Otter Tail Corp
Form 10-Q
August 10, 2015

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2015

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to

Commission file number 0-53713

OTTER TAIL CORPORATION
(Exact name of registrant as specified in its charter)

Minnesota	27-0383995
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

215 South Cascade Street, Box 496, Fergus Falls, Minnesota 56538-0496
(Address of principal executive offices) (Zip Code)

866-410-8780
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.:

Large accelerated filer	Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company)	Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined by Rule 12b-2 of the Exchange Act). Yes No

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock, as of the latest practicable date:

July 31, 2015 – 37,591,785 Common Shares ($5 par value)

OTTER TAIL CORPORATION

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Otter Tail Corporation Consolidated Balance Sheets
(not audited)

(in thousands)	**June 30, 2015**	**December 31, 2014**
Assets		
Current Assets		
Cash and Cash Equivalents	$--	$--
Accounts Receivable:		
Trade—Net	67,315	60,172
Other	18,248	13,179
Inventories	81,803	85,203
Deferred Income Taxes	54,498	49,482
Unbilled Revenues	14,352	17,996
Regulatory Assets	17,736	25,273
Other	8,588	7,187
Assets of Discontinued Operations	133	48,657
Total Current Assets	262,673	307,149
Investments	10,679	8,582
Other Assets	30,827	30,111
Goodwill	31,488	31,488
Other Intangibles—Net	10,863	11,251
Deferred Debits		
Unamortized Debt Expense	3,949	4,300
Regulatory Assets	127,475	129,868
Total Deferred Debits	131,424	134,168
Plant		
Electric Plant in Service	1,583,169	1,545,112
Nonelectric Operations	180,309	175,159
Construction Work in Progress	269,060	248,677
Total Gross Plant	2,032,538	1,968,948

Less Accumulated Depreciation and Amortization	699,113	700,418
Net Plant	1,333,425	1,268,530
Total Assets	$1,811,379	$1,791,279

See accompanying condensed notes to consolidated financial statements.

Otter Tail Corporation Consolidated Balance Sheets
(not audited)

(in thousands, except share data)	**June 30, 2015**	**December 31, 2014**
LIABILITIES AND EQUITY		
Current Liabilities		
Short-Term Debt	$43,040	$10,854
Current Maturities of Long-Term Debt	207	201
Accounts Payable	101,020	107,013
Accrued Salaries and Wages	14,077	19,256
Accrued Taxes	9,997	13,793
Derivative Liabilities	14,388	14,230
Other Accrued Liabilities	12,099	8,793
Liabilities of Discontinued Operations	3,260	27,559
Total Current Liabilities	198,088	201,699
Pensions Benefit Liability	93,545	102,711
Other Postretirement Benefits Liability	54,357	53,638
Other Noncurrent Liabilities	24,319	26,794
Commitments and Contingencies (note 9)		
Deferred Credits		
Deferred Income Taxes	248,581	230,810
Deferred Tax Credits	25,445	26,384
Regulatory Liabilities	77,972	77,013
Other	977	975
Total Deferred Credits	352,975	335,182
Capitalization		
Long-Term Debt, Net of Current Maturities	498,384	498,489
Cumulative Preferred Shares– Authorized 1,500,000 Shares Without Par Value; Outstanding - None	--	--
Cumulative Preference Shares – Authorized 1,000,000 Shares Without Par Value; Outstanding - None	--	--

Common Shares, Par Value $5 Per Share—Authorized, 50,000,000 Shares; Outstanding, 2015—37,565,590 Shares; 2014—37,218,053 Shares	187,828	186,090
Premium on Common Shares	287,066	278,436
Retained Earnings	119,239	112,903
Accumulated Other Comprehensive Loss	(4,422)	(4,663)
Total Common Equity	589,711	572,766
Total Capitalization	1,088,095	1,071,255
Total Liabilities and Equity	$1,811,379	$1,791,279

See accompanying condensed notes to consolidated financial statements.

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Otter Tail Corporation
Consolidated Statements of Income
(not audited)

(in thousands, except share and per-share amounts)	**Three Months Ended June 30, 2015**	**2014**	**Six Months Ended June 30, 2015**	**2014**
Operating Revenues				
Electric	$90,927	$92,903	$204,460	$211,951
Product Sales	97,226	101,461	186,534	197,379
Total Operating Revenues	188,153	194,364	390,994	409,330
Operating Expenses				
Production Fuel - Electric	4,183	12,603	18,782	34,633
Purchased Power - Electric System Use	19,684	16,476	43,376	38,261
Electric Operation and Maintenance Expenses	37,754	39,774	75,281	74,396
Cost of Products Sold (depreciation included below)	74,986	80,178	146,484	154,117
Other Nonelectric Expenses	8,823	12,722	21,286	22,673
Depreciation and Amortization	14,661	14,472	29,196	28,739
Property Taxes - Electric	3,262	3,387	6,764	6,358
Total Operating Expenses	163,353	179,612	341,169	359,177
Operating Income	24,800	14,752	49,825	50,153
Interest Charges	7,702	7,626	15,445	14,221
Other Income	567	844	1,139	2,379
Income Before Income Taxes—Continuing Operations	17,665	7,970	35,519	38,311
Income Tax Expense—Continuing Operations	4,008	84	8,081	8,646
Net Income from Continuing Operations	13,657	7,886	27,438	29,665
Discontinued Operations				
(Loss) Income - net of Income Tax (Benefit) Expense of ($1,329), $1,402, ($2,705) and $1,177 for the Respective Periods	(1,992)	2,107	(4,064)	1,758
Impairment Loss - net of Income Tax Benefit of $0 for the Six Months ended June 30, 2015	--	--	(1,000)	--
(Loss) Gain on Disposition - net of Income Tax (Benefit) Expense of ($280) and $4,536 for the three and six months ended June 30, 2015	(229)	--	6,997	--
Net (Loss) Income from Discontinued Operations	(2,221)	2,107	1,933	1,758
Net Income	11,436	9,993	29,371	31,423
Average Number of Common Shares Outstanding—Basic	37,433,318	36,409,753	37,338,218	36,325,052
Average Number of Common Shares Outstanding—Diluted	37,653,203	36,652,684	37,558,103	36,568,030
Basic Earnings (Loss) Per Common Share:				

Continuing Operations	$0.37	$0.21	$0.74	$0.82
Discontinued Operations	(0.06)	0.06	0.05	0.05
	$0.31	$0.27	$0.79	$0.87
Diluted Earnings (Loss) Per Common Share:				
Continuing Operations	$0.36	$0.21	$0.73	$0.81
Discontinued Operations	(0.06)	0.06	0.05	0.05
	$0.30	$0.27	$0.78	$0.86
Dividends Declared Per Common Share	$0.3075	$0.3025	$0.6150	$0.6050

See accompanying condensed notes to consolidated financial statements.

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Otter Tail Corporation
Consolidated Statements of Comprehensive Income
(not audited)

(in thousands)	**Three Months Ended June 30, 2015**	**2014**	**Six Months Ended June 30, 2015**	**2014**
Net Income	$11,436	$9,993	$29,371	$31,423
Other Comprehensive Income:				
Unrealized Gain on Available-for-Sale Securities:				
Reversal of Previously Recognized Gains Realized on Sale of Investments and Included in Other Income During Period	--	--	(3)	(17)
(Losses) Gains Arising During Period	(37)	36	(5)	19
Income Tax Benefit (Expense)	13	(13)	3	(1)
Change in Unrealized Gains on Available-for-Sale Securities – net-of-tax	(24)	23	(5)	1
Pension and Postretirement Benefit Plans:				
Amortization of Unrecognized Postretirement Benefit Losses and Costs (note 11)	207	51	411	101
Income Tax Expense	(83)	(20)	(165)	(40)
Pension and Postretirement Benefit Plans – net-of-tax	124	31	246	61
Total Other Comprehensive Income	100	54	241	62
Total Comprehensive Income	$11,536	$10,047	$29,612	$31,485

See accompanying condensed notes to consolidated financial statements.

Otter Tail Corporation
Consolidated Statements of Cash Flows
(not audited)

(in thousands)	**Six Months Ended June 30, 2015**	**2014**
Cash Flows from Operating Activities		
Net Income	$29,371	$31,423
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Net Gain from Sale of Discontinued Operations	(6,997)	--
Net Loss (Income) from Discontinued Operations	5,064	(1,758)
Depreciation and Amortization	29,196	28,739
Deferred Tax Credits	(939)	(907)
Deferred Income Taxes	12,707	13,402
Change in Deferred Debits and Other Assets	11,470	129
Discretionary Contribution to Pension Plan	(10,000)	(20,000)
Change in Noncurrent Liabilities and Deferred Credits	4,025	(936)
Allowance for Equity/Other Funds Used During Construction	(576)	(759)
Change in Derivatives Net of Regulatory Deferral	(123)	95
Stock Compensation Expense—Equity Awards	1,126	736
Other—Net	200	193
Cash (Used for) Provided by Current Assets and Current Liabilities:		
Change in Receivables	(5,918)	(15,736)
Change in Inventories	3,400	(10,070)
Change in Other Current Assets	1,913	1,523
Change in Payables and Other Current Liabilities	(21,294)	(8,208)
Change in Interest and Income Taxes Receivable/Payable	96	2,664
Net Cash Provided by Continuing Operations	52,721	20,530
Net Cash Used in Discontinued Operations	(10,966)	(16,359)
Net Cash Provided by Operating Activities	41,755	4,171
Cash Flows from Investing Activities		
Capital Expenditures	(83,418)	(79,574)
Net Proceeds from Disposal of Noncurrent Assets	2,628	1,386
Net Increase in Other Investments	(5,763)	(1,639)
Net Cash Used in Investing Activities - Continuing Operations	(86,553)	(79,827)
Net Proceeds from Sale of Discontinued Operations	32,765	--
Net Cash (Used in) Provided by Investing Activities - Discontinued Operations	(1,770)	630
Net Cash Used in Investing Activities	(55,558)	(79,197)
Cash Flows from Financing Activities		
Change in Checks Written in Excess of Cash	(947)	2,014
Net Short-Term Borrowings (Repayments)	32,186	(23,051)
Proceeds from Issuance of Common Stock	7,096	8,452
Common Stock Issuance Expenses	(248)	(310)

Payments for Retirement of Capital Stock	(1,421)	(459)
Proceeds from Issuance of Long-Term Debt	--	150,000
Short-Term and Long-Term Debt Issuance Expenses	(4)	(516)
Payments for Retirement of Long-Term Debt	(99)	(40,993)
Dividends Paid and Other Distributions	(23,035)	(22,029)
Net Cash Provided by Financing Activities – Continuing Operations	13,528	73,108
Net Cash Provided by Financing Activities – Discontinued Operations	322	760
Net Cash Provided by Financing Activities	13,850	73,868
Net Change in Cash and Cash Equivalents - Discontinued Operations	(47)	(849)
Net Change in Cash and Cash Equivalents	--	(2,007)
Cash and Cash Equivalents at Beginning of Period	--	2,007
Cash and Cash Equivalents at End of Period	$--	$--

See accompanying condensed notes to consolidated financial statements.

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OTTER TAIL CORPORATION

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(not audited)

In the opinion of management, Otter Tail Corporation (the Company) has included all adjustments (including normal recurring accruals) necessary for a fair presentation of the consolidated financial statements for the periods presented. The consolidated financial statements and condensed notes thereto should be read in conjunction with the consolidated financial statements and notes included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2014. Because of seasonal and other factors, the earnings for the three and six month periods ended June 30, 2015 should not be taken as an indication of earnings for all or any part of the balance of the year.

The following condensed notes are numbered to correspond to numbers of the notes included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2014.

1. Summary of Significant Accounting Policies

Revenue Recognition

Due to the diverse business operations of the Company, revenue recognition depends on the product produced and sold or service performed. The Company recognizes revenue when the earnings process is complete, evidenced by an agreement with the customer, there has been delivery and acceptance, and the price is fixed or determinable. Provisions for sales returns are recorded at the time of the sale based on historical information and current trends. In the case of derivative instruments, such as Otter Tail Power Company (OTP) forward energy contracts, marked-to-market and realized gains and losses are recognized on a net basis in revenue in accordance with the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 815, *Derivatives and Hedging*. Gains and losses on forward energy contracts subject to regulatory treatment, if any, are deferred and recognized on a net basis in revenue in the period realized.

For the Company's operating companies recognizing revenue on certain products when shipped, those operating companies have no further obligation to provide services related to such product. The shipping terms used in these instances are FOB shipping point.

Warranty Reserves

Certain products previously sold by the Company carried one to fifteen year warranties. Although the Company engaged in extensive product quality programs and processes, the Company's warranty obligations have been and may in the future be affected by product failure rates, repair or field replacement costs and additional development costs incurred in correcting product failures. The Company's warranty reserve balances as of June 30, 2015 and December 31, 2014 relate entirely to products that were produced by IMD, Inc. and Shrco, Inc. prior to the Company selling the assets of these companies and are included in liabilities of discontinued operations. See note 16 to consolidated financial statements.

Fair Value Measurements

The Company follows ASC Topic 820, *Fair Value Measurements and Disclosures* (ASC 820), for recurring fair value measurements. ASC 820 provides a single definition of fair value, requires enhanced disclosures about assets and liabilities measured at fair value and establishes a hierarchal framework for disclosing the observability of the inputs utilized in measuring assets and liabilities at fair value. The three levels defined by the hierarchy and examples of each level are as follows:

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reported date. The types of assets and liabilities included in Level 1 are highly liquid and actively traded instruments with quoted prices, such as equities listed by the New York Stock Exchange and commodity derivative contracts listed on the New York Mercantile Exchange (NYMEX).

Level 2 – Pricing inputs are other than quoted prices in active markets, but are either directly or indirectly observable as of the reported date. The types of assets and liabilities included in Level 2 are typically either comparable to actively traded securities or contracts, such as treasury securities with pricing interpolated from recent trades of similar securities, or priced with models using highly observable inputs, such as commodity options priced using observable forward prices and volatilities.

Level 3 – Significant inputs to pricing have little or no observability as of the reporting date. The types of assets and liabilities included in Level 3 are those with inputs requiring significant management judgment or estimation and may include complex and subjective models and forecasts.

The following tables present, for each of the hierarchy levels, the Company's assets and liabilities that are measured at fair value on a recurring basis as of June 30, 2015 and December 31, 2014:

June 30, 2015 *(in thousands)*	Level 1	Level 2	Level 3
Assets:			
Current Assets – Other:			
Forward Energy Contracts	$--	$--	$194
Investments:			
Money Market Deposit Escrow Account – AEV, Inc. and Foley Company Sales	2,500		
Corporate Debt Securities – Held by Captive Insurance Company		6,679	
U.S. Government-Sponsored Enterprises' Debt Securities – Held by Captive Insurance Company		1,221	
Other Assets:			
Money Market and Mutual Funds - Nonqualified Retirement Savings Plan	273		
Total Assets	$2,773	$7,900	$194
Liabilities:			
Derivative Liabilities - Forward Gasoline Purchase Contracts	$--	$219	$--
Derivative Liabilities - Forward Energy Contracts			14,169
Total Liabilities	$--	$219	$14,169

December 31, 2014 *(in thousands)*	Level 1	Level 2	Level 3
Assets:			
Current Assets – Other:			
Forward Energy Contracts	$--	$--	$257
Money Market and Mutual Funds - Nonqualified Retirement Savings Plan	120		
Investments:			
Corporate Debt Securities – Held by Captive Insurance Company		6,761	
U.S. Government-Sponsored Enterprises' Debt Securities – Held by Captive Insurance Company		1,253	
Other Assets:			
Money Market and Mutual Funds - Nonqualified Retirement Savings Plan	593		
Total Assets	$713	$8,014	$257
Liabilities:			
Derivative Liabilities - Forward Gasoline Purchase Contracts	$--	$342	$--
Derivative Liabilities - Forward Energy Contracts			13,888
Total Liabilities	$--	$342	$13,888

The valuation techniques and inputs used for the Level 2 fair value measurements in the table above are as follows:

Forward Gasoline Purchase Contracts – These contracts are priced based on NYMEX quoted prices for Reformulated Blendstock for Oxygenate Blending (RBOB) Gasoline contracts. Prices used for the fair valuation of these contracts are based on NYMEX daily reporting date quoted prices for RBOB contracts with the same settlement periods.

Corporate and U.S. Government-Sponsored Enterprises' Debt Securities Held by the Company's Captive Insurance Company – Fair values are determined on the basis of valuations provided by a third-party pricing service which utilizes industry accepted valuation models and observable market inputs to determine valuation. Some valuations or model inputs used by the pricing service may be based on broker quotes.

Fair values for OTP's forward energy contracts with delivery points that are not at an active trading hub included in Level 3 of the fair value hierarchy in the table above as of June 30, 2015 and December 31, 2014, are based on prices indexed to observable prices at an active trading hub. Prices at illiquid trading points are based on a basis spread between that trading point and more liquid trading hub prices. These basis spreads are determined based on available market price information and the use of forward price curve models. The June 30, 2015 Level 3 forward electric basis spreads ranged from $3.17 to $7.00 per megawatt-hour under the active trading hub price. The weighted average price was $32.71 per megawatt-hour.

In the table above, the fair value of the Level 3 forward energy contracts in derivative asset and derivative liability positions as of June 30, 2015 are related to power purchase contracts where OTP intends to take or has taken physical delivery of the energy under the contract. When OTP takes physical delivery of the energy purchased under these contracts the costs incurred are subject to recovery in base rates and through fuel clause adjustments. Any derivative assets or liabilities and related gains or losses recorded as a result of the fair valuation of these power purchase contracts will not be realized and are 100% offset by regulatory liabilities and assets related to fuel clause adjustment treatment of purchased power costs. Therefore, the net impact of any recorded fair valuation gains or losses related to these contracts on the Company's consolidated net income is $0 and the net income impact of any future fair valuation adjustments of these contracts will be $0. When energy is delivered under these contracts, they will be settled at the original contract price and any fair valuation gains or losses and related derivative assets or liabilities recorded over the life of the contracts will be reversed along with any offsetting regulatory liabilities or assets. Because of regulatory accounting treatment, any price volatility related to the fair valuation of these contracts had no impact on the Company's reported consolidated net income for the three or six month periods ended June 30, 2015 and 2014.

The following table presents changes in Level 3 forward energy contract derivative asset and liability fair valuations for the six month periods ended June 30, 2015 and 2014:

	Six Months Ended June 30,	
(in thousands)	2015	2014
Forward Energy Contracts - Fair Values Beginning of Period	$(13,631)	$(11,341)
Less: Amounts Reversed on Settlement of Contracts Entered into in Prior Periods	4,302	1,161
Net Changes in Fair Value of Contracts Entered into in Prior Periods	(3,732)	7,400
Cumulative Fair Value Adjustments of Contracts Entered into in Prior Years at End of Period	(13,061)	(2,780)
Net Loss Recognized as Regulatory Assets on Contracts Entered into in Period	(914)	--
Forward Energy Contracts - Net Derivative Liability Fair Values End of Period	$(13,975)	$(2,780)

<u>Inventories</u>

Inventories consist of the following:

(in thousands)	June 30, 2015	December 31, 2014
Finished Goods	$23,276	$ 27,998
Work in Process	10,877	10,628
Raw Material, Fuel and Supplies	47,650	46,577
Total Inventories	$81,803	$ 85,203

Goodwill and Other Intangible Assets

An assessment of the carrying amounts of the goodwill of the Company's reporting units reported under continuing operations as of December 31, 2014 indicated the fair values are in excess of their respective book values and not impaired.

The following table summarizes goodwill by business segment indicating no changes to the carrying amounts in the first six months of 2015:

(in thousands)	Gross Balance December 31, 2014	Accumulated Impairments	Balance (net of impairments) December 31, 2014	Adjustments to Goodwill in 2015	Balance (net of impairments) June 30, 2015
Manufacturing	$ 12,186	$ --	$ 12,186	$ --	$ 12,186
Plastics	19,302	--	19,302	--	19,302
Total	$ 31,488	$ --	$ 31,488	$ --	$ 31,488

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Intangible assets with finite lives are amortized over their estimated useful lives and reviewed for impairment in accordance with requirements under ASC Topic 360-10-35, *Property, Plant, and Equipment—Overall—Subsequent Measurement*. In the first quarter of 2015, OTP began purchasing emission allowances to apply against sulfur dioxide emissions from its Hoot Lake Plant. The cost of unused emission allowances is included in intangible assets on the Company's June 30, 2015 balance sheets. The following table summarizes the components of the Company's intangible assets at June 30, 2015 and December 31, 2014:

June 30, 2015 *(in thousands)*	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Remaining Amortization Periods
Amortizable Intangible Assets:				
Customer Relationships	$ 16,811	$ 6,208	$ 10,603	54-154 months
Other Intangible Assets Including Contracts	639	479	160	15 months
Emission Allowances	100	NA	100	Expensed as used
Total	$ 17,550	$ 6,687	$ 10,863	
December 31, 2014 *(in thousands)*				
Amortizable Intangible Assets:				
Customer Relationships	$ 16,811	$ 5,784	$ 11,027	60-160 months
Other Intangible Assets Including Contracts	639	415	224	21 months
Total	$ 17,450	$ 6,199	$ 11,251	

The amortization expense for these intangible assets was:

	Three Months Ended June 30,		Six Months Ended June 30,	
(in thousands)	2015	2014	2015	2014
Amortization Expense – Intangible Assets	$ 244	$ 244	$ 488	$ 488

The estimated annual amortization expense for these intangible assets for the next five years is:

(in thousands)	2015	2016	2017	2018	2019
Estimated Amortization Expense – Intangible Assets	$977	$945	$849	$849	$849

The following table presents a reconciliation of OTP's emission allowances balance for the six month period ended June 30, 2015:

(in thousands)	Six Months Ended June 30, 2015
Emission Allowances Beginning Balance	$ --
Allowances Purchased	168
Allowances Used	(68)
Emission Allowances Ending Balance	$ 100

<u>Supplemental Disclosures of Cash Flow Information</u>

(in thousands)	As of June 30, 2015	As of June 30, 2014
Noncash Investing Activities:		
Accounts Payable Outstanding Related to Capital Additions[1]	$31,455	$21,992
Accounts Receivable Outstanding Related to Joint Plant Owner's Share of Capital Additions[2]	$4,188	$4,373

[1]*Amounts are included in cash used for capital expenditures in subsequent periods when payables are settled.*

[2]*Amounts are deducted from cash used for capital expenditures in subsequent periods when cash is received.*

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Coyote Station Lignite Supply Agreement – Variable Interest Entity—In October 2012, the Coyote Station owners, including OTP, entered into a lignite sales agreement (LSA) with Coyote Creek Mining Company, L.L.C. (CCMC), a subsidiary of The North American Coal Corporation, for the purchase of lignite coal to meet the coal supply requirements of Coyote Station for the period beginning in May 2016 and ending in December 2040. The price per ton to be paid by the Coyote Station owners under the LSA will reflect the cost of production, along with an agreed profit and capital charge. CCMC was formed for the purpose of mining coal to meet the coal fuel supply requirements of Coyote Station from May 2016 through December 2040 and, based on the terms of the LSA, is considered a variable interest entity (VIE) due to the transfer of all operating and economic risk to the Coyote Station owners, as the agreement is structured so that the price of the coal would cover all costs of operations as well as future reclamation costs. The Coyote Station owners are also providing a guarantee of the value of the assets of CCMC as they would be required to buy certain assets at book value should they terminate the contract prior to the end of the contract term and are providing a guarantee of the value of the equity of CCMC in that they are required to buy the entity at the end of the contract term at equity value. Under current accounting standards, the primary beneficiary of a VIE is required to include the assets, liabilities, results of operations and cash flows of the VIE in its consolidated financial statements. No single owner of Coyote Station owns a majority interest in Coyote Station and none, individually, has the power to direct the activities that most significantly impact CCMC. Therefore, none of the owners individually, including OTP, is considered a primary beneficiary of the VIE and the Company is not required to include CCMC in its consolidated financial statements.

Under the LSA, all development period costs of the Coyote Creek coal mine incurred during the development period will be recovered from the Coyote Station owners over the full term of the production period, which commences with the initial delivery of coal to Coyote Station (anticipated in May 2016), by being included in the cost of production. The development fee and the capital charge incurred during the development period will be recovered from the Coyote Station owners over the first 52 months of the production period by being included in the cost of production during those months. The LSA was amended on March 16, 2015 to provide, among other things, that during any period between December 31, 2016 and any subsequent date on which CCMC makes initial delivery of coal, the Coyote Station owners will pay the following costs of production as advance payments for lignite: depreciation and amortization charges on capital assets and CCMC's obligations under its loans and leases. In addition, if the LSA terminates prior to the expiration of its term or the production period terminates prior to December 31, 2040 and the Coyote Station owners purchase all of the outstanding membership interests of CCMC as required by the LSA, the owners will satisfy, or (if permitted by CCMC's applicable lender) assume, all of CCMC's obligations owed to CCMC's lenders under its loans and leases. The Coyote Station owners have limited rights to assign their rights and obligations under the LSA without the consent of CCMC's lenders during any period in which CCMC's obligations to its lenders remain outstanding. OTP's 35% share of development period costs, development fees and capital charges incurred by CCMC through June 30, 2015 is $35.9 million. In the event the contract is terminated because regulations or legislation render the burning of coal cost prohibitive and the assets worthless, OTP's maximum exposure to loss as a result of its involvement with CCMC as of June 30, 2015 could be as high as $35.9 million.

New Accounting Standards

ASU 2014-09—In May 2014, the FASB issued ASU 2014-09, *Revenue from Contracts with Customers (Topic 606) (ASC 606)*. ASC 606 is a comprehensive, principles-based accounting standard which amends current revenue recognition guidance with the objective of improving revenue recognition requirements by providing a single comprehensive model to determine the measurement of revenue and the timing of revenue recognition. ASC 606 also requires expanded disclosures to enable users of financial statements to understand the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers.

ASU 2014-09 amendments to the ASC are effective for fiscal years beginning after December 15, 2016, however, in July 2015, the FASB voted to approve a one year deferral of the effective date. The deferral permits early adoption, but would not allow adoption any earlier than the original effective date of the standard. Application methods permitted are: (1) full retrospective, (2) retrospective using one or more practical expedients and (3) retrospective with the cumulative effect of initial application recognized at the date of initial application. The Company is currently reviewing ASU 2014-09, identifying key impacts to its businesses, reviewing revenue streams and contracts to determine areas where the amendments in ASU 2014-09 will be applicable and evaluating transition options. The Company does not plan to adopt the updated standards prior to January 1, 2018.

ASU 2015-03—In April 2015, the FASB issued ASU 2015-03, *Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs* (ASU 2015-03), which requires debt issuance costs related to a recognized debt liability to be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. ASU 2015-03 will become effective for interim and annual reporting periods beginning after December 15, 2015 with early adoption permitted. The Company will apply the updated standards in ASU 2015-03 to its consolidated financial statements beginning in the first quarter of 2016. If applied as of June 30, 2015, both the Company's consolidated long-term assets and long-term debt would be reduced by approximately $2.4 million—the balance of its consolidated unamortized debt issuance costs related to its outstanding long-term debt as of June 30, 2015.

ASU 2015-05—In April 2015, the FASB issued ASU 2015-05, *Intangibles—Goodwill and Other—Internal Use Software (Subtopic 350-40): Customers Accounting for Fees Paid in a Cloud Computing Arrangement*, to provide guidance to customers about whether a cloud computing arrangement includes a software license. The new accounting guidance is effective for interim and annual periods beginning after December 15, 2015 with early adoption permitted. The Company does not expect the adoption of the updated standard to have a material impact on its consolidated financial statements.

ASU 2015-07—In May 2015, the FASB issued ASU No. 201