WASHINGTON ELECTRIC COOPERATIVE, INC.

FINANCIAL STATEMENTS
DECEMBER 31, 2009 AND 2008
AND
INDEPENDENT AUDITOR'S REPORTS

WASHINGTON ELECTRIC COOPERATIVE, INC.

DECEMBER 31, 2009 AND 2008

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Mudgett
Jennett &
Krogh-Wisner, P.C.
Certified Public Accountants #435

INDEPENDENT AUDITOR'S REPORT

The Board of Directors
Washington Electric Cooperative, Inc.

We have audited the accompanying consolidated balance sheets of Washington Electric Cooperative, Inc., and subsidiary, as of December 31, 2009 and 2008 and the related consolidated statements of operations, equities, and cash flows for the years then ended. These financial statements are the responsibility of the Cooperative's management. Our responsibility is to express an opinion on these 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Washington Electric Cooperative, Inc. as of December 31, 2009 and 2008, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards* we have also issued a report dated March 24, 2010, on our consideration of Washington Electric Cooperative Inc.'s internal control over financial reporting and 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Mudgett, Jennett & Krogh-Wisner, P.C.

Montpelier, Vermont
March 24, 2010

141 Main Street • P.O. Box 937, Montpelier, Vermont 05601 • Phone (802) 229-9193

WASHINGTON ELECTRIC COOPERATIVE, INC.
BALANCE SHEETS
DECEMBER 31, 2009 AND 2008
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ASSETS	2009	2008
Electric plant, at cost:		
Electric plant in service	$ 63,296,613	$ 58,014,454
Less accumulated depreciation	18,546,103	17,267,098
Net electric plant in service	44,750,510	40,747,356
Construction work in progress	1,188,225	477,929
Construction work in progress - Coventry engine #5	-	505,015
	1,188,225	982,944
Net electric plant	45,938,735	41,730,300
Other assets:		
Restricted cash (Note 6)	1,907,470	143,435
Other investments (Note 2)	4,681,074	4,040,539
Total other assets	6,588,544	4,183,974
Current assets:		
Cash and cash equivalents	329,570	515,708
Receivables -		
Notes, less allowance for doubtful accounts of $3,000 in 2009 and 2008	1,941	3,699
Accounts, less allowance for doubtful accounts of $22,000 in 2009 and 2008	855,104	945,012
Renewable energy certificate revenue	1,341,469	1,296,806
Miscellaneous	114,984	153,831
Unbilled revenue	704,051	680,693
Inventories	304,823	264,947
Prepaid expenses	86,772	78,021
Total current assets	3,738,714	3,938,717
Deferred debits, net of amortization	306,721	368,041
Total assets	$ 56,572,714	$ 50,221,032

The notes to financial statements are an integral part of these statements.

WASHINGTON ELECTRIC COOPERATIVE, INC.
BALANCE SHEETS
DECEMBER 31, 2009 AND 2008
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	2009	2008
LIABILITIES AND EQUITIES		
Equities:		
Memberships issued and subscribed	$ 108,455	$ 106,530
Patronage capital assignable	654,169	615,254
Patronage capital credits	6,821,356	6,455,940
Donated capital	199,004	189,909
Contributions in aid of construction	9,484,262	9,260,560
Net equity	17,267,246	16,628,193
Long-term debt, excluding current installments (Note 3)	32,607,066	27,877,446
Current liabilities:		
Notes payable (Note 4)	1,378,054	1,075,558
Current installments of long-term debt (Note 3)	1,082,346	1,082,777
Accounts payable	656,679	700,079
Coventry construction accounts payable	616,064	-
Customer deposits	170,017	158,341
Accrued expenses	504,097	482,936
Total current liabilities	4,407,257	3,499,691
Coventry construction accounts payable	-	143,320
Deferred credits	2,291,145	2,072,382
	2,291,145	2,215,702
Commitments and contingencies (Notes 4 and 6)		
Total liabilities and equity	$ 56,572,714	$ 50,221,032

The notes to financial statements are an integral part of these statements.

WASHINGTON ELECTRIC COOPERATIVE, INC.
STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008

	2009	2008
OPERATING REVENUE	$ 13,616,575	$ 13,421,809
OPERATING EXPENSES:		
Purchased power	3,180,956	3,145,065
Power generation	1,256,433	1,247,159
Transmission	22,480	18,735
Distribution -		
Operations	1,352,970	1,248,400
Maintenance	1,459,832	1,507,871
Customer accounts	850,099	1,127,244
Administrative and general	1,345,615	1,242,534
Depreciation	2,022,779	1,896,914
Taxes	412,454	289,473
Other items, net	63,274	62,760
Total operating expenses	11,966,892	11,786,155
Margins from operations before interest charges	1,649,683	1,635,654
INTEREST CHARGES:		
Interest on long-term debt	1,463,722	1,365,499
Other interest	23,572	29,962
Total interest charges	1,487,294	1,395,461
Margins from operations	162,389	240,193
OTHER INCOME (EXPENSE):		
Interest and dividend income	445,752	370,225
Other nonoperating income	72,222	58,042
Other nonoperating expense	(26,066)	(47,562)
Income taxes	(128)	(5,644)
Total other income	491,780	375,061
Net margins	$ 654,169	$ 615,254

The notes to financial statements are an integral part of these statements.

WASHINGTON ELECTRIC COOPERATIVE, INC.
STATEMENTS OF EQUITIES
FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008

			Other Equities		
	Memberships Issued and Subscribed	Patronage Capital Assignable	Patronage Capital Credits	Donated Capital	Contributions in Aid of Construction
BALANCE, December 31, 2007	$ 101,475	$ 805,996	$ 5,991,688	$ 183,964	$ 8,945,102
New memberships issued or subscribed for	11,000	-	-	-	-
Transfers to donated capital	(5,945)	-	-	5,945	-
Transfers to patronage capital credits	-	(805,996)	805,996	-	-
Patronage rebates	-	-	(341,744)	-	-
Net margins for the year	-	615,254	-	-	-
New contributions in aid of construction, net	-	-	-	-	315,458
BALANCE, December 31, 2008	106,530	615,254	6,455,940	189,909	9,260,560
New memberships issued or subscribed for	11,020	-	-	-	-
Transfers to donated capital	(9,095)	-	-	9,095	-
Transfers to patronage capital credits	-	(615,254)	615,254	-	-
Patronage rebates	-	-	(249,838)	-	-
Net margins for the year	-	654,169	-	-	-
New contributions in aid of construction, net	-	-	-	-	223,702
BALANCE, December 31, 2009	$ 108,455	$ 654,169	$ 6,821,356	$ 199,004	$ 9,484,262

The notes to financial statements are an integral part of these statements.

WASHINGTON ELECTRIC COOPERATIVE, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008
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	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net margins	$ 654,169	$ 615,254
Noncash items included in earnings -		
Depreciation	2,022,779	1,896,914
Amortization of deferred charges	36,237	35,723
Loss (Gain) on disposal of assets	(36,382)	-
Restricted cash interest income	(14,035)	(3,876)
Changes in assets and liabilities -		
Decrease (increase) in accounts receivable	128,755	(383,270)
Decrease (increase) in renewable energy certificate revenue receivable	(44,663)	(226,721)
Decrease (increase) in unbilled revenue	(23,358)	1,023,028
Decrease (increase) in inventories	(39,876)	69,742
Decrease (increase) in prepaid expenses	(8,751)	(34,413)
Decrease (increase) in deferred debits	(4,595)	(106,111)
Increase (decrease) in accounts payable	429,344	221,155
Increase (decrease) in customer deposits	11,676	2,985
Increase (decrease) in accrued expenses	21,161	(28,799)
Increase (decrease) in deferred credits	218,763	284,537
Net cash provided by operating activities	3,351,224	3,366,148
CASH FLOWS FROM INVESTING ACTIVITIES:		
Retirement of notes receivable	1,758	2,818
Proceeds from sale of assets	37,798	-
Additions by construction work in progress	(5,514,944)	(2,081,659)
Additions to electric plant in service	(531,680)	(647,594)
Retirements of electric plant in service	(156,328)	(156,776)
Return of capital	54,457	71,509
Purchase of investments	(694,992)	(515,919)
Net cash used in investing activities	(6,803,931)	(3,327,621)

The notes to financial statements are an integral part of these statements.

WASHINGTON ELECTRIC COOPERATIVE, INC.
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008
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		2009		2008
CASH FLOWS FROM FINANCING ACTIVITIES:				
Contributions in aid of construction		223,702		315,458
Memberships issued, net of refunds		11,020		11,000
Patronage rebates		(249,838)		(341,744)
Deposits in restricted cash		(1,750,000)		-
Proceeds from short-term debt		2,730,666		3,018,523
Payments on short-term debt		(2,428,170)		(3,930,140)
Proceeds from Coventry financing		2,859,000		276,000
Proceeds from long-term debt		2,953,000		1,918,241
Principal payments on long-term debt		(1,082,811)		(1,085,474)
Net cash provided by financing activities		3,266,569		181,864
Net increase (decrease) in cash and cash equivalents		(186,138)		220,391
CASH AND CASH EQUIVALENTS, beginning of year		515,708		295,317
CASH AND CASH EQUIVALENTS, end of year	$	329,570	$	515,708

SUPPLEMENTAL CASH FLOW INFORMATION

Cash paid during the year for interest	$	1,487,294	$	1,395,115
Long-term financing payments of Coventry lines of credit	$	2,847,000	$	957,530

The notes to financial statements are an integral part of these statements.

1. Summary of significant accounting policies:

Washington Electric Cooperative, Inc. ("the Cooperative") provides residential and commercial electrical service to its patrons. 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 they have 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 financial statements.

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

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.

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, 2009 and 2008:

	2009	2008
Intangible plant	$ 609	$ 609
Generation (hydro) plant	3,731,366	3,729,820
Generation (landfill gas) plant	12,544,674	8,287,552
Transmission plant	2,282,067	2,248,609
Distribution plant	40,525,438	39,453,135
General plant	4,212,459	4,294,729
	$ 63,296,613	$ 58,014,454

1. Summary of significant accounting policies (continued):

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	2.5%
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 are accounted for as a component of patrons' equity rather than as a reduction of electric plant in service. 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.

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

2. Other investments:

Other investments include the following, at cost, at December 31, 2009 and 2008:

	2009	2008
Investments in associated organizations:		
National Rural Utilities Cooperative Finance Corporation (CFC) membership	$ 1,000	$ 1,000
CFC capital term certificates	460,511	462,705
CFC patronage capital certificates	104,879	96,576
NISC patronage capital certificates	49,500	47,547
Patronage capital certificates - other Cooperatives	8,508	6,361
Rural Electric Vermont Association membership	497	497
	624,895	614,686
Other investments:		
Vermont Electric Power Company - common stock, Class B	265,600	259,600
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	1,549,980	1,256,410
Vermont Transco LLC - Class B membership units	1,972,690	1,599,070
Central VT Memorial Civic Center - rural economic develop. loan	164,216	207,080
	4,056,179	3,425,853
	$ 4,681,074	$ 4,040,539

3. Long-term debt:

Long-term debt at December 31, 2009 and 2008 consists of the following:

	2009	2008
Mortgage notes payable, U.S. Department of Agriculture (RUS), 35-year terms at the following interest rates:		
5.0% mortgage notes	$ 17,309,910	$ 17,788,986
4.125% mortgage note	6,708,750	6,920,958
	24,018,660	24,709,944
Mortgage notes payable, National Rural Utilities Cooperative Finance Corporation (CFC), 35-year terms due between 2010 and 2028 at the following rates of interest:		
Fixed rate mortgage notes, 5.8% to 6.85% due quarterly, variable dates through July 1, 2028	2,080,020	2,195,046
Fixed rate mortgage notes, 4.6% to 4.85% due annually through December 31, 2011	106,551	229,490
	2,186,571	2,424,536

3. Long-term debt (continued):

	2009	2008
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	1,055,400	1,130,785
Line of credit for Coventry fifth engine construction, interest rate 5.0% at December 31, 2008, to be converted to Federal Financing Bank long-term debt	-	276,000
Mortgage notes payable, Federal Financing Bank (FFB) - at the following due dates and rates of interest: (unadvanced loan funds as of December 31, 2009 and 2008 were $4,947,000 and $0, respectively)		
4.287% to 8.335% advances, matures December 31, 2014	176,565	211,878
4.366% advances, matures December 31, 2034	3,135,000	-
4.472% advances, matures December 31, 2043	2,953,000	-
	6,264,565	211,878
Rural economic development loan, non-interest bearing, U.S. Department of Agriculture (RUS) loan:		
CVMCC-Payable in 168 monthly payments of $3,572 starting November 1999 through October 2013	164,216	207,080
	33,689,412	28,960,223
Less current installments	(1,082,346)	(1,082,777)
Long-term debt, excluding current installments	$ 32,607,066	$ 27,877,446

In January 2008, the Cooperative's Board of Directors approved the 2008-2011 Construction Work Plan (CWP) authorizing its submittal to RUS together with a financing application for a Federal Financing Bank (FFB) loan in the amount of $7.9 million. On February 11, 2009, the Cooperative signed the loan documents. The 2008-2011 Work Plan had an available balance of $4,947,000 at December 31, 2009. In February 2010, the Cooperative drew down an advance of $1,196,000 on this loan.

The Cooperative also signed on February 11, 2009 loan documents for the $3.135 million FFB loan used to finance the Coventry fifth engine. The balance of this loan fund was fully drawn in June 2009.

For both 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. The CWP loan must be fully paid by December 31, 2043. The Coventry fifth engine loan must be fully paid by December 31, 2034.

The available balance on the Coventry fifth engine line of credit was $2,724,000 at December 31, 2008. The Cooperative drew an additional $2,571,000 on this line of credit in 2009. The note was fully paid in June 2009.

3. Long-term debt (continued):

On February 8, 2008, the Cooperative received proceeds from the Cooperative Finance Corporation (CFC) issuance of CFC Clean Renewable Energy Bonds (CREBs) for the purpose of financing the cost of installing a fourth engine at the Coventry Generation Plant. The long-term financing note payable of $1,206,171 net of deferred debit bond costs of $98,698 was used to pay off the balance of the Coventry fourth engine line of credit on February 12, 2008, the balance of which was $957,530 at December 31, 2007. The loan is payable to CFC in quarterly level payments from March 2008 through December 2023. The nominal interest rate on the bonds is 0.400% and the effective interest rate is 1.494% per year. The bond costs are amortized over the life of the loan.

In November 1999, The Cooperative obtained a non-interest bearing rural economic development loan from the RUS 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.

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, 2009:

Year ending December 31,	
2010	$ 1,082,346
2011	1,276,034
2012	1,298,152
2013	1,337,464
2014	1,350,692
Thereafter	27,344,724
	$ 33,689,412

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 2009 and 2008.

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 these requirements in 2009 and 2008.

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 16, 2010. 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, 2009 was 4.95%. The available balance on the note was $1,221,946 at year end.

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. Contributions to the retirement plan from the Cooperative for the employees are recorded as pension expense. Pension expense was $396,523 for 2009 and $320,199 for 2008. Pension expense for the prior service costs was $14,580 for 2009 and 2008.

6. Commitments and contingencies:

<u>Regulatory matters</u> -

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 IRP projects the Cooperative's load and power supply requirements, and identifies committed and preferred resource options for the future, including demand-side management resources and renewables such as increased Coventry Project power and wind power. The Cooperative filed its first IRP in January 1992. As a result of PSB Docket 6290, a new IRP methodology and format was created for all utilities. The Cooperative filed its second IRP with the PSB in October 2003, and approval of the IRP under Docket 6896 was received in June 2005. The 2005 IRP supported the need for the Coventry (Methane Generation) Project, discussed below, which came on-line in July 2005. The IRP also identified future power supply needs. The Cooperative filed its most recent IRP on February 15, 2008. A stipulation regarding approval was entered with the DPS in August 2009; the plan and stipulation are still pending approval by the PSB in Docket 7432.

In 1999, the Public Service Board ordered the establishment of the Energy Efficiency Utility (EEU), which began operating in February 2000 under the name "Efficiency Vermont" ("EVT"). Certain efficiency services, primarily for commercial, industrial and multi-family housing, are now operated by the EEU and are no longer the responsibility of the Cooperative. In 2003, the "Residential New Construction Program," that had previously been part of the Cooperative's portfolio of services, became the responsibility of the EEU. The Cooperative continues to perform certain services associated with this program, as a subcontractor to the EEU. Pursuant to an order from the PSB, all Vermont utilities collect a monthly surcharge called the Energy Efficiency Charge (EEC) from customers. The total collected from the Cooperative's members was approximately $450,338 in 2009 and $450,000 in 2008. This amount is forwarded to a fiscal agent selected by the PSB and is not revenue to the Cooperative.

6. Commitments and contingencies (continued):

In October 2009, the Cooperative filed with the Public Service Board a Cost of Service Study and Rate Design proposal. The proposal is revenue neutral, but makes changes in allocations among rate classes as well as a number of other changes. For residential members, the proposal maintains the inclining rate structure the Cooperative presently has in place, while making changes based on the Cost of Service study. The Public Service Board opened Docket No. 7575 to consider the proposal and is likely to issue a decision in 2010.

Employee Benefits -

In December 2008, the Cooperative decided to change health care insurance providers effective January 1, 2009. As a result, the Cooperative discontinued the "high deductible with Health Savings Account" plan that had been in effect in 2007 and 2008, and changed to a more traditional premium-based plan.

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. The Cooperative manages these risks through commercial insurance packages purchased in the name of the Cooperative.

Power Supply -

Proposed First 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 Cooperative finalized a long-term Purchased Power Agreement with Vermont Wind in September 2009. The contract was filed by Vermont Wind with the PSB in June 2009 and the PSB approved it, in Docket 7156, in August 2009. It is hoped that the project will begin generating by the end of 2011.

Coventry Methane Generation Project -

The Cooperative owns and operates a generating facility powered by landfill gas at the Coventry Landfill in northern Vermont. A set of contractual agreements was executed in October 2003 between a wholly-owned special purpose subsidiary of the Cooperative, the Coventry Clean Energy Corporation (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 related to a generation facility at the Coventry Landfill, now owned and operated by CCEC. Briefly, these agreements provided that: (1) the Cooperative would finance and build the generation and transmission facilities; (2) CCEC would buy the gas collection system from NEWSVT; (3) CCEC would operate the generation facility and transmission interconnection after leasing them from the Cooperative. CCEC would further lease the gas rights and related easements, and the section of the landfill property on which the generation facility is located, from NEWSVT; and, (4) the Cooperative would purchase all the electrical output generated by CCEC (as well as any related renewable energy certificates (RECs), tax credits or other environmental attributes) on behalf of its patrons. These components are collectively referred to as the "Coventry Project".

6. Commitments and contingencies (continued):

In January 2005, the Cooperative and CCEC signed the following documents: (1) the Equipment and Facilities Lease whereby the Cooperative leases the generation and transmission interconnection to CCEC for a 33-year term with optional two-year term extensions; (2) the Electric Supply Agreement under which the Cooperative purchases all of the power and output generated by CCEC for a 33-year term with optional two-year term extensions. The Electric Supply Agreement was subsequently modified in January 2006 to eliminate the capacity charge; (3) the Promissory Note in the amount of $286,675 from the Cooperative to CCEC, which was used by CCEC to purchase the gas collection from NEWSVT and Casella Waste Systems, Inc. under a Facility Acquisition Agreement entered into as of October 3, 2003. The note has an interest rate of 5% and is payable in 30 equal quarterly installments beginning with the first full calendar quarter following the date that CCEC first produces power, and is expected to be retired on schedule in 2013; and, (4) the Security Agreement that grants the Cooperative a security interest in all properties, assets and rights of CCEC.

A fourth engine was added to the initial three engines and went on line in January 2007 increasing the plant's gross rated output to 6.4 MW. The costs were funded by long-term borrowing from CFC, as described in Note 3, under CFC's implementation of the Clean Renewable Energy Bond (CREB) program created under the Energy Tax Incentives Act of 2005.

In September 2008, the Cooperative received approvals from the PSB in Docket 7455, and from members at a vote held on October 7, 2008, to further increase the output from the Coventry Project by adding a fifth 1.6 MW engine to the facility. Construction began shortly after these approvals and the fifth engine went on line in June 2009, increasing the plant's gross rated output to 8.0 MW. The cost of this planned expansion was approximately $4.1 million. A portion of the financing, $3.1 million was approved by the Rural Utilities Service under the terms and conditions of a guaranteed loan to the Cooperative from the Federal Financing Bank, as described in Note 3. The remaining $1 million will be financed from the Cooperative's 2008-2011 Construction Work Plan by diverting funds previously earmarked for distribution projects to generation assets. The additional financing was necessary to support improvements to the gas collection system and building modifications in order to increase the production of methane at the plant.

The Coventry Project now provides more than 67% of the Cooperative's net energy requirements, an amount that should increase going forward.

CCEC entered into a new 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 with an automatic renewal for eight years. Compensation to IES is at the rate of 2.2 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 amount included in expense was $1,160,368 for 2009 and $1,101,345 for 2008.

<u>Other purchased power sources</u> -

<u>Wrighstville Hydro</u> - Besides the Coventry Project, the Cooperative also owns and operates the Wrightsville Hydroelectric Generation Station in Montpelier, Vermont, a largely run-of-the-river project that has a rated capacity of 933 kW, though it provides significantly less average output because it is dependent on precipitation and weather conditions during the year. Operating costs were $74,952 in 2009 and $75,105 in 2008. Fixed costs were $147,737 in 2009 and $146,328 in 2008.

6. Commitments and contingencies (continued):

The remaining energy needs of the Cooperative are provided by other utilities 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, 2009, are as follows.

NYPA - The Cooperative receives power from the 912 MW 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 new long-term contract it executed in 2007. The Cooperative anticipates no reductions in NYPA power supply going forward under the latest agreement, except when low water conditions exist. When such 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, particularly transmission-related, costs have increased in recent years.

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' 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 point. 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 $1,134,275 in 2009 and $1,198,265 in 2008.

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 foresees no exercise of the option in 2010.

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. The Cooperative continues to pay for the operating and maintenance expenses of the Highgate converter. In 2009, there was a credit of $28,716 in 2009 and an expense of $21,041 in 2008. These amounts are included in the total cost listed above for the Schedule B take or pay costs.

6. Commitments and contingencies (continued):

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 in 2008 $482,740 in Vermont Transco membership units, of which $297,500 was related to a settlement among certain Vermont utilities regarding the shared costs of the Lamoille County Project, and $185,240 was the Cooperative's share of an equity call to all Vermont utilities. In 2009, the Cooperative purchased an additional $667,190 in Vermont Transco equity units.

Small Power Producers - Vermont Public Service Board 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. This obligation, which for the Cooperative amounts to approximately 1% of the total small power producers' output, was $552,540 in 2009 and $640,521 in 2008 and is expected to increase moderately in the next couple of years, before declining beginning in 2013, according to the contracts that the state purchasing agent, currently the Vermont Electric Power Producers Inc. (VEPPI), has with the small power producers. Those contracts are expected to expire fully in the next eleven years.

The Cooperative, like all other utilities in New England, relies upon the New England Power Pool (NEPOOL), operator of the New England regional bulk transmission system, to receive power supply from outside Vermont. The Cooperative also relies upon the Independent System Operator of New England (ISO-NE), to effect economic dispatch of the regional power supply within New England and for wholesale spot purchases and sales of power in Vermont. NEPOOL and ISO-NE administer the operation of electric power supply and transmission facilities and the wholesale power supply and transmission markets in 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 power supply resources are combined in the CDA with other VPPSA participants, and dispatched as a group by ISO-NE. The CDA is intended to provide pooling savings to its members by taking advantage of supply and load diversity, where under the supply sources and loads of all of its Vermont participants are aggregated into a single entity for the purpose of ISO-NE settlement calculations. However, the VPPSA CDA does not socialize the group settlement, rather each utility participant is resettled thereunder based on its own loads and resources. 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).

6. Commitments and contingencies (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 for automatic hourly purchases and sales whenever they are energy deficient or have excess. The energy markets became locational in March 2003. Since then, generators in New England receive hourly locational marginal prices (LMPs) for energy production that are based on local supply and demand conditions, while load-serving entities (LSEs) like the Cooperative pay hourly zonal average LMPs for energy and related ancillary products based on the supply and demand conditions within their zone. Vermont is one of multiple zones in the ISO-NE system. New ISO-NE markets and rules continue to develop and undergo implementation. For example, ISO-NE received in 2006 approval from FERC to implement long-term, auction-based markets for forward reserves (an ancillary energy service) and forward installed capacity, both products with locational features. Those markets began implementation or transition to implementation in late 2006. Redesign of both markets, especially the forward installed capacity market, has increased the cost of these non-energy products.

The ISO-NE spot and longer-term markets augment the long-term power supply resources and agreements, and occasional shorter-term bilateral hedge contracts, that have been and are still used by the Cooperative to meet its power requirements. In particular, the Cooperative periodically hedges its market price exposure by contracting bilaterally for installed capacity and energy requirements, or entering into other financial hedges, while the balance of its needs are met with spot purchases and sales. This strategy limits, but does not entirely eliminate, the Cooperative's exposure to short-term market price and short-term and extraordinary fuel price variations. Furthermore, even bilateral or financial hedge contract prices can be subject to some volatility over the year, as they are driven by the volatile forward market price expectations for electricity and especially the underlying fuels used to generate electricity. However, consistent with its strategy to minimize exposure to volatility, the Cooperative's reliance on ISO-NE spot market purchases has been significantly reduced since the Coventry Landfill Gas Generation Project began operations in July 2005. In fact, since the Coventry Project's fourth engine has been in production, the Cooperative has had a surplus of energy relative to demand on an annual basis, selling back more energy to the spot market than it purchases on an hourly basis.

The percentage of power by source and kilowatt hour purchases of 75,132,917 in 2009 and 74,914,859 in 2008 is as follows:

	2009		2008	
	KWH	Percentage	KWH	Percentage
VDPS-NYPA	10,866,964	14.46	11,762,681	15.70
Hydro-Quebec	16,734,090	22.27	17,071,770	22.79
McNeil	-	-	2,229,656	2.98
Small Power Producers	4,164,396	5.54	4,462,541	5.95
Wrightsville	3,558,301	4.74	3,400,615	4.54
GMP Rate W - Jones Brook	581,400	0.77	568,300	0.75
Transmission Line Losses	(1,729,438)	(2.30)	(1,558,997)	(2.08)
VPPSA-CDA	(9,548,556)	(12.70)	(12,230,484)	(16.32)
	24,627,157	32.78	25,706,082	34.31
Purchased from Subsidiary - Coventry Clean Energy Corporation	50,505,760	67.22	49,208,777	65.69
	75,132,917	100.00	74,914,859	100.00

6. Commitments and contingencies (continued):

Renewable Energy Certificates

Beginning in 2004, bilateral and settlement markets for Renewable Energy Certificates (RECs) began operating in the New England ISO 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.

In late 2004, the Cooperative reached an agreement with the Cape Light Compact of Massachusetts for sale of the RECs from the Coventry facility in 2005-2006, with an option for 2007 and beyond, which Cape Light Compact did exercise. In 2007, the Cooperative and Cape Light Compact entered into a new contract for the sale of RECs associated with the Coventry facility for the years 2008-2011. The Cooperative records proceeds from the sale of RECs available from its Coventry Landfill Gas project in operating revenues. Proceeds for RECs sold are received in subsequent quarters due to the time required by the NEPOOL Generation Information System (GIS) and RECs market administrator to accurately account for the RECs generated.

The Cooperative sold $2,600,920 in 2009 and $2,534,203 in 2008 in RECs associated with the Coventry facility. There was $1,341,469 and $1,296,806 in REC receivables at December 31, 2009 and December 31, 2008 respectively.

In anticipation of additional generation and RECs resulting from the installation of the fifth engine, the Cooperative and Cape Light Compact reached an agreement in 2009 for sale of any additional RECs above 13,875 MWh per quarter at different terms than for the base output. However, no sales occurred during 2009 under the new provision. The contract also contains a provision that allows the contract price to be reset in 2010 and/or 2011 if market prices for RECs fall below a specified amount. At this time, it is not known whether such a reset will occur.

The Cooperative received RUS approval and an Accounting Order from the PSB in 2005 for a Rate Stabilization Plan. The plan allows the Cooperative to annually defer REC revenue from 2004 through 2009 in excess of what is needed to meet its lenders' requirements. The Cooperative deferred $200,000 and $220,000 of the revenue from the sale of REC's in 2009 and 2008, respectively. At December 31, 2009 the balance in this restricted account was $1,907,470. The Cooperative will begin drawing down these revenues in 2010 when margins are expected to be insufficient to cover lender requirements. The Cooperative anticipates filing in 2010 for a rate increase.

At December 31, 2009, the Cooperative had an uninsured/uncollateralized exposure of approximately $775,000 in its cash accounts. In 2009, the Cooperative adopted a policy specific to the Deferred Revenue Investments which stated investments will be based on a portfolio approach with the majority of the investments being held in secure options, not necessarily FDIC or NCUSIF insured accounts. The National Rural Utilities Cooperative Finance Corporation (NRUCFC) Commercial Paper was deemed as one such secure investment. The balance in NRUCFC's Commercial Paper at December 31, 2009 was approximately $600,000. The Policy also allowed funds to be deposited into a socially responsible investment option, not to exceed 10% of the portfolio. The Cooperative invested $50,000 in the Vermont Community Loan Fund Investment Account in 2009.

6. Commitments and contingencies (continued):

Contributions in Aid of Construction, PSB Docket No. 7554

In 2009, the Public Service Board 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). This may result in future changes in how CIAOC is accounted for, as described in Note 1.

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 share of the award is $969,356, which will obligate the Cooperative to match funds from its Construction Work Plan in a like amount over a period of three years.

7. Reclassifications

Certain prior year amounts in these financial statements have been reclassified to be more comparable to the current year balances.

Mudgett
Jennett &
Krogh-Wisner, P.C.
Certified Public Accountants #435

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 the consolidated financial statements of the Washington Electric Cooperative, Inc. (the Cooperative) as of and for the year ended December 31, 2009, and have issued our report thereon dated March 24, 2010. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Cooperative's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Cooperative's internal control over financial reporting.

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 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.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Cooperative's consolidated financial statements are free of 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.*

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We noted certain matters that we reported to management of the Cooperative in a separate letter dated March 24, 2010.

This report is intended solely for the information and use of the Board of Directors and management of Washington Electric Cooperative, the Rural Utilities Service, and supplemental lenders and is not intended to be and should not be used by anyone other than these specified parties.

Mudgett, Jennett & Krogh-Wisner, P.C.

Montpelier, Vermont
March 24, 2010