WESTERN FUELS ASSOCIATION, INC.

p.6 'We lost $583,000 in 1997, even though coal deliveries were substantially over 20 million tons. 1997's "red ink" was not due to adverse operational performance either in coal deliveries or by management. ...
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p.11 Total Revenue Less Described Costs = $7,838K, so the advocacy costs were at least $583K ~7%.

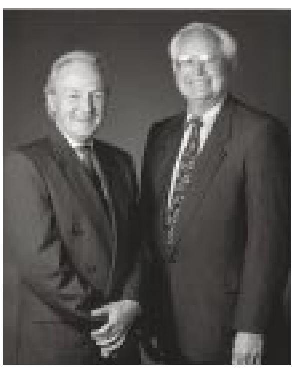
THE CO_2 ISSUE

ANNUAL REPORT 1998

PRESIDENT AND GENERAL MANAGER'S LETTER

The past year saw major progress by Western Fuels Association in all major areas of activity. In previous reports, we've identified our difficulties arising from market conditions confronting certain of our member/owners and specific projects we pursue through affiliated companies. Last year, we reported on the sale of our interest in Western Fuels-Utah and the Deserado Mine. This year, Cajun Electric Power Cooperative's continuing bankruptcy difficulties and market conditions facing Brushy Creek Mine began to improve. We can once again report good news for the Association.

Agreement has been reached with the Cajun Trustee concerning a buy-out of our interest in the Cajun coal supply agreements upon completion of the bankruptcy and the transfer of ownership of Big Cajun No. 2 to partners in the Louisiana Generating Company: Northern States Power (through a subsidiary), Southern Company Services and Zeigler Coal Holding Company.



Fredrick D. Palmer Robert L. McPhail

While negotiating the agreement with the Trustee, Cajun has continued performance under the existing coal supply relationships. Trustee rejection during the remaining pendency of the Cajun bankruptcy plan is an extremely remote possibility given the successful conclusion of a contract re-opener between Western Fuels and Triton Coal Company, a Zeigler subsidiary. The coal price now in effect for Cajun is substantially below spot market for coal of comparable quality. Western Fuels continues to provide a unit train to Cajun under a short-term lease at a price substantially below market. Association management has always maintained that the existing Cajun coal supply agreements are in the best interest of the Cajun bankruptcy estate. Developments over the past year have borne this out.

The Cajun bankruptcy may be concluded some time early in 1999. But, given the complexity of the proceeding, this is far from certain. Proponents of alternative plans include Enron and Southwestern Electric Power Company (SWEPCO).

Enron has told the bankruptcy court that it desires to affirm the Western Fuels' coal supply agreements and will perform in accordance with the terms. If Enron's plan succeeds, Western Fuels will be pleased to provide coal and coal supply services for Enron just as we have for Cajun.

SWEPCO maintains its stance, rejecting the Association and others in the fuel supply chain. We believe SWEPCO's posture is a fatal flaw in its effort to have its plan adopted.

Brushy Creek Mine continues operations at a million-ton-per-year production level. Adverse roof conditions have prevented us from achieving budgeted margins so far this year, but the mine is operating "in the black" and our major customers are taking coal in accordance with their contracts. We reached a successful agreement with the United Mine Workers of America. Our new agreement improves upon previous ones and is a major reason why Brushy Creek maintains operations at a profitable level, despite thin margins.

As to Brushy Creek's future, it is as uncertain as it has been for some time. While Illinois Basin market conditions appear to be stable, we know from past experience that this can change rapidly. Phase Two implementation of the Clean Air Act Amendments is fast approaching and Brushy Creek's medium sulfur content disadvantages its product. On the other hand, the need for Illinois Basin coal in Midwestern power plants continues, and Brushy Creek has thus far demonstrated an ability to market coal and operate successfully in a less-than-robust market.

Our relationships with both of the major railroads with whom we do business have deteriorated during the past year. We are involved in litigation with both Burlington Northern Santa Fe (BNSF) and the Union Pacific System (UP).

The BNSF litigation concerns application of productivity indices to terms and conditions of contracts for movement of coal to the Laramie River Station and to Sherco III power plant.

Basin Electric Power Cooperative operates Laramie River Station in behalf of its owners, including Tri-State Generation & Transmission Association and several public power systems which are Western Fuels Class C members. Northern States Power operates Sherco III for itself and Southern Minnesota Municipal Power Agency (SMMPA). SMMPA has a right to supply its share of coal for the power plant, and we are SMMPA's supplier.

Western Fuels has taken the position that the newly adopted Rail Cost Adjustment Factor–5 is the appropriate productivity index to be used in adjusting these contracts rather than the previously used RCAF–A. BNSF claims that the Surface Transportation Board Reauthorization Act abrogates application of rail transportation contract productivity adjusters, has billed us retroactively for past coal shipments, and has substantially increased current rates. We do not accept the validity of the retroactive billing, nor are we paying rates at currently billed levels. Instead, Western Fuels pays rates at a level consistent with the previous RCAF-A formula.

To protect ourselves and our members, Western Fuels filed litigation in Federal District Court in Wyoming seeking judicial restraint of BNSF's monopolistic practices with respect to captive customers

DELIVERIES
as of December 31, 1997

Basin Electric Power Cooperative
Tri-State Generation & Transmission Association
Laramie River Station
5,994,396 tons
Leland Olds Station
143,514 tons

Cajun Electric Power Cooperative
Big Cajun No. 2
5,750,377 tons

Tri-State Generation & Transmission Association
Craig Station
1,586,992 tons
Nucla Station
386,331 tons

Board of Public Utilities of Kansas City, Kansas
Nearman Creek Station
954,358 tons
Kaw & Quindaro Stations
471,655 tons

Southern Minnesota Municipal Power Agency
Sherco III
1,318,690 tons

Sunflower Electric Power Corporation
Holcomb Station
1,111,843 tons

Plains Electric Generation & Transmission Cooperative
Plains Escalante Generating Station
1,071,004 tons

Sikeston, Missouri, Board of Municipal Utilities
Sikeston Power Station
944,957 tons

Marion Coal Sales
Brushy Creek Mine
717,866 tons

TOTAL DELIVERIES
20,451,983 tons

like us. Discovery is complete and cross-motions for summary judgment have been filed, although no ruling has been made.

With respect to the Union Pacific System, our lawsuit stems from UP's inability to perform under what it claims is a "rail transportation contract" for movement of Powder River Basin (PRB) coal to the City of Sikeston, Missouri's Sikeston Station. PRB movements to Sikeston commenced at about the time of the UP operations meltdown in late-August, early-September. Because UP could not deliver coal to Sikeston in sufficient quantity to allow operation of the power plant, we contracted with BNSF for Sikeston coal deliveries. In retaliation, UP declared it would no longer honor terms and conditions of another contract with us for coal transportation to the Nearman Station, owned and operated by the Board of Public Utilities of Kansas City, Kansas. In doing so, UP disallowed a volume-related contract discount of nearly $1 million per year.

To protect ourselves and restrain monopolistic practices by a carrier we believe is abusing its relationship with us, Western Fuels initiated litigation in Federal District Court in the Eastern District of Missouri. We seek judicial protection from UP. Discovery is ongoing; no motions have been filed. It is difficult to guess when the matter might be resolved.

BNSF's and UP's actions with respect to the management of their relationships with us underscore the need for railroad regulatory reform at the federal level. Currently, a handful of Class I railroads are not restrained by the forces of competition and are without effective scrutiny by federal regulators. The regulators seem in a state of denial concerning the problems confronting major portions of the shipper community in the US, including the vital coal-chain industries. This encourages railroad highhandedness with respect to rates, terms and conditions of service — and also sets the stage for the kind of operational meltdown UP suffered, which continues to affect substantial portions of US commerce.

For these reasons, Western Fuels and other bulk shippers of diverse products have banded together as the Alliance for Rail Competition (ARC) which, together with our fellow members in Consumers United for Rail Equity (CURE), is pushing for regulatory reform in Congress. The outline of reform is clear: more competition in the rail industry, closer attention by federal regulators to problems confronting captive shippers and better use of power already available under current law.

We initiated and concluded a contract re-opener for Sunflower Electric Power Corporation's

Holcomb Station. The coal supplier is Kennecott Energy Company. We were able to complete the re-opener very quickly because of Kennecott's active cooperation.

Unfortunately, in another instance involving the Colowyo Mine, litigation has ensued between Western Fuels-Colorado and Colowyo, which is an affiliate of Kennecott. Kennecott has refused to discuss changes in the coal supply relationship for the Craig Station, which has a large (and growing) coal stockpile. To alleviate the stockpile situation, Western Fuels-Colorado initiated discussions with Kennecott to secure a contract buy-down price in the interest of both Kennecott and Tri-State Generation & Transmission Association. Western Fuels-Colorado purchases Colowyo coal for Tri-State.

Kennecott has refused to negotiate a buy-down. In addition, it is our view – as we have alleged in state court in Colorado – that W.R. Grace violated certain terms and conditions of the consent agreement and other project documents pertaining to the transfer of W.R. Grace's ownership interest in Colowyo to Kennecott. It is unfortunate that Kennecott is caught up in this dispute, but it is Colowyo's current owner and seemingly must suffer the consequences of W.R. Grace's and Colowyo's breach of their obligation to Western Fuels-Colorado and Tri-State.

Discovery is ongoing, and Kennecott recently filed dispositive motions for a judgment on the pleadings. We will vigorously oppose that motion and are preparing for the trial, scheduled to commence in June 1999.

Plains Electric Generation & Transmission Cooperative is in discussions with the federal government concerning reorganization of its financial affairs and is exploring various options, including sale of a portion of its assets such as Plains Escalante Generating Station (PEGS). Western Fuels supplies PEGS coal from Peabody COALSALES Company's Lee Ranch Mine. Plains also is discussing with Tri-State a potential merger even while exploring other relationships that might help it through the difficulties associated with PEGS' large debt.

Western Fuels delivers coal to PEGS using our Escalante-Western Railway, a railroad operation connecting the mine and power plant. While there have been comments with respect to the need to look at the current fuel supply relationship, no discrete suggestions have been made concerning specific changes, if changes even should be made, or what the relationship might be in the future. Because of our ownership of the railroad, the fact that the investment in the railroad will be paid off relatively soon, Lee Ranch Mine's proximity to the power plant, and because other sources of coal supply are a vast distance from the power plant, we believe the best long-term coal supply solution at PEGS continues to be Lee Ranch Mine.

But having said that, we have experienced both the Deseret Generation & Transmission Co-operative restructuring discussions and the Cajun bankruptcy and know we cannot be certain serious questions will not be posed with respect to our relationship at PEGS. As in those two situations, economics ultimately will determine how the matter goes forward. Because of our comfort with the fit between PEGS and Lee Ranch (as connected by the Escalante-Western), Western Fuels management is of the view that no matter how the Plains situation plays out, our economic interest in the relationship and our ability to supply low-cost coal to PEGS will not be impaired.

We lost $583,000 in 1997, even though coal deliveries were substantially over 20 million tons. 1997's "red ink" was not due to adverse operational performance either in coal deliveries or by management. In fact, the economics of our new shared-services agreement with Tri-State provide substantial benefit both to Western Fuels and for Tri-State. On an ongoing basis, Western Fuels is operating substantially "in the black." Our half-million dollar shortfall is due entirely to our advocacy in the area of climate change. The Board of Directors continues to provide financial support to programs designed to turn back efforts by the Clinton Administration to dial-out coal-fired generation in the US energy supply mix.

The Administration's efforts reached a new high late in 1997, with negotiations pursuant to the Rio Treaty at Kyoto, Japan. The resulting Kyoto Protocol would commit the US to a reduction in carbon dioxide emission levels to 7% below those in 1990. This would return our nation to roughly the equivalent of economic activity in 1981. Since 1981, there are 25 million new Americans. Another 20 million are anticipated within the next 12 years – 2010 being the mid-point of the time-table the Administration proposes to use in restraining our economic activity. Simple arithmetic demonstrates to anyone who cares to make the calculation that to accomplish this, coal production and consumption must be cut by more than half. All Americans will have to reduce by at least 30% their utilization of fossil fuels in the cars they drive, the products they consume and the electricity our society relies upon.

For anyone to identify with this kind of policy suggests they believe fossil fuels pose a unique

GREENING
EARTH
SOCIETY

Greening Earth Society provides sound information about CO_2 and fossil fuels to educators, students, business and media representatives, community leaders and policy makers.

threat to the human community. We believe the contrary. Fossil fuels are a gift of the Creator. For the world community to reach our economic potential, fossil fuels will have to be utilized in much greater quantities throughout the world, not just here. The Clinton Administration's vision of catastrophic global warming is driving US policy with respect to climate change. This was true in Kyoto and presumably will be so during negotiations in Buenos Aires, Argentina, later this year. This policy simply must be resisted.

It is not that the science associated with the vision of apocalypse is uncertain. It simply is wrong.

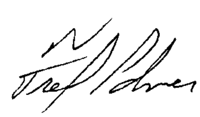
Western Fuels' ongoing activity, including our creation of Greening Earth Society (described elsewhere in this report), is designed to convince Americans that warm is good, cold is bad; using more fossil fuels benefits everyone; and by using fossil fuels, conditions are being created on earth for humans to grow, both in numbers and living standards.

Western Fuels Association's members are in a unique position to protect the interests of all electric consumers. In doing so, we protect the interest of all Americans in a robust economy and a free society. The leadership on our Board of Directors and of those companies associated with us (whether as Class C members or through Greening Earth Society), are to be congratulated for their courage and foresight in undertaking this effort.

Western Fuels does not stand alone, but we occupy a unique and important position with respect to a principled defense against the environmental onslaught that continues to come at American society under the rubric of apocalyptic global warming.

Individual requests for "The Greening of Planet Earth" *sky-rocketed last year. Worldwide circulation approaches 30,000. A sequel is in production.*

ROBERT L. MCPHAIL *President*



FREDRICK D. PALMER, *General Manager & Chief Executive Officer*


CHRIS HAUCK


LARRY ADAIR


BOB GILLESPIE


PERRY RUBART


BOB MCPHAIL


PETE HEROUX


JIM BROWNLEE


BILL KELLER


JIM SOEHNER


HUB THOMPSON


JAY COX


DAN MACLEOD


ED THROOP

BOARD OF DIRECTORS

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Chief Executive Officer & General Manager
Basin Electric Power Cooperative
Bismarck, ND

L. Christian Hauck
Vice President
President & Chief Executive Officer
Sunflower Electric Power Corporation
Hays, KS

Pierre J. Heroux
Secretary-Treasurer
Executive Director & Chief Executive Officer
Southern Minnesota Municipal Power Agency
Rochester, MN

Harold J. Thompson
Vice Secretary-Treasurer
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Board of Public Utilities of Kansas City, KS

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Cajun Electric Power Cooperative, Inc.

Jay W. Cox
Trustee
Plains Electric Generation & Transmission Cooperative, Inc.
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Robert Gillespie
Trustee
Plains Electric Generation & Transmission Cooperative, Inc.
Albuquerque, NM

J. William Keller
Director
Basin Electric Power Cooperative
Bismarck, ND

Daniel E. MacLeod
Executive Vice President & General Manager
Cajun Electric Power Cooperative, Inc.
Baton Rouge, LA

Perry E. Rubart
Director
Sunflower Electric Power Corporation
Hays, KS

C. Jim Soehner
Director
Tri-State Generation & Transmission Association, Inc.
Westminster, CO

Ed Throop
Manager of Finance
Board of Municipal Utilities
Sikeston, MO

MEMBER DIRECTORY

CLASS A MEMBERS

Basin Electric Power Cooperative
Bismarck, ND

Cajun Electric Power Cooperative, Inc.
Baton Rouge, LA

Plains Electric Generation & Transmission Cooperative, Inc.
Albuquerque, NM

Sunflower Electric Power Corporation
Hays, KS

Tri-State Generation & Transmission Association, Inc.
Westminster, CO

CLASS B MEMBERS

Board of Public Utilities of Kansas City, KS

Board of Municipal Utilities
Sikeston, MO

Southern Minnesota Municipal Power Agency
Rochester, MN

CLASS C MEMBERS

Arizona Electric Power Cooperative, Inc.
Benson, AZ

Arkansas Electric Cooperative Corporation
Little Rock, AR

Associated Electric Cooperative, Inc.
Springfield, MO

Black Diamond Energy, Inc.
(a wholly owned subsidiary of Oglethorpe Power Corporation)
Tucker, GA

Cooperative Power Association
Eden Prairie, MN

Department of Utilities
Fremont, NE

Heartland Consumers Power District
Madison, SD

Jacksonville Electric Authority
Jacksonville, FL

Lincoln Electric System
Lincoln, NE

Missouri River Energy Services
(formerly Missouri Basin Municipal Power Agency)
Sioux Falls, SD

Nebraska Public Power Agency
Columbus, NE

Platte River Power Authority
Fort Collins, CO

City of Santa Clara, CA

City Utilities
Springfield, MO

Turlock Irrigation District
Turlock, CA

CONSOLIDATED BALANCE SHEET

Combined 1997 financial statements of Western Fuels Association, Inc., Western Fuels-Illinois, Inc., and Western Fuels-Wyoming, Inc.

(in thousands)

	1997	1996
ASSETS		
Cash & Short-Term Investments	$17,326	$10,955
Restricted Cash	0	2,172
Accounts Receivable		
Member	17,057	16,737
Non-Member	9,378	6,490
Total Accounts Receivable	26,435	23,227
Inventory	492	487
Costs Recoverable Under Coal Purchase Agreements	13,648	11,757
Prepayment for Deferred Coal Shipments	7,028	7,028
Prepaid Expenses	2,407	1,333
Coal Resource Acquisition Costs	0	340
Plant & Property	121,866	113,646
Less: Accumulated Depreciation	81,532	78,858
	40,334	34,788
Furniture & Equipment At Cost	451	421
Less: Accumulated Depreciation & Amortization	200	187
	251	234
Investments	32,746	33,360
TOTAL ASSETS	**$140,667**	**$125,681**
LIABILITIES		
Accounts Payable	$29,383	$24,304
Accrued Interest Payable	3,293	3,653
Post Retirement Benefits Obligation	11,086	10,371
Advance Payments for Transportation & Coal Purchases	14,678	11,517
Notes Payable	25,251	25,784
Long-Term Debt	8,410	9,032
Capital Lease Obligations	43,167	34,915
Deferred Income	25	18
	135,293	119,594
MEMBERS' EQUITY		
Initial Member Fees	45	45
Patronage Capital Certificates	2,457	1,721
Per Unit Retain Certificates	2,564	2,564
Accumulated Margin	308	1,757
	5,374	6,087
TOTAL LIABILITIES & MEMBERS' EQUITY	**$140,667**	**$125,681**

CONSOLIDATED STATEMENT OF OPERATIONS

Combined 1997 financial statements of Western Fuels Association, Inc., Western Fuels-Illinois, Inc., and Western Fuels-Wyoming, Inc.

(in thousands)

	1997	1996
Coal Sales to Members	$218,714	$219,033
Less: Cost of Coal Sold		
Acquisition	131,448	133,604
Transportation & Delivery	80,223	78,403
	211,671	212,007
	7,043	7,026
Contract Buy-Out	0	2,300
Interest Income	786	941
Annual Membership Fees	9	9
Total Revenue Less Described Costs	**$7,838**	**$10,276**
General & Administrative Expenses	3,820	3,105
Interest Expense	4,024	4,678
Net Operating Margin	(6)	2,493
Non-Operating Margin:		
Other	(426)	(272)
Income Taxes	(151)	(363)
Net Margin	**($583)**	**$1,858**

p.6 'We lost $583,000 in 1997, even though coal deliveries were substantially over 20 million tons. 1997's "red ink" was not due to adverse operational performance either in coal deliveries or by management. ...
Our half-million dollar shortfall is due entirely to our advocacy in the area of climate change.'
That seems to mean they spent at least $583K on advocacy, compared to the $7,838K (Revenue vs Described Costs).

OFFICE LISTING

WASHINGTON, D.C.
4301 Wilson Boulevard, Suite #805
Arlington, VA 22203-4193
Phone (703) 907-6160
Fax (703) 907-6161
E-mail wfa@cais.com

Fredrick D. Palmer
General Manager & Chief Executive Officer

Ned Leonard
Manager of Communications & Governmental Affairs

WESTMINSTER, COLORADO
PO Box 33424
Denver, CO 80233-3424
Phone (303) 450-9976
Fax (303) 450-1042
E-mail wfalakewood@pcisys.net

Robert P. Norrgard
Manager of Finance & Administration

Kirk Nobis
Director of Operations

George O'Hara
Director of Technical Services

Murari Shrestha, P.E.
Director of Permitting & Contracting Affairs

Laraine Packard
Business Management Coordinator

WYOMING OPERATIONS
PO Box 1447
Gillette, WY 82717
Phone (307) 682-0851
Fax (307) 682-6468

Rod Wolf
Wyoming Operations Superintendent

BRUSHY CREEK MINE
4270 North America Road
Galatia, IL 62935
Phone (618) 252-8633
Fax (618) 252-3823

Paul Smock
General Superintendent

DRY FORK MINE
PO Box 1809
Gillette, WY 82717
Phone (307) 682-0213
Fax (307) 682-6468

Darold Koch
Mine Manager

NEW HORIZON MINE
PO Box 628
Nucla, CO 81424
Phone (970) 864-2165
Fax (970) 864-2168

R. Lance Wade
Mine Manager

ESCALANTE-WESTERN RAILWAY
PO Box 552
Prewitt, NM 87045
Phone (505) 876-2279
Fax (505) 876-2279

Karl Benz
New Mexico Operations Supervisor

CORPORATE COUNSEL
Rex E. Johnson, Esq.
Sherard Sherard & Johnson
PO Box 69
Wheatland, WY 82201
Phone (307) 322-2107

Western Fuels Association, Inc., is a cooperative enterprise operating on a not-for-profit basis to provide coal for the generation of electricity by consumer-owned utilities throughout the Great Plains, Rocky Mountain, and Southwest states, and in Louisiana. Western Fuels' 23 member/owners are rural electric generation & transmission cooperatives, municipal utilities, and other public power bodies.

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