

S Q U A R E B U T T E 2023 ANNUAL REPORT



Square Butte
ELECTRIC COOPERATIVE



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COOPERATIVE PROFILE

Square Butte Electric Cooperative owns Unit 2 at the Milton R. Young Station, a 455-megawatt, mine-mouth generating station located near Center, N.D. The lignite-based facility is named after Milton R. Young, the late United States senator from North Dakota. Square Butte was organized May 24, 1972, and the Young 2 generating station began commercial operation on May 6, 1977.

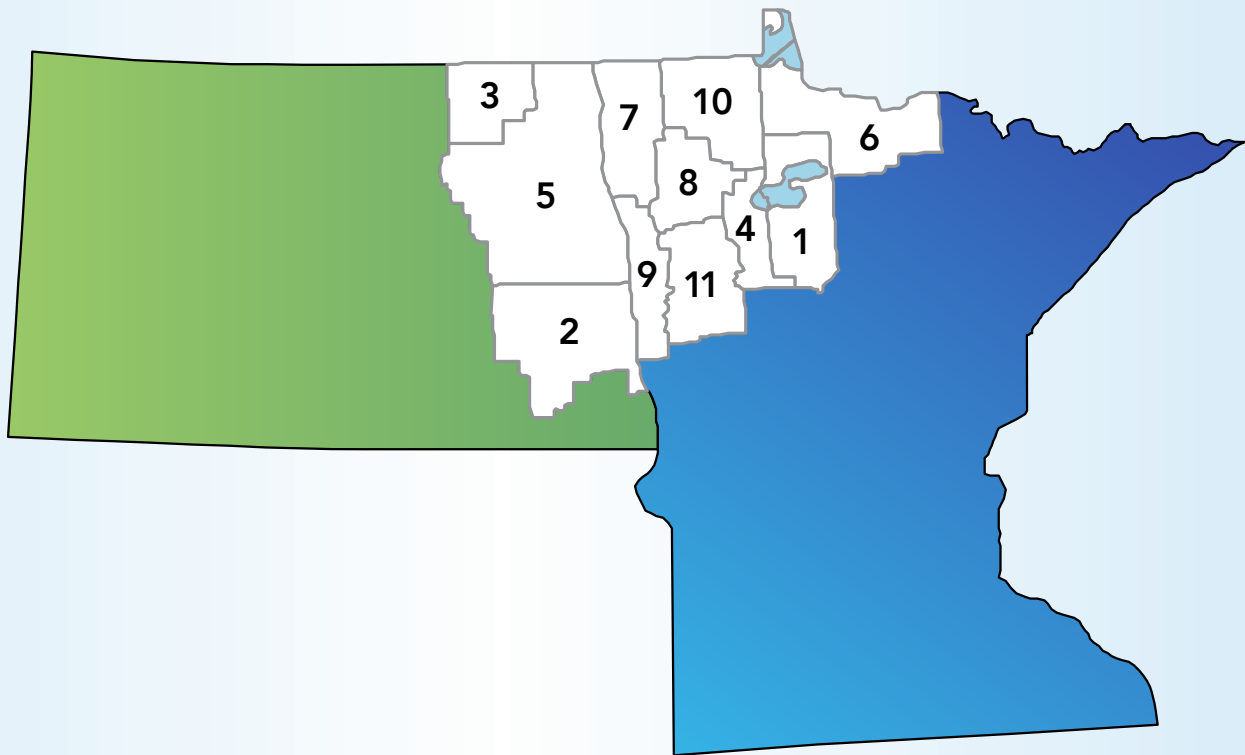
Square Butte is affiliated with Minnkota Power Cooperative, headquartered in Grand Forks, N.D., by reason of common ownership and management. Minnkota, acting as agent, also operates and maintains Young 2.

During the first seven years of operation, Square Butte sold the entire plant output to Minnesota Power, based in Duluth, Minn. Over time, Minnkota has exercised additional energy purchase options. Currently, Minnesota Power and Minnkota each purchase 50% of the Young 2 output from Square Butte. In addition, Minnkota purchases 37% of Minnesota Power's share under a separate agreement.

Since its inception, Square Butte has been committed to supplying reliable energy at the lowest possible cost while maintaining and preserving the natural environment.



MEMBER-OWNER COOPERATIVES



- 1. Beltrami Electric Cooperative, Inc.**
Bemidji, Minnesota
- 2. Cass County Electric Cooperative Inc.**
Fargo, North Dakota
- 3. Cavalier Rural Electric Cooperative, Inc.**
Langdon, North Dakota
- 4. Clearwater-Polk Electric Cooperative, Inc.**
Bagley, Minnesota
- 5. Nodak Electric Cooperative, Inc.**
Grand Forks, North Dakota
- 6. North Star Electric Cooperative, Inc.**
Baudette, Minnesota
- 7. PKM Electric Cooperative, Inc.**
Warren, Minnesota
- 8. Red Lake Electric Cooperative, Inc.**
Red Lake Falls, Minnesota
- 9. Red River Valley Cooperative Power Association**
Halstad, Minnesota
- 10. Roseau Electric Cooperative, Inc.**
Roseau, Minnesota
- 11. Wild Rice Electric Cooperative, Inc.**
Mahnomon, Minnesota

REPORT TO THE MEMBERS



Paul Aakre
President

As our nation's electric grid encounters increasing reliability challenges, Square Butte Electric Cooperative is committed to ensuring stability for the North Dakotans and Minnesotans we proudly serve. We take immense pride in delivering resilient electricity that's available when our members need it most. Through hard work, foresight and collaborative strength, Square Butte continued to generate value for its members in 2023, while also positioning itself to stay stride for stride with a fast-changing industry.



Mac McLennan
General Manager

We are proud of the employees at the Milton R. Young Station, who were creative and patient in addressing challenging circumstances. Following a major scheduled outage at the end of 2022, the Square Butte-owned Unit 2 started the year running with a temporary generator exciter to produce electricity – a resourceful solution due to ongoing supply chain challenges. Despite delays, a near-seamless transition to the permanent equipment was completed in March. Supply chain remains a key focus for plant staff, as they prepare for major maintenance activities on Unit 1 in 2024 and Unit 2 in 2025.

Variability in coal quality also required fast thinking from the Young Station team. Although there were additional maintenance activities beyond original expectations, Unit 2 was still

available for power production 82.6% of the time in 2023 – down from its budget target, but still above comparable coal-based generators in the United States. Crews were able to take advantage of the time offline to accomplish other projects and maintenance activities. We continue to be awed by their ability to turn every one-step-back occurrence into a moment of two-steps-forward progress.

Throughout the ups and downs of 2023, safety remained at the forefront. Young Station employees hit an incredible safety milestone of 1 million hours with no lost-time injuries – the second time the plant has reached this mark in its history. This safety record is yet another example of the great actions of the plant staff, who look out for each other to ensure everyone can return home to their families at day's end. Thank you for the focus and care you bring to your jobs every day of the year.

During 2023, Unit 2 generated 2.75 billion kilowatt-hours (kWh) with an average plant load of 381 megawatts (MW), down from 397 MW in 2022. Square Butte's 2023 average power cost was 63.0 mills per kWh compared to the 53.8 mills that was budgeted, allowing net power costs for the year to be \$172.3 million, or \$0.6 million under budget. Higher fuel costs were offset by lower expenses throughout the rest of the year.





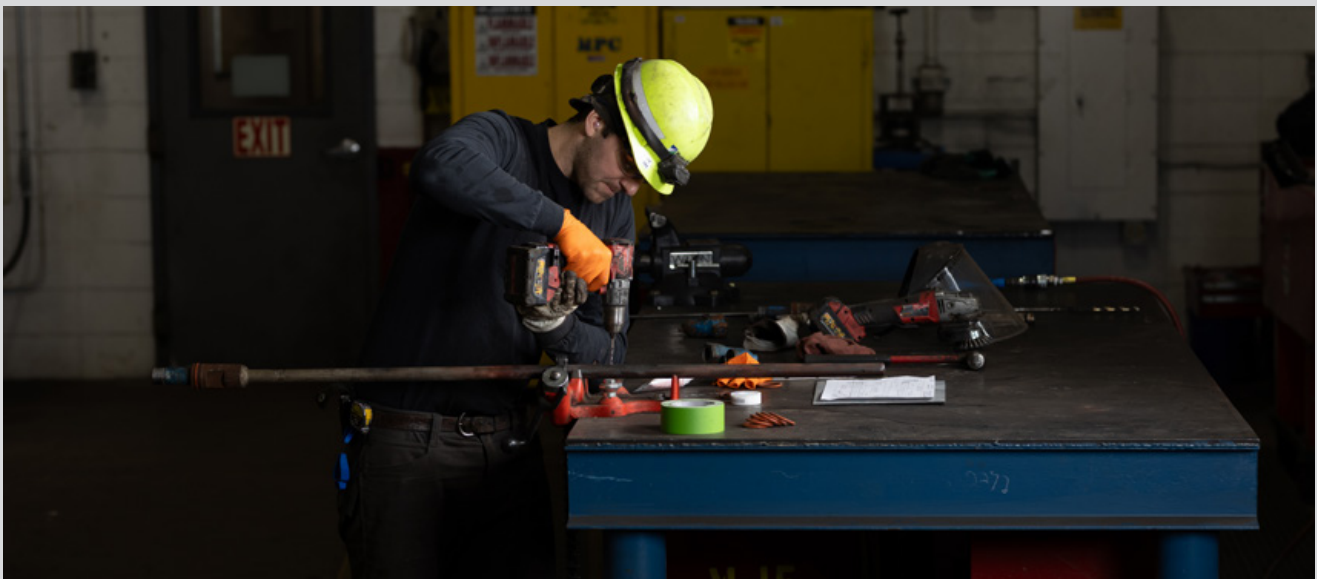
In addition to a solid operating year, the Young Station maintained 100% compliance with land, air and water quality standards in 2023. This strong record becomes increasingly difficult to maintain as rules and requirements rapidly change, but the Minnkota staff that run the Young Station prioritize staying ahead of every compliance curve. In the upcoming year, it is anticipated that the Environmental Protection Agency (EPA) will finalize new rules regulating greenhouse gas emissions and mercury emissions, while also making a determination on the state of North Dakota's regional haze plan. Each of these rules has the potential to have significant impacts on Square Butte and the Young Station, and it is anticipated that each will face litigation.

Square Butte remains committed to helping advocate for sensible regulation – especially considering the dire warnings that have been issued from grid operators and regulators on the troubling state of our region's grid. The North American Electric Reliability Corporation (NERC) – the entity responsible for developing and enforcing mandatory reliability standards for utilities in the United States and Canada – released its Long-Term Reliability Assessment in December. The report found an escalating risk of electricity reliability issues and identified the MISO region where Square Butte operates

as the area with the highest risk in the United States. We will be sharing these reports and information with policymakers, regulators and other key stakeholders, while looking to ensure reliable generators like Unit 2 remain on the grid.

With the potential for a carbon-managed future on the horizon, Minnkota and Square Butte are continuing to evaluate opportunities to construct a carbon capture facility at the Young Station – an initiative known as Project Tundra. Through the project, about 4 million metric tons of CO₂ would be captured and safely and permanently stored more than a mile underground. In June, Minnkota announced agreements with major project collaborators TC Energy, Mitsubishi Heavy Industries, and Kiewit and its affiliates to move Project Tundra into its final stage of development. These connections to commercialization, technology and construction entities will help Minnkota complete the engineering and financial assessments needed to make a final decision on whether to move forward with the venture.

In July, Project Tundra received approval for a \$150 million loan authorized by the North Dakota Industrial Commission through the state's Clean Sustainable Energy Authority (CSEA). This funding will be an addition to a \$100 million CSEA loan approved in 2022.





A few months later in December, project leaders announced up to \$350 million from the U.S. Department of Energy as Project Tundra was selected as a recipient of funding from the Bipartisan Infrastructure Law's Carbon Capture Demonstration Projects Program. This financial opportunity is a clear indicator of Project Tundra's support from both the state of North Dakota and the federal government, who understand the impact this new, innovative technology can make on the state, the nation and the entire world.

The boards of Square Butte Electric Cooperative and Minnkota Power Cooperative anticipate a great deal of deep thought and collaboration in 2024 as we receive finalized engineering, procurement and construction plans on the Project Tundra facility. There is still much work that needs to be done to reach a final decision, but we remain supportive of these efforts to preserve reliability and affordability of our power supply as we prepare for a carbon-managed future. The strength and

vibrancy of our region depends on it, and we believe Project Tundra is our way to deliver.

We thank you for the continuing honor of serving as president and general manager of Square Butte Electric Cooperative. We would not experience success without our steadfast partner in power production, BNI Coal. We are also eternally grateful for the relationships we have built with our customers, Minnkota and Minnesota Power. We could not execute great actions without the intellectual, physical and emotional commitment we receive from each person who supports our cooperative and helps us to generate responsible energy. You leave behind greatness in what you do for our communities – and that legacy will ripple through generations to come.

Paul Aakre, *President*

Mac McLennan, *General Manager*



BOARD OF DIRECTORS



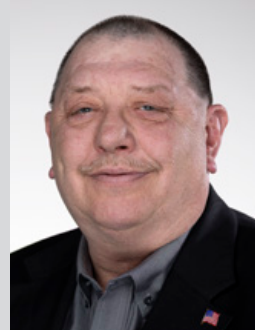
Paul Aakre
President
PKM Electric Cooperative
Warren, Minn.



Larry Sollie
Vice President
Wild Rice Electric Cooperative
Mahnomon, Minn.



Murl Nord
Secretary/Treasurer
Beltrami Electric Cooperative
Bemidji, Minn.



Shawn Gust
Roseau Electric Cooperative
Roseau, Minn.



Michael Hanson
North Star Electric Cooperative
Baudette, Minn.



David Kent
Nodak Electric Cooperative
Grand Forks, N.D.



Terry Kraft
Cass County Electric
Cooperative
Fargo, N.D.



Bill Lanners
Clearwater-Polk Electric
Cooperative
Bagley, Minn.



John Martinson
Cavalier Rural Electric
Cooperative
Langdon, N.D.



Peter Mosbeck
Red Lake Electric Cooperative
Red Lake Falls, Minn.



Trevor Sorby
Red River Valley Cooperative
Power Association
Halstad, Minn.



Mac McLennan
General Manager



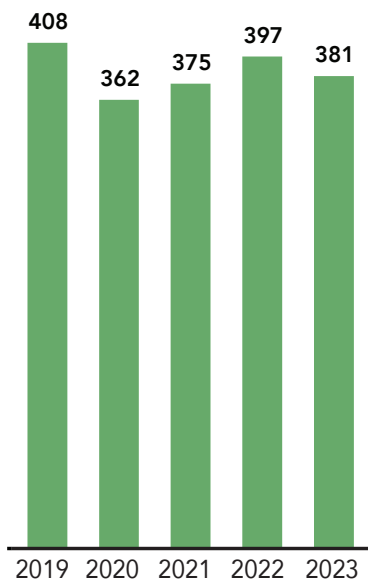
Gerad Paul
General Counsel

OPERATING STATISTICS

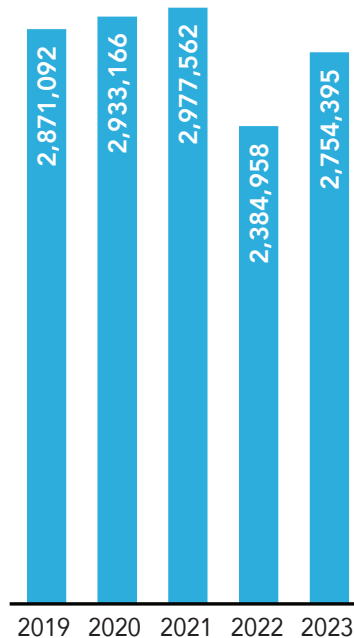
	<u>2023</u>	<u>2022</u>	<u>2021</u>
Plant availability (percent)	82.6	68.5	90.7
Hours of operation	7,232	6,003	7,947
Hours of outage	1,528	2,757	813
Total hours in year	8,760	8,760	8,760
Gross generation (MWh)	3,020,270	2,608,403	3,278,475
Net generation (MWh)	2,754,395	2,384,958	2,977,562
Station service (MWh)	265,876	223,445	300,913
Station service (percent)	8.8	8.6	9.2
Average net generation (MW)	381	397	375
Coal burned (tons)	2,459,629	2,142,140	2,620,453



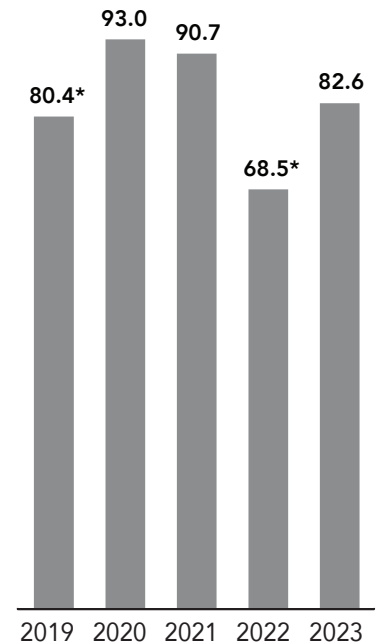
Average Net Generation
(MW)



Net Generation
(MWh)



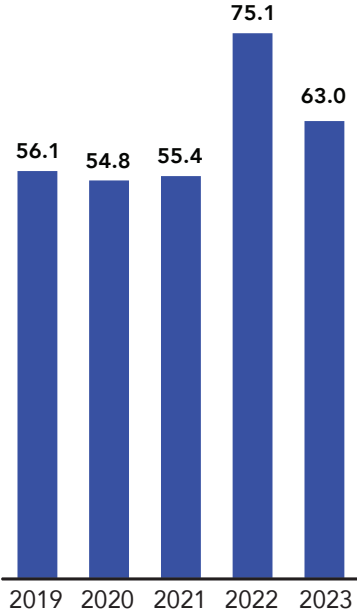
Plant Availability
(percent)



*Major outage years

POWER SOURCES AND ENERGY SALES

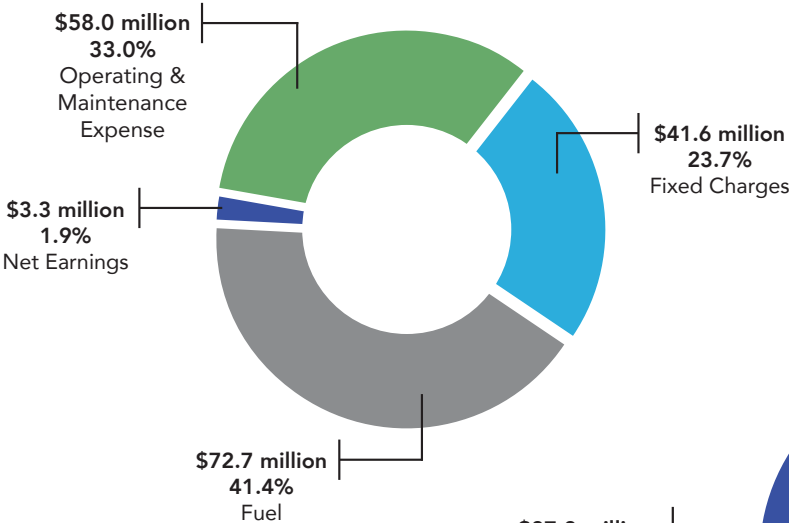
Average Power Cost (mills/kWh)



	<u>2023</u>	<u>2022</u>	<u>2021</u>
Power sources (MWh)			
Net generation – Young 2	2,754,395	2,384,958	2,977,562
Total sources	2,754,395	2,384,958	2,977,562
Energy sales (MWh)			
Minnesota Power	1,377,197	1,192,479	1,488,781
Minnkota	1,377,198	1,192,479	1,488,781
Total sales	2,754,395	2,384,958	2,977,562

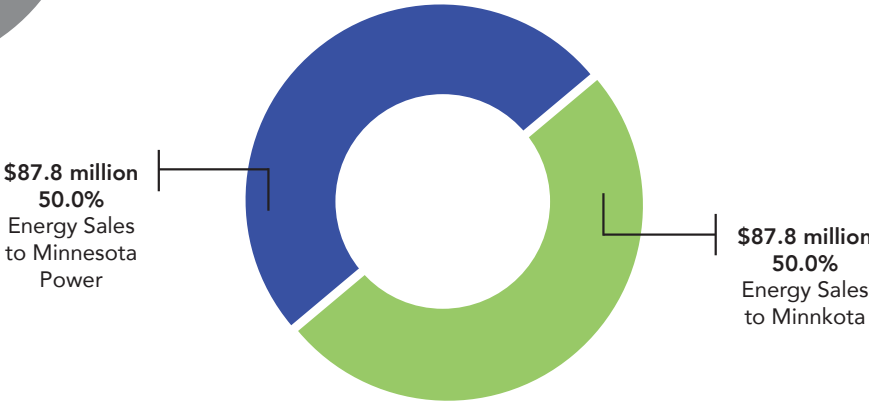
Expenses and Net Earnings

\$175.6 million



Revenues

\$175.6 million



TREASURER'S REPORT

The average power cost for Square Butte in 2023 was 63.0 mills per kilowatt-hour (kWh) – above the 53.8 budgeted mills per kWh and down from the 75.1 mills per kWh in 2022. Increased power costs were primarily driven by lower net generation during the year.

Revenues

Square Butte's revenues are set to cover expenses plus a calculated margin. Revenues in 2023 were \$175.6 million – \$0.3 million under budget. This decrease is due to expenses being under budget by a similar amount. Square Butte's expenses and margin are passed on to its two customers, Minnesota Power and Minnkota Power Cooperative. Minnesota Power and Minnkota each contributed \$87.8 million, or 50%, of Square Butte's revenues in 2023.

Expenses

Square Butte's expenses consist of fuel, operating and maintenance costs, and fixed charges. They totaled \$172.3 million in 2023, which is down \$0.6 million from budget.

Fuel costs totaled \$72.7 million in 2023, which was \$2.6 million over budget. Fuel costs consist primarily of coal provided by BNI Coal under a cost-plus contract and coal royalties paid to Minnkota at \$0.48 per ton. Higher fuel oil costs due to coal quality was the main reason for being over budget.

Operating and maintenance expenses amounted to \$58.0 million in 2023, which was \$1.9 million under budget. These expenses were under budget mainly due to reduced chemical usage.

Fixed charges include interest, depreciation and income taxes. They totaled \$41.6 million in 2023, which is \$1.3 million under budget. These expenses are down mainly due to the timing of new financing.

Net Earnings

Net earnings after income taxes were \$3.3 million in 2023 – right on budget. Earnings consist of a

margin calculated at 5% of the Square Butte operating and maintenance costs. Earnings also include capital credits allocated by other cooperatives to Square Butte.

Assets

Net electric plant was \$263.5 million at Dec. 31, 2023, and includes construction work in progress of \$2.1 million. Net electric plant decreased by \$13.4 million in 2023, primarily due to an additional year of depreciation.

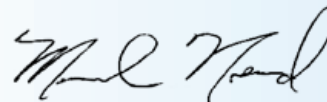
Also shown on the Balance Sheet are current assets of \$14.8 million, long-term investments of \$6.8 million and deferred expenses of \$12.1 million. Total assets were \$297.2 million at Dec. 31, 2023 – down \$30.8 million from last year.

Equities and Liabilities

Long-term debt amounted to \$145.9 million at Dec. 31, 2023 – a decrease of \$25.5 million from 2022. This decrease is mainly due to an additional year of debt principal payments. Other liabilities totaled \$86.2 million and include current liabilities, deferred credits and deferred income taxes. Retained earnings at Dec. 31, 2023, totaled \$65.1 million, including the net earnings in 2023 of \$3.3 million.

This has been a brief review of the 2023 financial statements. For further information, I urge you to review the financial statements, the notes to the financial statements and the independent auditor's report found in this annual report.

Respectfully submitted,



Murl Nord, Secretary-Treasurer



Murl Nord
Secretary-Treasurer

BALANCE SHEET

As of December 31

Assets

	2023	2022
ELECTRIC PLANT		
Plant in service	\$ 819,291,824	\$ 796,261,355
Construction work in progress	2,123,231	8,301,857
Total electric plant	821,415,055	804,563,212
Less accumulated depreciation	(557,873,568)	(527,577,361)
Net electric plant	263,541,487	276,985,851
OTHER PROPERTY AND INVESTMENTS		
Investments in associated companies	6,786,062	6,438,649
CURRENT ASSETS		
Cash and cash equivalents	100,829	1,079,543
Accounts receivable –		
Minnkota Power Cooperative, Inc.	4,373,646	10,738,026
Minnesota Power	4,086,896	10,454,245
Inventories –		
Fuel	3,772,953	4,337,320
Materials and supplies	1,607,333	658,745
Prepayments	895,785	909,696
Total current assets	14,837,442	28,177,575
DEFERRED EXPENSES	12,083,192	16,418,583
TOTAL ASSETS	\$ 297,248,183	\$ 328,020,658

See Notes to Financial Statements

Equities & Liabilities

As of December 31

	2023	2022
EQUITIES		
Memberships issued	\$ 110	\$ 110
Retained earnings	65,124,395	61,872,525
Total equities	<u>65,124,505</u>	<u>61,872,635</u>
LONG-TERM DEBT		
Less current maturities and unamortized debt issuance costs of \$416,247 in 2023 and \$452,351 in 2022	<u>145,887,630</u>	<u>171,344,320</u>
OTHER NONCURRENT LIABILITIES		
Deferred income taxes	<u>6,210,464</u>	<u>6,901,211</u>
CURRENT LIABILITIES		
Current maturities of long-term debt	25,492,796	38,393,920
Lines of credit	35,927,000	26,771,000
Accounts payable –		
Minnkota Power Cooperative, Inc.	5,850,856	9,344,399
Other	6,261,471	7,620,000
Income tax payable	651,973	668,000
Accrued liabilities –		
Property and other taxes	3,915	12,840
Interest	694,089	1,341,237
Total current liabilities	<u>74,882,100</u>	<u>84,151,396</u>
DEFERRED CREDITS	<u>5,143,484</u>	<u>3,751,096</u>
TOTAL EQUITIES AND LIABILITIES	<u>\$ 297,248,183</u>	<u>\$ 328,020,658</u>

See Notes to Financial Statements

REVENUES, EXPENSES AND RETAINED EARNINGS

For the Years Ended December 31

	2023	2022
OPERATING REVENUES		
Energy sales and other	\$ 175,609,328	\$ 167,180,404
OPERATING EXPENSES		
Fuel	72,710,290	58,843,964
Operating	34,268,533	31,708,830
Maintenance	23,745,333	21,105,121
Interest, net	10,557,635	10,255,500
Interest expense attributable to amortization of debt issuance costs	36,105	36,105
Depreciation	30,266,979	41,185,952
Total expenses	<u>171,584,875</u>	<u>163,135,472</u>
OPERATING MARGIN	<u>4,024,453</u>	<u>4,044,932</u>
Income taxes provision	772,583	1,275,736
NET EARNINGS AFTER TAXES	3,251,870	2,769,196
RETAINED EARNINGS, BEGINNING OF YEAR	<u>61,872,525</u>	<u>59,103,329</u>
RETAINED EARNINGS, END OF YEAR	<u>\$ 65,124,395</u>	<u>\$ 61,872,525</u>

See Notes to Financial Statements

CASH FLOWS

For the Years Ended December 31

	2023	2022
CASH FLOWS FROM OPERATING ACTIVITIES		
Net earnings	\$ 3,251,870	\$ 2,769,196
Adjustments to reconcile net earnings to net cash provided (used) by operating activities		
Depreciation	30,266,979	41,185,952
Interest expense attributable to amortization of debt issuance costs	36,105	36,105
Deferred income taxes	(690,747)	(3,414,675)
Amortization of deferred plant expenses	4,335,391	6,030,906
Addition (reduction) of asset retirement obligations, net	1,392,388	(304,126)
Capital credit allocations	(804,310)	(617,647)
Effects on operating cash flows due to changes in:		
Accounts receivable	12,731,729	924,386
Inventories	(384,221)	(1,022,358)
Prepayments	13,911	121,354
Accounts payable	(4,852,072)	9,308,614
Accrued liabilities	(672,100)	(621,179)
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	<u>44,624,923</u>	<u>54,396,528</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to electric plant, net	(16,822,615)	(31,319,298)
Additions to deferred plant expenses	–	(17,300,686)
Cash received from investments		
CoBank	296,788	360,224
Roughrider Electric Cooperative	90,496	39,824
National Rural Utilities Cooperative Finance Corporation	69,613	44,046
NET CASH PROVIDED (USED) BY INVESTING ACTIVITIES	<u>(16,365,718)</u>	<u>(48,175,890)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds (repayments) on lines of credit	9,156,000	7,302,000
Proceeds from long-term obligations	–	36,000,000
Repayments of long-term obligations	(38,393,919)	(48,454,189)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	<u>(29,237,919)</u>	<u>(5,152,189)</u>
NET CHANGE IN CASH AND CASH EQUIVALENTS	(978,714)	1,068,449
CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR	1,079,543	11,094
CASH AND CASH EQUIVALENTS AT END OF YEAR	<u>\$ 100,829</u>	<u>\$ 1,079,543</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW		
Cash paid during the year for interest paid	\$ 11,566,521	\$ 11,503,666

See Notes to Financial Statements

NOTES TO FINANCIAL STATEMENTS

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Square Butte Electric Cooperative (Square Butte or the Cooperative) is a North Dakota cooperative association organized in 1972 and is owned by 11 member-owner cooperatives. Membership in Square Butte is limited to organizations engaged in the business of generating, transmitting, or distributing electric power within the states of North Dakota and Minnesota.

Minnkota Power Cooperative, Inc. ("Minnkota"), acting as agent for Square Butte, operates and maintains Young 2. Substantially, all maintenance and other operating expenses of Square Butte represent costs incurred by Minnkota on Square Butte's behalf under the operating agreement discussed in Note 10. Such expenses are billed to Square Butte at cost.

Adoption of New Accounting Standards

The Cooperative adopted FASB ASC 326 effective January 1, 2023. The impact of the adoption was not considered material to the financial statements, and no adjustment to beginning retained earnings was recorded. The new standard primarily resulted in enhanced disclosures only.

Basis of Accounting

The financial statements of Square Butte have been prepared on the basis of accounting prescribed under the Power Sales Agreements with Minnesota Power (MP) and Minnkota in accordance with accounting principles generally accepted in the United States of America (GAAP), as codified by the Financial Accounting Standards Board. The Cooperative maintains its accounting records in accordance with the chart of accounts as adopted by the Rural Utilities Service (RUS).

Regulatory Accounting

As a result of the rate making process, the Cooperative applies Accounting Standards Codification (ASC) 980, *Regulated Operations*. The application of generally accepted accounting principles by the Cooperative differs in certain aspects from the application by non-regulated businesses as a result of applying ASC 980. Such differences are generally related to the time at which certain items enter into the determination of net margins in order to follow the principle of matching costs and revenues.

Revenues under the Power Sales Agreements are established at amounts sufficient to cover all costs of Square Butte plus a defined profit. Depreciation under the Power Sales Agreements includes the amount of principal applied to reduce the debt on First Mortgage Bonds, CoBank notes, First Mortgage notes, CFC notes, and RUS notes. If straight-line depreciation had been provided for these properties based on their estimated economic useful lives, depreciation expense would have decreased by approximately \$7,500,000 and \$7,600,000 for the years 2023 and 2022, respectively. Accumulated depreciation and amortization of the properties would have been increased by approximately \$32,489,000 and \$40,032,000 at December 31, 2023 and 2022, respectively.

Electric Plant and Retirements

The electric plant is stated at the book value plus the acquisition costs of formerly leased property, which includes certain indirect costs such as general and administrative expenses, interest and other financing costs. Normal repairs are charged to maintenance expense, whereas the costs of renewals and betterments of units of property are capitalized.

Depreciation

Depreciation of property, other than that financed by the First Mortgage Bonds, CoBank notes, First Mortgage notes, CFC notes, and RUS notes discussed above, is provided based on the straight-line method at rates designed to amortize the original cost of the properties over the estimated useful lives of each of the various classes of property or the remaining original term of the Power Sales Agreement, whichever is less. Beginning in 2011, all non-financed property is depreciated over the estimated useful life not beyond 2042.

Cash and Cash Equivalents

For the purpose of reporting cash flows, the Cooperative considers all highly liquid investments purchased with a maturity of three months or less to be cash equivalents.

Trade Receivables and Allowance for Credit Losses

Trade receivables are derived from sales to customers and are recorded at the invoice amount, less any allowance for credit losses. The net amount represents the amount expected to be collected as of the balance sheet date. Trade credit is generally extended on a short-term basis; thus, trade receivables do not

bear interest. Trade receivables are uncollateralized customer obligations due under normal trade terms requiring payment within 20 days from the billing date. Management has deemed that no late fees or interest charges are assessed to the receivables. Payments on trade receivables are allocated to the earliest unpaid billings.

The allowance for credit losses is based on management's expectation of the credit losses expected to arise over the life of the asset as of the balance sheet date (including consideration of prepayments) and is updated to reflect any changes in credit risk as of each subsequent reporting date. The Cooperative estimates its allowance for credit losses starting with an evaluation of historical credit loss write-offs, applied to an analysis of outstanding aged receivables, and updated for current economic conditions, and reasonable and supportable forecasted economic conditions. No significant adjustments to the allowance calculations for current or forecasted economic conditions were made during the current year. Receivables with unusual credit risk characteristics are evaluated individually. All other receivables are considered similar and are evaluated as one portfolio segment. Management's estimate of the allowance for credit losses, as well as the separate amounts of write-offs and recoveries were immaterial with respect to the financial statements as a whole as of December 31, 2023 and 2022.

Receivables are written off as a reduction in the allowance for credit losses when deemed uncollectible. Recoveries of accounts previously written off (if any) will be recognized as an offset to credit loss expense in the year of recovery.

Investments

Investments are patronage allocations from cooperatives and other affiliates stated at cost plus assigned capital credits less any capital paid to the Cooperative. Income from investments in cooperatives is recognized when capital credits are assigned.

Inventories

Fuel is recorded at cost using a LIFO (last-in, first-out) basis. Material and supplies are stated at lower of average cost or net realizable value.

Deferred Expenses

Deferred expenses consist of deferred outage expenses related to the Young 2 generation facility owned by the Cooperative, as well as deferred expenses related to the future retirement of long-lived assets. See also Note 4.

Allowance for Funds Used During Construction (AFUDC)

The allowance for funds used during construction is capitalized interest on all construction projects with a budgeted cost greater than \$50,000. AFUDC is classified as a reduction of interest expense.

Revenue Recognition

Revenues are primarily from electric sales to customers. Electric revenues are recognized over time as electricity is delivered to customers. Electric revenues are based on the reading of customer meters, which occurs on a systematic basis throughout each reporting period and represents the fair value of the electricity delivered.

Revenues are recognized equivalent to the value of the electricity supplied during each period, including amounts billed during each period and changes in amounts estimated to be billed at the end of each period. The Cooperative has elected to apply the invoice method to measure progress towards completing performance obligations to transfer electricity to their customers.

Business and Credit Risk

The Cooperative maintains its cash balances in a locally owned bank. Such balances are insured by the Federal Deposit Insurance Corporation up to \$250,000. The cash balances exceeded insurance coverage at various times during the fiscal years.

Fair Value Measurements

The Cooperative has determined the fair value of certain assets and liabilities in accordance with GAAP, which provides a framework for measuring fair value.

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date. Valuation techniques should maximize the use of observable inputs and minimize the use of unobservable inputs.

A fair value hierarchy has been established, which prioritizes the valuation inputs into three broad levels. Level 1 inputs consist of quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date. Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for the related asset or liability. Level 3 inputs are unobservable inputs related to the asset or liability.

The Cooperative does not have any assets or liabilities subject to the level 1, 2, or 3 valuation as of December 31, 2023 and 2022 and does not anticipate participating in transactions of this type in the future.

The fair value of the Cooperative's long-term debt was estimated based upon borrowing rates currently available to the Cooperative for bank loans with similar terms and average maturities. The estimated fair value of the Cooperative's long-term debt was \$157,000,000 and \$193,000,000 as of December 31, 2023 and 2022, respectively.

Accounting Estimates

The presentation 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.

Income Taxes

Deferred taxes are provided on a liability method whereby deferred tax assets are recognized for deductible temporary differences and operating loss and tax credit carryforwards and deferred tax liabilities are recognized for taxable temporary differences. Temporary differences are the differences between the reported amounts of assets and liabilities and their tax bases. Deferred tax assets are reduced by a valuation allowance when, in the opinion of management, it is more likely than not that some portion or all of the deferred tax assets will not be realized. Deferred tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of enactment.

The Cooperative's policy is to evaluate the likelihood that its uncertain tax positions will prevail upon examination based on the extent to which those positions have substantial support within the Internal Revenue Code and Regulations, Revenue Rulings, court decisions, and other evidence.

Debt Issuance Costs

Debt issuance costs are amortized over the period the related obligation is outstanding using the effective interest method. Debt issuance costs are included within long-term debt on the balance sheet. Amortization of debt issuance costs is included in interest expense attributable to amortization of debt issuance costs in the accompanying financial statements.

NOTE 2 - ELECTRIC PLANT

	2023	2022
Generation plant	\$ 802,707,669	\$ 779,677,200
Transmission plant	13,250,677	13,250,677
General plant	3,333,478	3,333,478
Electric plant in service	819,291,824	796,261,355
Construction work in progress	2,123,231	8,301,857
Total electric plant	<u>\$ 821,415,055</u>	<u>\$ 804,563,212</u>

The allowance for funds used during construction was \$356,786 and \$324,269 in 2023 and 2022, respectively.

NOTE 3 - INVESTMENTS IN ASSOCIATED COMPANIES

	2023	2022
Patronage capital allocations		
CoBank	\$ 5,838,704	\$ 5,607,739
Roughrider Electric Cooperative, Inc.	470,128	422,294
National Rural Utilities		
Cooperative Finance Corp. (CFC)	467,516	398,902
Minnkota Power Cooperative, Inc.	8,714	8,714
Memberships	1,000	1,000
Total investments in associated companies	<u>\$ 6,786,062</u>	<u>\$ 6,438,649</u>

NOTE 4 - DEFERRED EXPENSES

The Cooperative has expense deferral plans pertaining to outage expenditures at the Young 2 facility. The plans are in accordance with accounting principles generally accepted in the United States of America and were approved by RUS in 2019 and 2022. The total expenses are being charged to operations over a three and six year period for each respective plan. The Cooperative deferred expenses of \$0 and \$17,300,686 for the years ended December 31, 2023 and 2022, respectively.

The Cooperative recorded a deferred expense as a result of the timing difference of accounting for costs associated with the retirement of long-lived assets for financial reporting pursuant to accounting principles generally accepted in

the United States of America and for the purposes of rate-making. The Cooperative had total such deferred expenses of \$5,143,484 and \$3,751,096 as of December 31, 2023 and 2022, respectively. The following is a summary of changes in the deferred expenses:

	2023	2022
Deferred expenses – January 1	\$ 16,418,583	\$ 5,148,803
Addition of long-lived assets	2,031,201	–
Retirement of long-lived assets	(638,812)	(304,126)
Deferred outage costs added	–	17,300,686
Deferred outage costs expensed	(5,727,780)	(5,726,780)
Deferred expenses – December 31	<u>\$ 12,083,192</u>	<u>\$ 16,418,583</u>

Deferred expense balances are summarized below:

	2023	2022
Young 2 deferred outage expenses	\$ 6,939,708	\$ 12,667,487
Deferred expenses – retirement of long-lived assets	5,143,484	3,751,096
Deferred expenses – December 31	<u>\$ 12,083,192</u>	<u>\$ 16,418,583</u>

NOTE 5 - LONG-TERM DEBT

The long-term debt of the Cooperative consists of:

	2023	2022
Rural Utilities Service (RUS) mortgage notes		
Fixed rate notes (1.92%-4.77%) due in quarterly installments through 2026	\$ 15,307,594	\$ 20,161,508
First Mortgage		
Bond Series 1998A, 6.79% due in semi-annual installments through 2024 (based upon effective interest rate of 7.74%)	3,609,000	21,026,000
Less unamortized debt issuance costs	(5,074)	(6,766)
Fixed rate notes (4.48%-5.78%) due in semi-annual and quarterly installments through 2042 (based upon effective interest rate of 5.00%)	68,118,969	70,330,116
Less unamortized debt issuance costs	(375,646)	(399,665)
Total	<u>71,347,249</u>	<u>90,949,685</u>
CoBank mortgage notes		
Fixed and variable rate notes (5.21%-7.44%) due in quarterly installments through 2026 (based upon effective interest rate of 5.00%)	33,338,602	43,275,399
Less unamortized debt issuance costs	(35,527)	(45,920)
Total	<u>33,303,075</u>	<u>43,229,479</u>
National Rural Utilities Cooperative Finance Corporation (CFC) mortgage notes - fixed rates (3.55%-4.42%) due in quarterly installments through 2037	51,422,508	55,397,568
Total long-term debt	171,380,426	209,738,240
Less current maturities	(25,492,796)	(38,393,920)
Long-term debt	<u>\$ 145,887,630</u>	<u>\$ 171,344,320</u>

Scheduled maturities of long-term debt are as follows:

Years ending December 31	Amount
2024	\$ 25,492,796
2025	22,832,557
2026	24,099,180
2027	7,292,328
2028	7,599,125
Thereafter	84,480,687
Debt issuance costs	(416,247)
Total long-term debt	<u>\$ 171,380,426</u>

All loan funds advanced by RUS are deposited in a special trust bank account, the disbursements from which are restricted by the provisions of the loan agreement to purposes approved by RUS. All loan funds advanced from First Mortgage, CoBank, and CFC are deposited in the general checking bank account. At December 31, 2023, there were no unadvanced loan funds to the Cooperative.

NOTES TO FINANCIAL STATEMENTS

NOTE 6 - REVENUES FROM CONTRACTS WITH CUSTOMERS

The revenues of the Cooperative are primarily derived from providing wholesale electric service to its customers. Revenues from contracts with customers represent over 99% of all Cooperative revenues. Below is a disaggregated view of the Cooperative's revenues from contracts with customers as well as other revenues, including their location on the statement of revenues, expenses and retained earnings for December 31, 2023 and 2022:

Revenue Streams	Operating Revenue	
	2023	2022
Energy sales to customers	\$ 174,805,018	\$ 166,562,757
Total revenue contracts with customers	174,805,018	166,562,757
Capital credit allocations	804,310	617,647
Total revenue	\$ 175,609,328	\$ 167,180,404
Timing of revenue recognition		
Services transferred over time	\$ 174,805,018	\$ 166,562,757

Electric Revenue

Electric revenues consist of wholesale electric power sales to customers through the power sales agreement. All of the electric revenues meet the criteria to be classified as revenue from contracts with customers and are recognized over time as energy is delivered. Revenue is recognized based on the metered quantity of electricity delivered or transmitted at the applicable contractual rates.

Accounts receivable and contract balances with customers are as follows:

	Accounts Receivable	Contract Liabilities
January 01, 2022	\$ 22,026,360	\$ -
December 31, 2022	21,192,271	-
December 31, 2023	8,460,542	-

NOTE 7 - LINE OF CREDIT

The Cooperative has a line of credit agreement with U.S. Bank of North Dakota with available borrowings totaling \$5,000,000 expiring June 30, 2024. The line of credit had a variable interest rate of 7.24281% and 6.02396% at December 31, 2023 and 2022, respectively. Amounts outstanding on the line totaled \$3,927,000 and \$2,771,000 as of December 31, 2023 and 2022, respectively.

The Cooperative also has a line of credit agreement with CFC available for \$55,000,000 expiring June 30, 2025. The line had a variable borrowing rate of 6.86% and 5.73% at December 31, 2023 and 2022, respectively. At December 31, 2023 and 2022, there were outstanding borrowings on this line of credit totaling \$32,000,000 and \$24,000,000, respectively.

The Cooperative also has two \$10,000,000 lines of credit available for use, one each with Minnkota and MP. These lines have a variable interest rate (1% below the prime rate) and are automatically renewed each year. There were no amounts outstanding on these lines as of December 31, 2023 and 2022.

NOTE 8 - INCOME TAXES

Deferred tax assets and liabilities consist of the following components as of December 31, 2023 and 2022:

	2023	2022
Deferred tax assets		
Inventories	\$ (278,734)	\$ (278,734)
Amortization	(31,335)	(421,100)
Total deferred tax asset	(310,069)	(699,834)
Deferred tax liability		
Depreciation	6,520,533	6,375,982
Capitalized interest	-	1,225,063
Total deferred tax liability	6,520,533	7,601,045
Net deferred tax liabilities	\$ 6,210,464	\$ 6,901,211

The provision for income taxes charged to income for the years ended December 31, 2023 and 2022 consists of the following:

	2023	2022
Current provision	\$ 1,463,330	\$ 4,690,411
Deferred expense (benefit)	(690,747)	(3,414,675)
Balance	\$ 772,583	\$ 1,275,736

The 2023 and 2022 effective tax rates may differ from the federal tax rate primarily due to state income taxes.

It is the opinion of management that the Cooperative has no significant uncertain tax positions that would be subject to change upon examination. The federal income tax returns of the Cooperative are subject to examination by the IRS, generally for three years after they were filed. All required filings are current.

NOTE 9 - DEFERRED CREDITS

The deferred credits balance is made up of an asset retirement obligation resulting from the production of power at the Young 2 facility.

The FASB has issued guidance which provides accounting requirements for retirement obligations associated with tangible long-lived assets. Retirement obligations associated with long-lived assets are those for which there is a legal obligation to settle under existing or enacted law, statute, ordinance, written or oral contract or by legal constructions under doctrine of promissory estoppel.

Assets considered for potential asset retirement obligations include generating plants and transmission assets on property under easement agreement or license.

Management has determined that the Cooperative has a legal obligation to close its ash and sludge disposal ponds upon reaching the end of their useful lives resulting in the recording, at a discounted present value, a deferred expense and asset retirement obligation of \$5,143,484 and \$3,751,096 at December 31, 2023 and 2022, respectively. The deferred expenses were recognized in accordance with U.S. GAAP.

Under the power sales agreements with Minnkota and MP, the pass-through of closure costs are not due until the actual closure costs are incurred. Asset retirement obligations for generation plant are not recorded as a liability, due to the fact that governmental authorization for construction did not impose post-closure obligations.

NOTE 10 - SALES, OPERATING, COAL SUPPLY AGREEMENTS

Under the Power Sales Agreements dated May 29, 1998, which expire on January 2, 2027, MP was entitled to purchase 70.8333% and Minnkota was entitled to purchase 29.1667% of the entire output of Young 2 generation facility. Subsequent to the original agreement, certain options were available, and exercised, to increase Minnkota's percentage, respectively decreasing MP's percentage. Currently, MP and Minnkota each purchase 50% of the net capability of Young 2 as a result of exercising these options.

On December 30, 2009, Minnkota, Square Butte, and MP completed an agreement in which Minnkota receives additional energy and capability from Young 2. Between 2014 and 2026, Minnkota has the option to acquire MP's 50% allocation from Young 2. In 2014, Minnkota exercised this option and started purchasing an additional 22.5275% allocation of Young 2 from MP. This allocation increased to 28.022% on January 1, 2015. This allocation will increase by approximately 4.4% per year from 2022-2026. From 2027 through 2042, Minnkota will purchase 100% of the Young 2 output directly from Square Butte.

The power sales agreements provide for a pass-through on a percentage basis according to the respective entitlements to the output and capacity of Young 2, of all of Square Butte's costs, plus a margin of 5% of non-fuel operating expenses. Each purchaser is required to make full payment of the cost of power based on its percentage entitlement. The payment obligations of MP and Minnkota are several, not joint, and are not guarantees of any Square Butte obligations.

The Cooperative has an agreement with Minnkota whereby Minnkota operates Young 2. All costs associated with the operation of Young 2 are paid by the Cooperative. In addition, the Cooperative pays a minimum annual royalty of \$1,350,000 to Minnkota on coal purchased.

The Cooperative has a Coal Supply Agreement with BNI Coal Ltd. to purchase coal for Young 2. This agreement expires in 2037, with an additional 5-year extension at the Cooperative's option. The agreement provides for reimbursement to BNI Coal Ltd. of all fixed production costs and labor plus a specified profit on each ton of coal delivered. Billings from BNI Coal Ltd. to the Cooperative were approximately \$64,426,000 and \$56,084,000 for the years ended December 31, 2023 and 2022, respectively.

NOTE 11 - RELATED PARTY TRANSACTIONS

During the years ended December 31, 2023 and 2022, the Cooperative contracted services provided by Minnkota. The transactions conducted between the Cooperative and Minnkota were as follows:

	2023	2022
Energy sales	\$ 85,387,974	\$ 82,116,401
Accounts receivable from Minnkota	\$ 4,373,646	\$ 10,738,026
Accounts payable to Minnkota	\$ 5,850,856	\$ 9,344,399

NOTE 12 - SUBSEQUENT EVENTS

No significant events occurred subsequent to the Cooperative's year end. Subsequent events have been evaluated through February 9, 2024, which is the date these financial statements were available to be issued.

INDEPENDENT AUDITOR'S REPORT

To the Members and the Board of Directors
Square Butte Electric Cooperative
Grand Forks, North Dakota

REPORT ON THE FINANCIAL STATEMENTS

Opinion

We have audited the accompanying financial statements of Square Butte Electric Cooperative, which comprise the balance sheets as of December 31, 2023 and 2022, and the related statements of revenues, expenses and retained earnings, and cash flows for the years then ended, and the related notes to the financial statements.

In our opinion, the financial statements present fairly, in all material respects, the financial position of Square Butte Electric Cooperative as of December 31, 2023 and 2022, and the results of its operations and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Basis for Opinion

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Square Butte Electric Cooperative and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audit. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting principles generally accepted in the United States of America, and for 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about Square Butte Electric Cooperative's ability to continue as a going concern for twelve months beyond the financial statement date, including any currently known information that may raise substantial doubt shortly thereafter.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with generally accepted auditing standards and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with generally accepted auditing standards and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Square Butte Electric Cooperative's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about Square Butte Electric Cooperative's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control-related matters that we identified during the audit.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated February 9, 2024, on our consideration of Square Butte Electric Cooperative's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on effectiveness of Square Butte Electric Cooperative's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Square Butte Electric Cooperative's internal control over financial reporting and compliance.

Other Information Included in the Cooperative's Annual Report

Management is responsible for the other information included in the Cooperative's Annual Report. The other information comprises reports by management to the members, summarized statistical data, and the Officers and Director listing, but it does not include the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information, and we do not express an opinion or any form of assurance on it.

In connection with our audit of the financial statements, our responsibility is to read the other information and consider whether a material inconsistency exists between the other information and the financial statements, or the other information otherwise appears to be materially misstated. If, based on the work performed, we conclude that an uncorrected material misstatement of the other information exists, we are required to describe it in our report

BRADY, MARTZ & ASSOCIATES, P.C. GRAND FORKS, NORTH DAKOTA

February 9, 2024

