Washington Electric Cooperative, Inc.

FINANCIAL STATEMENTS

December 31, 2013

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Kittell Branagan & Sargent

Certified Public Accountants

Vermont License #167

INDEPENDENT AUDITOR'S REPORT

The Board of Directors
Washington Electric Cooperative, Inc.
East Montpelier, Vermont

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Washington Electric Cooperative, Inc. (a non-profit corporation), which comprise the consolidated statement of financial position as of December 31, 2013 and 2012, and the related consolidated statements of operations, equities and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Washington Electric Cooperative, Inc. as of December 31, 2013 and 2012, and the changes in its net assets and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated February 25, 2014 on our consideration of Washington Electric Cooperative, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Washington Electric Cooperative, Inc.'s internal control over financial reporting and compliance.

Kittell Branagan & Sargent

St. Albans, Vermont
February 25, 2014

Washington Electric Cooperative, Inc.
BALANCE SHEETS
December 31,

ASSETS

	2013	2012
ELECTRIC PLANT, at cost	$ 72,294,337	$ 70,025,431
Less accumulated depreciation	(23,650,896)	(22,490,696)
Electric plant in service, net	48,643,441	47,534,735
Construction work in progress	394,739	1,072,809
TOTAL ELECTRIC PLANT, net	49,038,180	48,607,544
CURRENT ASSETS		
Cash	448,463	711,228
Receivables -		
Notes, less allowance for doubtful accounts of $1,500 and $1,500 in 2013 and 2012	99	99
Accounts, less allowance for doubtful accounts of $27,500 and $25,500 in 2013 and 2012	1,308,640	1,263,483
Renewable energy certificate revenue	741,220	742,171
Miscellaneous	248,354	319,586
Unbilled revenue	770,257	788,296
Inventories	273,770	265,649
Prepaid corporate taxes	10,928	9,190
Prepaid expenses	144,738	91,458
TOTAL CURRENT ASSETS	3,946,469	4,191,160
OTHER ASSETS		
Other investments	6,311,943	5,901,731
Deferred charges	1,926,882	478,447
TOTAL OTHER ASSETS	8,238,825	6,380,178
TOTAL ASSETS	$ 61,223,474	$ 59,178,882

LIABILITIES AND EQUITY

	2013	2012
EQUITIES		
Memberships issued and subscribed	$ 124,020	$ 120,060
Patronage capital assignable	1,055,253	893,293
Patronage capital credits	19,211,651	18,587,794
Donated capital	229,999	221,979
NET EQUITY	20,620,923	19,823,126
LONG-TERM DEBT	36,096,018	34,565,309
CURRENT LIABILITIES		
Current portion of long-term debt	2,026,172	2,009,900
CFC line of credit	443,850	913,130
Accounts payable	1,017,079	852,268
Customer deposits	204,007	215,696
Other accrued expenses	660,068	641,834
TOTAL CURRENT LIABILITIES	4,351,176	4,632,828
DEFERRED CREDITS	155,357	157,619
TOTAL LIABILITIES AND EQUITY	$ 61,223,474	$ 59,178,882

See Accompanying Notes to Financial Statements

Washington Electric Cooperative, Inc.
STATEMENTS OF OPERATIONS
For the Years Ended December 31,

	2013	2012
OPERATING REVENUE		
Member revenue retail sales	$ 13,290,692	$ 13,269,314
Member revenue REC sales	2,231,438	1,656,757
Other	448,423	441,655
TOTAL OPERATING REVENUE	15,970,553	15,367,726
OPERATING EXPENSES		
Purchased power	3,966,779	3,713,419
Power generation	1,796,866	1,527,930
Transmission	75,299	33,839
Distribution:		
Operations	1,606,125	1,422,784
Maintenance	2,154,306	1,913,728
Customer accounts	836,763	927,780
Administrative and general	1,534,793	1,467,668
Depreciation	2,088,778	2,023,126
Taxes	146,479	332,878
Other deductions, net	21,658	21,658
TOTAL OPERATING EXPENSES	14,227,846	13,384,810
MARGINS FROM OPERATIONS BEFORE INTEREST CHARGES	1,742,707	1,982,916
INTEREST CHARGES		
Interest on long-term debt	1,391,782	1,619,999
Other interest	12,681	9,983
TOTAL INTEREST CHARGES	1,404,463	1,629,982
MARGINS FROM OPERATIONS	338,244	352,934
OTHER INCOME (EXPENSE)		
Interest and dividend income	669,550	594,979
Other non-operating income	74,651	32,625
Other non-operating expense	(87,489)	(86,995)
Cumulative effect on prior years change in accounting principal	63,040	-
Income taxes	(2,743)	(250)
TOTAL OTHER INCOME (EXPENSE)	717,009	540,359
NET MARGINS	$ 1,055,253	$ 893,293

See Accompanying Notes to Financial Statements

Washington Electric Cooperative, Inc.
STATEMENTS OF EQUITIES
For the Years Ended December 31,

			Other Equities	
	Memberships Issued and Subscribed	Patronage Capital Assignable	Patronage Capital Credits	Donated Capital
BALANCE, at December 31, 2011	$ 116,145	$ 832,315	$ 17,692,562	$ 214,014
New memberships issued and subscribed for	11,880	-	-	-
Transfers to donated capital	(7,965)	-	-	7,965
Transfers to patronage capital credits	-	(832,315)	832,315	-
Patronage rebates	-	-	(257,344)	-
Net margins for the year	-	893,293	-	-
Line construction contributed	-	-	320,261	-
BALANCE, at December 31, 2012	120,060	893,293	18,587,794	221,979
New memberships issued and subscribed for	11,980	-	-	-
Transfers to donated capital	(8,020)	-	-	8,020
Transfers to patronage capital credits	-	(893,293)	893,293	-
Patronage rebates	-	-	(248,576)	-
Net margins for the year	-	1,055,253	-	-
Line construction refunded to member	-	-	(20,860)	-
BALANCE, at December 31, 2013	$ 124,020	$ 1,055,253	$ 19,211,651	$ 229,999

See Accompanying Notes to Financial Statements

Washington Electric Cooperative, Inc.
STATEMENTS OF CASH FLOWS
For the Years Ended December 31,

	2013	2012
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 1,055,253	$ 893,293
Noncash expenses (income) included in earnings:		
Depreciation	2,088,778	2,207,451
Amortization of deferred charges	205,413	110,955
Gain on sale of assets	(20,682)	(4,214)
Changes in assets and liabilities:		
Decrease (increase) in accounts receivable	26,075	279,158
Decrease (increase) in renewable energy certificate revenue receivable	951	(208,593)
Decrease (increase) in unbilled revenue	18,039	3,219
Decrease (increase) in inventories	(8,121)	(25,713)
Decrease (increase) in prepaid expenses	(55,018)	116,497
Decrease (increase) in deferred debits	1,310	(380,845)
Increase (decrease) in accounts payable	164,811	(224,299)
Increase (decrease) in customer deposits	(11,689)	17,438
Increase (decrease) in accrued expenses	18,234	31,711
Increase (decrease) in deferred credit	(2,262)	(84,268)
NET CASH PROVIDED BY OPERATING ACTIVITIES	3,481,092	2,731,790
CASH FLOWS FROM INVESTING ACTIVITIES		
Investment in CD over 3 months	-	250,000
Proceeds from sales of assets	34,139	4,252
Additions to electric plant in service and construction work in progress	(2,755,265)	(5,017,514)
Return of capital	57,785	52,168
Purchase of investments	(467,996)	(657,922)
NET CASH (USED) IN INVESTING ACTIVITIES	(3,131,337)	(5,369,016)

See Accompanying Notes to Financial Statements

Washington Electric Cooperative, Inc.
STATEMENTS OF CASH FLOWS
For the Years Ended December 31,

	2013	2012
CASH FLOWS FROM FINANCING ACTIVITIES		
Contributions in aid of construction	(20,860)	320,261
CIAOC from the American Recovery and Reinvestment Act Grant	261,688	1,199,317
CIAOC from FEMA Grants	-	3,852
Memberships issued, net of refunds	11,980	11,880
Patronage rebates	(248,576)	(257,344)
Proceeds from short-term debt	4,618,322	3,750,628
Payments on short-term debt	(5,087,602)	(2,837,499)
Proceeds from long-term debt	1,900,000	1,800,000
Principal payments on long-term deb	(2,047,472)	(1,393,971)
NET CASH PROVIDED (USED) BY FINANCING ACTIVITIES	(612,520)	2,597,124
NET (DECREASE) IN CASH	(262,765)	(40,102)
CASH - Beginning of Year	711,228	751,330
CASH - End of Year	$ 448,463	$ 711,228
SUPPLEMENTARY CASH FLOW INFORMATION		
Cash paid during the year for interest	$ 1,402,055	$ 1,627,677
Non-cash financing & operating activities	$ 1,694,453	$ -

See Accompanying Notes to Financial Statements

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Washington Electric Cooperative, Inc. ("the Cooperative") is a vertically integrated utility with monopoly franchise rights granted by the state of Vermont to provide residential and commercial electric service in its franchise service territory. Operating revenue is generated from sales of electric power and related activity to the Cooperative's patrons located primarily within the State of Vermont.

Regulatory jurisdictions

The Cooperative is under the jurisdiction of the Federal Energy Regulatory Commission (FERC), the Rural Utilities Service (RUS), formerly known as the Rural Electrification Administration (REA), the Public Service Board of Vermont (PSB), and the Vermont Department of Public Service (DPS). The PSB has the primary responsibility for regulating the Cooperative's rates. The Cooperative utilizes the Uniform System of Accounts established by the RUS, except where the PSB has prescribed other treatment.

Corporate structure and income taxes

The Cooperative is a nonprofit and nonstock membership corporation organized under provisions of the Electric Cooperative Act of Vermont. The Cooperative is an organization described in Section 501(c)(12) of the Internal Revenue Code, and has been recognized by the Internal Revenue Service as an organization exempt from taxes on related income under Section 501(a).

Effective January 1, 2009, the Cooperative adopted the guidance on uncertain tax positions in the Financial Accounting Standards Board (FASB) Accounting Standards Codification 740, Income Taxes (formerly FASB Interpretation No. 48) that requires the Cooperative to evaluate its income tax positions to determine if there are any positions that would require any adjustments to the financial statements. The Cooperative has determined that it has no uncertain income tax positions that need to be recorded or reported in the financial statements.

In July 2003, the Board of Directors authorized the creation of, and a $5,000 investment in, the Coventry Clean Energy Corporation (CCEC), a wholly-owned subsidiary. CCEC is a for profit corporation. Since its operations began in 2006, CCEC financial statements have been consolidated with the Cooperative's financial statements.

The tax years ending December 31, 2013, 2012, 2011 and 2010 are still open to audit for both federal and state purposes.

Consolidation policy

The consolidated financial statements include the accounts of the Cooperative and CCEC. All intercompany accounts and transactions are eliminated in consolidation.

Electric plant and retirements

Electric plant is stated at cost. The cost of additions to electric plant includes contracted work, direct labor and materials, and allocable overheads. Listed below are the major classes of electric plant as of December 31,:

	2013	2012
Intangible plant	$ 609	$ 609
Generation (hydro) plant	3,746,570	3,746,556
Generation (landfill gas) plant	12,299,794	12,551,623
Transmission plant	2,628,957	2,286,713

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

	2013	2012
Distribution plant	48,283,589	46,116,286
General plant	5,334,818	5,323,644
	$ 72,294,337	$ 70,025,431

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Depreciation and plant retirement

The Cooperative follows the policy of charging to operating expenses annual amounts of depreciation which allocate the cost of the electric plant over its estimated useful life. The Cooperative employs the straight-line and straight-line composite methods for determining the annual charge for depreciation. The estimated useful lives and rates for electric plant are as follows:

	Life in Years	Composite Rate
Generation plant	20-50	2-5%
Transmission plant	35	2.748%
Distribution plant	35	2.796%
Buildings and structures	10-50	2.50%
Transportation equipment	4-10	10-25%
General plant	5-15	6-20%

Maintenance and repairs are charged to expense as incurred. When assets are retired or otherwise disposed of, the costs are removed from plant, and such costs, plus removal costs, less salvage, are charged to accumulated depreciation.

Amortization

The Cooperative follows the policy of charging to operating expenses annual amounts of amortization which allocate the cost of various deferred charges over periods established by management for rate-making purposes. The Cooperative employs the straight-line method for determining the annual charge for amortization.

Cash and cash equivalents

The Cooperative considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

Inventories

Inventories are stated at the lower of average cost or market, determined by the first-in, first-out method.

Contributions in aid of construction

As explained above, the Cooperative follows RUS accounting guidelines, except as otherwise allowed or prescribed by its state regulator, the PSB. In accordance with state regulatory requirements, contributions in aid of construction prior to 2013 were accounted for as a component of patrons' equity rather than as a reduction of electric plant in service. Beginning in January, 2013 the Cooperative began netting all contributions in aid of construction received from its members with the fixed assets placed in service for all new line construction. All contributions in aid of construction come from patrons of the Cooperative. The Cooperative is allowed to recover its gross investment in plant in its rates.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Use of estimates
The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities. These estimates are made at the date of the financial statements and are based on the reported amounts of revenues and expenses during the reporting period, and other factors. Actual results could differ from those estimates.

Revenue recognition
The Cooperative recognizes revenue for electric service in the month that service is rendered. The amount shown as unbilled revenue represents an estimate of the amounts used from the last meter reading through the end of the year.

Investments
Investments are recorded at cost. Because these investments are not publicly traded, market values are not readily determinable.

Presentation
Certain amounts have been reclassified in the 2012 financial statements in order to conform with the 2013 presentation.

NOTE 2 OTHER INVESTMENTS

Other investments include the following, at cost, at December 31,:

	2013	2012
Investments in associated organizations:		
National Rural Utilties Cooperative Finance Corporation (CFC) membership	$ 1,000	$ 1,000
CFC capital term certificates	450,211	453,034
CFC patronage capital certificates	143,723	126,029
NISC patronage capital certificates	75,798	64,911
Patronage capital certificates - other Cooperatives	15,381	15,003
Rural Electric Vermont Association membership	497	497
	686,610	660,474
Other Investments		
Vermont Electric Power Company - common stock, Class B	265,600	265,600
Vermont Electric Power Company - common stock, Class C	101,900	101,900
Vermont Electric Power Company - preferred stock, Class C	1,793	1,793
Vermont Transco LLC - Class A membership units	2,312,670	2,128,000
Vermont Transco LLC - Class B membership units	2,943,370	2,708,340
Central VT Memorial Civic Center - rural economic development loan	-	35,624
	5,625,333	5,241,257
TOTAL OTHER INVESTMENTS	$ 6,311,943	$ 5,901,731

NOTE 3 LONG-TERM DEBT

Long-term debt at December 31, 2013 and 2012 consists of the following:

	2013	2012
Mortgage notes payable, U.S. Department of Agriculture (RUS) 35-year terms at the following interest rates:		
4.125% mortgage notes	$ 5,766,884	$ 6,017,094
Mortgage notes payable, National Rural Utilities Cooperative Finance Corporation (CFC), 35-year terms due between 2016 and 2031 at the following rates of interest:		
Fixed rate mortgage notes, 6.10% to 6.45% due quarterly, variable dates through July 1, 2028.	1,592,730	1,723,069
Fixed rate mortgage notes, 2.10% to 4.35% due annually, through June 30, 2031.	14,670,017	15,776,069
Fixed rate mortgage note, 3.0% due annually matures June 30, 2023.	1,656,889	-
	17,919,636	17,499,138
CFC Clean Renewable Energy Bond, nominal interest rate 0.400% effective interest rate 1.497%, quarterly payments of $17,304 from March 2008 through December 2023.	753,857	829,242
Mortgage notes payable, Federal Financing Bank (FFB) at the following due dates and rates of interest (unadvanced loan funds as of December 31, 2013 and 2012 were $3,700,000 and $5,600,000, respectively):		
4.287% to 8.335% advances, matures December 31, 2014	35,313	70,626
4.366% advances, matures December 31, 2033	2,726,087	2,862,391
4.472% advances, matures December 31, 2043	2,684,545	2,774,030
4.272% advances, matures December 31, 2043	1,087,272	1,123,515
3.707% advances, matures December 31, 2043	756,364	781,576
3.328% advances, matures December 31, 2043	580,000	599,333
4.193% advances, matures December 31, 2043	621,069	641,771
3.999% advances, matures December 31, 2043	1,144,186	1,182,326
3.134% advances, matures December 31, 2043	346,977	358,543
2.281% advances, matures December 31, 2046	500,000	500,000
2.418% advances, matures December 31, 2046	800,000	800,000
2.625% advances, matures December 31, 2046	500,000	500,000
2.633% advances, matures December 31, 2046	900,000	-
3.411% advances, matures December 31, 2046	1,000,000	-
	13,681,813	12,194,111

NOTE 3 LONG-TERM DEBT (continued)

	2013	2012
Rural economic development loan, non-interest bearing, U.S. Department of Agriculture (RUS) loan:		
CVMCC - Payable in 168 monthly payments of $3,572 beginning November 1999 through October 2013.	-	35,624
	38,122,190	36,575,209
Less current installments:	(2,026,172)	(2,009,900)
Long-term debt, excluding current installments	$ 36,096,018	$ 34,565,309

The 2008-2011 Construction Work Plan (CWP) loan from the Federal Financing Bank (FFB) in the amount of $7.9 million was fully drawn in September 2011. In June 2011, the Cooperative's Board of Directors approved the 2012-2015 CWP authorizing its submittal to RUS together with a financing application for an FFB loan in the amount of $7.4 million. On February 21, 2012, the Cooperative signed the loan documents. For this loan the first principal payment is due March 31, 2014. The last day for an advance is January 17, 2017 and the final maturity date is December 31, 2046.

For FFB loans, the interest rate of an advance is determined at the time of the advance. At the time of the advance, the Cooperative can select, subject to RUS approval, either a short-term maturity date or a long-term maturity date. Payments on the advances are to be made quarterly.

Following PSB approval in November 2012, the Cooperative refinanced $15,776,069 of its RUS debt in December 2012 with a promissory note and loan agreement from CFC. The terms of the Loan provide for multiple advances with varying interest rates between 1.95% and 4.35%. The Cooperative estimates approximately $4,200,000 in interest expense savings over the 19 year refinance period ending June 2031.

The non-interest bearing rural economic development loan from the RUS to the Cooperative was used to partially finance the construction of the Central Vermont Memorial Civic Center (CVMCC) in the City of Montpelier. As security, the Cooperative received a 14-year note for $600,000 and first mortgages on real estate and leasehold estates from CVMCC, and four Irrevocable Letters of Credit from various banks as security for the loan. This loan was paid in full as of October 2013.

All of the assets of the Cooperative are pledged as security under the above-mentioned notes.

The following is a schedule of required principal payments on long-term debt in subsequent fiscal years from December 31, 2013:

2014	$ 2,026,172
2015	2,022,346
2016	2,040,538
2017	2,042,468
2018	2,052,161
Thereafter	27,938,505
	$ 38,122,190

NOTE 3 LONG-TERM DEBT (continued)

Loan covenants

Under the terms of the loan agreements, the Cooperative must maintain at least a times interest earned ratio (TIER) of 1.05 on the FFB debt, and 1.25 on the remaining long-term debt together with a debt service coverage (DSC) ratio of not less than 1.25, determined by averaging the two highest annual ratios during the three most recent calendar years. As required by the 1997 and subsequent RUS loan agreements, the Cooperative also must maintain an operating times interest earned ratio (OTIER) of 1.05 on the FFB debt and 1.10 on the remaining long-term debt together with an operating debt service coverage (ODSC) of 1.10, determined by averaging the two highest annual ratios during the three most recent calendar years. The Cooperative met these requirements in both 2013 and 2012.

Under the terms of the 2003 financing with CFC, the Cooperative must maintain a modified debt service coverage (MDSC) of not less than 1.35 determined by averaging the two highest annual ratios during the three most recent calendar years. The Cooperative met this requirement in 2013 and 2012.

NOTE 4 SHORT-TERM DEBT

A line of credit agreement executed with CFC provides the Cooperative with a short-term loan in an amount up to $2,600,000. This short-term loan operates on a revolving basis for a period of twelve months to June 14, 2014. Interest rates on the advances are variable and not to exceed the prevailing bank prime rate as published in the Eastern edition of the *Wall Street Journal*, "Money Rates" column, plus one percent. The interest rate at December 31, 2013 was 2.9%. The available balance on the note was $2,156,150 at year end.

NOTE 5 PENSION PLAN

All eligible employees of the Cooperative participate in the NRECA Retirement and Security Program, a defined benefit pension plan qualified under Section 401 and tax-exempt under Section 501(a) of the Internal Revenue Code. In this multi-employer plan, which is available to all member cooperatives of NRECA, the accumulated benefits and plan assets are not determined or allocated separately by individual employer. The plan sponsor’s Employer Identification Number is 53-0116145 and the Plan Number is 333.

A unique characteristic of multiemployer plans compared to a single employer plan is that all plan assets are available to pay benefits to any plan participant. Separate asset accounts are not maintained for participating employers. This means that assets contributed by one employer may be used to provide benefits to employees of other participating employers.

The Cooperative’s contributions to the RS Plan in 2013 and 2012 represent less than 5 percent of the total contributions made to the plan by all participating employers. At December 31, 2013 and 2012 the Cooperative made contributions to the plan of $2,208,293 and $643,648, respectively. Contributions in 2013 are significantly higher than those in 2012 due to the Cooperative electing to participate in the prepayment option offered to participating employers in 2013. See footnote description below for more information on the prepayment program. Pension expense for the prior service costs was $14,580 in both 2013 and 2012.

In the RS Plan, a “zone status” determination is not required, and therefore not determined, under the Pension Protection Act (PPA) of 2006. In addition, the accumulated benefit obligations and plan assets are not determined or allocated separately by individual employer. In total, the RS Plan was over 80 percent funded on January 1, 2013 and between 65 percent and 80 percent funded on January 1, 2012 based on the PPA funding target and PPA actuarial value of assets on those dates.

NOTE 5 PENSION PLAN (continued)

Because the provisions of the PPA do not apply to the RS Plan, funding improvement plans and surcharges are not applicable. Future contribution requirements are determined each year as part of the actuarial valuation of the plan and may change as a result of plan experience.

At the December 2012 meeting of the I&FS Committee of the NRECA Board of Directors, the Committee approved an option to allow participating cooperatives in the RS Plan to make a contribution prepayment and reduce future required contributions. The prepayment amount is a cooperative's share, as of January 1, 2013, of future contributions required to fund the RS Plan's unfunded value of benefits earned to date using RS Plan actuarial valuation assumptions. The prepayment amount will typically equal approximately 2.5 times a cooperative's annual RS Plan required contribution as of January 1, 2013. After making the prepayment, for most cooperatives the billing rate is reduced by approximately 25%, retroactive to January 1, 2013. The 25% differential in billing rates is expected to continue for approximately 15 years. However, changes in interest rates, asset returns and other plan experience different from expected, plan assumption changes and other factors may have an impact on the amount and duration of the differential in billing rates. The prepayment, which was made by the Cooperative during 2013, was for $1,694,453 and is being amortized over a 13 year period. On June 28, 2013, the Vermont Public Service Board authorized the financing of the pension prepayment in Docket #8062.

NOTE 6 COMMITMENTS AND CONTINGENCIES

Regulatory matters

The Cooperative has provided a portfolio of member energy services since 1992, in part due to regulatory requirements and Vermont law requiring all utilities to develop and file Integrated Resource Plans (IRPs). The timing for filing a utility's IRP is based on a three year statutory requirement.

The IRP projects the Cooperative's load, power supply requirements and electrical infrastructure needs. It is used to identify committed and preferred resource options for the future, including demand-side management resources and renewable sources of power such as increased Coventry Project power and Sheffield wind power. The IRP also includes information relative to WEC's transmission and distribution planning. It identifies where investments and upgrade work are needed on the WEC electric system for delivery of power to its members. The 2005 IRP supported the need for the Coventry (Methane Generation) Project, discussed below, which came online in July 2005.

The Cooperative filed an updated IRP on February 15, 2008. A stipulation regarding approval was entered with the DPS in August 2009; the plan and stipulation were approved by the PSB on December 13, 2012 in Docket No. 7432. In its Order, the PSB acknowledged its delay in approving the 2008 IRP and set December 6, 2013 as the filing date for the Cooperative's next IRP.

WEC filed a new IRP on December 6th commensurate with the PSB ordered filing date. This recently filed IRP is pending approval and is subject to regulatory review by the DPS and PSB. In the IRP, WEC demonstrates that it is projected to have sufficient sources of power from contracts and owned generation to meet its projected power supply needs for the next 20 years. WEC also notes that it is well positioned to meet various renewable energy goals and targets which are outlined in the State's Comprehensive Energy Plan based on its current resource mix.

NOTE 6 COMMITMENTS AND CONTINGENCIES (continued)

In 1999, the PSB ordered the establishment of the Energy Efficiency Utility (EEU), which began operating in February 2000 under the name "Efficiency Vermont" ("EVT"). Most efficiency services for commercial, industrial, residential and multi-family housing are now operated by the EEU and are no longer the responsibility of the Cooperative. The Cooperative continues to perform certain services associated with the "Residential New Construction Program" in coordination with the EEU. Pursuant to an order from the PSB, all Vermont utilities collect a monthly surcharge called the Energy Efficiency Charge (EEC) from customers. For December 31, 2013 and 2012 the total collected from the Cooperative's members was approximately $686,822 and $630,669, respectively. This amount is forwarded to a fiscal agent selected by the PSB and is not revenue to the Cooperative.

The Cooperative, along with other Vermont utilities, petitioned the PSB in Docket No. 7670 to enter various agreements that will enable it to receive power from HQ Energy Services US (HQUS) beginning in November 2016. The agreements provide for delivery of primarily on-peak energy and associated environmental attributes seven days per week, 16 hours per day. There are no capacity credits or other ancillary market products included in the contract. The Cooperative will obtain 4.0 MW of power through the Vermont Public Power Supply Authority (VPPSA). In addition, the Cooperative has entered into an agreement with the Vermont Electric Cooperative (VEC) to transfer its portion of HQUS power to VEC until a need exists in the Cooperative's power supply portfolio. Proceedings in front of the PSB were underway in 2010 and through 2011. The PSB issued its decision in 2011 and approved WEC's participation in the various agreements that enable it to obtain HQUS power.

<u>Contributions in Aid of Construction. PSB Docket No. 7554</u>

In 2009, the PSB opened Docket No. 7554 to consider whether or not to make regulatory changes in how electric cooperatives account for Contributions in Aid of Construction (CIAOC). In February 2011, the PSB issued a final order that required the Cooperative to make changes in how it accounts for CIAOC beginning in 2013. This resulted in changes in how CIAOC is currently accounted for, as described in Note 1, and it rescinded the previous PSB rulings on this matter. The Cooperative began following generally accepted accounting principles effective January 1, 2013 which reduces fixed assets constructed by the contribution toward the construction. The CIAOC in equity was allocated to active patrons in January 2014 based on their patronage for 2013.

<u>Risk Management</u>

The Cooperative is exposed to various risks of loss related to torts; theft of, damage to and destruction of or misuse of assets; injuries to individuals; and natural disasters. In addition to a system of internal controls, the Cooperative manages these risks through commercial insurance packages purchased in the name of the Cooperative.

NOTE 7 COMMITMENTS AND CONTINGENCIES - POWER SUPPLY

<u>Coventry Methane Generation Project</u>

The Cooperative owns and operates a generating facility powered by landfill gas at the Coventry Landfill in northern Vermont. The plant first began generating in July 2005 and was subsequently expanded in 2007 and 2009, to a present generating nameplate capacity of 8 MW. A set of contractual agreements was executed in 2003 between CCEC and New England Waste Services of Vermont, Inc. (NEWSVT), a wholly owned subsidiary of Casella Waste Systems, Inc. which owns the Coventry Landfill. These agreements codify the relationship of the parties.

NOTE 7 COMMITMENTS AND CONTINGENCIES - POWER SUPPLY (continued)

The initial project was financed by an RUS loan. The 2007 expansion was financed by CFC under their implementation of the Clean Renewable Energy Bond Program (CREB). The 2009 expansion was financed by an RUS-guaranteed FFB loan and by reallocating funds in the 2008-2011 CWP from distribution projects to generation assets.

The summary of project costs and outstanding notes payable as of December 31, 2013 are:

	Plant Cost	Note Balance
Phase 1 - Initial Construction, Engines 1-3	$ 8,502,732	$ 5,766,884
Phase 2 - Engine 4	1,238,397	753,857
Phase 3 - Engine 5 plus building modifications	4,133,419	2,726,087
Systems Upgrades financed with general funds	335,216	-
	$ 14,209,764	$ 9,246,828

Costs for each phase have been capitalized to both generation and transmission plant, with the majority in generation.

Of the $14,209,764 plant cost, $12,299,794 is capitalized to generation plant with the balance included in transmission plant.

In 2013 the Coventry Project provided approximately 54% of the Cooperative's total power supply output which made up 66% of the Cooperative's load requirements as measured by the Independent System Operator of New England (ISO-NE).

CCEC has a Landfill Gas Project Agreement with Innovative Energy Systems, Inc. (IES), a New York corporation, to operate the Coventry Generating Facility. The contract was effective on July 1, 2007. Services provided by IES include day-to-day management, operation, maintenance, plant repair, monitoring and adjustment of the gas collection system. The contract is for nine years (July 2016) with a renewal option for eight years. Compensation to IES is at the rate of 2.423 cents per kWh of electricity produced monthly, which is adjusted for inflation each year by the GDP-IPD index, the gross domestic product implicit price deflator index. At December 31, 2013 and 2012 the amount included in expense was $1,256,561 and $1,191,488, respectively.

Wrightsville Hydro

The Cooperative also owns and operates the Wrightsville Hydroelectric Generation Station in Montpelier, Vermont, a largely run-of-the-river project that has a nameplate capacity of 1,000 kW, though it provides significantly less average output because it is dependent on precipitation and weather conditions during the year. Operating costs were $107,482 and $80,345 at December 31, 2013 and 2012, respectively. Fixed costs were $111,524 and $137,987 over that same period, respectively.

The remaining energy needs of the Cooperative are provided by other entities or generators through contractual obligations. A brief summary of the long-term financial obligations and the more significant sources of total energy, as of December 31, 2013, are as follows.

NOTE 7 COMMITMENTS AND CONTINGENCIES – POWER SUPPLY (continued)

Sheffield Wind Project

In May 2005, the Cooperative executed an Advance Purchase Fee Agreement with wind developer UPC Wind Vermont, LLC (UPC), which subsequently became Vermont Wind, LLC ("Vermont Wind") for up to a 4 MW share of the output of its proposed 40 MW project in Sheffield. The PSB awarded UPC the required Certificate of Public Good for the project in August 2007. In January 2009, the Vermont Supreme Court unequivocally upheld the PSB Order. The contract was filed by Vermont Wind with the PSB in June 2009 and the PSB approved it, in Docket No. 7156, in August 2009. The Cooperative finalized a long-term Purchased Power Agreement with Vermont Wind in September 2009. Vermont Wind began construction in 2010 and the project reached its commercial operation date on October 19, 2011. WEC began receiving power generated from the wind project at that time. Sheffield Wind accounted for 9% of WEC's total power supply in 2013 and served roughly 11% of WEC's load needs.

NYPA

The Cooperative receives power from the Franklin D. Roosevelt-St. Lawrence and Niagara hydroelectric projects in New York, through the DPS, which contracts with the New York Power Authority (NYPA). NYPA power is currently being provided through the DPS under a long-term contract in which an extension was executed in 2007 for the St. Lawrence portion. The Cooperative anticipates no reductions in NYPA power supply going forward under the latest agreements, except when low water conditions exist. When low water conditions do exist, NYPA makes available replacement energy at a higher cost, but purchase of such replacement power is optional. The Niagara project, the largest provider of NYPA power to the Cooperative, was recently relicensed. This relatively low-cost resource is expected to continue to be available to the Cooperative's residential customers far into the future, though some related costs have increased in recent years, particularly transmission. NYPA accounted for 10% of WEC's total power supply in 2013 and served roughly 12% of WEC's load.

Hydro Quebec - On January 7, 1991, the PSB conditionally approved the Cooperative's purchase of 2.589 MW of Hydro-Quebec (HQ) Schedule B power for a term from September 23, 1995 through October 31, 2015. The Cooperative purchases this power as an assignee of rights under the Vermont Joint Owners' (VJO) contract with HQ. Under Vermont Statutes, a required vote of the membership took place at a special membership meeting on March 26, 1991, authorizing the Cooperative's participation in Schedules A and B of the HQ contract. Schedule A power terminated in 1995. The membership also voted to approve the transfer of the Cooperative's entitlement to any Schedule C power to the Village of Stowe Electric Department at that time.

The remaining Schedule B power is must-take at a 75% annual capacity factor, subject to a limited number of annual options for adjustments by either party, all of which have been exercised at this time. If the power is not received by the Cooperative at the must-take level, then the Cooperative must pay a penalty equal to the difference between the must-take contract level and the actual level of contract power received. The Schedule B take or pay costs were $1,226,017 and $1,117,465 at December 31, 2013 and 2012, respectively.

The Cooperative contracted in 1996 for a sale of power to HQ, at Schedule B contract prices, and a purchase of the same amount of power from HQ at lower, market-based prices. This contract extended from November 1, 1995 to November 1, 1999, and has expired. However, under this sellback contract, HQ has the option, upon four years notice, of reducing its deliveries to the Cooperative by up to 30% for the duration of the Schedule B portion of the HQ contract. This option has remained unexercised, and the Cooperative does not expect HQ to exercise the option in 2014. HQ Schedule B accounted for 19% of WEC's total power supply in 2013 and served roughly 23% of WEC's load needs.

NOTE 7 COMMITMENTS AND CONTINGENCIES – POWER SUPPLY (continued)

Highgate Converter Station (VPPSA)

The Cooperative has agreed to pay the Vermont Public Power Supply Authority (VPPSA) for its proportionate share of VPPSA's costs and obligations associated with the Highgate Converter, a transmission facility which allows interconnection with the HQ electric system. This arrangement allows the Cooperative access to wheeling transfer capability over Highgate and allows the Cooperative to import its share of power from HQ for the VJO contract. The Cooperative continues to pay for the operating and maintenance expenses of the Highgate converter. In 2013 the net cost was $38,509 while in 2012, there was a net credit for the converter of $1,229. These amounts are included in the total cost above for the Schedule B take or pay costs.

Small Power Producers

Vermont PSB Rule 4.100 requires all electric utilities to purchase power from Vermont's non-utility small power producers, on the basis of prior year energy sales as a share of total Vermont utility energy sales. The state purchasing agent, currently the Vermont Electric Power Producers Inc. (VEPPI), administers the contracts and allocates costs to the Vermont utilities. This obligation, which for the Cooperative amounts to approximately 1% of the total small power producers' output, was $412,934 in 2013 and $454,905 in 2012. The Cooperative's costs are expected to decrease moderately through time for VEPPI resources as contracts expire. The contract for the largest VEPPI unit (Ryegate) which accounts for roughly half of the VEPPI power was due to expire in October 2012. The Vermont PSB opened a docket (7782) to determine the rate to be charged to Vermont utilities upon the expiration of the existing Rule 4.100 contract. A new contract specifically covering Ryegate was finalized in 2013 and WEC is currently being allocated roughly 1% of the power from the Ryegate facility. The remaining Rule 4.100 contracts which are hydro-based resources are expected to expire fully by 2020.

NET METERING and Sustainably Priced Energy Enterprise Development (SPEED)

Since 1998, under Vermont’s net metering statute, electric utilities must allow eligible forms of renewable energy generation “behind” the consumer/member’s meter. Members must register with the PSB for installations of less than 10kw, or obtain a Certificate of Public Good (CPG) for capacity up to 500kw. The statute provides that a utility shall allow net metering up to 4% of its peak demand.

The Cooperative’s net metered resources reached 4% of its peak demand during 2012. The Cooperative evaluated the impact on its system to account for the revenue effect and costs incurred to compensate net metering members for “net excess generation”. At this time some 206 members possessing net-metered generation with a nameplate capacity totaling 1,559 kW have registered or received CPG’s to inject power into the grid. In February 2013 the Cooperative notified the PSB of the fact that the 4% capacity level had been reached, and requested that the PSB take no immediate action. In August 2013, WEC notified the PSB that it had reached 6% of its peak from net metering installations, and thereby had exceeded the statutorily set cap of 4%. As a result of WEC’s notification, the PSB requested that WEC file a revised tariff to its net metering program. WEC filed a revised tariff and sought to exceed the cap and to limit installations of 5kW and less. The filing was suspended by the PSB to consider threshold legal issues. Ultimately WEC withdrew the filing due to simultaneous efforts by Vermont law makers to change the net metering statute. These new laws, if enacted, will increase the limit to 15% of peak and will provide other changes that WEC will consider once the laws are ratified. As of December 2013 new net metering installations have not been allowed on the WEC system due to the PSB tariff suspension.

NOTE 7 COMMITMENTS AND CONTINGENCIES – POWER SUPPLY (continued)

SPEED is a feed-in tariff program for developers, available under the auspices of the PSB, and authorized by the legislature, through various PSB dockets (#7523 and #7533). The Cooperative has one such SPEED facility on its distribution system, a 2.1 MW photovoltaic (PV) project in Williamstown. WEC does not take power from this facility. Another proposed photovoltaic project which would be interconnected to the Cooperative's subtransmission line in Coventry is pending before the PSB. WEC plans to institute an Open Access Transmission Tariff to wheel power from projects connected to its sub-transmission lines to the VELCO grid.

VELCO

The Cooperative has entered into contracts with the Vermont Electric Power Corporation (VELCO), which operates Vermont's bulk transmission system, to participate in Phase I of the Hydro-Quebec Interconnection, a 450 kV HVDC transmission line directly connecting the HQ electric system with the New England Power Pool. Under these agreements, the Cooperative provided capital for the cost of construction through purchase of VELCO Class C preferred stock, and will provide support for the operation of its 0.1133% (.782 MW) interest of the line. The Cooperative is currently leasing this capacity to the Village of Stowe so that the Village can receive Hydro-Quebec/VJO Schedule C Purchased Power.

Vermont Transco LLC was officially established on June 30, 2006. Vermont Transco LLC is a limited liability company formed by VELCO and Vermont's distribution company owners, including the Cooperative. Vermont Transco LLC is now the owner of Vermont's high-voltage electric transmission system. VELCO is the manager of the LLC and, in that capacity, operates and maintains Vermont's electric transmission system, as it has for over fifty years.

Under collateral call arrangements associated with the Cooperative's ownership in VELCO and Vermont Transco LLC, the Cooperative purchased $419,700 and $641,010 in Vermont Transco equity units in 2013 and 2012, respectively.

In 2012 the PSB approved the merger of Central Vermont Public Service and Green Mountain Power. As part of its approval, the PSB ordered changes in the governance structure of VELCO to assure that the merged company would not control a majority of seats on its board. Consumer-owned utilities now appoint two additional independent directors, and a separate process was established for the appointment of three independent "public good" directors.

ISO-NE

The Cooperative, like all other utilities in New England, relies upon the ISO-NE, operator of the New England regional bulk transmission system, to dispatch generation and settle load obligations in the New England power markets. The Cooperative relies upon the ISO-NE to maintain reliability of the bulk power system and to administer the electricity markets within New England.

Through its joint ownership in VELCO and under the Cooperative's Central Dispatch Agreement (CDA) with the Vermont Public Power Supply Authority (VPPSA), the Cooperative is a member of the New England Power Pool (NEPOOL). The Cooperative's power supply resources are combined in the CDA with other VPPSA participants, and settled as one entity with ISO-NE. The CDA is intended to provide pooling savings to its members by taking advantage of economies of scale through sharing staff resources through VPPSA and load diversity, where under the CDA supply sources and loads of all of its participants are aggregated into a single entity for the purpose of ISO-NE settlement calculations. The Cooperative became a member of the CDA effective July 1, 1998. The Cooperative can withdraw from the arrangement on a short-term notice (30 days including any additional time required by ISO-NE to reflect such a change).

NOTE 7 COMMITMENTS AND CONTINGENCIES – POWER SUPPLY (continued)

Over the past decade, the ISO-NE market structure has continued to evolve. Spot markets for energy, capacity and ancillary power products were developed, upon which New England utilities such as the Cooperative depend to achieve reliability of the bulk power system. In recent years, significant investments in transmission in the ISO-NE region have contributed to increased power costs for the Cooperative and other utilities.

In 2013 the Cooperative's energy settlement load obligation with the ISO-NE was 77,729,681 kWh (this value represents the Cooperative's retail sales, distribution and transmission losses, and uncollected accounts). To hedge its load obligation the Cooperative's power sources in 2013 totaled 94,010,263 kWh. The following table summarizes the Cooperative's sources of power:

	2013		2012	
	KWH	Percentage	KWH	Percentage
VDPS - NYPA	9,424,095	10.02%	9,775,599	10.93%
Hydro - Quebec	18,024,130	19.17%	16,079,870	17.98%
Small Power Producers & Ryegate	3,720,376	3.96%	2,758,164	3.08%
Wrightsville	2,994,804	3.19%	2,791,902	3.12%
GMP Rate W - Jones Brook	564,900	0.60%	530,900	0.59%
Coventry Clean Energy Corporation	50,908,300	54.15%	49,394,000	55.24%
Vermont Wind	8,373,658	8.91%	8,084,151	9.04%
	94,010,263	100.00%	89,414,586	100.00%
Load Obligation	77,729,681		76,532,664	
Excess Resources	16,280,582		12,881,922	

GMP Subtransmission Tariff

Following the approval by the PSB and the Federal Energy Regulatory Commission (FERC) of the merger of CVPS and GMP, the merged company filed an updated subtransmission tariff with FERC affecting all wholesale customers including the Cooperative. Seven of the Cooperative’s eight substations are served by GMP. The new tariff increases subtransmission costs by over 80% with the full impact phased in over a period of almost 15 years. The Cooperative has intervened in the FERC case along with two other Vermont utilities, and seeks to lessen the total impact of the increase and its implementation. The parties have been engaged in settlement discussions. The outcome of these discussions resulted in a 15 year phase in of costs and the litigation before FERC is expected to be completed in 2014.

Beginning in 2004, bilateral and settlement markets for Renewable Energy Certificates (RECs) began operating in the ISO-New England region as a result of renewable portfolio standards (RPS) legislation passed in a number of New England states. The markets allow for the renewable attributes of a generation source to be sold separately from the energy itself. RECs are directly associated with the generation of electricity produced or purchased by the Cooperative from qualified resources, particularly the Coventry Project and Vermont Wind’s Sheffield wind project. The Vermont Legislature may at some point establish an RPS. This would require the Cooperative to retire rather than sell a portion of its RECs in future years.

NOTE 8 RENEWABLE ENERGY CERTIFICATES

The Cooperative records proceeds from the sale of RECs in operating revenues. Proceeds for RECs sold are received in subsequent quarters due to the lag time required by the NEPOOL Generation Information System (GIS) and RECs market administrator to accurately account for the RECs generated. In 2011, the Cooperative's Board adopted a portfolio strategy for sale of RECs for 2012 and beyond, and is selling RECs to multiple buyers for varying terms.

At December 31, 2013 and 2012 the Cooperative recorded REC revenue of $2,231,438 and $1,656,757, respectively. There was $741,220 and $742,171 in REC receivables at December 31, 2013 and 2012, respectively.

NOTE 9 BANK DEPOSITS IN EXCESS OF INSURED LIMITS

At December 31, 2013 the Cooperative had uninsured exposure of approximately $282,230 in its cash accounts held by financial institutions. The Cooperative mitigates this exposure through the use of repurchase agreements with an area bank. The bank utilizes a sweep account arrangement. The target balance is $2,500. Amounts in excess of this are swept into the repurchase account whereby the bank invests the excess in U.S. Government Securities. These underlying U.S. Government Securities serve as collateral for the Cooperative based on this agreement. The balance held in the repurchase account at December 31, 2013 was approximately $478,668.

NOTE 10 AMERICAN RECOVERY AND REINVESTMENT ACT (ARRA)

The Cooperative, along with other Vermont electric distribution utilities, and the state's transmission provider, Vermont Electric Power Company (VELCO), applied for and were awarded a Smart Grid Investment Grant (SGIG) from the Department of Energy (DOE) in December 2009. The total award is for $68.9 million dollars state-wide; the distribution utilities and VELCO are obligated to match the award amount; the total state-wide project amount is $137.8 million dollars. The Cooperative's original share of the award was $969,356, which will obligate the Cooperative to provide matching funds from its Construction Work Plan in an equal amount over a period of three years. In January 2011 the Cooperative was notified that up to an additional $1,000,000 in ARRA grant funding would be made available to the Cooperative to implement its Advanced Metering Infrastructure (AMI) proposal. In 2012 the Cooperative was notified that an additional $250,000 was available for its AMI project. The Cooperative included AMI deployment in its current CWP, financing for which was approved by the PSB in 2011. The Cooperative submitted its AMI Plan for approval to the PSB, which approved the plan in early 2012. The Cooperative completed substantially full deployment by late 2013.

NOTE 11 AMORTIZATION OF STRANDED METER COSTS

In 2012, the Cooperative had a net loss on the early retirement of its meters in the amount of $373,587. This loss was due to the fact that the Cooperative began replacing all of its existing meters with an Advanced Metering Infrastructure (AMI), and the old meters were not fully depreciated. The Cooperative received approval from RUS to amortize this loss over a five year period starting in 2012. The amortization of the loss was $72,859 and $74,717 in 2013 and 2012, respectively.

NOTE 12 CHANGE IN ACCOUNTING PRINCIPLE

In 2013, the Cooperative decided to begin recording unbilled revenue for small and large commercial customer accounts in the current period rather than the month subsequent to year end. By doing so the Cooperative is changing to a principle that is considered more acceptable than what had been consistently used in years past. For the year ended December 31, 2013 there is unbilled commercial revenues of $61,704 for 2013 and $63,040 from 2012 recorded in the current year.

NOTE 13 SUBSEQUENT EVENTS

In accordance with professional accounting standards, the Cooperative has evaluated subsequent events through February 25, 2014, which is the date the financial statements were available to be issued. All subsequent events requiring recognition as of December 31, 2013, have been incorporated into the financial statements herein.

ADDITIONAL REPORTS

KBS
Kittell Branagan & Sargent
Certified Public Accountants
Vermont License # 167

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

The Board of Directors
Washington Electric Cooperative, Inc.

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of Washington Electric Cooperative, Inc., which comprise the statement of financial position as of December 31, 2013, and the related statements of operations, equities, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated February 25, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered Washington Electric Cooperative, Inc.'s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of Washington Electric Cooperative, Inc.'s internal control. Accordingly, we do not express an opinion on the effectiveness of Washington Electric Cooperative, Inc.'s internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Washington Electric Cooperative, Inc.'s consolidated financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Kittell Branagan & Sargent

St. Albans, Vermont
February 25, 2014