 million in economic development projects throughout 2017. Funds helped cities upgrade infrastructure, develop marketing plans, prepare for growth and more. Small business owners, budding entrepreneurs and established enterprises utilized programs to assist with construction and expansion as well as the development of new business ventures.

2017 Program Recap



Low-interest financing key to project completion

The Heartland Economic development Loan Program (HELP) Fund finances projects involving business ownership and expansion, job creation and retention, and entrepreneurial endeavors. Utilizing money from USDA's Intermediary Relending Program, the HELP Fund is designed to help businesses and the communities in which they're located succeed.

The HELP Fund typically boasts an interest rate lower than traditional bank rates with favorable terms. We also promote local lending institutions by requiring participants to partner with them for financing.

Perhaps the biggest advantage of the HELP Fund is that it's revolving. Every loan dollar paid back to Heartland, plus interest, can be put back to work in our customer communities.

Heartland issued ten HELP Fund loans in 2017 totaling nearly $1.6 million. Most recipients utilized financing for the construction of new or expanded business facilities while one recipient used funding to merge with another local business.

The city of Colman was the lone municipal recipient and acquired financing to complete an underground electrical project.

Because the HELP Fund utilizes funding from USDA, each project funded must demonstrate the creation or saving of jobs. The HELP Fund helped secure 100 jobs in 2017.

More fortuity is on the horizon. The HELP Fund was recapped with $1 million in 2017 from USDA Rural Development, the fourth time it has been replenished from the Intermediary Relending Program. Heartland must apply for funds, and USDA determines how much to award based on several factors, including jobs created, past success and more.

A new $1.6 million multi-use facility will open in White, South Dakota in 2018. The community building will provide much-needed services to the rural community as well as create job opportunities. Project officials kicked off construction in 2017 with a wall-breaking ceremony in the existing building, a former senior care center.

Notable for this most recent recap is expanded coverage. The use of IRP funds is subject to certain rules and provisions established by USDA, such as the number of counties that may be served. The latest recap provided for the addition of Grove City, Minnesota, and Heartland's newest customer, Valentine, Nebraska as eligible recipients.

Accompanying Heartland's HELP Fund is low-interest financing through USDA's Rural Economic Development Loan and Grant program, or REDLG.

REDLG provides zero-interest loans to local utilities, which they, in turn, pass through to local businesses. The program aims to promote rural economic development and job creation projects. Utilizing REDLG funds, Heartland awarded three additional low-interest loans totaling $1.15 million in 2017.

Grants support local economies

Heartland awards economic development grants to municipal customers and their local development corporations for ventures that spark progress. Qualifying projects promote economic prosperity, support new business opportunities or improve the social and economic well-being of residents.

Economic development grants are strategic investments. In some cases, the money is the difference between seeing a project to fruition or being left with a missed opportunity.

Eleven customer communities earned economic development grants in 2017. Many projects involved updating infrastructure and services to accommodate future growth. Several were tied to housing developments, as housing is vital to workforce development, while others boosted community marketing efforts.

Our grant program continues to be a reliable resource for customers and often provides the extra incentive needed to move a project forward. It allows Heartland to serve as a valued partner in local development.

Incentives spur, reward growth

Part of supporting economic stability is stimulating growth. However, business recruitment, retention and expansion are not often achieved without assistance.

Heartland's growth incentive program encourages job creation using hiring incentives and utility rebates.

Qualifying businesses in Heartland's customer communities are eligible for cash payments for new jobs created. Additionally, we partner with the local utility to provide rebates on retail electric bills for new and growing businesses. Rebates are based on energy consumption and disbursed over the course of three years, equaling one year of free power.

Cosmetologist Krystal Williams received low-interest financing through the HELP Fund to construct a 2,500 square-foot building, pictured under construction, on Main Street of Tyndall, South Dakota. Williams will occupy the facility's salon space and lease three office spaces to other local enterprises.

Recurring theme: Preparedness

Numerous cities and development corporations took a proactive approach to community development in 2017. Heartland's economic development grant program invested nearly $28,000 in projects related to housing, industrial parks and preparations to welcome new and expanding businesses.

$10K

Housing

Plankinton and Aurora, South Dakota received grants to help develop lots and install infrastructure in housing developments in their respective communities

$8.8K

Industrial Development

Arlington and Colman, South Dakota earned grants to help their local industrial parks earn Certified Ready Site status from the Governor's Office of Economic Development

$9K

Business Recruitment

Howard, Volga and White, South Dakota utilized grants to maintain and improve facilities and infrastructure for new businesses moving to their respective communities

The program gives businesses an extra boost at a time that often includes growing pains. The program is an asset for the city as it has become a valuable recruiting tool.

A business looks at many factors when considering an expansion or relocation. Access to programs that help with cash flow during periods of growth is a true advantage of doing business in a Heartland customer community.

Eighteen businesses in nine cities collectively earned over $75,000 in growth incentives in 2017. They generated an additional 1,681 megawatt-hours of energy, with 1,485 megawatt-hours of energy attributed to new businesses.

Energy ONE Incentive pays off, gains traction

First introduced in 2013, Heartland's Energy ONE Incentive provides a special energy-only rate for new retail electric loads with an approximate demand of one megawatt or larger. For communities with a population of 3,000 or less, the incentive may be offered to new loads with a demand of 500 kilowatts or larger.

The Energy ONE rate is fixed for three years which provides consistent and predictable utility pricing, results in extensive savings and allows businesses to establish use patterns and better plan for the future.

The Denny Sanford PREMIER Center in Sioux Falls, South Dakota, was the inaugural Energy ONE participant, beginning in September of 2014. The events center marked its three-year anniversary in 2017 and recorded over $400,000 in savings since its opening.

Heartland partnered with the city of Volga, South Dakota in 2017 to provide the Energy ONE Incentive to Prairie AquaTech, an aquaculture technology company based in Brookings, South Dakota. Prairie AquaTech plans to build a multi-million-dollar facility just outside of Volga, and will utilize the city's infrastructure for water, electricity and sewer. The energy-only rate was instrumental in attracting the

2017 Growth Incentive Recap

$75K
Awarded

9
Customers Represented

20
Participating Businesses

1,681
MWh New or Expanding Energy

5. Building From Within

Kraft Heinz has been part of the New Ulm, Minnesota community (population 13,258) for over 60 years and is the city's third largest employer. The company's $100 million expansion included the addition of 50 jobs and four new production lines.

Heartland partnered with New Ulm Public Utilities to offer Kraft the Energy ONE Incentive for its first three years of operation post-expansion. Heartland provides 65% of the electricity to the expansion with NUPU providing the remaining 35%, all at the Energy ONE rate.

new industry. The company plans to break ground in 2018 and be operational in 2019.

Kraft Heinz in New Ulm, Minnesota, underwent a $100 million expansion that included the addition of 50 jobs and four new production lines. The expansion qualified for the Energy ONE Incentive and brought back the production of retail-sized Velveeta loaves to New Ulm, a production that was moved to Illinois in 2012.

Keeping costs down is always a priority for any business. Savings, such as those provided by the Energy ONE Incentive, allows a company to provide greater value to their customers.

A shared goal

Owning a business involves taking a leap of faith. Fortunately for Heartland customer communities, there are many entrepreneurs out there who want to see rural communities thrive.

At Heartland, we have the same goal, so we strive to help businesses succeed. Our economic development programs are designed to entice businesses to choose a Heartland community when deciding where to locate, and to make it a little easier for existing businesses to expand.

Heartland is committed to our customers and that's why we continue to invest in the communities we serve. We strive to create economic stability and a superior quality of life as well as to be a trusted partner. What's good for one customer is good for all, and we're proud to be part of any customer community's success.

Powering

Forward

Advocacy in Action: Each year, Heartland board and staff members travel to Washington, D.C. to take part in American Public Power Association's Legislative Rally. We meet with senators and representatives from each of the states in which we have a customer or resource and champion on behalf of our customers, promoting ideas essential to the affordable, reliable delivery of electricity.

Pictured from left to right: Heartland Board President Mark Joffer, U.S. Senator Mike Rounds (R-SD), American Public Power Association CEO Sue Kelly, U.S. Senator John Thune (R-SD) and Heartland Board Vice President Lisa Rave.

It is Heartland's vision to be a trusted leader and partner of choice. Adding value includes providing resources to help our customers succeed.

Protecting Utility Assets

Today's utilities operate in the modern world of technology. While computers, the internet and smartphones all make our jobs easier, they also increase risk. Just like any business, utilities need to ensure the appropriate security controls are in place to protect confidential information as well as prevent delay in providing services.

Heartland partners with SBS Cybersecurity to help customers implement a solid cybersecurity framework. Services are offered in five different phases, with Heartland covering half the cost of any phase.

New Ulm, MN was proactive in their efforts to ensure their resources were protected in 2017. SBS performed their Phase 1 assessment for the city with the goal being to understand where cybersecurity risk was located.

New Ulm took many corrective steps based on the assessment to protect sensitive information and prevent intruders from accessing their system and causing damage or holding information hostage.

Optimizing Use

Heartland's comprehensive energy efficiency program, Power Forward, provides customers with valuable tools, including a comprehensive incentive program to offer their residential and commercial customers, as well as grants to help with projects that optimize electric energy use at city facilities.

Purchasing an energy efficient product may cost more upfront, but the savings realized over the life of the product typically more than make up for the additional investment. Partnering with our customer utilities, Heartland provides rebates for certain purchases, including water heaters, heating and cooling equipment, LED lights and commercial refrigeration.

In 2017, Heartland issued over $50,000 to incentivize the replacement of 1,478 commercial lighting fixtures, the purchase of 93 residential LED bulbs, 3 air conditioners, 1 heat pump, 59 water heaters and for 28 refrigeration upgrades.

Not only do municipal utilities provide electricity, they consume it at city offices, libraries, parks and in street lighting. To help ease the initial burden of making investments in energy efficiency, Heartland provides grants.

Fourteen Heartland customers received energy efficiency grants in 2017. Combined savings from the incentivized projects were $31,000 and 312,000 kWh annually. The average payback period was 4.2 years.

Cybersecurity is a growing concern for all businesses, including municipalities. In October, Heartland utilized social media during National Cybersecurity Month to draw attention to this important topic.

More and more utilities are upgrading to LED street lights. As technology advances and prices continue to lower, cities can choose the best style of LED to fit with their community, providing brighter light and energy savings for years to come.

Heartland helped customers upgrade 441 street lights to LED in 2017.

2017 Energy Efficiency Rebates & Incentives

REFRIGERATION

$2,450 Awarded

18 - LED Case Lighting

4 - Refrigerators

6 - Freezers

HEATING & COOLING

$800 Awarded

3 - Air Conditioners

1 - Heat Pump

LIGHTING

$31,065 Awarded

93 - Residential LED Bulbs

1,478 - Commercial Lighting Fixtures

WATER HEATERS

$17,400 Awarded

59 - Water Heaters

2017 Energy Efficiency Grants

14

Customer Recipients

$31,380

Annual Dollar Savings

312,000 KWH

Annual Energy Savings

4.2 YEARS

Average Payback Period

Essential Services

One of the most valuable services Heartland provides is reporting assistance. The Energy Policy Act of 1992 requires Western Area Power Administration long-term firm power customers to prepare and submit integrated resource plans as a means to promote stable, efficient and economical use of electrical generation and conservation resources.

The IRP is an action plan that describes how a utility intends to serve its load in the future. Plans must be submitted every five years, along with annual updates and reports. Because the reporting can be quite cumbersome, Heartland created a coordinated effort to facilitate the submittal of IRPs and annual reports to WAPA.

Heartland completed annual updates for 22 Heartland customers in 2017, ensuring they retain their valuable federal hydropower allocations.

Heartland also assists with various other reporting throughout the year including those required by the Energy Information Administration.

Advocacy in Action

As public power providers, we are fortunate to not have to worry about the pocketbooks of our investors, because we don't have any. We are, however, concerned about the pocketbooks of the business owners and residents in our customer communities.

Regulations imposed at the federal level can have an impact on those pocketbooks. People in the Midwest spend a large portion of their income on energy. Each year we travel to our nation's capital and remind our members of Congress of this fact and that affordable electricity is necessary for a successful rural America. We also stress the importance of local control and provide education on the benefits of public power.

Heartland led the charge in 2017 against a proposal by the Trump Administration to divest the transmission assets of the federal power marketing administrations, including WAPA.

Many of Heartland's customers receive reliable, cost-based power generated at the federal hydropower dams through WAPA. Millions of Americans served by public power utilities and rural cooperatives depend on the PMAs and they are crucially important to rural communities.

Heartland created an extensive social media campaign using the hashtag #NoPMASale with a variety of graphics and messages stressing the value the PMAs provide. Our social media campaign earned an Excellence in Public Power Communications award from the American Public Power Association. We also submitted letters to the editor to local papers to raise awareness of the proposal.

Teamwork

As a consumers power district, Heartland operates under the state of South Dakota's consumers powers district laws that were originally adopted in the 1950s. In 2017, South Dakota Governor Dennis Daugaard signed Senate Bill 60, an act to revise certain provisions regarding the sale of consumers power district assets.

Existing state statutes limited the sale of a consumers power district's assets to another district, rural electric association, cooperative, municipality or other public body. SB 60 eliminated those

Heartland's social media campaign against the proposal to divest of federal PMA transmission assets mixed facts with fun, all to raise awareness of the importance of reliable, cost-based federal hydropower.

Heartland Customer Relations Manager Steve Moses was awarded the Distinguished Service Award from Minnesota Municipal Utilities Association for his years of utility service. Joining him at the banquet where he was announced as the winner were some of his co-workers who nominated him for the award. Pictured from left to right are Director of Economic Development Casey Crabtree, Communications Manager Ann Hyland, Moses, CEO Russell Olson and CFO Mike Malone.

restrictions, allowing a district to sell an asset to anyone, as approved by the board of directors.

SB 60 gives us greater flexibility moving forward and Heartland received overwhelming support from our customers in South Dakota for the bill, reaching out to senators and representatives asking for their backing of the bill. SB 60 passed both the Senate and House overwhelmingly which proves the impact those calls and emails had as well as what we can accomplish when we work together.

Service First

Excellent customer service has been Heartland's priority since the power started flowing 40 years ago. The year 2017 was no exception.

Heartland Customer Relations Manager Steve Moses was recognized by Minnesota Municipal Utilities Association in 2017 for his # years of outstanding service, not only during his tenure at Heartland but also for his time as utilities manager at Madelia Municipal Light & Power in Madelia, Minnesota.

Making Customers a Priority

Heartland continued working with the Customer Connections Committee to provide regular updates and solicit feedback. Jerry Jongeling of Sioux Falls, SD took over as chair of the committee in 2017.

The committee met quarterly, typically in conjunction with Heartland's monthly board of directors' meetings. Members provided input on Heartland conferences and meetings, reviewed Heartland's 2018 budget, heard updates on new customers and discussed power supply.

Heartland continued our partnership with local radio station KJAM in 2017, naming nine students of the month from customer communities within their listening area including Howard, Madison, Arlington, Colman and Volga, SD. Winning students were recognized on air, in the local newspapers and in Heartland's monthly newsletter.

We look forward to continuing our strong partnership with customers in 2018 and beyond, adding value to the communities we serve.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Financials

Independent Auditor's Report

Board of Directors
Heartland Consumers Power District
Madison, South Dakota

We have audited the accompanying financial statements of Heartland Consumers Power District (the District), as of and for the years ended December 31, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit 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.

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 Heartland Consumers Power District as of December 31, 2017 and 2016, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

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

Other Information

Our audits were conducted for the purpose of forming an opinion on the financial statements that collectively comprise the District's basic financial statements. The schedules of transmission operation and maintenance expenses and of administrative and general expenses as listed in the table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The schedules of transmission operation and maintenance expenses and of administrative and general expenses have not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on them.

BKD, LLP

Lincoln, Nebraska

April 9, 2018

Management's Discussion and Analysis

This discussion and analysis of Heartland Consumers Power District's (Heartland or HCPD) financial statements provides the reader an overview of the financial activities for 2017, 2016 and 2015. Heartland's financial statements are comprised of three components: (1) Management's Discussion and Analysis, (2) financial statements, and (3) notes to the financial statements. Please read this in conjunction with the audited financial statements and footnotes contained herein.

Overview of Financial Statements

The balance sheets present information on Heartland's assets and deferred outflows of resources, and liabilities and deferred inflows of resources, with the difference reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of Heartland is improving or deteriorating.

Heartland's overall financial position is summarized below (in thousands). This information is derived from the financial statements and records of Heartland.

	Net Position as of December 31,			Fiscal Year-to-Year Percentage Change	
	2017	2016	2015	From 2016 to 2017	From 2015 to 2016
Current assets	$ 27,285	$ 28,769	$ 25,552	(5.2)%	12.6%
Capital assets, net	22,155	20,402	20,260	8.6%	0.7%
Other noncurrent assets	6,633	5,500	8,601	20.6%	(36.1)%
Total assets	56,073	54,671	54,413	2.6%	0.5%
Deferred outflows of resources	801	675	536	18.7%	(5.9)%
Total assets and deferred outflows of resources	$ 56,874	$ 55,346	$ 54,949	2.8%	0.7%
Current liabilities	$ 4,885	$ 10,727	$ 14,464	(54.5)%	(25.8)%
Noncurrent liabilities	9,867	5,650	12,667	74.6%	(55.4)%
Total liabilities	14,752	16,377	27,131	(9.9)%	(39.6)%
Deferred inflows of resources	1,914	1,776	426	7.8%	316.9%
Net investment in capital assets	16,855	12,250	4,789	37.6%	155.8%
Restricted for debt service	-	5,660	6,668	(100.0)%	(15.1)%
Restricted for pensions	-	-	370	-%	100.0%
Unrestricted	23,353	19,283	15,565	21.1%	23.9%
Total net position	40,208	37,193	27,392	8.1%	35.8%
Total liabilities, deferred inflows of resources and net position	$ 56,874	$ 55,346	$ 54,949	2.8%	0.7%

7. Financials

Heartland's overall net position increased in 2017, 2016 and 2015 by $3,015,031, $9,801,428 and $11,742,652, respectively.

The decrease in customer revenue in both 2017 and 2016 was a result of two of Heartland's long-term contracts ending June 30, 2016, with the most significant being Marshall, MN. Heartland received over 10 years advance notice of the contract termination. Generation and transmission facilities represent 95% of Heartland's total capital assets. The remaining 5% of capital assets includes Heartland's headquarters building, transportation equipment, and office equipment. The level of assets should remain reasonably stable until such time as Laramie River Station (LRS) requires substantial capital improvements.

The statements of revenues, expenses and changes in net position present information showing how Heartland's net position changed during the most recent fiscal year.

Heartland's results for the current and prior two years are summarized in the following table. This information is derived from the financial statements and records of Heartland.

Results of Operations

A summary of revenues and expenses is provided in the table that follows (in thousands except power sales).

				Fiscal Year-to-Year Percentage Change	
	2017 Actual	2016 Actual	2015 Actual	From 2016 to 2017	From 2015 to 2016
Power sales					
Customer energy (MWh)	425,050	637,252	855,651	(33.3)%	(25.5)%
Customer cumulative demand (kW)	762,089	1,085,799	1,433,896	(29.8)%	(24.3)%
Revenues					
Customer revenue	$ 36,217	$ 50,071	$ 62,717	(27.7)%	(20.2)%
Contracted requirements revenue	15,455	17,893	12,609	(13.6)%	41.9%
Surplus sales revenue	4,098	2,557	2,976	60.3%	(14.1)%
Other operating revenue	1,899	4,041	969	(53.0)%	317.0%
Transfer for rate stabilization	-	(1,750)	-	100.0%	-%
Total operating revenue	57,669	72,812	79,271	(20.8)%	(8.1)%
Expenses					
LRS production and O&M	7,020	7,732	8,470	(9.2)%	(8.7)%
Cost of power	34,229	41,368	46,543	(17.3)%	(11.1)%
Transmission	7,544	6,400	5,439	17.9%	17.7%
Depreciation	1,073	1,323	1,242	(18.9)%	6.5%
Taxes	628	447	199	40.5%	124.6%
Administration and general	3,645	3,947	4,264	(7.7)%	(7.4)%
Amortization	203	1,108	203	(81.7)%	445.8%
Total operating expenses	54,342	62,325	66,360	(12.8)%	(6.1)%
Operating income	3,327	10,487	12,911	(68.3)%	(18.8)%
Total nonoperating expenses, net	(312)	(686)	(1,168)	(54.5)%	(41.3)%
Change in net position	3,015	9,801	11,743	(69.2)%	(16.5)%
Net position, beginning of year	37.193	27,392	15,649		
Net position, end of year	$ 40,208	$ 37,193	$ 27,392		

Operating revenues include firm power sales to Heartland's wholesale rate customers, other contracted sales, short-term energy sales on the surplus market, and other revenues. Demand and energy sales for 2017 were 762 MW and 425,050 MWh, respectively. This reduction is from the customer contract ending June 30, 2016. Heartland's customer peak was 73.5 MW in 2017. Demand and energy sales for 2016 were 1,086 MW and 637,252 MWh, respectively. The 2016 peak demand of Heartland's long-term wholesale customers was 126.7 MW. Heartland's wholesale customer demand and energy sales for 2015 were 1,443 MW and 855,651 MWh, respectively. Heartland's wholesale customer peak demand for 2015 was 135.7 MW.

Heartland has other energy sales contracts, in addition to its wholesale customers. The contracted requirements revenue mitigates exposure to the surplus market for excess power and the contracts typically contain fixed pricing and quantities. Many of these contracts are unit contingent and Heartland is not required to provide replacement power. These revenues were less in 2017 due to more scheduled and unscheduled unit outages compared to 2016.

Surplus energy sales are the sales of energy produced by Heartland's resources in excess of the energy required by Heartland's customers and other contracts. These sales are considered short term and nonfirm. The quantity of surplus energy and revenue is dependent upon multiple factors including availability of resources, customer and other contract requirements, and market and contractual pricing.

The operating expenses fluctuated in some areas. Production expenses (the cost for coal, transportation, and operations and maintenance at Laramie River Station (LRS)) decreased by 9.2% and 8.7% in 2017 and 2016, respectively. The largest reason for the decrease was a reduction in generation. LRS unit 1 had a long outages for environmental improvements in both 2017 and 2016.

Heartland purchases power, in addition to its ownership share in LRS, to meet the total contract resource obligations to its customers. The purchased power contracts include base-load resources, renewable generation facilities, market purchases, and additional capacity purchases required to comply with the resource reserve requirements for maintaining regional reliability.

Heartland is a member of Public Power Generation Agency (PPGA), an interlocal agency created under Nebraska statute to build WEC2, a 220 megawatt coal-fired project near Hastings, Nebraska. Heartland's participation in PPGA is for 80 megawatts. PPGA financed construction of WEC2 directly, rather than obtaining funding from its members. Heartland has a contract with Hastings Utilities for an additional share of WEC2. This contract decreases annually. Heartland also has a contract with North Iowa Municipal Electric Cooperative Association (NIMECA) in which NIMECA purchases output of WEC2 for the life of the unit. NIMECA's contract includes all owners' costs and increases annually until 2019. The combination of the Hastings Utilities contract reduction and the NIMECA contract increases resulted in reduced cost of power in 2017 and 2016. Also attributing to the reduction in the cost of power was a short-term power supply contract that corresponded with the end date of Marshall's contract in 2016.

The nonoperating revenues/expenses include interest on bonds, investment income, and amortization of costs recoverable from future billings.

Heartland made principal payments of $5,600,000 on its Electric System Second Lien Revenue Bonds, Series 2011 in 2017, and also paid down $600,000 on its operating line related to the previously outstanding Electric System Second Lien Revenue Note, Series 2010. Heartland called the Electric System Second Lien Revenue Note, Series 2010, in 2015 and the remaining balance was moved to Heartland's line of credit. This allowed Heartland to take advantage of the lower short-term interest rates on the line of credit compared to the 4.29% of the Series 2010 Note.

Fitch assigned an underlying rating of A- to Heartland and Moody's assigned A3.

Contact Information

This financial report is designed to provide a general overview of Heartland's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Micheal Malone, P.O. Box 248, Madison, SD 57042.

Balance Sheets
December 31, 2017 and 2016

Assets and Deferred Outflows of Resources

	2017	2016
Current Assets		
Cash and cash equivalents	$ 10,052,900	$ 7,965,003
Restricted cash and cash equivalents	-	5,810,693
Short-term investments	4,649,471	1,977,173
Accounts receivable	7,240,446	7,777,416
Notes receivable, current portion	581,330	435,732
Plant operation assets	4,715,107	4,769,254
Prepaid expenses and other current assets	45,428	33,279
Total current assets	27,284,682	28,768,550
Noncurrent Assets		
Notes receivable, net of allowance of $539,907 for 2017 and $343,781 for 2016	4,233,487	2,743,898
Long-term investments	215,662	273,044
Capital assets, net	22,154,984	20,402,110
Costs recoverable from future billings	1,080,970	1,388,285
Net pension asset	7,850	-
Other noncurrent assets	1,095,000	1,095,000
Total noncurrent assets	28,787,953	25,902,337
Deferred Outflows of Resources		
Deferred outflows for pensions	801,578	674,873
Total assets and deferred outflows of resources	$ 56,874,213	$ 55,345,760

See Notes to Financial Statements

Liabilities, Deferred Inflows of Resources and Net Position

		2017		2016
Current Liabilities				
Current maturities of long-term debt	$	273,595	$	5,873,946
Accounts payable		4,275,336		4,197,886
Accrued expenses		331,732		500,361
Accrued interest payable		4,514		155,312
Total current liabilities		4,885,177		10,727,505
Noncurrent Liabilities				
Line of credit		5,300,000		2,300,000
Long-term debt, net		4,310,842		2,783,366
Net pension liability		-		296,707
Other noncurrent liabilities		256,443		269,750
Total noncurrent liabilities		9,867,285		5,649,823
Total liabilities		14,752,462		16,377,328
Deferred Inflows of Resources				
Deferred inflows for pensions		163,842		21,891
Reductions of future billings		1,750,000		1,753,663
Total deferred inflows of resources		1,913,842		1,775,554
Net Position				
Net investment in capital assets		16,855,030		12,250,422
Restricted for debt service		-		5,659,735
Unrestricted		23,352,879		19,282,721
Total net position		40,207,909		37,192,878
Total liabilities, deferred inflows of resources and net position	$	56,874,213	$	55,345,760

Statements of Revenues, Expenses and Changes in Net Position
Years Ended December 31, 2017 and 2016

	2017	2016
Operating Revenues		
Customer requirements	$ 36,217,321	$ 50,070,249
Other contracted requirements	15,455,330	17,893,259
Surplus sales revenue	4,098,323	2,557,198
Other operating revenue	1,898,491	4,041,568
Transfer for rate stabilization	-	(1,750,000)
Total operating revenues	57,669,465	72,812,274
Operating Expenses		
Cost of power	41,248,568	49,099,837
Depreciation and amortization	1,275,897	2,430,760
Transmission	7,544,266	6,400,660
Other	4,274,014	4,394,270
Total operating expenses	54,342,745	62,325,527
Operating Income	3,326,720	10,486,747
Nonoperating Revenues (Expenses)		
Investment income	197,498	133,171
Interest expense	(74,081)	(386,639)
Amortization expense	(54,253)	(238,825)
Other	(380,853)	(193,026)
Net nonoperating expenses	(311,689)	(685,319)
Change in Net Position	3,015,031	9,801,428
Net Position, Beginning of Year	37,192,878	27,391,450
Net Position, End of Year	$ 40,207,909	$ 37,192,878

See Notes to Financial Statements

Statements of Cash Flows
Years Ended December 31, 2017 and 2016

	2017	2016
Operating Activities		
Receipts from customers	$ 36,459,241	$ 51,349,152
Receipts from others	21,747,194	23,518,676
Payments to suppliers	(51,321,654)	(63,773,731)
Payments to employees	(1,782,428)	(1,422,534)
Net cash provided by operating activities	5,102,353	9,671,563
Noncapital Financing Activities		
Proceeds from issuance of promissory notes	1,782,486	225,000
Payments on promissory notes	(255,361)	(273,851)
Other non operating payments	(184,727)	(176,020)
Net cash provided by (used in) noncapital financing activities	1,342,398	(224,871)
Capital and Related Financing Activities		
Advances on revolving line of credit	3,600,000	-
Payments on revolving line of credit	(600,000)	(1,700,000)
Purchase of capital assets	(3,077,819)	(1,365,219)
Payments on revenue bonds and notes	(5,600,000)	(5,750,000)
Interest paid	(224,878)	(488,147)
Net cash used in capital and related financing activities	(5,902,697)	(9,303,366)
Investing Activities		
Proceeds from sales and maturities of investment securities	2,057,358	7,183,717
Purchases of investment securities	(4,674,402)	(4,756,393)
Issuance of notes receivable	(2,745,000)	(436,407)
Repayments of notes receivable	913,687	483,903
Investment income received	183,507	175,184
Net cash provided by investing activities	(4,264,850)	2,650,004
Change in Cash and Cash Equivalents	(3,722,796)	2,793,330
Cash and Cash Equivalents, Beginning of Year	13,775,696	10,982,366
Cash and Cash Equivalents, End of Year	$ 10,052,900	$ 13,775,696
Composition of Cash and Cash Equivalents		
Cash and cash equivalents	$ 10,052,900	$ 7,965,003
Restricted cash and cash equivalents	-	5,810,693
Total	$ 10,052,900	$ 13,775,696

See Notes to Financial Statements

Statements of Cash Flows, continued

Years Ended December 31, 2017 and 2016

	2017	2016
Reconciliation of Operating Income to Net Cash Provided by Operating Activities		
Operating income	$ 3,326,720	$ 10,486,747
Adjustments to reconcile operating income to net cash provided by operating activities		
Depreciation and amortization	1,275,897	2,430,760
Amortization of advance payment received under energy purchase contract	-	(1,191,877)
Changes in balance sheet operating items		
Accounts receivable	536,970	305,554
Plant operation assets	54,147	(1,209,165)
Prepaid expenses and other assets	50,728	(665,175)
Net pension asset (liability)	(304,557)	666,712
Deferred outflows for pensions	(126,705)	(245,450)
Accounts payable	329,138	(2,450,289)
Accrued liabilities	(181,936)	122,637
Deferred inflows for pensions	141,951	(328,891)
Deferred inflows for rate stabilization	-	1,750,000
Net Cash Provided by Operating Activities	$ 5,102,353	$ 9,671,563
Supplemental Cash Flows Information		
Capital asset acquisitions included in accounts payable	$ -	$ 251,688
Increase in allowance for notes receivable	$ 196,126	$ 17,007

See Notes to Financial Statements

Notes to Financial Statements
December 31, 2017 and 2016

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Heartland Consumers Power District (Heartland) is a public corporation and a political subdivision of the State of South Dakota created under the Consumers Power District Law for the purpose of supplying electric energy. Heartland is empowered by the Consumers Power District Law to finance, own, and operate, either singly or jointly with others and anywhere within or without the boundaries of Heartland or the State of South Dakota, any electric light and power plants, lines, and systems or interest therein for the generation and transmission of electric power and energy. Heartland has firm power customers in the four-state region of Minnesota, Kansas, Iowa and South Dakota.

Rates for wholesale electric service are set by the Heartland Board of Directors. Neither the South Dakota Public Utilities Commission nor any other commission has jurisdiction over Heartland with respect to Heartland's rates and charges for power sales to its customers.

Reporting Entity

In evaluating how to define the entity for financial reporting purposes, management has considered all potential component units for which financial accountability may exist. The determination of financial accountability includes consideration of a number of criteria, including: (1) Heartland's ability to appoint a voting majority of another entity's governing body and to impose its will on that entity, (2) the potential for that entity to provide specific financial benefits to or impose specific financial burdens on Heartland and (3) the entity's fiscal dependency on Heartland. Based upon the above criteria, Heartland has determined that it has no reportable component units.

Basis of Accounting

Heartland's activities are accounted for on the flow of economic resources measurement focus and use the accrual basis of accounting. Heartland's accounting records are maintained in accordance with accounting principles generally accepted in the United States of America for regulated utilities and generally follow the Uniform System of Accounts for Public Utilities and Licenses prescribed by the Federal Energy Regulatory Commission (FERC). Heartland prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB).

Notes to Financial Statements
December 31, 2017 and 2016

Note 1: Nature of Operations and Summary of Significant Accounting Policies, continued

Basis of Accounting, continued

Heartland's accounting policies also follow the regulated operations provisions of GASB Statement No. 62, which permits an entity with cost-based rates to defer certain costs or income that would otherwise be recognized when incurred to the extent that the rate-regulated entity is recovering or expects to recover such amounts in rates charged to its customers. This method includes the philosophy that debt service requirements, as opposed to depreciation or amortization, are a cost for rate making purposes.

Use of Estimates

The preparation of 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, liabilities and deferred inflows and outflows of resources and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues, expenses and other changes in net position during the reporting period. Actual results may differ from those estimates.

Cash Equivalents

Heartland considers all highly liquid investments with an original maturity of three months or less at the date of purchase to be cash equivalents. At December 31, 2017 and 2016, cash equivalents consisted of money market funds.

Investments and Investment Income

Investments in money market mutual funds are carried at cost, which approximates fair value. Investments in U.S. Treasury securities and U.S. agency obligations are carried at fair value. Fair value is determined based on quoted market prices or yields currently available on comparable securities of issuers with similar credit ratings.

Investment income consists of interest income and realized and unrealized gains and losses.

Accounts and Notes Receivable

Accounts receivable are stated at the amount billed to customers. Accounts receivable are ordinarily due 20 days after the issuance of the invoice. Delinquent receivables are charged off as they are deemed uncollectible. Management does not believe an allowance for doubtful accounts is necessary for accounts receivable at December 31, 2017 and 2016, as there were no delinquent accounts. Notes receivable relate to Heartland's economic development program (see Note 3), and amounts due generally follow amortization schedules contained within the related note agreements. Management has established an allowance for doubtful accounts for notes receivable of $539,907 and $343,781 at December 31, 2017 and 2016, respectively.

Plant Operation Assets

The operation of the Laramie River Station (LRS) requires the establishment of certain operating assets, primarily fuel inventories, supplies, and operating cash. These assets are managed by the operating agent for LRS and are stated at cost.

Capital Assets

Capital assets are recorded at cost at the date of acquisition. Depreciation is computed using the straight-line method over the estimated useful life of each asset, which is normally 20 - 30 years for utility plant, 5 - 10 years for vehicles, furniture, and various office equipment and 40 years for buildings.

Compensated Absences

Employees earn vacation days at varying rates depending on years of service. In the event of termination, an employee is reimbursed for accumulated vacation time. Expense and the related liability are recognized when earned and vacation benefits are redeemable as time off or in cash. Employees earn sick leave at the rate of approximately one day per month. Upon normal retirement, an employee can use any accumulated sick time to pay for certain qualified medical expenses. Expense and the related liability for sick leave benefits are recognized when earned to the extent the employee is expected to realize the benefit in cash determined using the termination payment method. Compensated absences expected to be used during the next fiscal year are classified as a current liability in accrued expenses. The remaining balance is reflected as a noncurrent liability.

Regulated Operations

Rates for Heartland's regulated operations are established and approved by the Board of Directors. Heartland applies the regulated operations provisions of GASB Statement No. 62, which provide for the deferral of expenses which are expected to be recovered through customer rates over some future period (costs recoverable from future billings) and reductions in earnings to cover future expenditures (reductions of future billings). Costs recoverable from future billings are primarily comprised of charges incurred in relation to Heartland's bond issuances and costs incurred by Heartland for initial payments made on long-term capacity contracts. These costs are being amortized in future rate periods when such costs are included in the revenue requirements to establish electric rates. Reductions of future billings are comprised of the unrealized net gains on investments and a Board approved transfer for rate stabilization.

Notes to Financial Statements
December 31, 2017 and 2016

Note 1: Nature of Operations and Summary of Significant Accounting Policies, continued

Pensions

For purposes of measuring the net pension asset and liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension revenue and expense, information about the fiduciary net position of the South Dakota Retirement System (SDRS) and additions to/deductions from SDRS's fiduciary net position have been determined on the same basis as they are reported by SDRS. Heartland's contributions and net pension asset and liability are recognized on the accrual basis of accounting.

Net Position Classification

Net position is required to be classified into three components – net investment in capital assets; restricted; and unrestricted. These classifications are defined as follows:

Net investment in capital assets - This component of net position consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets. Deferred outflows of resources and deferred inflows of resources that are attributable to the acquisition, construction, or improvement of those assets or related debt are included in this component of net position. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of net investment in capital assets.

Restricted - This component of net position consists of constraints placed on net position use through external constraints imposed by creditors (such as through debt covenants), contributors, or law or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.

Unrestricted - This component of net position consists of the net amount of the assets, liabilities and deferred inflows and outflows of resources that do not meet the definition of "restricted" or "net investment in capital assets."

When both restricted and unrestricted resources are available for use, it is Heartland's policy to use restricted resources first, then unrestricted as they are needed.

Classification of Revenues

Operating revenues and expenses generally result from providing services in connection with Heartland's ongoing operations. The principal operating revenues are charges to customers for services. Operating expenses include the cost of service, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Taxes

Heartland is exempt from federal income taxes as it is a political subdivision of the state of South Dakota. Heartland may be subject to franchise taxes in states in which it operates. Tax expense was $1,960 and $3,880 in 2017 and 2016, respectively.

Note 2: Deposits, Investments and Investment Return

Heartland's investing is performed in accordance with the investment policy adopted by its Board of Directors and applicable state statutes. Heartland may invest in certificates of deposit, time deposits, repurchase agreements, and various U.S. Treasury securities and U.S. agency obligations.

Deposits

State statutes require banks either to give bond or to pledge government securities to Heartland in the amount of Heartland's deposits. Heartland's cash deposits, including certificates of deposit, are insured up to $250,000 by the Federal Deposit Insurance Corporation (FDIC). Any cash deposits or certificates of deposit in excess of the $250,000 FDIC limits are covered by collateral held in a Federal Reserve Bank pledge account or by an agent for Heartland and thus, no custodial risk exists. No legal opinion has been obtained regarding the enforceability of any collateral arrangements.

Notes to Financial Statements
December 31, 2017 and 2016

Note 2: Deposits, Investments and Investment Return, continued

Investments

At December 31, 2017 and 2016, Heartland had the following investments and maturities:

				Maturities in Years					
		Carrying value		Less than 1		1-5		6-10	Credit Ratings (Moody's)
December 31, 2017									
Money market mutual funds	$	8,660,744	$	8,660,744	$	-	$	-	$ Aaa-mf
U.S. Treasury securities		4,675,044		4,675,044		-		-	N/A
U.S. agency obligations		190,089		-		-		190,089	Aaa
	$	13,525,877	$	13,335,788	$	-	$	190,089	$
December 31, 2016									
Money market mutual funds	$	12,257,085	$	12,257,085	$	-	$	-	$ Aaa-mf
U.S. Treasury securities		2,002,110		-		2,002,110		-	N/A
U.S. agency obligations		248,107		-		-		248,107	Aaa
	$	14,507,302	$	12,257,085	$	2,002,110	$	248,107	$

Disclosures About Fair Value of Assets and Liabilities

Fair value is 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. Fair value measurements must maximize the use of observable inputs and minimize the use of unobservable inputs. There is a hierarchy of 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 supported by little or no market activity and are significant to the fair value of the assets or liabilities

Heartland's investments in money market mutual funds are carried at cost and thus are not included within the fair value hierarchy. Heartland's investments in U.S. Treasury securities and U.S. agency obligations are measured at fair value on a recurring basis, and are classified within Level 2 of the fair value hierarchy at December 31, 2017 and 2016.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Heartland's investment policy provides limitations on the maturities of the various types of investments as a means of managing its exposure to fair value losses arising from interest rate fluctuations.

Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Heartland's investment policy establishes requirements for all investment securities to be in compliance with ratings established in bond indentures, for which substantially all investments are held.

Custodial Credit Risk

For an investment, custodial credit risk is the risk that, in the event of a failure of the counterparty, Heartland would not be able to recover the value of its investment securities that are in the possession of an outside party. Heartland's investments in U.S. agency obligations are held in a book entry system in an account designated as a customer account at the Federal Reserve and the custodian's internal records identify Heartland as owner.

Concentration of Credit Risk

Concentration of credit risk is the risk associated with the amount of investments Heartland has with any one issuer that exceeds 5% or more of its total investments. Investments issued or explicitly guaranteed by the U.S. Government are excluded from this requirement. Heartland's investment policy limits the amount of its investment portfolio that may be invested in any one issuer, other than U.S. government securities, to 10%. No investments at December 31, 2017 or 2016 exceeded 5%.

Summary of Carrying Values

The carrying values of deposits and investments shown above are included in the balance sheets at December 31, 2017 and 2016 as follows:

	2017	2016
Carrying value		
Deposits	$ 1,392,156	$ 1,518,611
Investments	13,525,877	14,507,302
	$ 14,918,033	$ 16,025,913

Notes to Financial Statements
December 31, 2017 and 2016

Note 2: Deposits, Investments and Investment Return, continued

Summary of Carrying Values, continued

Included in the following balance sheet captions:

	2017	2016
Current Assets		
Cash and cash equivalents		
Operating funds	$ 352,987	$ 545,812
General reserve funds	8,510,584	3,715,507
Revolving loan fund program accounts	1,189,216	1,122,798
Rate stabilization fund	113	2,580,886
Total	10,052,900	7,965,003
Restricted cash and cash equivalents		
Energy efficiency and incentive grant fund	-	59,730
Debt service funds	-	5,750,963
Total	-	5,810,693
Short-term investments - rate stabilization fund	4,649,471	1,977,173
Noncurrent Assets		
Long-term investments - rate stabilization fund	215,662	273,044
	$ 14,918,033	$ 16,025,913

Investment Return

Investment return for the years ended December 31, 2017 and 2016 consisted of interest income and realized gains of $120,380 and $92,257, respectively. Unrealized gains and losses on restricted investments are deferred and reported as reductions of future billings shown as a deferred inflow of resources in accordance with the regulated operations provisions of GASB Statement No. 62.

Note 3: Notes Receivable

Type of Notes	2017 January 1,	Additions	Reductions	December 31,	Due Within One Year
4.0% to 4.5% notes in connection with Heartland's economic development rogram, payable in annual installments through December 2018	$ 139,835	$ -	$ 6,963	$ 132,872	$ -
3.0% to 5.0% notes in connection with the Intermediary Relending Program Promissory Note (see Note 13), due in monthly installments through September 2027	1,126,035	1,595,000	540,663	2,180,372	262,867
0.0% to 3.0% notes in connection with the Rural Economic Development Loan Agreement and Rural Economic Development Grant Agreement (see Note 13), due in monthly installments through November 2028	2,257,541	1,150,000	366,061	3,041,480	318,463
Allowance for notes receivable	(343,781)	(196,126)	-	(539,907)	-
Total notes receivable, net	$ 3,179,630	$ 2,548,874	$ 913,687	$ 4,814,817	$ 581,330

Type of Notes	2016 January 1,	Additions	Reductions	December 31,	Due Within One Year
4.0% to 4.5% notes in connection with Heartland's economic development program, payable in annual installments through December 2018	$ 161,218	$ 2,657	$ 24,040	$ 139,835	$ 9,461
3.0% to 6.25% notes in connection with the Intermediary Relending Program Promissory Note (see Note 13), due in monthly installments through January 2024	842,593	433,750	150,308	1,126,035	116,715
Interest-free notes in connection with the Rural Economic Development Loan Agreement and Rural Economic Development Grant Agreement (see Note 13), due in monthly installments through November 2028	2,567,096	-	309,555	2,257,541	309,556
Allowance for notes receivable	(326,774)	(17,007)	-	(343,781)	-
Total notes receivable, net	$ 3,244,133	$ 419,400	$ 483,903	$ 3,179,630	$ 435,732

Interest income on these notes totaled $77,118 and $40,914 for 2017 and 2016, respectively, and is included within investment income on the statements of revenues, expenses and changes in net position.

Notes to Financial Statements
December 31, 2017 and 2016

Note 4: Capital Assets

Capital assets at December 31, 2017 and 2016 consisted of the following:

	2017	2016
Depreciable assets		
Missouri Basin Power Project	$ 56,663,387	$ 56,029,934
Transmission Project I (TP I)	1,085,293	1,085,293
Groton substation (TP III)	415,292	408,641
Heartland headquarters building	2,837,333	2,837,333
General plant	821,526	811,285
Total depreciable assets	61,822,831	61,172,486
Nondepreciable assets		
Land	80,402	80,402
Construction in progress	3,035,525	1,030,796
Total nondepreciable assets	3,115,927	1,111,198
	$ 64,938,758	$ 62,283,684

Capital assets activity for 2017 and 2016 was:

	2017				
	Beginning Balance	Additions	Retirements	Transfers	Ending Balance
Missouri Basin Power Project	$ 56,029,934	$ -	$ (135,755)	$ 769,208	$ 56,663,387
Transmission Project I (TP I)	1,085,293	-	-	-	1,085,293
Groton substation (TP III)	408,641	6,651	-	-	415,292
Heartland headquarters building	2,837,333	-	-	-	2,837,333
General plant	811,285	45,543	(35,302)	-	821,526
Land	80,402	-	-	-	80,402
Construction in progress	1,030,796	2,773,937	-	(769,208)	3,035,525
Total capital assets	62,283,684	2,826,131	(171,057)	-	64,938,758
Less accumulated depreciation	(41,881,574)	(1.073,257)	171,057	-	(42,783,774)
Capital assets, net	$ 20,402,110	$ 1,752,874	$ -	$ -	$ 22,154,984

	2016									
	Beginning Balance		Additions		Retirements		Transfers		Ending Balance	
Missouri Basin Power Project	$	54,555,764	$	66,704	$	(189,150)	$	1,596,616	$	56,029,934
Transmission Project I (TP I)		1,085,293		-		-		-		1,085,293
Transmission Project II (TP II)		6,752,305		-		(6,752,305)		-		-
Groton substation (TP III)		408,641		-		-		-		408,641
Heartland headquarters building		2,837,333		-		-		-		2,837,333
General plant		759,685		51,600		-		-		811,285
Land		80,402		-		-		-		80,402
Construction in progress		1,280,756		1,346,656		-		(1,596,616)		1,030,796
Total capital assets		67,760,179		1,464,960		(6,941,455)		-		62,283,684
Less accumulated depreciation		(47,499,907)		(1,323,122)		6,941,455		-		(41,881,574)
Capital assets, net	$	20,260,272	$	141,838	$	-	$	-	$	20,402,110

Heartland is a 24% of 75% (total of 18%) owner of TP I, which consists of approximately eight miles of 115 kv transmission line and associated switching equipment.

TP II consisted of 3 115/69 kv substations, certain improvements to three East River Electric Power Cooperative (East River) 69/12.5 kv substations, three microwave towers and associated facilities, and approximately 51 miles of additions to East River 115 kv and 69 kv transmission lines, the additions owned jointly by Heartland and East River as tenants in common. Heartland held a 99% ownership interest and East River a 1% ownership interest in those additions. East River has 100% use of this East River Section of TP II and purchased 100% of the total capacity of this section on a take-or-pay basis. In accordance with the terms of the agreement described in Note 7, East River executed its option to acquire Heartland's interest in TP II during 2016.

TP III consists of a 345/115 kv substation located near Groton, South Dakota; a 115 kv tie line between the Groton substation and the substation owned by Western Area Power Administration (WAPA); and a 115 kv circuit breaker in addition to the WAPA Groton substation for the termination of the tie line. Heartland owns a 3.9% share in TP III.

Heartland is also a 3% co-owner of the Missouri Basin Power Project, which includes Laramie River Station (LRS), a three-unit, 1,650 MW, coal-fired power supply station in eastern Wyoming, and a related transmission system.

Note 5: Credit Facilities

Line of Credit

In March 2015, Heartland entered into a revolving credit agreement with a financial institution that provides for borrowings up to $25,000,000; secured by a subordinate lien on the revenues of Heartland's electric system. The agreement expires on March 23, 2018, and can be extended at the option of Heartland. Borrowings under the credit agreement bear interest at varying rates, and cannot exceed a maximum rate, as defined in the agreement (1.92% and 1.41% at December 31, 2017 and 2016, respectively). The agreement also provides for standby letters of credit, not to exceed $5,000,000 in the aggregate. The amount available under Heartland's revolving credit agreement is reduced by the amount of any issued standby letters of credit. Heartland had outstanding borrowings of $5,300,000 and $2,300,000 on this line at December 31, 2017 and 2016, respectively. Heartland management has created an internal loan amortization schedule to

Note 5: Credit Facilities, continued

Line of Credit, continued

document their intent of repayment of the outstanding balance on the line of credit by February 2019. This internal amortization schedule shows principal repayments of $3,350,000 and $1,950,000 in 2018 and 2019, respectively.

Letter of Credit

As financial security for Heartland's performance under certain financial transmission rights and transmission congestion rights in regional transmission organizations in which Heartland participates, Heartland has obtained a standby letter of credit for $1.5 million at December 31, 2017 and 2016. The letter of credit expires September 30, 2018, and can be renewed for an additional one-year term.

Note 6: Long-term Liabilities

Long-term liabilities at December 31, 2017 consisted of the following:

	2017				
Type of Debt	January 1,	Additions	Reductions	December 31,	Due Within One Year
4.75-5.25% Electric System Second Lien Revenue Bonds, Series 2011, with interest payments due semi-annually and principal payments due on January 1, 2016 and 2017	$ 5,600,000	$ -	$ 5,600,000	$ -	$ -
1.0% Intermediary Relending Program Promissory Note, due annually on October 16 with a final payment due October 16, 2036	573,283	-	26,105	547,178	26,366
1.0% Intermediary Relending Program Promissory Note, due annually on June 25 with a final payment due June 25, 2040	579,322	88,736	25,933	642,125	25,417
1.0% Intermediary Relending Program Promissory Note, due annually on November 10, beginning in 2020, with a final payment due November 10, 2046	225,000	693,750	-	918,750	-
0% Rural Economic Development Promissory Note, with principal payments due in monthly installments of $6,852 through July 31, 2019	212,396	-	75,372	137,024	82,224
0% Rural Economic Development Promissory Note, with principal payments due in monthly installments of $3,299 through April 30, 2031	567,307	-	36,289	531,018	39,588
0% Rural Economic Development Promissory Note, with principal payments due in monthly installments of $8,333 through December 31, 2025	900,004	-	91,662	808,342	100,000
0% Rural Economic Development Promissory Note, with principal payments due in monthly installments of $10,417, beginning in October 2019, through September 21, 2027	-	1,000,000	-	1,000,000	-
Total bonds and notes payable	8,657,312	1,782,486	5,855,361	4,584,437	273,595
Compensated absences	327,770	137,961	117,781	347,950	91,507
Total long-term liabilities	$ 8,985,082	$ 1,920,447	$ 5,973,142	$ 4,932,387	$ 365,102

Long-term liabilities at December 31, 2016 consisted of the following:

	2016				
Type of Debt	January 1,	Additions	Reductions	December 31,	Due Within One Year
4.75-5.25% Electric System Second Lien Revenue Bonds, Series 2011, with interest payments due semi-annually and principal payments due on January 1, 2016 and 2017	$ 11,350,000	$ -	$ 5,750,000	$ 5,600,000	$ 5,600,000
1.0% Intermediary Relending Program Promissory Note, due annually on October 16 with a final payment due October 16, 2036	599,130	-	25,847	573,283	26,105
1.0% Intermediary Relending Program Promissory Note, due annually on June 25 with a final payment due June 25, 2040	605,518	-	26,196	579,322	26,029
1.0% Intermediary Relending Program Promissory Note, due annually on November 10, beginning in 2020, with a final payment due November 10, 2046	-	225,000	-	225,000	-
0% Rural Economic Development Promissory Note, with principal payments due in monthly installments of $6,852 through July 31, 2019	294,620	-	82,224	212,396	82,224
0% Rural Economic Development Promissory Note, with principal payments due in monthly installments of $3,299 through April 30, 2031	606,895	-	39,588	567,307	39,588
0% Rural Economic Development Promissory Note, with principal payments due in monthly installments of $8,333 through December 31, 2025	1,000,000	-	99,996	900,004	100,000
Total bonds and notes payable	14,456,163	225,000	6,023,851	8,657,312	5,873,946
Compensated absences	327,804	99,682	99,716	327,770	82,572
Total long-term liabilities	$ 14,783,967	$ 324,682	$ 6,123,567	$ 8,985,082	$ 5,956,518

Debt service requirements at December 31, 2017 are as follows:

	Principal	Interest	Total
2018	$ 273,595	$ 19,847	$ 293,442
2019	271,103	20,563	291,666
2020	350,649	20,065	370,714
2021	351,535	19,179	370,714
2022	352,405	18,309	370,714
2023-2027	1,544,101	78,222	1,622,323
2028-2032	607,316	55,153	662,469
2033-2037	466,375	30,892	497,267
2038-2042	285,418	10,849	296,267
2043-2047	81,940	852	82,792
	$ 4,584,437	$ 273,931	$ 4,858,368

Heartland has executed four credit agreements with two financial institutions, two for $740,000 and two for $1,000,000, which are renewed annually. The credit agreements allow Heartland to retain drawing capacity at least equal to the issued and outstanding amount of the Rural Economic Development Promissory Notes. There were no amounts outstanding under these credit agreements at December 31, 2017 and 2016.

The principal and interest on the revenue notes and bonds are payable solely from, and secured solely by, a pledge of and lien on: (1) the revenues of Heartland's electric system, subject to prior payments there from of operation and maintenance expense; (2) the proceeds of the sale of the notes or bonds; and (3) all accounts established under the Bond Resolution, including income, if any, from investments thereof. The debt was paid in full by Heartland in January 2017. Principal and interest for the current year and total operating revenues were $5,747,000 and $57,669,465, respectively.

Notes to Financial Statements
December 31, 2017 and 2016

Note 7: Power Sales Agreements

Heartland is a party to electric power sales agreements with municipalities in South Dakota, Minnesota, Kansas and Iowa, whereby Heartland has undertaken to provide primary power to and to supplement existing power sources of the parties. Rates are established annually by the Board of Directors. The majority of these agreements expire in 2040.

Heartland had a power sales agreement with Northern Electric Cooperative, Inc. (Northern) to provide supplemental electric service to a small portion of Northern's service area under the same terms and conditions as the agreements with Heartland's municipal customers. This agreement expired in 2016. Heartland also has power sales agreements with the State of South Dakota to provide service to various state institutions.

Heartland had an agreement with East River Electric Power Cooperative whereby East River will pay approximately 95% of the operating expenses of TP II on a take-or-pay basis. The payments were set to underwrite the cost of debt service on the associated bonds along with Heartland's overhead expenses. East River operated and maintained the facilities at its own expense. The contract continued until 2016, at which time East River executed its option under the agreement and acquired Heartland's interest for $1,000.

Heartland entered into power sales agreements with Basin Electric Power Cooperative (Basin) whereby Heartland will sell and deliver approximately 50 MW of power to Basin through May 31, 2021. The agreements provide for a fixed energy rate throughout the term of the contracts.

Note 8: Commitments

Public Power Generation Agency (PPGA)

Heartland has entered into an agreement with other utilities, creating an interlocal, PPGA. In connection with PPGA, Heartland has also entered into a long-term participation power agreement whereby Heartland has agreed to share in the energy output of the Whelan Energy Center Unit 2, a 220 MW coal-fired power plant, which became commercially operational in May 2011. Heartland's commitment is for 36.36%, or 80 MW, of the output of the project, which extends to the later of the life of the project or January 2041, which represents the date of final maturity on the bonds issued by PPGA for the project.

Energy Purchase Contracts

Heartland entered into an energy purchase contract with a national energy company to purchase 30 MW of energy at a fixed price during the period of January 1, 2014 through June 30, 2016. In connection with the agreement, Heartland received a $6,000,000 advance payment from the energy company in 2012. This advance payment was recorded as unearned revenue and was recognized over the term of the contract as a reduction of the cost of the power purchased under the agreement.

Note 9: Retirement Plans

Defined Benefit Plan

Plan Description

Heartland contributes to the South Dakota Retirement System (the Plan), which is a cost-sharing, multiple-employer, public employee retirement system, providing retirement, disability and survivors benefits. The Plan is a defined benefit plan covering all full-time employees of Heartland. Authority for establishing, administering and amending plan provisions are found in South Dakota Codified Law 3-12. In accordance with the provisions of GASB Statement No. 68, Heartland accounts for and reports its participation in the Plan, based on its calculated proportionate share of contributions to the Plan. The Plan issues a publicly available financial report that includes financial statements and required supplementary information for the Plan. That report may be obtained at http://www.sdrs.sd.gov/publications/ or by to writing the South Dakota Retirement System, P.O. Box 1098, Pierre, SD 57501-1098.

Contributions

Covered employees are required by state statute to contribute a percentage of their salary (6%) to the Plan, and Heartland is required to match the employee contribution. The contribution requirements of plan members and Heartland are established and may be amended by the Plan's board of trustees. Contributions made to the Plan by Heartland were $107,920 and $103,771 during 2017 and 2016, respectively, and were in accordance with statutory rates. The employees' contributions during 2017 and 2016 were $88,534 and $84,452, respectively, and were in accordance with statutory rates.

Benefits

The Plan provides retirement, disability, and survivor benefits based on an employer's membership class within the Plan. Heartland is a Class A member in the Plan. Class A members who retire after age 65 with three years of service are entitled to an unreduced annual retirement benefit. An unreduced annual retirement benefit is also available after age 55 for Class A members, where the sum of age and credited service is greater than or equal to 85. The annual increase in benefits payable is indexed to the consumer price index annually on July 1st, with further adjustments based on the funded status of the Plan. The right to receive benefits vests after three years of credited service.

Pension Assets and Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At December 31, 2017, Heartland reported an asset of $7,850 for its proportionate share of the collective net pension asset for the Plan. At December 31, 2016, Heartland reported a liability of $296,707 for its proportionate share of the collective net pension liability for the Plan. The net pension asset and net pension liability were measured as of June 30, 2017 and 2016, respectively, and the total pension liability used to calculate these amounts was determined by an actuarial valuation as of those dates. Heartland's proportionate share of the net pension asset and net pension liability was based on Heartland's share of contributions to the Plan relative to all employer contributions to the Plan for the

Note 9: Retirement Plans, continued

Defined Benefit Plan, continued

Pension Assets and Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions, continued

measurement period. At December 31, 2017 and 2016, Heartland's proportion was 0.086% and 0.088%, respectively.

For the years ended December 31, 2017 and 2016, Heartland recognized pension revenue of $289,311 and pension expense of $92,371, respectively. At December 31, 2017 and 2016, Heartland reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	December 31, 2017		December 31, 2016	
	Deferred Outflows of Resources	Deferred Inflows of Resources	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	$ 125,778	$ -	$ 103,290	$ -
Net difference between projected and actual earnings on pension plan investments	-	150,923	330,039	-
Changes of assumptions	609,500	-	177,714	-
Change in Heartland's proportionate share	-	12,919	-	21,891
Heartland contributions subsequent to the measurement date	66,300	-	63,830	-
Total	$ 801,578	$ 163,842	$ 674,873	$ 21,891

The deferred outflows of resources related to pensions resulting from Heartland contributions subsequent to the measurement date will be recognized as a reduction of pension expense in the fiscal year ending December 31, 2018. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

Year Ending December 31,	
2018	$ 149,521
2019	262,127
2020	195,631
2021	(35,843)
	$ 571,436

Actuarial assumptions – The total pension liability in the June 30, 2017 and 2016 actuarial valuations was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2017 - 2.25% 2016 - 3.25%
Salary increases	2017 - 6.50% at entry to 3.0% after 25 years of service 2016 - 5.83% at entry to 3.87% after 30 years of service
Discount rate	2017 - 6.50%, net of pension plan investment expense 2016 - 7.50%, net of pension plan investment expense

Mortality rates for the June 30, 2017 actuarial valuation were based on the RP-2014 Mortality Table, projected generationally with Scale MP-2016. Mortality rates for the June 30, 2016 actuarial valuation were based on the RP-2000 Mortality Table, projected generally with Scale BB and with rates reduced to fit recent experience.

The actuarial assumptions used in the June 30, 2017 and 2016 valuations were based on the results of an actuarial experience study, which covered the five-year period ending June 30, 2011.

The long-term expected rate of return on pension plan investments was determined using a method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and best estimates of arithmetic real rates of return for each major asset class as of December 31, 2017 and 2016, are summarized in the following table:

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Global Equity	58.0%	4.8%
Fixed Income	30.0%	1.8%
Real Estate	10.0%	4.6%
Cash	2.0%	0.7%
Total	100.0%	

Discount rate – The discount rate used to measure the total pension liability in 2017 and 2016 was 6.50% and 7.50%, respectively. The projection of cash flows used to determine the discount rate assumed that contributions from plan members will be made at the current contribution rate, and that contributions from employers will be made at contractually required rates. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

Sensitivity of Heartland's proportionate share of the net pension (asset) liability to changes in the discount rate – The following presents Heartland's proportionate share of the net pension (asset) liability calculated using the discount rate of 6.50%, as well as what Heartland's proportionate share of the net pension (asset) liability would be if it were calculated using a discount rate that is one

Note 9: Retirement Plans, continued

Defined Benefit Plan, continued

Pension Assets and Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions, continued

percentage point lower (5.50%) or one percentage point higher (7.50%) than the current rate.

	1% Decrease (5.50%)	Current Discount Rate (6.50%)	1% Increase (7.50%)
Heartland's proportionate share of the net pension asset (liability)			
December 31, 2017	$ 1,437,718	$ (7,850)	$ (1,185,012)

Pension Plan Fiduciary Net Position

Detailed information about the pension plan's fiduciary net position is available in the separately issued South Dakota Retirement System financial report.

Defined Contribution Plan

In addition to the above retirement plan, Heartland has a savings plan with the National Rural Electric Cooperative Association, which is a defined contribution plan. Employees are eligible to participate in this plan after one month of service. The National Rural Electric Cooperative Association board of directors has the authority to establish and amend provisions to the plan. Heartland matches up to 4% of participating employees' salaries; employees must contribute a minimum of 1% of their salaries. The contributions made by, and related expense of, Heartland for the years ended December 31, 2017 and 2016 were $60,611 and $57,691, respectively. No forfeitures were used to reduce Heartland's contributions during 2017 and 2016. The contributions made by Heartland employees for the years ended December 31, 2017 and 2016 were $92,281 and $85,966, respectively.

Note 10: Significant Estimates and Concentrations

Major Customers

Sales to one and two customers were approximately 20% and 27%, respectively, of total operation revenues for the years ended December 31, 2017 and 2016, respectively. Approximately 34% and 38% of total accounts receivable were owed from three customers at December 31, 2017 and 2016, respectively.

Proposed Environmental Standards

In June 1999, the Environmental Protection Agency (EPA) issued final regulations for a Regional Haze Program. The purpose of the regulations is to improve visibility in the form of reduced regional haze in 156 national parks and wilderness areas across the country. The EPA's claim is that haze is formed, in part, from emissions of SO2 (sulfur dioxide) and NO2 (nitrogen dioxide). Heartland is impacted by these regulations through its co-ownership of Laramie River Station (LRS) in Wyoming.

As part of the EPA's Clean Air Act regulations, each state is required to submit a state implementation plan (SIP) identifying the emission control technology proposed to comply with the Regional Haze Program. The State of Wyoming submitted its SIP to the EPA in 2011, which included plans for LRS. In January 2014, the EPA issued their final ruling on this SIP, requiring installation of selective catalytic reduction (SCR) NO2 removal technology for five coal plants in Wyoming, including the three units at LRS. Negotiations continued through 2016 until a tentative agreement was reached late in 2016. The agreement would require LRS to install non-SCR technology on two units and SCR technology on one unit, which results in significant cost savings over installing SCR technology on all three units. Although initial estimates of these costs have been calculated, the level of regulatory and legal uncertainty related to these facilities makes it impractical to quantify the specific potential financial impacts at this time.

Note 11: Risk Management

Heartland is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions, injuries to employees and others; and natural disasters. Heartland carries commercially available insurance, subject to certain limits and deductibles, to reduce the financial impact for claims arising from such matters. Claims have not exceeded this commercial coverage in any of the three preceding years.

Note 12: Statutory Reporting Requirement

Section 3 of Chapter 49-38 of the South Dakota Codified Laws requires that certain information be set forth in the annual reports of consumer power districts. Additional information, as required, is as shown below:

	2017	2016
Employees (unaudited)	12	12
Total salaries	$ 1,506,831	$ 1,422,500
Maintenance expense	$ 326,624	$ 220,820
Total kilowatt hours sold (unaudited)	956,328,108	1,282,757,118

Notes to Financial Statements
December 31, 2017 and 2016

Note 13: Segment Information

In accordance with the provisions of the Intermediary Relending Program Loan Agreements, Rural Economic Development Loan Agreement and Rural Economic Development Grant Agreement, Heartland is required to create and maintain a revolving loan fund. Heartland administers this revolving loan fund as a division within its Heartland operations. Condensed 2017 and 2016 financial information for the revolving loan fund is presented below:

Condensed Balance Sheet

	2017	2016
Current assets	$ 1,775,976	$ 1,551,824
Other assets	4,233,487	2,613,527
Total assets	$ 6,009,463	$ 4,165,351
Liabilities		
Current liabilities	$ 283,110	$ 278,623
Noncurrent liabilities	4,310,842	2,783,367
Total liabilities	4,593,952	3,061,990
Net Position	1,415,511	1,103,361
Total liabilities and net position	$ 6,009,463	$ 4,165,351

Condensed Statement of Revenues, Expenses and Changes in Net Position

	2017	2016
Nonoperating revenues (expenses)		
Investment income	$ 75,288	$ 37,871
Interest expense	(19,746)	(12,017)
Bad debt recoveries (expense)	(63,260)	(17,007)
Other	(17,645)	(20,448)
Capital contributions	337,513	-
Increase (Decrease) in Net Position	312,150	(11,601)
Net Position, Beginning of Year	1,103,361	1,114,962
Net Position, End of Year	$ 1,415,511	$ 1,103,361

Condensed Statement of Cash Flows

	2017	2016
Net cash provided by (used in)		
Noncapital financing activities	$ 1,489,895	$ (80,608)
Investing activities	(1,423,477)	63,114
Increase (Decrease) in Cash	66,418	(17,494)
Beginning of Year	1,122,798	1,140,292
End of year	$ 1,189,216	$ 1,122,798

Required Supplementary Information

Schedule of Heartland's Proportionate Share of the Net Pension Asset (Liability)

South Dakota Retirement System

December 31, 2017

	2017	2016	2015	2014
Heartland's proportion of the net pension asset (liability)	0.086%	0.088%	0.087%	0.097%
Heartland's proportionate share of the net pension asset (liability)	$ 7,850	$ (296,707)	$ 370,005	$ 697,294
Heartland's covered payroll	$ 1,458,085	$ 1,394,520	$ 1,390,734	$ 1,404,232
Heartland's proportionate share of the net pension asset (liability) as a percentage of its covered payroll	0.54%	-21.28%	26.61%	49.66%
Plan fiduciary net position as a percentage of the total pension liability	100.10%	96.89%	104.10%	107.29%

Note: This schedule is presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, Heartland will present information for only those years for which information is available. Information presented in this schedule has been determined as of Heartland's measurement date (June 30) of the collective net pension asset (liability) in accordance with GASB 68.

Schedule of Heartland's Contributions

South Dakota Retirement System
December 31, 2017

	2017	2016	2015	2014
Statutorily required contribution	$ 107,920	$ 103,771	$ 99,453	$ 97,153
Contributions in relation to the statutorily required contribution	(107,920)	(103,771)	(99,453)	(97,153)
Contribution deficiency (excess)	$ -	$ -	$ -	$ -
Heartland's covered payroll	$ 1,506,831	$ 1,422,500	$ 1,377,344	$ 1,414,132
Contributions as a percentage of covered payroll	7.16%	7.29%	7.22%	6.87%

Note: This schedule is presented to illustrate the requirement to show information for 10 years. However, until a full 10-year trend is compiled, the Heartland will present information for only those years for which information is available. Information presented in this schedule has been determined as of Heartland's most recent fiscal year-end (December 31) in accordance with GASB 68.

Other Information

Schedule of Transmission Operation and Maintenance Expenses

FERC Uniform System of Accounts Classification
Year Ended December 31, 2017

		Amount
Operation		
560 - Operation Supervision and Engineering	$	55,399
561 - Load Dispatching		-
561.1 - Load Dispatch - Reliability		-
561.2 - Load Dispatch - Monitor and Operate Transmission System		-
561.3 - Load Dispatch - Transmission Service and Scheduling		-
561.4 - Scheduling, System Control and Dispatch Services		-
561.5 - Reliability, Planning and Standards Development		-
561.6 - Transmission Service Studies		-
561.7 - Generation Interconnection Studies		-
561.8 - Reliability, Planning and Standards Development Service		-
562 - Station Expenses		24,959
563 - Overhead Lines Expenses		26,182
564 - Underground Lines Expenses		-
565 - Transmission of Electricity by Others		7,284,775
566 - Miscellaneous Transmission Expenses		23,254
567 - Rents		-
Total Operation Expense		**7,414,569**
Maintenance		
568 - Maintenance Supervision and Engineering		-
569 - Maintenance of Structures		-
569.1 - Maintenance of Computer Hardware		-
569.2 - Maintenance of Computer Software		-
569.3 - Maintenance of Communication Equipment		-
569.4 - Maintenance of Miscellaneous Regional Transmission Plant		-
570 - Maintenance of Station Equipment		20,782
571 - Maintenance of Overhead Lines		37,843
572 - Maintenance of Underground Lines		-
572 - Maintenance of Miscellaneous Transmission Plant		71,072
Total Maintenance Expense		**129,697**
Total Transmission O&M Expense	**$**	**7,544,266**

Schedule of Administrative and General Expenses
FERC Uniform System of Accounts Classification
Year Ended December 31, 2017

	Amount
Customer Accounts Expenses	
901 - Supervision	$ -
902 - Meter Reading Expenses	-
903 - Customer Records and Collection Expenses	-
904 - Uncollectible Accounts	-
905 - Miscellaneous Customer Accounts Expenses	-
Total Customer Accounts Expense	**-**
Customer Service and Informational Expenses	
907 - Supervision	231,170
908 - Customer Assistance Expenses	308,550
909 - Informational Instructional Expenses	-
910 - Miscellaneous Customer Service and Informational Expenses	-
Total Customer Service and Informational Expenses	**539,720**
Sales Expenses	
911 - Supervision	-
912 - Demonstrating and Selling Expenses	-
913 - Advertising Expenses	-
916 - Miscellaneous Sales Expenses	-
Sales Expenses	
Administrative and General Expenses	
920 - Administrative and General Salaries	1,284,085
921 - Office Supplies and Expenses	170,179
922 - Administrative Expenses Transferred Credit	-
923 - Outside Services Employed	405,136
924 - Property Insurance	7,182
925 - Injuries and Damages	14,772
926 - Employee Pension and Benefits	123,395
927 - Franchise Requirements	-
928 - Regulatory Commission Expenses	22,249
929 - Duplicate Charges Credit	-
9301.1 - General Advertising Expenses	36,858
930.2 - Miscellaneous General Expenses	738,918
931 - Rents	-
935 - Maintenance of General Plant	196,927
Administrative and General Expenses	**2,999,701**

Board of Directors

President

MARK JOFFER
Electrical Engineer
Board Member since 2009

Vice President

LISA RAVE
Pharmacist
Board Member since 2009

Secretary

JEFF HEINEMEYER
Retired City Finance Officer
Board Member since 2013

Treasurer

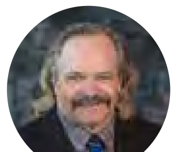
DAVE WESTBROCK
Retired GM of Heartland
Board Member since 2009

Assistant Secretary/ Treasurer

ROGER FRITZ
Farmer
Board Member since 2005

PAT ANDERSON
Retired Middle School Principal
Board Member since 2016

DAVE HAHLER
Former owner of Hahler Auto
Board Member since 2015



LARRY NIELSON
Farmer
Board Member since 2011

VERN HILL
Utility Superintendent
Board Member since 2017

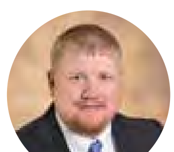
LEE ANN WHEELER
Property and Casualty Producer
Board Member since 2015

BILL LEWELLEN
Electric Superintendent
Board Member since 2017

Staff

RUSSELL OLSON
Chief Executive Officer

CASEY CRABTREE
Director of Economic Development



ADAM GRAFF
Director of Power Supply

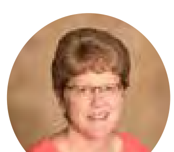
ANN HYLAND
Communications Manager

NATE JONES
Chief Operations Officer

MIKE MALONE
Chief Financial Officer

STEVE MOSES
Customer Relations Manager

KATIE HAHN
Administrative Assistant



SHARLA FEDELER
Accountant

DANIELLE ROSHEIM
Projects & Marketing Coordinator

THERESA SCHAEFER
Benefits Administrator

MCCORD STOWATER
Energy Scheduler

Celebrating 40 years

Heartland has served Howard, South Dakota (population 794) since 1994. Located within an hour's drive of the state's metro areas, the rural community has created over 200 jobs since 2001.

HEARTLAND

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