

# **Southwest Power Pool, Inc.**

Independent Auditor's Report and Financial Statements

December 31, 2017 and 2016



**Southwest Power Pool, Inc.**  
**December 31, 2017 and 2016**

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## Independent Auditor's Report

Board of Directors  
Southwest Power Pool, Inc.  
Little Rock, Arkansas

We have audited the accompanying financial statements of Southwest Power Pool, Inc., which comprise the balance sheets as of December 31, 2017 and 2016, and the related statements of income, changes in members' deficit, and cash flows for the years then ended, and the related notes to the financial statements.

### ***Management's Responsibility for the Financial Statements***

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

### ***Auditor's Responsibility***

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

An audit 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.

Board of Directors  
Southwest Power Pool, Inc.  
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***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Southwest Power Pool, Inc. as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

*BKD, LLP*

Little Rock, Arkansas  
April 9, 2018

**Southwest Power Pool, Inc.**  
**Balance Sheets (in Thousands)**  
**December 31, 2017 and 2016**

**Assets**

	2017	2016
<b>Current Assets</b>		
Cash and cash equivalents	\$ 100,496	\$ 75,715
Restricted cash deposits	340,612	223,964
Accounts receivable, net	74,391	63,702
Prepaid expenses and other	8,539	9,291
Total current assets	524,038	372,672
 <b>Property and Equipment, at Cost</b>		
Land	4,812	4,812
Building	67,650	67,338
Furniture and fixtures	10,380	10,211
Equipment and machinery	52,007	46,210
Software	177,480	170,701
Software in development	2,844	5,205
Equipment under capital lease	4,876	4,876
	320,049	309,353
Less accumulated depreciation and amortization	240,275	216,663
	79,774	92,690
 <b>Investments (Note 2)</b>	24,456	10,835
 <b>Other Assets, Net</b>	5,499	4,628
	\$ 633,767	\$ 480,825

## Liabilities and Members' Deficit

	<u>2017</u>	<u>2016</u>
<b>Current Liabilities</b>		
Accounts payable	\$ 75,844	\$ 66,927
Customer deposits	340,612	223,964
Current maturities of long-term debt ( <i>Note 4</i> )	21,469	21,410
Current maturities of obligations under capital lease ( <i>Note 5</i> )	1,890	1,817
Accrued expenses	98,801	54,310
Deferred revenue	3,928	5,127
	<u>542,544</u>	<u>373,555</u>
<b>Long-term Debt (<i>Note 4</i>)</b>	214,479	235,948
Less unamortized debt issuance costs	(803)	(898)
	<u>213,676</u>	<u>235,050</u>
<b>Obligation Under Capital Lease (<i>Note 5</i>)</b>	1,966	3,856
<b>Other Long-term Liabilities</b>	32,302	35,044
	<u>32,302</u>	<u>35,044</u>
<b>Members' Deficit</b>	<u>(156,721)</u>	<u>(166,680)</u>
	<u>\$ 633,767</u>	<u>\$ 480,825</u>

**Southwest Power Pool, Inc.**  
**Statements of Income (in Thousands)**  
**Years Ended December 31, 2017 and 2016**

	<u>2017</u>	<u>2016</u>
<b>Operating Income</b>		
Tariff fees and member assessments	\$ 190,343	\$ 171,464
Other member services	6,278	5,131
	<u>196,621</u>	<u>176,595</u>
<b>Operating Expenses</b>		
Salaries and benefits	94,650	90,186
Employee travel	2,023	1,919
Administrative	4,656	4,764
Regulatory assessment	21,663	18,648
Meetings	1,040	974
Communications system	3,504	3,915
Maintenance	16,099	14,775
Consulting services	12,620	15,065
Depreciation	27,716	58,025
	<u>183,971</u>	<u>208,271</u>
<b>Operating Income (Loss)</b>	<u>12,650</u>	<u>(31,676)</u>
<b>Other Income (Expense)</b>		
Investment income	234	191
Interest expense	(10,164)	(10,687)
Change in fair market value of interest rate swaps	789	682
Other expense	(1,483)	(431)
	<u>(10,624)</u>	<u>(10,245)</u>
<b>Income (Loss) Before Unrealized Gain and Change in Funded Status of Employee Benefit Plans</b>	2,026	(41,921)
<b>Unrealized Gain on Investments</b>	1,499	659
<b>Change in Funded Status of Employee Benefit Plans</b>	<u>6,434</u>	<u>3,998</u>
<b>Net Income (Loss)</b>	<u>\$ 9,959</u>	<u>\$ (37,264)</u>

**Southwest Power Pool, Inc.**  
**Statements of Members' Deficit (*in Thousands*)**  
**Years Ended December 31, 2017 and 2016**

	<u>2017</u>	<u>2016</u>
<b>Balance, Beginning of Year</b>	\$ (166,680)	\$ (129,416)
Net income (loss)	<u>9,959</u>	<u>(37,264)</u>
<b>Balance, End of Year</b>	<u>\$ (156,721)</u>	<u>\$ (166,680)</u>

**Southwest Power Pool, Inc.**  
**Statements of Cash Flows (in Thousands)**  
**Years Ended December 31, 2017 and 2016**

	2017	2016
<b>Operating Activities</b>		
Net income (loss)	\$ 9,959	\$ (37,264)
Items not requiring cash		
Depreciation and amortization	27,813	58,120
Change in funded status of employee benefit plans	(6,434)	(3,998)
Unrealized gain on investments	(1,499)	(659)
Loss on disposal of fixed assets	6	-
Impairment loss	-	82
Change in fair market value of interest rate swaps	(789)	(682)
Changes in assets and liabilities		
Accounts receivable	(10,689)	(23,912)
Prepaid expenses and other	752	(871)
Other assets	(871)	431
Accounts payable	8,917	36,318
Accrued expenses	43,293	10,027
Other long-term liabilities	4,479	4,456
	74,937	42,048
<b>Investing Activities</b>		
Acquisition of property and equipment	(14,807)	(14,317)
Purchase of investments	(12,216)	(825)
Proceeds from sale of investments	94	-
	(26,929)	(15,142)
<b>Financing Activities</b>		
Repayments of long-term debt	(21,409)	(23,603)
Repayments of capital lease obligation	(1,818)	(591)
Repayment of borrowings under line of credit	-	(16,000)
Borrowings under line of credit	-	14,000
Issuance of long-term debt	-	33,000
	(23,227)	6,806
<b>Increase in Cash and Cash Equivalents</b>	<b>24,781</b>	<b>33,712</b>
<b>Cash and Cash Equivalents, Beginning of Year</b>	<b>75,715</b>	<b>42,003</b>
<b>Cash and Cash Equivalents, End of Year</b>	<b>\$ 100,496</b>	<b>\$ 75,715</b>
<b>Supplemental Cash Flows Information</b>		
Interest paid on long-term debt (net of interest capitalized of \$63 and \$121 in 2017 and 2016, respectively)	\$ 10,074	\$ 10,591
Property and equipment purchases in accounts payable and accrued liabilities	\$ 3,149	\$ 1,991

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (*in Thousands*)**  
**December 31, 2017 and 2016**

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

***Nature of Operations***

Southwest Power Pool, Inc. (the Company) is a not-for-profit entity formed in 1941 and incorporated in 1994. The Company is a Federal Energy Regulatory Commission (FERC)-approved regional transmission organization (RTO) serving more than 17.5 million ultimate customers across all or parts of 14 states. The Company's membership consists of investor-owned utilities, municipal systems, generation and transmission cooperatives, state authorities, federal agencies, independent power producers, contract participants, power marketers and independent transmission companies.

Major services provided by the Company to its members and customers include tariff administration, reliability coordination, regional scheduling, market operations and regional transmission expansion planning. Market operations encompass day-ahead and real-time markets, transmission congestion rights, reliability unit commitment, operating reserve market and consolidated balancing authority.

***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 and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

***Cash and Cash Equivalents and Deposits***

The Company considers all highly liquid interest-earning investments with stated maturities and coupon rate reset dates of no more than three months to be cash equivalents. At December 31, 2017 and 2016, the Company's cash and cash equivalents, including restricted deposits, are invested primarily in money market funds, mutual funds and repurchase agreements. These investments are typically revalued to the market each day and, in the case of repurchase agreements, are collateralized by U.S. government and federal agency securities. The Company's cash and cash equivalents consist primarily of funds accumulated for general operating purposes. Restricted cash deposits consist primarily of customer security deposits, amounts deposited for engineering studies and funds set aside for disputed invoices.

***Investments***

The Company's investments include equity and fixed income mutual funds and government securities. These investments are recorded at fair value, with unrealized gains and losses reported as nonoperating income. Dividends, interest income and realized gains and losses are reported as investment income. The Company's investments are intended to be utilized in funding benefits associated with the Company's postretirement health care plan and 457f deferred compensation plan in addition to maintaining collections under Schedule 12 to be utilized for the annual FERC assessment.

***Income Taxes***

The Company is exempt from income taxes under Section 501c(6) of the Internal Revenue Code and a similar provision of state law. However, the Company is subject to federal income tax on any unrelated business taxable income.

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (*in Thousands*)**  
**December 31, 2017 and 2016**

***Accounts Receivable***

Accounts receivable are stated at the amount billed to members, customers and others plus any accrued and unpaid interest. The Company provides an allowance for doubtful accounts, when necessary, which is based upon a review of outstanding receivables, historical collection information and existing economic conditions. Accounts that are unpaid after the due date are subject to interest at a rate set by FERC. No allowance for doubtful accounts was recorded at December 31, 2017. The Company had recorded an allowance for doubtful accounts of \$822 at December 31, 2016.

***Property and Equipment***

Property and equipment are recorded at cost and depreciated on a straight-line basis over the estimated useful life of each asset. The estimated useful lives are as follows:

Building	20 years
Building improvements	Shorter of useful life or remaining life of building
Furniture and fixtures	5 years
Vehicles	5 years
Equipment and machinery	3 years
Software	3 years

The Company capitalizes interest cost incurred on funds used to construct property, plant and equipment. The capitalized interest is recorded as part of the asset to which it relates and is amortized over the asset's estimated useful life. Interest cost capitalized was \$63 and \$121 in 2017 and 2016, respectively.

The Company capitalizes development costs, including interest, for internal use software costs. These costs are included in software in development. Management of the Company is of the opinion that all costs capitalized in association with the software in development are fully recoverable over the anticipated life of the asset.

***Long-Lived Asset Impairment***

The Company evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate the carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value.

No asset impairment was recognized during the year ended December 31, 2017. In 2016, the Company recorded an impairment loss of \$82 for previously capitalized costs associated with the development of an engineering software tool. The amount is recorded as an impairment loss in the accompanying Statement of Income and is included in other income (expense).

***Revenue Recognition***

Revenues, consisting of member assessments, tariff administrative fees, contract services and miscellaneous revenues are recognized when earned, and expenses are recognized when incurred.

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (*in Thousands*)**  
**December 31, 2017 and 2016**

***Customer Deposits***

Customers may be required to make deposits with the Company prior to the performance of transmission services, market transactions and engineering studies. An offsetting liability equal to the deposit balance is recorded in current liabilities. Funds set aside for disputed invoices are also recorded as customer deposits under current liabilities.

***Tariff Fees and Member Assessments***

An administrative charge is applied to all transmission service under the Company's Open Access Transmission Tariff (tariff) to cover the expenses related to its administration. The charge is calculated in accordance with the terms of the Company's tariff. The administrative rate used for the calculation is established by the board of directors.

Members are assessed monthly based on their prior year average 12-month peak demand multiplied by the total hours in a month and by the monthly assessment rate as established by the board of directors.

A member's monthly assessment is offset dollar for dollar for qualifying tariff administrative fees collected from a member in any given assessment period.

The Company collects a membership fee from each member annually. The amount of the membership fee is established by the board of directors of the Company. For 2017 and 2016, all members paid a \$6 membership fee.

The Company also bills transmission customers and transmission owners a charge under Schedule 12 on all energy delivered under point-to-point transmission service and network integration transmission service. This provides a mechanism for recovering from transmission customers the annual charges the Company pays to FERC.

***Deferred Revenue***

Revenues for contract services received in advance are recognized over the periods to which the revenues relate.

***Other Member Services***

The Company provides reliability, tariff administration and scheduling for non-members on a contract basis. The Company also provides engineering study services for long-term transmission service and generation interconnection requests.

***Withdrawing Members***

Members wishing to withdraw their membership from the Company must provide 24 months' written notice and are responsible for their portion of the Company's existing obligations as defined in the bylaws, which include unpaid membership fees, any assessments imposed prior to the effective withdrawal date, any costs or expenses imposed upon the Company as a direct consequence of the member's withdrawal and the member's share of long-term obligations and related interest. Withdrawing members may also be responsible for all financial obligations incurred and costs allocated to its load for transmission facilities approved prior to their withdrawal. As of December 31, 2017, the Company had not been notified by any member of their intent to withdraw their membership from the Company.

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (in Thousands)**  
**December 31, 2017 and 2016**

***Concentration of Credit Risk***

The Company is exposed to credit risk primarily through accounts receivable and uninsured cash balances. During 2017 and 2016, the Company maintained cash balances, including transaction accounts and short-term investment accounts that are not insured by the Federal Deposit Insurance Corporation. At December 31, 2017 and 2016, the Company did not have transaction accounts exceeding federal insurance limits. The Company's investment accounts were primarily invested in highly liquid short-term investments such as money market funds, mutual funds and repurchase agreements. The Company also requires the financial institutions holding its cash balances to be rated A or better by nationally recognized rating agencies.

The Company considers its accounts receivable to be highly probable of collection. No allowance for doubtful accounts was recorded at December 31, 2017. The Company had recorded an allowance of \$822 at December 31, 2016.

The Company requires its customers to meet certain minimum standards of financial condition and creditworthiness to receive unsecured credit from the Company. If these standards cannot be met by a customer, the Company requires the posting of defined financial security instruments to cover potential liabilities.

**Note 2: Investment and Investment Returns**

Investments at December 31 consisted of the following:

	<u>2017</u>	<u>2016</u>
<b>Mutual Funds</b>		
Equity	\$ 9,359	\$ 7,789
Fixed income	<u>3,430</u>	<u>3,046</u>
Total mutual funds	<u>12,789</u>	<u>10,835</u>
<b>U.S. Government Securities</b>		
Treasury Notes	<u>11,667</u>	<u>-</u>
Total Government Securities	<u>11,667</u>	<u>-</u>
	<u>\$ 24,456</u>	<u>\$ 10,835</u>

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (in Thousands)**  
**December 31, 2017 and 2016**

Total investment return is comprised of the following:

	2017	2016
Interest and dividends reported at fair value	\$ 234	\$ 191
Net realized and unrealized gains on investments reported at fair value	1,499	659
	\$ 1,733	\$ 850

Interest, dividends and realized gains and losses are reported as investment income, while unrealized gains and losses are reported separately in the Statements of Income.

**Note 3: Line of Credit**

The Company has a \$30,000 revolving line of credit expiring in 2019. At December 31, 2017 and 2016, no amounts were borrowed against this line. The agreement has a variable interest rate equal to the London Interbank Offered Rate (LIBOR) plus a credit margin. The interest rate at December 31, 2017, was 2.82%. The Company's line of credit requires compliance with certain financial and non-financial covenants as well as periodic reporting requirements. The Company was in compliance with the covenant and reporting requirements throughout and at December 31, 2017.

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (in Thousands)**  
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**Note 4: Long-term Debt and Interest Rate Swaps**

*Long-term Debt*

	2017	2016
Variable Rate Term Note due 2027 (A)	\$ 2,930	\$ 3,136
4.82% Series 2010-A and B Senior Notes due 2042 (B)	59,518	60,722
3.55% Series 2010-C Senior Notes due 2024 (C)	43,750	50,750
3.00% Series 2012-D-1 Senior Notes due 2024 (D)	31,250	36,250
3.25% Series 2012-D-2 Senior Notes due 2024 (E)	33,750	38,750
3.80% Series 2014-E Senior Notes due 2025 (F)	37,000	37,000
Floating Series Note - 2024 (G)	27,750	30,750
	235,948	257,358
Less unamortized debt issuance costs	803	898
Less current maturities	21,469	21,410
	\$ 213,676	\$ 235,050

- (A) Due February 1, 2027; principal and interest are payable quarterly based on a 25-year amortization. Payments commenced on May 1, 2007. The interest rate adjusts quarterly based on LIBOR plus 0.85%. At December 31, 2017 and 2016, the interest rate was 2.25% and 1.75%, respectively. The note is secured by a first mortgage on the Company's operation facility.
- (B) Due December 30, 2042; principal and interest are payable quarterly based on a 32-year amortization. Principal payments commenced on March 30, 2013. The interest rate is fixed at 4.82%. The notes are unsecured.
- (C) Due March 30, 2024; principal and interest are payable quarterly based on a 13-year amortization. Principal payments commenced on June 30, 2014. The interest rate is fixed at 3.55%. The notes are unsecured.
- (D) Due March 30, 2024; principal and interest are payable quarterly based on a 10-year amortization. Principal payments commenced on June 30, 2014. The interest rate is fixed at 3.00%. The notes are unsecured.
- (E) Due September 30, 2024; principal and interest are payable quarterly based on a 10-year amortization. Principal payments commenced on December 30, 2014. The interest rate is fixed at 3.25%. The notes are unsecured.
- (F) Due December 30, 2025; principal and interest are payable quarterly based on an 11 year and 9 months amortization. Principal payments commence on March 30, 2024. The interest rate is fixed at 3.80%. The notes are unsecured.
- (G) Due March 30, 2024; principal and interest are payable monthly based on an eight-year amortization. Payments commenced on June 30, 2016. The interest rate adjusts monthly based on LIBOR plus 1.75%. At December 31, 2017 and 2016, the interest rate was 3.11% and 2.37%, respectively. The note is unsecured.

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (in Thousands)**  
**December 31, 2017 and 2016**

Aggregate annual maturities of long term debt at December 31, 2017, are:

2018	\$	21,469
2019		22,281
2020		22,596
2021		23,414
2022		23,735
Thereafter		<u>122,453</u>
	<u>\$</u>	<u>235,948</u>

Certain of the Company's term notes require compliance with financial and nonfinancial covenants, as well as periodic reporting requirements. The Company was in compliance with the covenant and reporting requirements throughout and at December 31, 2017.

***Variable-to-Fixed Interest Rate Swap***

As a strategy to maintain acceptable levels of exposure to the risk of changes in future cash flows due to interest rate fluctuations, the Company enters into interest rate swap agreements.

On September 15, 2006, the Company entered into an interest rate swap agreement with U.S. Bank National Association. The agreement provides for the Company to receive interest from the counterparty at LIBOR and to pay interest to the counterparty at a fixed rate of 5.51% on notional amounts of \$2,907 and \$3,111 at December 31, 2017 and 2016, respectively. Under the agreement, the Company pays or receives the net interest amount quarterly, with the quarterly settlements included in interest expense. The swap was established to hedge interest rate risk on its floating rate debt obligation (Loan A).

The Company entered into another interest rate swap agreement on March 10, 2014, with Regions Bank. The agreement provides for the Company to receive interest from the counterparty at LIBOR and to pay interest to the counterparty at a fixed rate of 3.225% on notional amounts of \$27,750 and \$30,750 at December 31, 2017 and 2016, respectively. Under the agreement, the Company pays or receives the net interest amount monthly, with the monthly settlements included in interest expense. The swap was established to hedge interest rate risk on its floating rate debt obligation (Loan G).

The table below presents certain information regarding the Company's interest rate swap agreements.

	<u>2017</u>	<u>2016</u>
Fair value of interest rate swap agreements	\$ 1,717	\$ 2,506
Balance sheet location of fair value amounts	Other Long-term Liabilities	Other Long-term Liabilities
Gain recognized in statement of income	\$ 789	\$ 682
Location of gain recognized in statement of income	Change in Fair Market Value of Interest Rate Swaps	Change in Fair Market Value of Interest Rate Swaps

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (*in Thousands*)**  
**December 31, 2017 and 2016**

**Note 5: Capital Lease Obligation**

The Company entered into a capital lease obligation on February 1, 2015, in the amount of \$6,901 to finance data storage equipment. The term of the financing is five years and expires on November 1, 2019. At December 31, 2017 and 2016, accumulated depreciation for equipment purchased under the capital lease was \$4,740 and \$3,115, respectively. Future minimum payments on the capital lease obligation at December 31, 2017, are:

2018	\$	2,015
2019		<u>2,015</u>
Total minimum lease payments		4,030
Less: Amount representing interest		<u>174</u>
Present value of minimum lease payments	<u>\$</u>	<u>3,856</u>
Current portion of minimum lease payments	\$	1,890
Long-term portion of minimum lease payments		<u>1,966</u>
Total	<u>\$</u>	<u>3,856</u>

**Note 6: Employee Benefit Plans**

***Pension and Other Postretirement Benefit Plans***

The Company has a noncontributory defined benefit pension plan covering all employees meeting eligibility requirements. The Company's funding policy is to make the minimum annual contribution that is required by applicable regulations, plus such amounts as the Company may determine to be appropriate from time to time. The Company expects to contribute approximately \$4,590 to the plan in 2018.

The Company has a noncontributory defined benefit postretirement health care plan covering eligible retirees, including those retiring between the ages of 55–65 and hired prior to January 1, 1996. Employees hired after June 1, 2006, are not eligible to participate in the noncontributory defined postretirement health care plan. Eligible retirees are provided monies through a tax-free health reimbursement account to pay for individual Medicare supplemental health insurance plans or other eligible health care expenses.

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (in Thousands)**  
**December 31, 2017 and 2016**

The Company uses a December 31 measurement date for the plans. Information about the plans' funded status is as follows:

	Pension Benefits		Postretirement Health Care Benefits	
	2017	2016	2017	2016
Benefit obligation	\$ 85,888	\$ 76,969	\$ 9,474	\$ 9,426
Fair value of plan assets	70,183	57,739	-	-
Funded status	<u>\$ (15,705)</u>	<u>\$ (19,230)</u>	<u>\$ (9,474)</u>	<u>\$ (9,426)</u>

Amounts recognized in the balance sheets:

	Pension Benefits		Postretirement Health Care Benefits	
	2017	2016	2017	2016
Other long-term liabilities	\$ (15,705)	\$ (19,230)	\$ (9,474)	\$ (9,426)

Amounts recognized in members' equity not yet recognized as components of net periodic benefit cost as of December 31, 2017 and 2016, consist of:

	Pension Benefits		Postretirement Health Care Benefits	
	2017	2016	2017	2016
Net loss	\$ 13,324	\$ 18,681	\$ 4,501	\$ 5,538
Prior service credit	(24)	(23)	(1,322)	(1,405)
Transition obligation	49	66	13	18
	<u>\$ 13,349</u>	<u>\$ 18,724</u>	<u>\$ 3,192</u>	<u>\$ 4,151</u>

The accumulated benefit obligation for the defined benefit pension plan was \$68,960 and \$61,476 at December 31, 2017 and 2016, respectively.

Other significant balances and costs are:

	Pension Benefits		Postretirement Health Care Benefits	
	2017	2016	2017	2016
Employer contributions	\$ 5,200	\$ 5,380	\$ -	\$ -
Benefits paid	786	713	101	91
Benefit costs	7,049	7,182	1,108	1,210

In 2017, no amounts were funded by the Company into the investment account holding assets intended to be utilized in providing benefits for eligible retirees. The Company transferred \$250 into the investment account in 2016.

**Southwest Power Pool, Inc.**  
**Notes to Financial Statements (in Thousands)**  
**December 31, 2017 and 2016**

The following amounts have been recognized in the Statements of Income for the years ended December 31, 2017 and 2016:

	Pension Benefits		Postretirement Health Care Benefits	
	2017	2016	2017	2016
Amounts arising during the period				
Net gain	\$ 4,759	\$ 2,092	\$ 819	\$ 783
Amounts recognized as benefit components of net periodic cost of the period				
Net loss	785	985	255	315
Net prior service credit	1	1	(83)	(83)
Net transition obligation	16	16	4	4

The estimated net loss, prior service cost and transition obligation for the defined benefit pension plan that will be amortized from members' equity into net period benefit cost over the next fiscal year are \$338, \$1 and \$16, respectively. The estimated net loss, prior service cost and net obligation for the defined benefit postretirement health care plan that will be amortized from members' equity into net periodic benefit cost over the next fiscal year are \$197, \$83 and \$4, respectively.

Weighted-average assumptions used to determine benefit obligations and costs:

	Pension Benefits		Postretirement Health Care Benefits	
	2017	2016	2017	2016
Discount rate benefit obligation	5.0%	5.0%	5.0%	5.0%
Expected return on plan assets	7.0%	7.0%	N/A	N/A
Rate of compensation increase	4.0%	4.0%	N/A	N/A

The Company has estimated the long term rate of return on plan assets based primarily on historical returns on plan assets, adjusted for changes in target portfolio allocations and recent changes in long-term interest rates based on publicly available information.

For measurement purposes, a 9% annual rate of increase in the per capita cost of covered health care benefits in the next year was assumed for 2017 and 2016. The rate was assumed to decrease gradually to 5% by the year 2022 and remain at that level thereafter.

**Southwest Power Pool, Inc.**  
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The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid as of December 31:

	<b>Pension Benefits</b>	<b>Postretirement Health Care Benefits</b>
2018	\$ 1,016	\$ 149
2019	1,199	187
2020	1,292	202
2021	1,491	221
2022	1,796	246
2023-2027	15,556	1,933

The Company's investment strategy is based on an expectation that equity securities will outperform fixed income securities over the long term. Accordingly, the composition of the Company's plan assets is broadly characterized as a 70/30 allocation between equity and fixed income securities. The strategy utilizes indexed and actively managed mutual fund instruments as well as direct investment in individual equity and fixed income securities. Investments in the plan must adhere to the Investment Policy Statement developed by the Company. The Investment Policy Statement limits investments in foreign securities to 20% of the total fair value of plan assets. The Investment Policy Statement is reviewed annually.

At December 31, 2017 and 2016, plan assets by category are as follows:

	<b>Pension Plan Assets</b>	
	<b>2017</b>	<b>2016</b>
Fixed income securities	32%	27%
Equity securities	63	67
Cash and equivalents	5	6
	<u>100%</u>	<u>100%</u>

***Pension Plan Assets***

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

Where quoted market prices are available in an active market, plan assets are classified within Level 1 of the valuation hierarchy. Level 1 plan assets include cash, money market accounts, closed-end mutual funds and common and foreign company stock. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of plan assets with similar characteristics or discounted cash flows. Level 2 plan assets include open-end mutual funds, corporate debt obligations, foreign corporate debt obligations and foreign government securities.

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In certain cases where Level 1 or Level 2 inputs are not available, plan assets are classified within Level 3 of the hierarchy. At December 31, 2017 and 2016, the Company does not hold any plan assets valued using Level 3 inputs.

The fair values of the Company's pension plan assets at December 31, 2017 and 2016, by asset category are as follows:

	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>2017</b>				
<b>Money market mutual funds</b>	\$ 3,598	\$ 3,598	\$ -	\$ -
<b>Mutual funds</b>				
Equity funds	37,621	24,386	13,235	-
Fixed income funds	12,522	7,741	4,781	-
Other funds	2,190	320	1,870	-
	<u>52,333</u>	<u>32,447</u>	<u>19,886</u>	<u>-</u>
<b>Domestic common stock</b>				
Financials	2,736	2,736	-	-
Healthcare	1,502	1,502	-	-
Industrials	895	895	-	-
Telecommunications	701	701	-	-
Other	601	601	-	-
	<u>6,435</u>	<u>6,435</u>	<u>-</u>	<u>-</u>
<b>Corporate debt obligations</b>	7,615	-	7,615	-
<b>Foreign government securities</b>	201	-	201	-
<b>Total</b>	<u>\$ 70,182</u>	<u>\$ 42,480</u>	<u>\$ 27,702</u>	<u>\$ -</u>
<b>2016</b>				
<b>Money market mutual funds</b>	\$ 3,518	\$ 3,518	\$ -	\$ -
<b>Mutual funds</b>				
Equity funds	28,500	19,766	8,734	-
Fixed income funds	8,795	5,785	3,010	-
Other Funds	1,363	255	1,109	-
	<u>38,658</u>	<u>25,805</u>	<u>12,853</u>	<u>-</u>
<b>Domestic common stock</b>				
Energy	3,456	3,456	-	-
Financials	1,536	1,536	-	-
Healthcare	1,961	1,961	-	-
Other	1,858	1,858	-	-
	<u>8,811</u>	<u>8,811</u>	<u>-</u>	<u>-</u>
<b>Foreign stocks</b>	303	303	-	-
<b>Corporate debt obligations</b>	5,945	-	5,945	-
<b>Foreign government securities</b>	505	-	505	-
<b>Total</b>	<u>\$ 57,739</u>	<u>\$ 38,436</u>	<u>\$ 19,302</u>	<u>\$ -</u>

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***Defined Contribution Plans***

The Company has a 401(k) defined contribution plan covering substantially all employees. The Company matches contributions at 4.75% for those employees deferring 6% of compensation, with the match fluctuating from 1% to 4.75% for each percentage of compensation contributed under 6%. Contributions to the plan were \$2,752 and \$2,600 for 2017 and 2016, respectively.

The Company has a 457(b) non-qualified tax-deferred compensation plan. This plan is an unfunded plan maintained for the purpose of providing deferred compensation for a select group of management or highly compensated employees and, therefore, is intended to be exempt from the participation, vesting, funding and fiduciary requirements of Title I of the *Employee Retirement Income Security Act of 1974* (ERISA). Accumulated contributions and earnings of \$2,597 and \$1,924 are recorded in other long-term liabilities at December 31, 2017 and 2016, respectively. The Company also offers a 457(f) non-qualified tax-deferred compensation plan to a select group of executive management. The 457(f) plan was intended to be exempt from the participation, vesting, funding and fiduciary requirements of Title I of ERISA and serves to further supplement benefits lost due to IRS limits on compensation and benefits. There were accrued benefits of \$938 and \$460 recorded in other long-term liabilities for the 457(f) plan participants at December 31, 2017 and 2016, respectively.

**Note 7: Related Party Transactions**

General disbursements of the Company are apportioned to members based on the formula described in the bylaws of the Company (see *Note 1*). The Company's receivables from members totaled \$21,137 and \$19,661 as of December 31, 2017 and 2016, respectively. The Company recognized revenues of \$137,780 and \$124,652, including assessments and tariff administrative fees, from members for the years ended December 31, 2017 and 2016, respectively.

The Southwest Power Pool Regional State Committee (RSC) was incorporated on April 7, 2004, in the state of Arkansas. The RSC is comprised of commissioners from public service commissions or equivalent, having regulatory authority over Company members. FERC, in its February 20, 2004 order regarding the Company's RTO application, stated, "the RSC should have primary responsibility for determining regional proposals and the transition process for funding of regional transmission enhancements, rate structure for a regional access charge and allocation of transmission rights." The RSC prepares budgets annually for the expected costs of its operations. This budget is submitted to the Company's board of directors for approval. The Company includes in its annual budget funds sufficient to cover 100% of the operating costs of the RSC. During 2017 and 2016, the Company incurred \$202 and \$257, respectively, in expenses attributable to the RSC operations. Management of the Company expects such expenditures for 2018 to be approximately \$381.

**Note 8: Open Access Transmission and Market Operations**

The Company provides short- and long-term firm and non-firm point-to-point transmission services and network integration transmission service across 43 providers in 14 states. The Company is responsible for the billing of the transmission customers for the respective services and the remittance of the subsequent collections to the transmission owners on a monthly basis. Billings for these transmission services are not included in the statements of income. The Company receives a fee for facilitating the transmission process, which is recorded as tariff fees in the Company's Statements of Income.

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For the years ended December 31, 2017 and 2016, the Company billed transmission customers \$2,130,538 and \$2,009,809, respectively. For the years ended December 31, 2017 and 2016, the Company remitted to transmission owners \$1,914,880 and \$1,850,198, respectively. At December 31, 2017 and 2016, the Company was due to collect from customers and remit to owners transmission service charges of \$178,581 and \$161,852, respectively.

The Company's Integrated Marketplace includes a day-ahead market with transmission congestion rights, a reliability unit commitment process, a real-time balancing market, an operating reserve market and a consolidated balancing authority. Weekly settlements of market participants' energy transactions are not reflected in the Company's Statements of Income since they do not represent revenues or expenses of the Company, as the Company merely acts as an intermediary in the settlement process. In this role, the Company receives and disburses funds to/from market participants on a weekly basis. At December 31, 2017 and 2016, the Company held \$56,757 and \$19,694, respectively, in cash collections from the settlement of auction revenue rights in accordance with terms of the Company's tariff. These funds are disbursed annually in June for collections from the previous twelve months. A corresponding liability is reflected in accrued expenses on the Balance Sheets.

**Note 9: Commitments and Contingencies**

***Litigation and Regulatory Matters***

The Company is engaged in various legal and regulatory proceedings at both the federal and state levels. The Company is also subject to claims and lawsuits that arise primarily in the ordinary course of business.

It is the opinion of management that the disposition or ultimate resolution of such proceedings, claims and lawsuits will not have a material adverse effect on the financial position, results of operations and cash flows of the Company.

**Note 10: Disclosures About Fair Value of Financial Instruments**

ASC Topic 820, *Fair Value Measurements*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Topic 820 also specifies a fair value hierarchy, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
- Level 3** Unobservable inputs that are supported by little or no market activity and are significant to the fair value of the assets or liabilities

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	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>December 31, 2017</b>				
Cash equivalents	\$ 15,112	\$ 15,112	\$ -	\$ -
Mutual funds				
Equity	9,359	-	9,359	-
Fixed income	3,430	-	3,430	-
U.S. Government Securities				
Treasury Notes	11,667	11,667	-	-
Interest rate swap agreements	(1,717)	-	(1,717)	-

	Fair Value	Fair Value Measurements Using		
		Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<b>December 31, 2016</b>				
Cash equivalents	\$ 29,799	\$ 29,799	\$ -	\$ -
Mutual funds				
Equity	7,789	-	7,789	-
Fixed income	3,046	-	3,046	-
Interest rate swap agreements	(2,506)	-	(2,506)	-

Following is a description of the valuation methodologies used for assets and liabilities measured at fair value on a recurring basis and recognized in the accompanying Balance Sheets, as well as the general classification of such assets and liabilities pursuant to the valuation hierarchy. There have been no significant changes in the valuation techniques during the year ended December 31, 2017.

***Investments***

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. If quoted market prices are not available, then fair values are estimated by using quoted prices of securities with similar characteristics or independent asset pricing services and pricing models, the inputs of which are market-based or independently sourced market parameters, including, but not limited to, yield curves, interest rates, volatilities, prepayments, defaults, cumulative loss projections and cash flows. Such securities are classified in Level 2 of the valuation hierarchy. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy. At December 31, 2017 and 2016, the Company does not hold any assets valued using Level 3 inputs.

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***Interest Rate Swap Agreements***

The fair value is estimated using forward-looking interest rate curves and discounted cash flows that are observable or that can be corroborated by observable market data and, therefore, are classified within Level 2 of the valuation hierarchy.

***Cash Equivalents***

The fair value of money market mutual funds included in cash equivalents is estimated using quoted prices in active markets for identical assets or liabilities and, therefore, is classified within Level 1 of the valuation hierarchy.

The Company has no assets or liabilities measured and recognized in the accompanying Balance Sheets on a nonrecurring basis.

The following methods were used to estimate the fair value of all other financial instruments recognized in the accompanying Balance Sheets at amounts other than fair value.

***Restricted Cash Deposits***

For these short-term instruments, the carrying amount is a reasonable estimate of fair value.

***Customer Deposits***

The carrying amount is a reasonable estimate of fair value.

***Long-term Debt and Capital Lease Obligations***

Fair value is estimated based on the borrowing rates currently available to the Company for bank loans with similar terms and maturities.

The following table presents estimated fair values of the Company's financial instruments at December 31, 2017 and 2016:

	2017		2016	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<b>Financial assets</b>				
Cash and cash equivalents	\$ 100,496	\$ 100,496	\$ 75,715	\$ 75,715
Restricted cash deposits	\$ 340,612	\$ 340,612	\$ 223,964	\$ 223,964
Investments	\$ 24,456	\$ 24,456	\$ 10,835	\$ 10,835
<b>Financial liabilities</b>				
Customer deposits	\$ 340,612	\$ 340,612	\$ 223,964	\$ 223,964
Capital lease obligations	\$ 3,856	\$ 3,902	\$ 5,673	\$ 5,791
Long-term debt	\$ 235,948	\$ 238,802	\$ 257,358	\$ 256,665
Swap agreements	\$ 1,717	\$ 1,717	\$ 2,506	\$ 2,506

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**Note 11: Subsequent Events**

Subsequent events have been evaluated through the April 9, 2018, which is the date the financial statements were available to be issued.