Washington Electric Cooperative, Inc.

FINANCIAL STATEMENTS

December 31, 2015

Washington Electric Cooperative, Inc.
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KBS
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, 2015 and 2014, 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 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 financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 financial statements.

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

Opinions

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, 2015 and 2014, and the changes in its operations, equities 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 22, 2016 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 22, 2016

Washington Electric Cooperative, Inc.
BALANCE SHEETS
December 31,

ASSETS

	2015	2014
ELECTRIC PLANT, at cost	$ 75,532,498	$ 73,915,896
Less accumulated depreciation	(26,920,800)	(25,291,852)
Electric plant in service, net	48,611,698	48,624,044
Construction work in progress	347,040	349,104
TOTAL ELECTRIC PLANT, net	48,958,738	48,973,148
CURRENT ASSETS		
Cash	726,524	286,034
Receivables -		
Notes, less allowance for doubtful accounts of $1,500 in 2015 and 2014	99	99
Accounts, less allowance for doubtful accounts of $30,500 and $27,500 in 2015 and 2014	1,263,847	1,234,553
Renewable energy certificate revenue	682,848	829,795
FEMA receivable	-	225,300
Miscellaneous	222,240	235,358
Unbilled revenue	621,245	765,586
Inventories	282,472	271,931
Prepaid corporate taxes	62,929	-
Prepaid expenses	248,109	127,330
TOTAL CURRENT ASSETS	4,110,313	3,975,986
OTHER ASSETS		
Other investments	6,786,914	6,756,445
Deferred charges	1,464,231	1,905,898
TOTAL OTHER ASSETS	8,251,145	8,662,343
TOTAL ASSETS	$ 61,320,196	$ 61,611,477

LIABILITIES AND EQUITY

	2015	2014
EQUITIES		
Memberships issued and subscribed	$ 131,445	$ 126,975
Patronage capital assignable	1,273,484	1,295,102
Patronage capital credits	20,972,691	19,989,768
Donated capital	246,854	238,164
NET EQUITY	22,624,474	21,650,009
LONG-TERM DEBT	34,396,706	35,686,450
CURRENT LIABILITIES		
Current portion of long-term debt	2,089,746	2,052,503
CFC line of credit	-	61,981
Accounts payable	1,036,402	1,101,164
Customer deposits	213,179	194,678
Other accrued expenses	766,322	692,699
TOTAL CURRENT LIABILITIES	4,105,649	4,103,025
DEFERRED CREDITS	193,367	171,993
TOTAL LIABILITIES AND EQUITY	$ 61,320,196	$ 61,611,477

See Accompanying Notes to Financial Statements

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

	2015	2014
OPERATING REVENUE		
Member revenue retail sales	$ 13,735,844	$ 13,565,655
Member revenue REC sales	2,917,628	2,934,152
Other	464,859	462,297
TOTAL OPERATING REVENUE	17,118,331	16,962,104
OPERATING EXPENSES		
Purchased power	4,439,913	4,781,634
Power generation	2,130,815	1,783,269
Transmission	95,708	87,118
Distribution:		
Operations, including vehicle depreciation expense of $164,220 and $155,093 in 2015 and 2014, respectively	1,766,347	1,620,868
Maintenance	1,998,454	2,001,198
Customer accounts	880,792	810,806
Administrative and general	1,428,489	1,445,827
Depreciation	2,234,331	2,190,058
Taxes	154,449	153,445
Other deductions, net	6,169	21,658
TOTAL OPERATING EXPENSES	15,135,467	14,895,881
MARGINS FROM OPERATIONS BEFORE INTEREST CHARGES	1,982,864	2,066,223
INTEREST CHARGES		
Interest on long-term debt	1,382,064	1,409,835
Other interest	4,747	7,680
TOTAL INTEREST CHARGES	1,386,811	1,417,515
MARGINS FROM OPERATIONS	596,053	648,708
OTHER INCOME (EXPENSE)		
Interest and dividend income	777,793	717,489
Other non-operating income	74,448	80,628
Other non-operating expense	(174,510)	(89,180)
Income taxes	(300)	(62,543)
TOTAL OTHER INCOME (EXPENSE)	677,431	646,394
NET MARGINS	$ 1,273,484	$ 1,295,102

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, 2013	$ 124,020	$ 1,055,253	$ 19,211,651	$ 229,999
New memberships issued and subscribed for	11,120	-	-	-
Transfers to donated capital	(8,165)	-	-	8,165
Transfers to patronage capital credits	-	(1,055,253)	1,055,253	-
Patronage rebates	-	-	(277,136)	-
Net margins for the year	-	1,295,102	-	-
BALANCE, at December 31, 2014	126,975	1,295,102	19,989,768	238,164
New memberships issued and subscribed for	13,160	-	-	-
Transfers to donated capital	(8,690)	-	-	8,690
Transfers to patronage capital credits	-	(1,295,102)	1,295,102	-
Patronage rebates	-	-	(312,179)	-
Net margins for the year	-	1,273,484	-	-
BALANCE, at December 31, 2015	$ 131,445	$ 1,273,484	$ 20,972,691	$ 246,854

See Accompanying Notes to Financial Statements

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

	2015	2014
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	$ 1,273,484	$ 1,295,102
Noncash expenses (income) included in earnings:		
Depreciation	2,398,551	2,345,151
Amortization of deferred charges	288,300	20,984
Gain on sale of assets	(4,764)	(6,200)
Loss on abandonment	85,377	-
Changes in assets and liabilities:		
Decrease (increase) in accounts receivable	209,124	(138,217)
Decrease (increase) in renewable energy certificate revenue receivable	146,947	(88,575)
Decrease (increase) in unbilled revenue	144,341	4,671
Decrease (increase) in inventories	(10,541)	1,839
Decrease (increase) in prepaid expenses	(183,708)	28,336
Decrease (increase) in deferred debits	122,322	-
Increase (decrease) in accounts payable	(64,762)	84,085
Increase (decrease) in customer deposits	18,501	(9,329)
Increase (decrease) in accrued expenses	73,623	32,631
Increase (decrease) in deferred credit	21,374	16,636
NET CASH PROVIDED BY OPERATING ACTIVITIES	4,518,169	3,587,114
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sales of assets	11,500	6,373
Additions to electric plant in service and construction work in progress	(2,445,208)	(2,280,291)
Return of capital	35,030	35,819
Purchase of investments	(65,500)	(480,321)
NET CASH (USED) IN INVESTING ACTIVITIES	(2,464,178)	(2,718,420)

See Accompanying Notes to Financial Statements

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

	2015	2014
CASH FLOWS FROM FINANCING ACTIVITIES		
Memberships issued, net of refunds	13,160	11,120
Patronage rebates	(312,179)	(277,136)
Proceeds from short-term debt	1,045,725	1,284,235
Payments on short-term debt	(1,107,706)	(1,666,105)
Proceeds from long-term debt	800,000	1,650,000
Principal payments on long-term deb	(2,052,501)	(2,033,237)
NET CASH (USED) BY FINANCING ACTIVITIES	(1,613,501)	(1,031,123)
NET INCREASE (DECREASE) IN CASH	440,490	(162,429)
CASH - Beginning of Year	286,034	448,463
CASH - End of Year	$ 726,524	$ 286,034
SUPPLEMENTARY CASH FLOW INFORMATION		
Cash paid during the year for interest	$ 1,386,839	$ 1,415,875

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).

Accounting Standards Codification 740, Income Taxes (formerly FASB Interpretation No. 48) 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, 2015, 2014, 2013, and 2012 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,:

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

	2015	2014
Intangible plant	$ 609	$ 609
Generation (hydro) plant	3,746,792	3,746,570
Generation (landfill gas) plant	12,275,937	12,379,065
Transmission plant	2,630,969	2,630,969
Distribution plant	51,499,264	49,817,164
General plant	5,378,927	5,341,519
	$ 75,532,498	$ 73,915,896

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.

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

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.

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.

Deferred charges
The Cooperative established deferred charges for costs associated with the recovery of various expenses that are deferred and amortized over a specified number of years. These deferred charges are regulatory in nature and approved by the Board of Directors and Public Service Board and RUS.

NOTE 2 OTHER INVESTMENTS

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

	2015	2014
Investments in associated organizations:		
National Rural Utilities Cooperative Finance Corporation (CFC) membership	$ 1,000	$ 1,000
CFC capital term certificates	444,000	447,203
CFC patronage capital certificates	201,481	173,520
Cooperative Response Center (CRC)	10,000	10,000
CRC patronage capital certificates	1,166	-
National Information Solutions Cooperative patronage capital certificates	88,860	84,002
Patronage capital certificates - other Cooperatives	14,977	15,290
Rural Electric Vermont Association membership	497	497
	761,981	731,512
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	2,488,490	2,488,490
Vermont Transco LLC - Class B membership units	3,167,150	3,167,150
	6,024,933	6,024,933
TOTAL OTHER INVESTMENTS	$ 6,786,914	$ 6,756,445

NOTE 3 LONG-TERM DEBT

Long-term debt at December 31, 2015 and 2014 consists of the following:

	2015	2014
Mortgage notes payable, U.S. Department of Agriculture (RUS) 35-year terms at the following interest rates:		
4.125% mortgage notes, due January 2030	$ 5,234,478	$ 5,506,158

NOTE 3 LONG-TERM DEBT (continued)

	2015	2014
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, 6.1% to 6.45% due quarterly, variable dates through July 1, 2028.	1,306,227	1,453,964
Fixed rate mortgage notes, 2.15% to 4.35% due annually, through June 30, 2031.	12,915,526	13,796,230
Fixed rate mortgage note, 3.0% due annually matures June 30, 2023.	1,346,054	1,503,794
	15,567,807	16,753,988
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.	603,085	678,471
Mortgage notes payable, Federal Financing Bank (FFB) at the following due dates and rates of interest (unadvanced loan funds as of December 31, 2015 and 2014 were $1,250,000 and $2,050,000, respectively):		
4.366% advances, matures December 31, 2033	2,453,478	2,589,783
4.472% advances, matures December 31, 2043	2,505,576	2,595,061
4.272% advances, matures December 31, 2043	1,014,788	1,051,030
3.707% advances, matures December 31, 2043	705,940	731,152
3.328% advances, matures December 31, 2043	541,333	560,667
4.193% advances, matures December 31, 2043	579,664	600,366
3.999% advances, matures December 31, 2043	1,067,907	1,106,047
3.134% advances, matures December 31, 2043	323,845	335,411
2.281% advances, matures December 31, 2046	469,697	484,848
2.418% advances, matures December 31, 2046	751,515	775,757

NOTE 3 LONG-TERM DEBT (continued)

	2015	2014
2.625% advances, matures December 31, 2046	469,697	484,848
2.633% advances, matures December 31, 2046	845,455	872,727
3.411% advances, matures December 31, 2046	939,394	969,697
3.258% advances, matures December 31, 2046	778,279	792,942
2.797% advances, matures December 31, 2046	834,514	850,000
2.655% advances, matures December 31, 2046	800,000	-
	15,081,082	14,800,336
	36,486,452	37,738,953
Less current installments:	(2,089,746)	(2,052,503)
Long-term debt, excluding current installments	$ 34,396,706	$ 35,686,450

In June 2011, the Cooperative's Board of Directors approved the 2012-2015 Construction Work Plan (CWP) authorizing its submittal to RUS together with a financing application for an Federal Financing Bank (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 was due March 31, 2014. The last day for an advance is January 17, 2017 and the final maturity date is December 31, 2046. As of December 31, 2015 there is $1,250,000 available to draw.

In March 2014, the Cooperative’s Board of Directors approved the 2014-2017 CWP. In August 2014, the Cooperative’s Board of Directors authorized the submission of the financing application to RUS for an FFB loan in the amount of $7,141,000 to finance its 2014-2017 CWP. On June 2, 2015, the Cooperative signed the loan documents. For this loan the first principal payment is due June 30, 2017. The last day for an advance is April 1, 2020.

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.

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

NOTE 3 LONG-TERM DEBT (continued)

The following is a schedule of required principal payments on long-term debt in subsequent fiscal years from December 31, 2015:

2016	$ 2,089,746
2017	2,093,808
2018	2,126,149
2019	2,121,851
2020	2,140,715
Thereafter	25,914,183
	$ 36,486,452

Loan covenants

Under the terms of the loan agreements, the Cooperative must maintain at least a times interest earned ratio (TIER) of 1.25 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 1.10 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 2015 and 2014.

Under the terms of the loan agreements 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 2015 and 2014.

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 12, 2016 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, 2015 was 2.9%. The available balance on the note was $2,600,000 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.

NOTE 5 PENSION PLAN (continued)

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 2015 and 2014 represented less than 5 percent of the total contributions made to the RS plan by all participating employers. WEC made contributions to the RS Plan of $496,137 in 2015 and $463,177 in 2014. There have been no significant changes that affect the comparability of 2015 and 2014 contributions. Pension expense for the prior service costs was $8,172 in 2015 and $14,580 in 2014.

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, 2015 and over 80 percent funded on January 1, 2014 based on the PPA funding target and PPA actuarial value of assets on those dates.

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 is included in deferred charges on the balance sheet, was made by the Cooperative during 2013 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.

NOTE 6 COMMITMENTS AND CONTINGENCIES (continued)

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 6, 2013 and an amended IRP on March 21, 2014 to comply with a memorandum of understanding reached with DPS. WEC's filed IRP was approved by the PSB in December 2014. 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 noted 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. WEC's next IRP is due March 31, 2017.

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, 2015 and 2014 the total collected from the Cooperative's members was approximately $802,327 and $744,497, 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.

NOTE 6 COMMITMENTS AND CONTINGENCIES (continued)

Risk Management

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

Coventry Methane Generation Project

The Cooperative owns and CCEC 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.

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, 2015 are:

	Plant Cost	Note Balance
Phase 1 - Initial Construction, Engines 1-3	$ 8,502,732	$ 5,234,478
Phase 2 - Engine 4	1,238,397	603,085
Phase 3 - Engine 5 plus building modifications	4,133,419	2,453,478
Systems Upgrades financed with general funds	313,373	-
	$ 14,187,921	$ 8,291,041

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

Of the $14,187,921 plant cost, $12,275,937 is capitalized to generation plant with the balance included in transmission plant.

In 2015 the Coventry Project provided approximately 59% of the Cooperative's total power supply output which made up 73% of the Cooperative's load requirements as measured by the Independent System Operator of New England (ISO-NE).

NOTE 7 COMMITMENTS AND CONTINGENCIES - POWER SUPPLY (continued)

CCEC has a Landfill Gas Project Agreement with Innovative Energy Systems, Inc. (IES), (now Aria Energy with corporate headquarters in Novi, Michigan). The contract was effective on July 1, 2007. Services provided by Aria 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 Aria is at the rate of 2.426 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. The Cooperative is negotiating with Aria for new contract terms and it seeks to assure continuity of operations at the plant. As part of the negotiations to extend operation and maintenance (O&M) services with Aria and due to unexpected higher maintenance costs currently experienced at the plant, CCEC began to pay increased fees for O&M services effective May 2015. At December 31, 2015 and 2014 the amount included in expense was $1,540,677 and $1,214,826, 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 $101,559 and $118,153 at December 31, 2015 and 2014, respectively. Fixed costs were $93,445 and $109,994 over that same period, respectively. All debt associated with this station has been paid in full as of December 31, 2014.

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, 2015, are as follows.

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") and is now part of SunEdison 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 2015 and served roughly 11% of WEC’s load needs.

NOTE 7 COMMITMENTS AND CONTINGENCIES - POWER SUPPLY (continued)

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 11% of WEC’s total power supply in 2015 and served roughly 14% 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 $964,680 and $1,170,387 at December 31, 2015 and 2014, 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. HQ Schedule B accounted for 15% of WEC’s total power supply in 2015 and served roughly 18% of WEC’s load needs.

WEC, along with other Vermont utilities, petitioned the Vermont Public Service Board in 2010 in Docket 7670 to approve various agreements related to obtaining power from H.Q. Energy Services (US) Inc. through a Purchase Power Agreement (HQUS PPA). WEC is participating as a buyer of power under the Vermont Public Power Supply Authority (VPPSA), through a sub-allocation arrangement. WEC will be allocated energy products from the HQUS PPA through VPPSA in the amount of 4 MW from November 1, 2016 through October 31, 2038.

NOTE 7 COMMITMENTS AND CONTINGENCIES - POWER SUPPLY (continued)

The energy from this contract will be delivered 7 days a week from hour ending 08:00 to hour ending 23:00 on a firm basis through an Internal Bilateral Transaction (IBT) settled through the ISO-NE markets. There is no capacity accompanying the energy, but environmental attributes will be delivered with a minimum guarantee that 90% of the power will come from hydro resources.

WEC has a contract entitlement from this resource of up to 4 MW. Currently WEC assigns this power to Vermont Electric Cooperative (VEC) through a sleeve arrangement. Starting on November 1, 2016, WEC is contractually required to take back this power to meet its load if other committed resources are insufficient. The amount of power WEC must take is specified by a formulaic process in the sleeve agreement. This agreement states:

- WEC must begin to take power back from VEC with a one year notice period if its coverage ratio falls below 97% over the preceding prior 12 month period.

- The amount of power WEC takes back is defined by formula which includes a coverage band tied to the amount of power needed to bring WEC's coverage ratio to 100%.

- Once WEC takes power back, it must retain that power through the end of the contract term in 2038.

- WEC can temporarily take back power in the event of an unplanned outage from an existing resource.

Twelve months after the month the coverage ratio falls below 97%, WEC will begin to take back power up to the amount of the energy deficit for the current month, provided the desired amount of energy falls between the coverage ratio limits. If it falls outside these limits, then the amount WEC will take reflects the coverage band lower or upper bound. Once WEC takes back a certain amount of power, that amount will remain in the WEC resource portfolio.

This calculation is continued each month of the study period. If the coverage band and energy deficit grow, the amount of power needed from the contract increases over prior levels. Accordingly, the amount of power WEC takes back increases until the maximum amount of power (4 MW) is taken back.

WEC power prices under this contract reflect the specific pricing terms in the HQ US contract, including all reference prices, adjustment mechanisms, ratchets, and escalators.

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. The total costs were $8,034 and $27,687 at December 31, 2015 and 2014, respectively. These amounts are included in the total cost above for the Schedule B take or pay costs.

NOTE 7 COMMITMENTS AND CONTINGENCIES – POWER SUPPLY (continued)

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 $393,324 in 2015 and $386,667 in 2014. 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, expired in October 2012. However in 2011 lawmakers through Act 471 mandated the establishment of a standard offer price for certain baseload renewable power. In an Order dated October 29, 2012, the PSB established a standard-offer price schedule for baseload renewable power (Ryegate biomass facility) that is represented by a levelized price of $0.10 per kWh and that included a fuel pass-through mechanism, by which the price will be adjusted to reflect changes in Ryegate's fuel costs. The new contract began November 2012 at the termination of Ryegate's Rule 4.100 contract. The new contract for Ryegate is in effect for ten years from November 2012 through October 2022. WEC is currently being allocated roughly 1.3% 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 provided 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". 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. New net metering laws were passed in 2014. Act 99 increased the limit to 15% of peak demand and provided WEC an opportunity through an "achievement provision" to introduce a separate net metering tariff.

WEC filed a net metering tariff and received approval from the PSB to implement the new program in July 2014. As of December 31, 2015, WEC has 203 members totaling 1,397 kW participating under the original net metering plan (referred to internally as the legacy net metering program). In the new net metering program, WEC has 48 members totaling 299kW participating. WEC's net metering programs combined include 251 members with installations or pending applications and equate to a total of 1,696 kW nameplate rated distributed generation systems.

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 Vermont 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 2.2 MW photovoltaic project was approved by the PSB and is now interconnected to the Cooperative's sub-transmission line in Coventry. WEC plans to institute an Open Access Transmission Tariff for wheeling power from projects connected to its sub-transmission lines to the VELCO grid and to charge for that service.

VELCO

The Cooperative has entered into contracts with the Vermont Electric Power Company, Inc. (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 in 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 $399,600 in Vermont Transco equity units in 2014. There were no equity calls in 2015. Over the next four years, Vermont Transco, LLC, anticipates additional collateral calls. The Cooperatives' estimated investment would be nearly $1.3 million over this period.

In 2012 the PSB approved the merger of Central Vermont Public Service (CVPS) and Green Mountain Power (GMP). 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.

NOTE 7 COMMITMENTS AND CONTINGENCIES – POWER SUPPLY (continued)

Through its joint ownership in VELCO and under the Cooperative's participation in the 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, 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).

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 2015 the Cooperative's energy settlement load obligation with the ISO-NE was 77,007,769 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 2015 totaled 96,237,041 kWh. The following table summarizes the Cooperative's sources of power:

	2015		2014	
	kWh	Percentage	kWh	Percentage
VDPS - NYPA	10,401,850	10.81%	9,872,660	11.06%
Hydro - Quebec	14,097,420	14.65%	16,780,560	18.79%
Small Power Producers & Ryegate	3,556,729	3.70%	3,405,859	3.81%
Wrightsville	2,569,597	2.67%	2,301,693	2.58%
GMP Rate W - Jones Brook	534,300	0.56%	541,400	0.61%
Coventry Clean Energy Corporation	56,325,531	58.53%	47,524,264	53.23%
Sheffield Wind	8,751,614	9.09%	8,858,369	9.92%
	96,237,041	100.00%	89,284,805	100.00%
Load Obligation	77,007,769		77,176,986	
Excess Resources	19,229,272		12,107,819	

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 Cooperative intervened in the FERC case along with two other Vermont utilities, and sought to lessen the total impact of the increase and its implementation. The parties engaged in settlement discussions. The outcome of these discussions resulted in a 15 year phase in of costs and the litigation before FERC was completed in 2014.

NOTE 7 COMMITMENTS AND CONTINGENCIES – POWER SUPPLY (continued)

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 SunEdison's Sheffield wind project. The Vermont Legislature passed legislation in 2015 and created a Renewable Energy Standard (RES) in Act 56. This new law is applicable to the supply portfolios of Vermont electric utilities, with requirements that start in 2017. The RES establishes three categories that utilities must comply with:

- Tier 1: Converts existing total renewables targets into a total renewable energy requirement that rises from 55 percent of a utility's sales in 2017 to 75 percent in 2032. A utility may meet this requirement by owning renewable energy generation or entitlement through a purchase power agreement or renewable energy credits (RECs) from any plant, as long as the plant's energy is capable of delivery to New England.

- Tier 2: Creates a distributed renewable generation category that rises from one percent of a utility's sales in 2017 to 10 percent in 2032. A utility may meet this category through renewable energy generation or entitlement through a purchase power agreement or RECs from plants that come into service after June 30, 2015 and are five MW or less and directly connected to the Vermont utility grid or are net metering systems for which the utility retires the RECs. This category counts toward the total renewable energy category.

- Tier 3: Creates a separate energy transformation category that rises from two percent in 2017 to 12 percent in 2032, except that small municipal utilities will not have to meet this category until 2019. A utility may meet this category through additional distributed renewable generation or "energy transformation projects." Energy transformation projects must have commenced on or after January 1, 2015 and deliver energy goods or services other than electric generation and must result in a net reduction in fossil fuel consumption by a utility's customers and the attributable greenhouse gases. The statute states that energy transformation projects may include home weatherization or other thermal energy efficiency measures, air source or geothermal heat pumps, and other measures.

As part of the legislation there is a provision for utilities like WEC that are already 100 percent renewable to limit the requirements under the distributed generation provision (Tier 2). The law allows utilities that as of January 1, 2015 were 100 percent renewable to have satisfied the distributed generation requirements of Tier 2 as long as they continue to accept applications in a PSB approved net metering tariff. WEC believes it is eligible for this consideration and hence will be relieved of the annual requirement to reach certain levels of distributed generation in Tier 2. Failure to reach the required levels as outlined in the various tiers will result in penalty payments being assessed through an Alternative Compliance Payment (ACP). The first year ACP for Tier 1 is set at $0.01 per kWh and Tier 2 and 3 are set at $0.06 per kWh. The rates increase by CPI annually.

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, 2015 and 2014 the Cooperative recorded REC revenue of $2,917,628 and $2,934,152, respectively. There was $682,848 and $829,795 in REC receivables at December 31, 2015 and 2014, respectively.

WEC sells Class 1 RECs from various resources in its power portfolio, and therefore claims of renewability of those resources (such as wind and landfill gas) are transferred to buyers with the sale of RECs. In order to green back up its mix, WEC purchases lower cost RECs in various Class 2 markets in New England. This allows WEC to retain and claim renewability of the power mix to serve WEC load. WEC only purchases the number of RECs it needs to meet its retail load. WEC has more Class 1 RECs to sell than are needed for load and therefore WEC purchases fewer Class 2 RECs than it sells in the Class 1 markets.

NOTE 9 BANK DEPOSITS IN EXCESS OF INSURED LIMITS

At December 31, 2015 the Cooperative had cash balances of $909,276 of which $516,274 is insured by FDIC, $337,594 is insured by a repurchase agreement and $55,408 is offset by debt. The Cooperative mitigates the exposure of uninsured cash 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.

NOTE 10 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 replaced 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 $74,900 in both 2015 and 2014.

NOTE 11 DECEMBER 2014 STORM COSTS

The Cooperative was impacted by an unprecedented winter storm in December 2014. Heavy wet snow loading brought down trees and power lines. The conditions caused widespread outages, and some of the Cooperative's members suffered from multi-day long interruptions in service. Restoration efforts took over 10 days. Permanent repairs continued into 2015.

NOTE 11 DECEMBER 2014 STORM COSTS (continued)

The storm resulted in restoration costs impacting the income statement totaling $640,837. The storm's impact on the state of Vermont was recognized by the Federal Emergency Management Agency (FEMA) as a national disaster and was declared eligible for public assistance on February 3, 2015. The Cooperative's FEMA reimbursement of eligible expenses is estimated to be 75% of the storm restoration expenses but only for two out of the four counties the Cooperative serves. The Cooperative recorded an estimated receivable of $225,300 from FEMA. The Cooperative received $365,529 from FEMA in 2015.

NOTE 11 DECEMBER 2014 STORM COSTS (continued)

On January 27, 2015 the Vermont Public Service Board issued an accounting order allowing for the deferral of storm costs of up to $526,067. The total amount deferred as of December 31, 2014, net of the receivable, is $225,767 and is categorized as a deferred regulatory asset for future rate recovery and amortization. The funds received from FEMA in 2015 in excess of the estimated receivable were used to offset a portion of the deferral. The remaining balance of the deferral, $85,537 was amortized to the income statement in 2015.

NOTE 12 SUBSEQUENT EVENTS

On January 7, 2016 the Cooperative entered into a sale and purchase agreement with the State of Vermont for the disposal of a .55 acre parcel on the other side of the relocated Rte. 14 from the Cooperative's office building consisting of land and buildings for a cash consideration of $128,000.

In accordance with professional accounting standards, the Cooperative has evaluated subsequent events through February 22, 2016, which is the date the financial statements were available to be issued. All subsequent events requiring recognition as of December 31, 2015, 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, 2015, 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 22, 2016.

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 22, 2016