



## **Keweenaw Land Association, Limited (A Michigan Corporation)**

**Quarterly Report for the period ended September 30th, 2019**

**1801 East Cloverland Drive, PO Box 188**

**Ironwood, MI 49938**

**(Address of principal executive offices)**

**Issuer's telephone number: (906) 932-3410**

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## GLOSSARY

The following abbreviations, acronyms, or terms may be used in this document and shall have the adjacent meanings set forth below:

Board Foot (BF)	A measurement of lumber 12 inches x 12 inches x 1 inch. When used in conjunction with sawtimber or logs, it is a measurement system to approximate the output of lumber that can be expected from a given quantity of sawtimber or logs when the measurement system was developed in the 1800's. Sawmill technology has changed since the scale was originally created and the actual output of lumber from Board Feet of Logs varies from mill to mill, depending on their technology, but it is the standard unit of measurement for buying and selling logs.
Cord	A measurement of logs containing 128 cubic feet.
Cord Equivalent (cd-eq)	A measurement of logs in cords including logs converted in measurement from other measurement methods. Example – one thousand board feet (MBF) equals approximately 2.2 cords.
MBF	A thousand board feet.
Production Mix	The ratio of a category of production to total production.
Pulpwood	Logs cut primarily to be converted to wood pulp for the manufacture of paper, fiberboard, or other wood fiber products.
REIT	Real Estate Investment Trust
Sawbolts	A lower grade or smaller size sawtimber typically sawn for the manufacture of pallets or other coarse wood products.
Sawlogs	A higher grade or larger size sawtimber sawn for the manufacture of furniture grade lumber, flooring lumber, or other high-quality wood products.
Sawtimber	A category of logs suitable for veneer, sawlogs, or sawbolts.
TRS	Taxable REIT Subsidiary
Veneer	A category of sawtimber clear of defects suitable for manufacture as veneer paneling, furniture, and cabinetry veneer.

## CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

Certain statements contained in this Quarterly Report of Keweenaw Land Association, Limited and subsidiaries (“Keweenaw Land Association”, “Keweenaw”, “KLA”, “the Company”, “we”, “our”, or “us”) may be considered forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). In addition, Keweenaw Land Association, or the executive officers on Keweenaw Land Association’s behalf, may from time to time make forward-looking statements in reports and other documents or in connection with written or oral statements made to the press, potential investors, or others. Keweenaw intends for all such forward-looking statements to be covered by the applicable safe harbor provisions for forward-looking statements contained in the Securities Act and the Exchange Act.

Forward-looking statements can generally be identified by our use of forward-looking terminology such as “may”, “will”, “expect”, “intend”, “anticipate”, “estimate”, “believe”, “continue”, or other similar words. However, the absence of these or similar words or expressions does not mean that a statement is not forward-looking. Forward-looking statements are not a guarantee of performance and are based on certain assumptions, discuss future expectations, describe plans and strategies, contain projections of results of operations or of financial condition or state other forward-looking information. Forward-looking statements in this report relate to anticipated delivery of income, value and long-term returns through sustainable harvests, well-timed sales, and selective acquisitions; expected uses of cash generated from operations; expected sources and adequacy of capital resources and liquidity; change in depletion rates; change in merchantable timber book value and standing timber inventory volume; and other factors that may lead to fluctuations in future net income (loss).

Any such forward-looking statements are based on a number of assumptions involving judgments and are subject to risks, uncertainties, and other factors that could cause actual results to differ materially from our historical experience and our present expectations. These reports represent interim financial results and additional risk factors that are contained in our annual report under Section 1A *Risk Factors*, which can be found on the [keweenaw.com](http://keweenaw.com) website. With respect to our ongoing business, these risks and uncertainties include, but are not limited to, the risks discussed in Section 1A of the annual report. Accordingly, readers are cautioned not to place undue reliance on our forward-looking statements, which speak only as of the date of this report. Keweenaw makes no representations or warranties (express or implied) about the accuracy of any such forward-looking statements contained in this report, and Keweenaw does not intend to publicly update or revise any forward-looking statements, whether as a result of new information, future events, or otherwise, except as required by law.

### **Section 1. FINANCIAL INFORMATION**

The information furnished in the accompanying unaudited consolidated balance sheets and related consolidated income statements, stockholders’ equity, and cash flows reflects all adjustments, consisting solely of normal and recurring adjustments that are, in managements opinion, necessary for a fair and consistent presentation of the aforementioned financial statements. These results of operations for the three and nine months ended September 30, 2019, are not necessarily indicative of the operating results expected for the full year.

**KEWEENAW LAND ASSOCIATION, LIMITED AND SUBSIDIARIES**  
**Consolidated Income and Comprehensive Income Statements**  
(Unaudited)

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
<b>Revenues</b>				
Timber Sales	\$ 5,112,135	\$ 4,587,232	\$ 11,454,623	\$ 10,645,574
Land Sales	4,370,600	1,484,000	5,059,600	1,510,000
Lease Income, Mineral Royalties and Service Fees	38,618	98,573	193,846	322,873
<b>Total Sales</b>	<b>9,521,353</b>	<b>6,169,805</b>	<b>16,708,069</b>	<b>12,478,447</b>
<b>Cost of Sales</b>				
Timber Cost of Sales	3,509,750	3,300,326	8,291,163	7,783,172
Land Cost of Sales	4,277,739	429,511	4,330,555	443,629
Timber Operations Forestry Expense	204,065	202,414	551,938	545,502
Land Management Costs	120,811	104,767	329,299	333,678
<b>Total Cost of Sales</b>	<b>8,112,365</b>	<b>4,037,018</b>	<b>13,502,955</b>	<b>9,105,981</b>
<b>Gross Profit</b>	<b>1,408,988</b>	<b>2,132,787</b>	<b>3,205,114</b>	<b>3,372,466</b>
<b>Selling, Management &amp; Administration Expenses</b>	595,688	448,089	1,738,774	1,468,493
<b>Nonrecurring Expenses</b>	37,350	284,012	192,869	2,014,917
<b>Operating Income</b>	775,950	1,400,686	1,273,472	(110,944)
<b>Other Income</b>	-	13,096	1,503,226	59,154
<b>Other Expense</b>				
Interest Expense	137,889	178,592	495,688	495,552
<b>Earnings (Loss) Before Income Taxes</b>	<b>638,060</b>	<b>1,235,190</b>	<b>2,281,009</b>	<b>(547,342)</b>
<b>Provisions (Benefit) for State and Federal Income Taxes</b>	173,857	17,059	574,804	(187)
<b>Net Income (Loss)</b>	<b>464,204</b>	<b>1,218,131</b>	<b>1,706,206</b>	<b>(547,155)</b>
<b>Other Comprehensive Income (Loss), Net of Tax</b>				
<b>Unrealized Gains (Losses) on Securities</b>				
Unrealized Holding Gains Arising During the Period	-	207,314	206,110	43,087
Less: Reclassification Adj. For Gains Included in Net Income	-	-	(1,180,365)	-
<b>Other Comprehensive Income (Loss)</b>	<b>-</b>	<b>207,314</b>	<b>(974,255)</b>	<b>43,087</b>
<b>Comprehensive Income (Loss)</b>	<b>\$ 464,204</b>	<b>\$ 1,425,445</b>	<b>\$ 731,951</b>	<b>\$ (504,069)</b>
<b>Net Income (Loss) Per Share:</b>				
Basic	\$ 0.36	\$ 0.94	\$ 1.31	\$ (0.42)
Diluted	\$ 0.36	\$ 0.94	\$ 1.31	\$ (0.42)
<b>Weighted Average Shares Outstanding:</b>				
Basic	1,306,746	1,301,550	1,306,746	1,301,550
Diluted	1,307,096	1,301,550	1,307,096	1,301,550

*See accompanying notes.*

**KEWEENAW LAND ASSOCIATION, LIMITED AND SUBSIDIARIES**  
**Consolidated Balance Sheets**  
(Unaudited)

	<u>September 30,</u> <u>2019</u>	<u>December 31,</u> <u>2018</u>
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and Cash Equivalents	\$ 5,653,613	\$ 2,739,990
Accounts Receivable, Net of Allowances for Doubtful Accounts	1,189,536	750,752
\$18,513 and \$13,422 at September 30th, 2019 and December 31st, 2018		
Investments in Marketable Securities	-	2,338,726
Prepaid Assets	386,078	283,644
Log Inventory	60,930	167,426
Federal Income Tax Receivable	247,363	49,705
Other Current Assets	36,999	36,066
<b>Total Current Assets</b>	<b><u>7,574,519</u></b>	<b><u>6,366,309</u></b>
<b>Non-Current Assets</b>		
Timber and Timberlands, Net of Depletion	27,061,423	31,700,536
Prepaid Developed Lot Costs	379,808	379,808
Property, Plant and Equipment, Net of Depreciation	1,223,610	1,307,713
<b>Total Non-Current Assets</b>	<b><u>28,664,841</u></b>	<b><u>33,388,057</u></b>
<b>TOTAL ASSETS</b>	<b><u>\$ 36,239,360</u></b>	<b><u>\$ 39,754,366</u></b>
<b>LIABILITIES &amp; STOCKHOLDERS' EQUITY</b>		
<b>Current Liabilities</b>		
Accounts & Deposits Payable	\$ 409,989	\$ 67,096
Current State and Federal Deferred Income Tax Liability	-	167,784
Other Accrued Liabilities	535,949	714,274
<b>Total Current Liabilities</b>	<b><u>945,938</u></b>	<b><u>949,154</u></b>
<b>Non-Current Liabilities</b>		
Long Term Debt	14,030,929	18,513,236
Non-Current State and Federal Deferred Income Tax Liability	51,697	197,521
<b>Total Non-Current Liabilities</b>	<b><u>14,082,626</u></b>	<b><u>18,710,757</u></b>
<b>Total Liabilities</b>	<b><u>15,028,564</u></b>	<b><u>19,659,911</u></b>
<b>Stockholders' Equity</b>		
Common Stock Issued	85,451	85,111
Accumulated Other Comprehensive Income	-	974,255
Retained Earnings	21,125,345	19,035,089
<b>Total Stockholders' Equity</b>	<b><u>21,210,796</u></b>	<b><u>20,094,455</u></b>
<b>TOTAL LIABILITIES &amp; STOCKHOLDERS' EQUITY</b>	<b><u>\$ 36,239,360</u></b>	<b><u>\$ 39,754,366</u></b>

*See accompanying notes.*

**KEWEENAW LAND ASSOCIATION, LIMITED AND SUBSIDIARIES**  
**Consolidated Statements of Stockholders' Equity**  
(Unaudited)

	<b>Common Stock Issued</b>	<b>Accumulated Other Comprehensive Income</b>	<b>Retained Earnings</b>	<b>Total Shareholders' Equity</b>
<b>December 31, 2018 Balance</b>	\$ 85,111	\$ 974,255	\$ 19,035,089	\$ 20,094,455
<b>Changes during 2019:</b>				
Comprehensive Income:				
Net Income (Loss)	-	-	1,706,206	1,706,206
Other Comprehensive Income:				
Unrealized Gains on Securities, Net of Tax Expense of \$263,049	-	(974,255)	-	(974,255)
Impact of Shares Issued to Directors & Officers	340	-	384,050	384,390
<b>September 30, 2019 Balance (Unaudited)</b>	<b>\$ 85,451</b>	<b>\$ -</b>	<b>\$ 21,125,346</b>	<b>\$ 21,210,796</b>

*See accompanying notes.*

**KEWEENAW LAND ASSOCIATION, LIMITED AND SUBSIDIARIES**  
**Consolidated Statements of Cash Flows**  
(Unaudited)

	Three Months Ended September 30		Nine Months Ended September 30	
	2019	2018	2019	2018
<b>Cash Flows From Operating Activities</b>				
Net Income (Loss)	\$ 464,204	\$ 1,218,130	\$ 1,706,206	\$ (547,156)
<b>Adjustments to Reconcile Net Income (Loss) to Net Cash From (For) Operating Activities:</b>				
Depletion, Depreciation and Amortization	201,979	182,959	473,322	479,625
Amortization of Loan Costs	5,898	5,947	17,693	18,039
Changes in Operating Assets and Liabilities				
Decrease (Increase) in Accounts Receivable	(436,044)	(261,103)	(438,784)	(153,211)
Decrease (Increase) in Prepaid Assets	21,642	6,051	(102,433)	(69,189)
Decrease (Increase) in Log Inventory	8,831	59,529	106,495	(2,268)
Decrease (Increase) in Federal Income Tax Receivable	(211,730)	-	(197,658)	(10,091)
Decrease (Increase) in Other Current Assets	(2,394)	(868)	(3,327)	(2,433)
Increase (Decrease) in Deposits and Accounts Payable	155,819	16,420	342,893	126,083
Increase (Decrease) in Deferred State and Federal Income Tax	(74,878)	17,463	(54,629)	(47,788)
Increase (Decrease) in Other Accrued Liabilities	59,190	(912,819)	(178,325)	72,314
(Gain) Loss on Sale of Securities	-	-	(1,494,133)	-
(Gain) Loss on Sale of Land	(92,861)	(1,054,489)	(729,045)	(1,066,371)
<b>Net Cash Flow From (For) Operating Activities</b>	<b>99,656</b>	<b>(722,780)</b>	<b>(551,725)</b>	<b>(1,202,446)</b>
<b>Cash Flow From (For) Investing Activities:</b>				
Sales (Purchases) of Property and Equipment	22,315	(5,700)	(8,141)	(145,102)
Proceeds from Sale of Securities	-	-	2,599,625	-
Primary Road Construction	(10,320)	(22,950)	(18,167)	(24,145)
Proceeds (Expenditures) from Land Sales/Development Net of Closing	4,349,806	1,251,067	5,007,641	1,274,798
<b>Net Cash Flow From (For) Investing Activities</b>	<b>4,361,801</b>	<b>1,222,417</b>	<b>7,580,958</b>	<b>1,105,551</b>
<b>Cash Flows From (For) Financing Activities</b>				
(Decrease) in Long Term Debt	-	-	(4,500,000)	-
Term Loan Borrowing	-	-	-	-
Issuance of Common Stock	284,673	-	384,390	120,000
<b>Net Cash Flow From (For) Financing Activities</b>	<b>284,673</b>	<b>-</b>	<b>(4,115,610)</b>	<b>120,000</b>
<b>Net Cash Flows</b>	<b>4,746,130</b>	<b>499,637</b>	<b>2,913,623</b>	<b>23,105</b>
<b>Beginning Cash and Cash Equivalents</b>	<b>907,483</b>	<b>2,430,166</b>	<b>2,739,990</b>	<b>2,906,698</b>
<b>Ending Cash and Cash Equivalents</b>	<b>\$ 5,653,613</b>	<b>\$ 2,929,803</b>	<b>\$ 5,653,613</b>	<b>\$ 2,929,803</b>

*See accompanying notes.*



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

### 1. Summary of Significant Accounting Policies

#### *Basis of Presentation and Principles of Consolidation*

The consolidated financial statements include the accounts of the Company and all of its wholly-owned subsidiaries. Significant inter-company accounts and transactions have been eliminated. The financial statements are prepared in accordance with Generally Accepted Accounting Principles (GAAP) of the United States of America.

#### *Use of Estimates*

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

#### **Recent Accounting Pronouncements:**

In February 2016, the FASB issued guidance that revised the accounting for leases. The guidance is intended to improve financial reporting of leasing transactions by requiring lessees to record right-of-use assets and corresponding lease liabilities on the balance sheet. The guidance is effective for our first quarter of fiscal year 2020 with early adoption permitted and is required to be applied using a modified retrospective approach to each prior reporting period. We are currently evaluating the impact of this guidance but have not yet determined the effect on our consolidated financial statements.

In May 2014, the FASB issued guidance on the recognition of revenue from contracts with customers. The core principle of the guidance is that a company should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration which the Company expects to receive in exchange for those goods or services. In July 2015, the FASB decided to defer the effective date for this new revenue standard by one year, which will make the guidance effective for our first quarter of fiscal year 2019 financial statements. Management has reviewed the guidance and believes that there is no material impact to the financial statements.

#### *Cash and Equivalents*

Highly liquid investments with maturity of three months or less when purchased are generally considered to be cash equivalents.

#### *Accounts Receivables and Bad Debts*

The Company extends unsecured credit to some of its customers and uses the allowance method for accounting for bad debts. Management evaluates all accounts receivables at the balance sheet date to determine the allowance.

### *Investment in Marketable Securities*

Management determines the appropriate classification of its investments in marketable securities at the time of purchase and re-evaluates such determination at each balance sheet date. Marketable securities are classified as available for sale and are carried at fair market value, with the unrealized gains and losses, net of state and federal income taxes, reported as accumulated other comprehensive income in a separate component of stockholders' equity. All marketable securities were sold during the first quarter 2019.

### *Log Inventory*

Log inventory is valued at the lower of cost or market using the average cost method.

### *Timber and Timberlands*

Timber and Timberlands consist of the recorded costs of holdings. Timber depletion charges are based on these recorded values and the properties' estimated reserves, utilizing the pooling method. In addition, permanent logging road construction costs incurred net of related depreciation have been capitalized and included in timber and timberlands.

### *Road Building Costs*

The Company has an accounting policy to identify, classify, and depreciate or capitalize road-building costs consistent with GAAP. Logging roads constructed under the policy are classified as either permanent or secondary logging roads. Permanent logging roads are those roads, culverts, bridges, and other improvements constructed to provide regional access to a series of timber stands and/or other logging roads, which are continuously maintained for an indefinite period. Secondary logging roads are those roads, culverts, bridges, and other improvements constructed for the sole purpose to provide access to particular, identifiable stands of timber for the purpose of harvest and transport of logs from those specific stands. The accounting treatment adopted is that costs expended on permanent roads are capitalized. Roadbed costs are treated as permanent costs of the land. Costs of road surfacing, culverts, bridges, and other improvements on permanent roads are capitalized and depreciated over 15 years. All expenditures for secondary roads are charged to prepaid expense and written off over the period of the scheduled, related timber stand harvest.

### *Prepaid Developed Lot Costs*

Prepaid developed lot costs include the costs of those properties assigned for development, as well as all accumulated expenditures for lot development.

### *Property, Plant, and Equipment*

Assets are individually identified on the depreciation schedule. Assets are carried at cost and the provision for depreciation is generally computed using the straight-line method over the estimated useful lives of the assets. Salvage value is assigned to vehicles and other significant assets and for those assets, depreciation is used over the useful life until the salvage value is reached. Management reviews the salvage value of each of these assets at the end of each year to determine if the salvage value is reasonable. If the estimated fair market value is less than the salvage value, the asset is written down to the estimated fair market value.

### *Deferred Income Taxes*

Deferred income taxes are determined utilizing a liability approach. This method gives consideration to the future tax consequences associated with the differences between the financial accounting and tax basis of assets and liabilities. The Company early adopted ASU 2018-02, Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income and elected to reclassify the income tax effects of the Tax Cuts and Jobs Act from accumulated other comprehensive income to retained earnings in 2017.

### *Common Stock*

All Keweenaw common shares previously purchased by the Company are considered authorized but unissued shares. The cost basis for Keweenaw's common shares was determined to be \$0.065392 per share. This is the amount credited to common stock when stock is issued. The excess of the issue price over cost is credited to retained earnings.

## **2. Investments in Marketable Securities**

There were no securities classified as available for sale as of September 30, 2019. All securities were sold in March 2019.

Realized gains and losses are determined using the specific identification method.

The following is a summary of investment securities classified as available for sale as of December 31, 2018:

	<u>Cost</u>	<u>Unrealized Holding Gains</u>	<u>Fair Value</u>
<b>Current Investments:</b>			
Equity Securities	\$ 1,105,492	\$ 1,233,234	\$ 2,338,726
<b>Investments Available for Sale</b>	<u>\$ 1,105,492</u>	<u>\$ 1,233,234</u>	<u>\$ 2,338,726</u>

### 3. Timber and Timberlands

The following is a summary of the timber and timberlands and permanent logging roads at cost, less accumulated depletion and road depreciation as of September 30, 2019:

	<b>September 30, 2019</b>	<b>December 31, 2018</b>
Land and Mineral Holdings	\$ 9,744,989	\$ 14,000,200
Timber	23,345,901	23,369,163
Permanent Logging Roads	1,047,539	1,029,372
Properties at Cost	<u>34,138,428</u>	<u>38,398,735</u>
Less: Accumulated Timber Depletion	(6,600,131)	(6,243,758)
Less: Accumulated Road Depreciation	(476,874)	(454,441)
<b>Net Carrying Value</b>	<b><u>\$ 27,061,423</u></b>	<b><u>\$ 31,700,536</u></b>

The timber depletion expense and depreciation expense for permanent logging roads is as follows:

	<b>3 Months Ended September 30</b>		<b>9 Months Ended September 30</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
Timber Depletion Expense	\$162,819	\$142,079	\$356,221	\$361,364
Depreciation Expense for Permanent Logging Roads	\$ 7,430	\$ 7,388	\$ 22,463	\$ 22,139

During Q3 2019 the Company did not complete any timberland acquisitions.

### 4. Prepaid Developed Lot Costs

The Company capitalizes the development costs for lots available for sale and these costs plus the cost of the lots is shown on the balance sheet. There were no lot sales in Q3 2019 and one lot sale in Q3 2018. At September 30, 2019, there were 23 lots remaining for sale.

## 5. Property, Plant, and Equipment

A summary of property, plant, and equipment, at cost, less accumulated depreciation is as follows:

	<b>September 30, 2019</b>	<b>December 31, 2018</b>
Buildings	\$ 415,862	\$ 412,413
Furniture, Equipment, and Accessories	1,102,949	1,107,189
Machinery and Vehicles	407,792	481,215
Land Improvements	827,781	827,781
Equipment at Cost	2,754,384	2,828,598
Less: Accumulated Depreciation	(1,530,774)	(1,520,885)
<b>Equipment, Net of Depreciation</b>	<b>\$ 1,223,610</b>	<b>\$ 1,307,713</b>

The Company recorded depreciation expense for property, plant and equipment as follows:

	<b>3 Months Ended September 30</b>		<b>9 Months Ended September 30</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
Depreciation Expense	\$ 31,729	\$ 33,492	\$ 94,638	\$ 96,121

## 6. Lines of Credit and Long-Term Debt

Keweenaw Land Association, Limited maintains banking relationships with Wells Fargo Bank, N.A., and Metropolitan Life (MetLife).

The Company has a combined unsecured line of credit with Wells Fargo Bank in the amount of \$1,000,000 to be used as an operating line of credit, and also for the purpose of standby letter of credit availability at a variable interest rate equal to the Wells Fargo Bank prime rate plus 0.25% for a one-year commitment and interest to be paid monthly. Significant covenants of Wells Fargo Bank require Keweenaw to ensure working capital as of the end of the year of not less than \$1,000,000 and maintain a debt service ratio of 1.25 to 1.00.

A ten-year interest-only loan with MetLife at 3.05% per annum, principal balance of \$5,000,000, dated December 9, 2016, had a balance of \$5,000,000 at December 31, 2018. According to the terms of the loan, up to 10% of the original principal balance can be repaid annually during the life of the loan without penalty. The maturity date on this loan is December 9, 2026. In Q1 2019, \$500,000 was paid down without

penalty. The current balance outstanding is \$4,500,000. Keweenaw also maintains a five-year revolving line of credit in the amount of \$25,000,000 with a maturity date of December 6, 2021, with MetLife which carries an interest rate of 3-month LIBOR plus 150 basis points and .0875% on the uncommitted funds if the average unused portion is more than 50% of the maximum draw. If the average unused portion is 50% or less of the maximum draw, interest of .0375% is charged. Once the facility is used, there is the option of terming out the amount borrowed at the existing 10-year Treasury note rate plus 150 basis points. In Q2 2019, \$4,000,000 from a combination of proceeds from the sale of securities and cash on hand was applied to the outstanding balance of the MetLife line of credit. A total of \$9,700,000 and \$13,700,000 had been drawn on this line of credit as of September 30, 2019, and December 31, 2018, respectively. Significant covenants of MetLife require Keweenaw to not allow the outstanding principal balance of the loan to exceed 35% of the value of the timberlands owned by Keweenaw.

In addition to these financial covenants listed above, the debt agreements include customary covenants that limit the incurrence of debt and the disposition of assets, among others. At September 30, 2019, Keweenaw was in compliance with all applicable covenants.

At September 30, 2019, there were two standby letters of credit amounting to \$29,000 for the purpose of backing performance bonds required by the USDA Forest Service in connection with on-going timber stumpage and road-use contracts with the Company. A third standby letter in the amount of \$500,000 existed as a payment bond to the Forest Service. No balance was owed on the \$529,000 committed against the \$1,000,000 line of credit as of September 30, 2019, and December 31, 2018.

The following table summarizes the long-term debt of the Company at September 30, 2019, and December 31, 2018:

	<u>September 30,</u> <u>2019</u>	<u>December 31,</u> <u>2018</u>
Long-term Debt	\$ 4,500,000	\$ 5,000,000
Five-year Revolver	9,700,000	13,700,000
Less Unamortized Loan Costs	(169,071)	(186,764)
<b>Total</b>	<b><u>\$ 14,030,929</u></b>	<b><u>\$ 18,513,236</u></b>

## 7. Retirement Plans

The Company is the sponsor of a 401(K) deferred compensation plan. The Company made matching contributions equal to 50 percent of employee elective deferrals, not to exceed 5 percent of compensation as defined in the plan. In addition, the Company made discretionary contributions to the plan in the amount of 5 percent of base compensation. Expenses related to the Company's 401(K) plan were:

	<b>3 Months Ended</b>		<b>9 Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
Total Pension Expense	\$ 21,291	\$ 20,128	\$ 60,533	\$ 67,001

## 8. Concentration of Credit Risk

Keweenaw is located in Ironwood, Michigan. The Company grants credit without collateral to its approved customers, most of whom are located in Wisconsin and Upper Michigan. The Company has not experienced any significant losses from uncollectible customer accounts. During the quarter ending September 30, 2019, four customers accounted for approximately 22%, 14%, 12% and 11% of the Company's consolidated receivables.

The total cash held by the Company on September 30, 2019, and December 31, 2018, includes \$5,653,613 and \$2,739,990, respectively. Cash and cash equivalents consist of cash on hand and demand deposits in banks. The Company considers all highly-liquid investments purchased with original maturities of three months or less to be cash and cash equivalents. The Company, at times throughout the year, may, in the ordinary course of business, maintain cash balances in excess of federally insured limits. Management does not believe the Company is exposed to any unusual risks on such deposits.

## 9. Leases

In 2016, the Company began leasing logging equipment under long-term leases. The leases are operating leases. During the quarters ending September 30, 2019 and 2018, lease expense was \$52,679, respectively. The Company has the option to purchase the two pieces of equipment for \$150,000 and \$90,000, respectively, at the end of the lease. The Company has the option to renew the leases for monthly payments of \$7,729 and \$4,569 for 12 monthly payments. If the renewal option is selected, the option to purchase drops to \$65,000 and \$40,000, respectively.

Future minimum obligations over the primary terms of the Company's long-term leases as of September 30, 2019, are as follows:

<b>Year</b>	<b>Lease Obligations</b>
Payments remaining 2019	\$ 52,680
2020	82,551
<b>Total</b>	<b>\$ 135,231</b>

## **Section 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following discussion and analysis should be read in conjunction with our accompanying consolidated financial statements and notes thereto. See also “Cautionary Note Regarding Forward-Looking Statements”.

### **Overview**

As of September 30, 2019, Keweenaw, a land and timber management company, owned 183,559 acres of surface land and 401,867 acres of subsurface mineral rights in the western Upper Peninsula of Michigan and northern Wisconsin. Keweenaw derives the majority of our net income from the sale of logs harvested from our forestlands, and from the purchase of stumpage from public and private timber sources. Keweenaw also generates other revenue from recreational leases, mineral rights leases, sale of sand and gravel, and by providing wood scaling and inventory management services for various customers.

### **Liquidity and Capital Resources**

Keweenaw’s net cash flows were \$2,913,623 in 2019 YTD versus \$23,105 in 2018 for the same period. The Company is focused on reducing existing debt, and principal payments of (\$500,000) and (\$4,000,000) respectively have been applied to the long-term loan and five-year revolver year to date. The next payment windows for the long-term loan is January 2020 and for the five-year revolver it is November 30, 2019.

There were no capital expenditures in Q3 2019 other than primary road building for less than \$10,500.

In Q3 2019, no dividends were paid to shareholders and 3,754 new shares were issued. On September 30, 2019, Keweenaw had \$5,653,613 in cash and cash equivalents on hand compared to \$2,739,990 at the end of Q3 2018. The increased cash was due to closing on the conservation easement sale in September 2019.

The Company has a single credit arrangement at Wells Fargo Bank, N.A., which provides for a total of \$1,000,000 operating line-of-credit availability to satisfy short-term operating cash needs and to also fund standby letters-of-credit in guarantee of performance on public bid timber stumpage contracts with the USDA Forest Service.

Keweenaw did not borrow on its short-term line of credit with Wells Fargo in Q3 2019 or 2018. On September 30, 2019, there was no outstanding balance on its short-term line of credit. If necessary, short-term borrowing and repayment would occur using the automatic balance transfer feature of Keweenaw’s primary business checking account and its operating line of credit. On Keweenaw’s \$1,000,000 operating line of credit, three letters of credit totaling \$529,000 were outstanding at the end of Q3 2019, though no



balance was owed on any of the letters.

In December 2016, the Company borrowed \$5,000,000 from MetLife at an interest rate of 3.05%. Terms of the 10-year interest-only loan with MetLife include quarterly interest payments at 3.05%. Up to 10% of the principal balance may be paid annually without prepayment penalty. The maturity date on the loan is December 9, 2026. Total interest paid in Q3 2019 on this loan was \$34,313. In Q3 2019, no amount was paid on the principal. The current loan balance was \$4,500,000 as of September 30, 2019.

Also, in December 2016, Keweenaw secured a debt facility with MetLife in the form of a \$25,000,000 revolver allowing the Company immediate access to cash for general and corporate purposes. In March 2017, the Company borrowed \$12,700,000 against the revolver to fund the purchase of 14,356 acres of timberland in Iron County, Wisconsin. An additional \$1,000,000 was borrowed to fund the purchase of 2,784 acres in Gogebic County. At the end of Q3 2019, after a principal payment was made in the amount of \$4,000,000, a total of \$15,300,000 is now available for the strategic needs of the Company. Fees and interest associated with the revolver include quarterly payments on the unused facility of 0.0875%. Once the facility is used, there is the option to finance the amount borrowed at the existing 10-year Treasury note rate plus 150 basis points. Interest paid in Q3 2019 on this loan totaled \$97,679. Current debt facility outstanding balance is \$9,700,000 as of September 30, 2019.

## **Results of Operations**

### ***Timber Sales & Operations***

Q3 2019 timber harvest volumes were strong at 40,893 cords. These results are higher than the same period last year due to increased planned harvests from both Company and procured stumpage, favorable logging conditions and improved product mix. Q3 2019 harvest volume was 18.7% higher than Q3 2018 volume of 34,443 cords. Q3 2019 harvest volume included 38,736 cords from Company land and 2,157 procured cords versus Q3 2018 volume of 33,614 cords from Company land and 829 procured cords.

The overall Q3 2019 gross timber revenue was up 11.4% at \$5,112,135 versus Q3 2018 gross revenues of \$4,587,232. Company land gross revenue was \$4,835,211 up 7.8% over Q3 2018 Company land gross revenue of \$4,484,169. Q3 2019 gross sales from procured stumpage was \$276,924 and \$103,063 from Q3 2018, an increase of 169%.

The overall increase in Q3 2019 gross revenue was a result of increased sales volume and an improvement in price/mix. The volume increase of 18.7% and stronger sales contributed to an overall increase of 11.4% in gross revenue during the third quarter.

Timber sales volumes, sales product mix and net margin as a quarter to quarter comparison are shown in the following tables:

	3 Months Ended			9 Months Ended		
	September 30			September 30		
	2019	2018	% Change	2019	2018	% Change
<b>Timber Sales Volume (cd-eq.)</b>						
Veneer	862	835	3.2%	1,880	1,706	10.2%
Sawlog	4,990	3,849	29.6%	8,846	7,203	22.8%
Sawbolt	4,802	3,937	22.0%	12,324	10,612	16.1%
Pulpwood	30,240	25,823	17.1%	67,669	64,954	4.2%
<b>Total</b>	<b>40,893</b>	<b>34,443</b>	<b>18.7%</b>	<b>90,719</b>	<b>84,475</b>	<b>7.4%</b>
<b>Product Mix</b>						
Veneer	2.1%	2.4%		2.1%	2.0%	
Sawlog	12.2%	11.2%		9.8%	8.5%	
Sawbolt	11.7%	11.4%		13.6%	12.6%	
Pulpwood	73.9%	75.0%		74.6%	76.9%	
<b>Total</b>	<b>100.0%</b>	<b>100.0%</b>		<b>100.0%</b>	<b>100.0%</b>	
<b>Gross Timber Margin (per cd-eq.)*</b>						
Veneer	\$ 286.93	\$ 296.20	\$ (9.27)	\$ 290.56	\$ 304.99	\$ (14.43)
Sawlog	123.65	117.13	6.51	108.10	100.52	7.57
Sawbolt	63.94	59.42	4.52	60.29	57.93	2.36
Pulpwood	14.26	13.74	0.52	13.56	15.45	(1.89)
<b>Total</b>	<b>\$ 39.18</b>	<b>\$ 37.36</b>	<b>1.82</b>	<b>\$ 34.87</b>	<b>\$ 33.88</b>	<b>0.99</b>

\* Gross timber margin per cord are net of logging, freight, road, depletion/stumpage and other costs  
Other costs includes sort yard and inventory change

The increase in Q3 2019 timber revenues over Q3 2018 was driven by both price/mix and volume changes year over year. The total impact of those changes is reflected below:

Sales	3 Months Ended		Volume	\$/Mix	9 Months Ended		Volume	\$/Mix
	September 30				September 30			
	2019	2018			2019	2018		
Veneer	\$ 342,411	\$ 348,757	3.2%	-5.0%	\$ 780,942	\$ 718,573	10.3%	-1.6%
Sawlog	\$ 1,123,317	\$ 950,065	29.6%	-11.4%	\$ 2,047,023	\$ 1,724,425	22.8%	-4.1%
Sawbolt	\$ 699,758	\$ 565,906	22.0%	1.7%	\$ 1,771,379	\$ 1,508,387	16.1%	1.3%
Pulpwood	\$ 2,946,648	\$ 2,722,504	17.1%	-8.9%	\$ 6,855,279	\$ 6,694,189	4.2%	-1.8%
<b>Total</b>	<b>\$ 5,112,135</b>	<b>\$ 4,587,233</b>	<b>18.7%</b>	<b>-7.8%</b>	<b>\$ 11,454,623</b>	<b>\$ 10,645,574</b>	<b>7.4%</b>	<b>-1.7%</b>

## *Costs of Operations*

Contract logging and freight costs represent the majority of log production expense.

On a per unit basis Q3 2019 logging costs decreased by \$4.88 per cord to \$41.55 per cord versus Q3 2018's per unit cost of \$46.43 per cord. The per unit decrease is due to the sale of 5,056 cords of stumpage in which no logging costs was incurred against the harvest volume that was sold.

On a per unit basis, Q3 2019 freight costs decreased by \$5.29 per cord to \$31.10 per cord versus Q3 2018's per unit cost of \$36.39 per cord. Like the decrease in logging cost the decrease in Q3 freight cost is due to the sale of 5,056 cords of stumpage in which no freight cost was incurred against the harvest volume sold.

Costs associated with construction, maintenance and improvement of the Company's logging roads is a major element of Keweenaw's production cost. Q3 2019 road costs was down by \$0.29 per cord to \$4.89 per harvested cord versus Q3 2018 at \$5.18 per harvested cord driven by higher volumes harvested. Year to date road building cost are up \$0.41 per harvested cord due to increased winter road maintenance as a result of above average snowfall during the winter logging season.

Production costs per cord for the 3-month period ending Q3 2019 and Q3 2018 and YTD 2019 and 2018 are listed below.

Production Costs per Cord	3 Months Ended September 30		9 Months Ended September 30	
	2019	2018	2019	2018
Logging	\$ 41.55	\$ 46.43	\$ 43.91	\$ 45.62
Freight	31.10	36.39	33.30	33.24
Roads	4.89	5.18	5.62	5.21
Depletion/Stumpage	5.39	5.01	5.31	4.73
Sort Yard (Other)	2.90	2.81	3.25	3.34
Total	<u>\$ 85.83</u>	<u>\$ 95.82</u>	<u>\$ 91.39</u>	<u>\$ 92.14</u>

## *Other Revenue and Income*

Other Q3 2019 income including mineral royalties, lease and rental income, investment earnings, service fees and land sales was \$131,479, down from \$1,166,158 in Q3 2018. Year to date other income is up \$977,917 with the key drivers being the gain of \$1,494,133 in the sale of the securities portfolio and the eight real estate transactions netting \$1,037,586.

Income from these various sources is unpredictable in nature and can vary widely from year to year. The breakdown of other income by category is reflected below.

The summary of other revenue and income is as follows:

	<b>3 Months Ended</b>		<b>9 Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
Lease Income, Mineral Royalties and Service Fees	\$ 38,618	\$ 98,573	\$ 193,846	\$ 322,873
Investments	\$ -	\$ 13,096	9,093	59,154
Securities Sales	\$ -	\$ -	1,494,133	-
Conservation Easement	\$ (308,541)	\$ -	(308,541)	-
Real Estate (net)	\$ 401,402	\$ 1,054,489	1,037,586	1,066,371
<b>Total Other Income</b>	<b>\$ 131,479</b>	<b>\$ 1,166,158</b>	<b>\$ 2,426,117</b>	<b>\$ 1,448,398</b>

Real estate sales summary is included below:

<b>Real Estate Sales</b>	<b>3 Months Ended</b>		<b>9 Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
Acres Sold	125	1,801.7	404	1,807.5
Gross	\$ 429,600	\$ 1,484,000	\$ 1,118,600	\$ 1,510,000
\$ Acre/Gross	\$ 3,443	\$ 824	\$ 2,770	\$ 835

The conservation easement closed on September 9, 2019:

<b>Conservation Easement</b>	<b>3 Months Ended</b>		<b>9 Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
Conservation Easement Sale	\$ 3,941,000	\$ -	\$ 3,941,000	\$ -
Conservation Easement Value (Book)	\$ 4,249,541	\$ -	\$ 4,249,541	\$ -
Net Loss on Sale	\$ (308,541)	\$ -	\$ (308,541)	\$ -

### ***Selling, Management and Administrative Expense***

Q3 2019 Selling, Management and Administrative expenses were \$595,688, which was higher than Q3 2018 primarily due to legal fees and professional services regarding corporate governance.

## *Non-recurring Expenses*

	<b>3 Months Ended</b>		<b>9 Months Ended</b>	
	<b>September 30</b>		<b>September 30</b>	
	<b>2019</b>	<b>2018</b>	<b>2019</b>	<b>2018</b>
REIT Services	\$ -	\$ 34,417	\$ 27,151	\$ 162,376
Change of Control Agreements	-	249,595	-	1,532,888
Proxy Costs/Governance/Auditing Standards	37,350	-	165,718	319,653
Total	<u>\$ 37,350</u>	<u>\$ 284,012</u>	<u>\$ 192,869</u>	<u>\$ 2,014,917</u>

Non-recurring charges in Q3 2019 relate to some corporate transition and consulting costs. Non-recurring fees Q3 2019 are less than the same period in Q3 2018 and about the same as Q2 2019.

### **Section 3. OTHER MANAGEMENT DISCUSSIONS**

#### *Sale of Conservation Easement*

On September 9, 2019, Keweenaw announced the completion of the sale of 14,342 conservation easement to the State of Wisconsin, Department of Natural Resources (WIDNR). A press release was issued on September 9, 2019, announcing the sale and can be viewed on our website [www.keweenaw.com](http://www.keweenaw.com). The net proceeds to Keweenaw was \$3.94 million.

### **Section 4. LEGAL PROCEEDINGS**

From time to time, we are party to legal proceedings, which arise in the ordinary course of our business. We are not currently involved in any legal proceedings of which the outcome is reasonably likely to have a material effect on our results of operations or financial condition, nor are we aware of any such legal proceedings contemplated by governmental authorities.

### **Section 5. RISK FACTORS**

There have been no material changes from the risk factors disclosed in the “Risk Factors” section of our Annual report for the year ended December 31, 2018, which can be found on our website [www.keweenaw.com](http://www.keweenaw.com).

### **Section 6. SUBSEQUENT EVENTS**

None at this time.