PRESQUE ISLE ELECTRIC & GAS CO-OP

REPORT ON FINANCIAL STATEMENTS

YEARS ENDED DECEMBER 31, 2011 AND 2010

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PRESQUE ISLE ELECTRIC & GAS CO-OP
BOARD OF DIRECTORS
DECEMBER 31, 2011

John F. Brown	Chairperson
Allen L. Barr	Vice Chairperson
David W. Smith	Secretary
Daryl Peterson	Treasurer
Robert W. Wegmeyer	Director
Allan Berg	Director
Bernice C. Krajniak	Director
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Sally Knopf	Director

President & Chief Executive Officer

Brian J. Burns

HARRIS GROUP
Certified Public Accountants

Independent Auditor's Report

The Board of Directors
Presque Isle Electric & Gas Co-op
Onaway, Michigan

We have audited the accompanying balance sheets of **Presque Isle Electric & Gas Co-op** as of December 31, 2011 and 2010, and the related statements of revenue and patronage capital, and cash flows for the years then ended. These financial statements are the responsibility **of Presque Isle Electric & Gas Co-op'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 audit 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 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 **Presque Isle Electric & Gas Co-op** as of December 31, 2011 and 2010, 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.

Harris Group

Certified Public Accountants
March 15, 2012

PRESQUE ISLE ELECTRIC & GAS CO-OP
BALANCE SHEETS
DECEMBER 31, 2011 AND 2010

	2011	2010
ASSETS		
UTILITY PLANT:		
In-Service – at cost	$ 120,682,867	$ 117,331,926
Construction work in progress	852,911	654,672
SUBTOTAL	121,535,778	117,986,598
Less accumulated depreciation and amortization	45,954,018	42,985,018
NET UTILITY PLANT	75,581,760	75,001,580
OTHER ASSETS AND INVESTMENTS		
Investments on associated organizations	20,885,708	20,330,630
CURRENT ASSETS:		
Cash and temporary cash investments	$ 1,830,054	1,577,131
Accounts Receivable, less allowance for possible losses of $118,000 in 2011 and 2010.	4,725,144	4,910,699
Materials and supplies (at average cost)	1,285,871	1,233,075
Other current assets	292,889	122,217
TOTAL CURRENT ASSETS	8,133,958	7,843,122
DEFERRED DEBITS	155,512	177,497
TOTAL ASSETS	$ 104,756,938	$ 103,352,829

The accompanying notes are an integral part of these statements.

	2011	2010
EQUITIES AND LIABILITIES		
EQUITIES:		
Memberships	$ 233,595	$ 227,440
Patronage capital	38,937,908	37,823,325
Other equities	(1,301,485)	(1,571,251)
TOTAL EQUITIES	37,870,018	36,479,514
LONG-TERM DEBT, NET OF CURRENT MATURITIES:		
Mortgage notes to National Rural Utilities Cooperative Finance Corporation (CFC)	50,559,819	52,422,254
Accrued post – retirement benefits	2,923,738	2,815,152
TOTAL LONG-TERM DEBT	53,483,557	55,237,406
CURRENT LIABILITIES:		
Current maturities of long-term debt	1,888,300	1,788,000
CFC line of credit	6,200,310	5,056,478
Accounts payable, purchased energy	2,416,786	2,305,001
Accounts payable, other	370,984	315,305
Patronage capital payable		
Customer deposits	339,378	303,186
Accrued property taxes	446,614	438,153
Accrued interest	362,326	357,993
Accrued sick and vacation pay	529,592	563,326
Accrued other	432,519	263,743
TOTAL CURRENT LIABILITIES	12,986,809	11,391,185
DEFERRED CREDITS	416,554	244,724
TOTAL EQUITIES AND LIABILITIES	$ 104,756,938	$ 103,352,829

PRESQUE ISLE ELECTRIC & GAS CO-OP
STATEMENTS OF REVENUE
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

	2011	2010
OPERATING REVENUES	$ 40,303,746	$ 38,555,890
OPERATING EXPENSES:		
Cost of energy	23,596,605	23,085,268
Distribution – operation	1,204,016	1,167,656
Distribution – maintenance	3,461,054	3,328,321
Consumers accounts	1,599,022	1,699,273
Customer service and information expense	472,386	442,083
Administrative and general	1,641,310	1,600,432
Depreciation and amortization	3,267,176	3,149,984
Taxes – property	1,016,906	1,002,340
Taxes – other	74,474	74,303
TOTAL OPERATING EXPENSES	36,332,949	35,549,660
OPERATING MARGIN BEFORE FIXED CHARGES	3,970,797	3,006,230
FIXED CHARGES:		
Interest	3,151,240	3,183,335
Other deductions		509
TOTAL FIXED CHARGES	3,151,240	3,183,844
OPERATING MARGINS AFTER FIXED CHARGES	819,557	(177,614)
CAPITAL CREDITS:		
Generation and transmission capital credits	1,106,541	
Other capital credits	387,422	389,126
TOTAL CAPITAL CREDITS	1,493,963	389,126
NET OPERATING MARGINS	2,313,520	211,512

The accompanying notes are an integral part of these statements.

PRESQUE ISLE ELECTRIC & GAS CO-OP
STATEMENTS OF REVENUE
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010
(Continued)

	2011	2010
NET OPERATING MARGINS (from previous page)	$ 2,313,520	$ 211,512
NON-OPERATING MARGINS:		
Interest and dividend income	60,411	60,446
Other	(295,732)	(167,865)
TOTAL NON-OPERATING MARGINS	(235,321)	(107,419)
NET MARGINS	$ 2,078,199	$ 104,093

The accompanying notes are an integral part of these statements.

PRESQUE ISLE ELECTRIC & GAS CO-OP
STATEMENT OF CHANGES IN PATRONAGE CAPITAL
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

	Memberships	Patronage Capital	Other Equities	Accumulated Other Comprehensive Loss	Total
Balance, January 1, 2010	$ 221,615	$ 37,713,491	$ 788,009	$ (2,359,330)	$ 36,363,785
Capital credits retired					
Memberships retired	5,825				5,825
Other equity transactions		5,741	70		5,811
Net margin		104,093			104,093
Balance, December 31, 2010	227,440	37,823,325	788,079	(2,359,330)	36,479,514
Capital credits retired		(963,309)	269,459		(693,850)
Memberships retired	6,155				6,155
Other equity transactions		(307)	309		
Amortize other comprehensive Loss					
Net margin		2,078,199			2,078,199
Balance, December 31, 2011	$ 233,595	$ 38,937,908	$ 1,057,845	$ (2,359,330)	$ 37,870,018

The accompanying notes are an integral part of these statements.

PRESQUE ISLE ELECTRIC & GAS CO-OP
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash received from consumers	$ 40,434,565	$ 38,424,665
Cash paid to suppliers and employees	(31,220,331)	(30,889,184)
Interest received	60,411	60,446
Interest paid	(3,281,902)	(3,306,910)
Taxes paid	(1,311,519)	(1,317,696)
Net Cash Provided by Operating Activities	4,681,224	2,971,321
CASH FLOWS FROM INVESTING ACTIVITIES:		
Construction and acquisition of plant	(3,774,458)	(3,731,081)
Plant removal costs	(37,657)	(284,571)
(Increase) decrease in:		
Material inventory	(52,796)	(120,146)
Investments – associated organizations	938,885	192,242
Net Cash Used In Investing Activities	(2,926,026)	(3,943,556)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Advances	21,443,831	25,521,230
Payment of debt	(22,062,135)	(24,150,880)
Memberships issued	6,155	5,825
Patronage capital retired	(963,309)	
Increased (decrease) in:		
Consumer deposits	36,195	32,114
Deferred credits	306,825	(414,396)
Other equities	(269,837)	(71)
Net cash Provided (Used) by Financing Activities	(1,502,275)	993,822
NET INCREASE IN CASH AND CASH EQUIVALENTS	252,923	21,587
CASH AND CASH EQUIVALENTS, beginning of year	1,577,131	1,555,544
CASH AND CASH EQUIVALENTS, end of year	$ 1,830,054	$ 1,577,131

The accompanying notes are an integral part of these statements.

PRESQUE ISLE ELECTRIC & GAS CO-OP
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010
(Continued)

	2011	2010
RECONCILIATION OF NET MARGINS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net Margins	$ 2,078,199	$ 104,093
Adjustments to reconcile net margins to net cash provided by Operating activities:		
Depreciation and amortization	3,608,124	3,490,932
(Gain) loss on disposition of assets	163,103	177,564
G&T and other capital credits	(1,493,963)	(389,126)
(Increase) decrease in:		
Customer and other accounts receivable	185,595	(193,433)
Other currents assets	(170,672)	(2,989)
Deferred debits	21,985	30,185
Amortization of debt discount	(134,995)	(134,995)
Increase (decrease) in:		
Accounts payable	167,426	(218,969)
Accrued property taxes	8,461	(51,171)
Accrued interest payable	4,333	11,420
Current and accrued liabilities – other	243,628	147,810
Total Adjustments	2,603,025	2,867,228
NET CASH PROVIDED BY OPERATING ACTIVITIES	$ 4,681,224	$ 2,971,321
NON-CASH ITEMS – INVESTING & FINANCING		
Capital credits from associated organizations	$ 1,493,963	$ 389,126

The accompanying notes are an integral part of these statements.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of the accounting policies adopted by Presque Isle Electric & Gas Co-op which have a significant effect on the financial statements.

Organization

Presque Isle Electric & Gas Co-op (Presque Isle) is a non-profit organization generally exempt from income tax under Section 501(c)(12) of the United States Internal Revenue Code. Presque Isle is subject to the Michigan Business Tax Act of the State of Michigan.

The process of preparing financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions regarding certain types of assets, liabilities, revenues and expenses. Such estimates primarily relate to unsettled transactions and events as of the date of the financial statements. Accordingly, upon settlement, actual results may differ from estimated amounts.

Utility Plant

Additions, with a life expectancy of more than one year, are recorded at cost, less contributions in aid of construction received from customers. As items are retired or otherwise disposed of, the asset account is credited for the cost and the accumulated depreciation account is charged. The cost of removal, less salvage, is charged to the loss on disposition of utility plant account, and shown on the Statement of Revenue.

Investments

The carrying values of investments in associated organizations are stated at cost, adjusted for capital credits earned or retired. Short-term investments are stated at cost, which approximates market value.

Cash

For purposes of the statement of cash flows, Presque Isle considers all short-term debt securities purchased with a maturity of three months or less to be cash equivalents.

Consumer Energy Prepayments and Unbilled Revenues

Seasonal account billings are accounted for as deferred credits and recognized as income on a straight-line basis over a period of one year. There were no estimated net unbilled revenues for the year.

Accounts receivable

Accounts receivable consist primarily of amounts due from members for electric and gas service. An allowance for doubtful accounts has been estimated based on collection history. When a member's account becomes past due and uncollectible, the member's service is terminated. The Board of Directors approve all accounts charged off.

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Materials and Supplies

Electrical and natural gas materials and supplies are valued at average cost. Merchandise held for resale is valued on the first-in, first-out basis.

Retirement Plan

Presque Isle has a retirement savings plan for substantially all employees. Under the terms of the plan, Presque Isle is required to contribute 10 to 16 percent of the employee's total base earnings to the retirement plan.

Flex Benefit Plan

Presque Isle has a Flexible Benefits Plan. The purpose of the plan is to provide eligible employees a choice between cash and the specified welfare benefits described in the plan. Pre-Tax Premium elections under the plan are intended to qualify for the exclusion from income provided in Section 125 of the Internal Revenue Code of 1986.

Contributions in Aid of Construction

Contributions in aid of construction are received from customers on electrical and gas installations and re-applied against the construction costs.

NOTE 2: ASSETS PLEDGED

Substantially all assets are pledged as collateral on long-term debt payable to the National Rural Utilities Cooperative Finance Corporation (CFC).

NOTE 3: ELECTRIC AND GAS PLANT AND DEPRECIATION RATES AND PROCEDURES

Major classes of electric and gas plant as of December 31, 2011 and 2010 consisted of:

	2011	2010
Intangible plant	$ 1,025,480	$ 1,025,480
Distribution plant	112,770,473	109,749,475
General plant	6,886,914	6,556,970
	120,682,867	117,319,925
Construction work in progress	852,911	654,673
TOTAL	$ 121,535,778	$ 117,986,598

NOTE 4: ELECTRIC AND GAS PLANT AND DEPRECIATION RATES AND PROCEDURES - continued

Provision has been made for depreciation of the distribution plant at a straight-line rate of 10 to 50 years for all distribution plant additions.

General plant depreciation rates have been applied on a straight-line basis as follows for the year ended December 31, 2011:

	Years
Structures and improvements	10-50
Office furniture equipment	3-7
Transportation equipment	4-7
Power operated equipment	3-16
Other	4-5

Depreciation and amortization of electric and gas plant in service was charged as follows for the years ended December 31, 2011 and 2010:

	2011	2010
Charged to:		
Classified as depreciation and amortization	$ 3,267,176	$ 3,149,984
Classified in other operating expenses	132,805	139,753
	3,399,981	3,289,737
Charged to construction	212,518	201,195
TOTAL DEPRECIATION AND AMORTIZATION	$ 3,612,499	$ 3,490,932

NOTE 5: INVESTMENTS IN ASSOCIATED ORGANIZATIONS

Investments in associated organizations consisted of the following at December 31, 2011 and 2010:

	2011	2010
Wolverine Power Supply Coop. Inc. - capital credits	$ 9,302,060	$ 9,517,385
Wolverine Power Supply Coop. Inc. - PSDF	7,980,339	7,352,748
National Rural Utilities Cooperative Finance Corp.:		
Capital term certificates maturing October 1, 2020 through October 1, 2080 at interest rates between 3% and 7.50%	1,767,552	1,788,697
Patronage capital certificates	1,340,347	1,199,398
Other	495,410	472,402
TOTAL	$ 20,885,708	$ 20,330,630

NOTE 6: SHORT-TERM INVESTMENTS - RESTRICTED

On March 20, 1984, the Michigan Public Service Commission issued its opinion and order in Case No. U-7901, directing Michigan's Rural Electric Cooperatives to maintain power supply cost recovery over-collections and refundable contributions in restricted accounts to be used only for the purpose for which they are intended.

In order to accomplish the objectives of the Commission, a non-complex mechanism acceptable to CFC and a workable approach acceptable to Presque Isle Electric & Gas Co-op, Inc., on December 17, 1985, entered into an agreement with CFC to escrow power supply cost recovery over-collections and refundable contributions. A monthly certification is to be included with the monthly form advising CFC as to amounts included in the special funds representing power supply cost recovery over-collections and refundable contributions.

Presque Isle is to provide CFC a copy of the monthly certification described above which will serve as notice to CFC as to the amount below which the fund should not fall. Under the provisions of the agreement with CFC when the amount of deposits held by CFC falls below the level set forth in the latest available certification furnished CFC, CFC will advise the Commission if Presque Isle has not remedied the deficiency within three business days of notification by CFC to Presque Isle.

There were no amounts required to be restricted as of December 31, 2011 and 2010.

NOTE 7: CASH AND INVESTMENTS

Statements of Financial Accounting Standards (SFAS) No. 105 require disclosure of significant concentrations of credit risk arising from cash deposits in excess of federally insured limits.

	Per Institution	Per Book
Insured	$ 884,444	$ 671,260
Uninsured	1,157,294	1,157,294
Cash in banks, credit union & CFC	$ 2,041,738	1,828,554
Working funds		1,500
Total per books		$ 1,830,054

NOTE 8: DEFERRED DEBITS

The Cooperative has recorded deferred debits in the following amounts:

	2011	2010
Prepaid tap fees	$ 67,363	$ 69,359
Prepaid years of service	79,950	93,656
Regulatory prepaid asset	8,199	14,482
TOTAL	$ 155,512	$ 177,497

NOTE 9: MEMBERSHIPS

The following is a summary of changes in memberships for the years ended December 31, 2011 and 2010:

	2011	2010
Balance, beginning	$ 227,440	$ 221,615
Membership and subscriptions issued	6,155	5,825
Adjustment		
Balance, ending	$ 233,595	$ 227,440

Memberships have been adjusted to reflect the number of members currently receiving service. In accordance with the Co-op by-laws, memberships are not refunded when a member leaves the service area. The membership fee is transferred to donated capital when the member terminates service.

NOTE 10: PATRONAGE CAPITAL

Patronage capital balances as of December 31, 2011 and 2010 consisted of:

	2011	2010
Assignable	$ 2,078,199	$ 104,093
Assigned to date	41,969,901	41,866,115
	44,048,100	41,970,208
Less retirements to date	5,110,192	4,146,883
Balance	$ 38,937,908	$ 37,823,325

NOTE 10: PATRONAGE CAPITAL - continued

Under the provisions of the Mortgage Agreement, until the equities and margins equal or exceed twenty percent of the total assets of the Cooperative, the return to patrons of capital contributed by them is limited generally to twenty-five percent of the patronage capital or margins received by the Cooperative in the next preceding year. The equities and margins of Presque Isle represent 35.9% and 35.3% of the total assets for the years 2011 and 2010, respectively. There were capital credits retired of $963,309 and $0 during 2011 or 2010, respectively.

NOTE 11: MORTGAGE NOTES

Long-term debt is composed of 4.85 percent to 6.65 percent mortgage notes payable to the National Rural Utilities Cooperative Finance Corporation (CFC). All mortgage notes to CFC will be repriced and the interest rate adjusted accordingly during the next 10 years in accordance with the policy and procedure governing such repricing. The notes are for 35 year periods each, with principal and interest installments due either quarterly or semiannually. The notes are scheduled to be fully repaid at various times from June 2013 through February 2045.

There were unadvanced loan funds available at December 31, 2011 in the amount of $19,500,000.

Detail of the long-term debt is as follows:

	2011	2010
National Rural Utilities Cooperative Finance Corporation mortgage notes bearing interest at 4.85% to 6.65% per annum for 2011 and 2010	$ 52,448,119	$ 54,210,254
	52,448,119	54,210,254
Less current maturities	1,888,300	1,788,000
TOTAL LONG-TERM DEBT	$ 50,559,819	$ 52,422,254

Maturities of long-term debt for each of the next five years are as follows:

2012	$	1,888,300
2013	$	1,981,900
2014	$	2,080,900
2015	$	2,199,200
2016	$	1,396,900

NOTE 12: LINE OF CREDIT

Presque Isle had available a short-term line of credit from CFC for 2011 and 2010 of $8,000,000, with a revolving credit and term of sixty months. The agreement requires that within 360 days of the first advance, the cooperative will reduce to zero for a period of at least five consecutive business days amounts outstanding. The Cooperative was in compliance with this provision during 2011 and 2010. Balance available at December 31, 2011 and 2010 was $8,000,000. The outstanding balance at December 31, 2011 and 2010 was $-0-.

Additionally, Presque Isle has an $8,000,000 unsecured revolving line-of-credit agreement with CoBank. Interest on outstanding borrowings is payable monthly and is computed at 3.05% at December 31, 2011. Presque Isle had an outstanding balance of $6,200,310 for 2011 and $5,056,478 in 2010.

NOTE 13: DEFERRED CREDITS

Following is a summary of the amounts recorded as deferred credits as of December 31, 2011 and 2010:

	2011	2010
Deferred gain from extinguishments of debt	$ 539,982	$ 604,978
Customer energy prepayments	(123,428)	(360,254)
TOTAL	$ 416,554	$ 244,724

NOTE 14: RETIREMENT PLAN

Retirement plan benefits for substantially all employees are provided through participation in a defined contribution SelectRE pension plan with 401k option with cash and deferred arrangement of the National Rural Electric Cooperative Association (NRECA) and its member systems. The income earned by funds while held under the plan is tax-exempt under Code Sections 401 and 501 of the Internal Revenue Code. Contributions to the savings program, which are based on a percentage of the employees' compensation were $383,070 in 2011 and $399,385 in 2010.

NOTE 15: POWER SUPPLY COST RECOVERY CLAUSE

On October 12, 1982, the Governor of the State of Michigan signed PA 304 of 1982 into law creating the Power Supply Cost Recovery Clause (PSCR), a power cost recovery mechanism.

Wolverine Power Supply Cooperative, Inc. (Wolverine) and the member-distribution Cooperatives including Presque Isle, obtained authority to implement and apply PSCR clauses and monthly factors. Presque Isle's monthly factor may not exceed 24.18 mills per KWH for the current period.

Due to fluctuations in market conditions, over-collections or under-collections could result between the generation cooperative and distribution cooperative as well as between the distribution cooperatives and their member-consumers.

The PSCR clause includes provisions whereby power cost recovery over-collections must be remedied by refunds and power cost recovery under-collections must be remedied by additional collections.

NOTE 15: POWER SUPPLY COST RECOVERY CLAUSE - continued

Presque Isle's balance sheets reflect an amount due to member-consumers for over collections in the amounts of $(193,144) and $(120,017) at December 31, 2011 and 2010, respectively. These amounts are included in the accounts receivable balance.

On September 1, 2009, Presque Isle Electric & Gas Co-op implemented a new rate setting mechanism for its natural gas operations in 34 of its 36 franchised jurisdictions. This included a Gas Cost Recovery (GCR) mechanism. Due to fluctuations in market conditions, over-collections and under-collections of natural gas supply costs could result between the distribution cooperative and its member-consumers.

The GCR mechanism includes provisions whereby gas cost recovery over-collections must be remedied by refunds and gas cost recovery under-collections must be remedied by additional collections. Presque Isle's balance sheet reflects an amount due from member-consumers for under collections in the amounts of $5,928 and $13,816 for the years ended December 31, 2011 and 2010, respectively. This amount is recorded in accounts receivable.

NOTE 16: POST-RETIREMENT BENEFITS OTHER THAN PENSIONS

The cooperative has chosen to recognize the accounting method required by the Statement of Financial Accounting Standards No. 106 for Employer's Accounting for Post-retirement Benefits Other Than Pensions. The statement requires a transition from accounting, for these benefits, on a pay-as-you go (cash basis) to recognizing the benefit cost as they are earned (accrual basis). The change in accounting method requires the accounting for costs incurred to date but unpaid, which is called the Transition amount. This amount may be either expensed in the year of transition or it may be amortized over either the benefit period or twenty-years.

The plan sponsored by the company is a defined benefit post-retirement plan that covers all employees who retire from the cooperative before April 1, 1997 after (i) attainment of age 55 and completion of 30 years of service, or (ii) attainment of age 62. Spouses of pensioners are also insured until the pensioner's death.

At the end of 2011 there were no active participants and the accounting rules of the Financial Accounting Standards Board Statement No. 88 regarding curtailment must be recognized. The reconciliation of the funded status at December 31, 2011 is as follows:

	2011	2010
(Accrued) post-retirement benefit costs, beginning	$ (2,815,152)	$ (2,707,397)
Net periodic post-retirement benefit (costs)	(315,967)	(313,693)
Contributions made	207,381	205,938
(Accrued) post-retirement benefit cost, end of year	$ (2,923,738)	$ (2,815,152)

NOTE 16: POST-RETIREMENT BENEFITS OTHER THAN PENSIONS - continued

Net periodic post-retirement benefit cost includes the following components:

	2011	2010
Interest cost	$ 148,665	$ 148,665
Early buyout cost	2,274	
Net amortization and deferral	165,028	165,028
Net periodic post-retirement benefit cost	$ 315,967	$ 313,693

For measurement purposes a 10.0% annual rate of increase in the per capita cost of covered health care benefits was assumed for 2011; the rate was assumed to decrease gradually to an ultimate rate of 5.0% per annum. The health care cost trend rate assumption has a significant effect on the amounts reported. To illustrate, increasing the assumed health care cost trend rates by 1 percentage point in each year would increase the accumulated post-retirement benefit obligation $122,019 and the aggregate of the service and interest cost components of the net periodic benefit cost by $8,299. Decreasing the assumed health care cost trend rates by 1 percentage point in each year would decrease the accumulated post-retirement benefit obligation $106,201 and the aggregate of the service and interest cost components of the net periodic benefit cost by $7,519.

The weighted-average discount rate used in determining the accumulated post-retirement benefit obligation was 7.5 percent.

NOTE 17: EARLY RETIREMENT INCENTIVE

The cooperative has made available at different times certain voluntary separation incentives to encourage early retirement. The incentive consists of two distinct benefits: a monthly cash payment and a continuation of health care benefits, both for a period of no longer than 48 months. The cash portion consists of a monthly payment equal to $10 for each full-year of service that the employee has with the Cooperative. The health care benefit consists of a continuation of the existing health insurance being provided to the employee by the Cooperative, with the employee being liable for the costs of continuing coverage for their spouse and dependents. There are five employees who have opted to receive this early retirement incentive. The Cooperative has accrued a liability to account for this contractual obligation. The obligation is detailed below:

	2011	2010
Cash portion	$ 82,050	$ 28,750
Health insurance portion	128,447	20,232
Total early retirement incentive liability	$ 210,497	$ 49,982

NOTE 17: FLEX BENEFIT PLAN - under Section 125 of the Internal Revenue Code

The Flexible Benefit Plan is for the benefit of substantially all employees who have been employed for at least 30 days. The Cooperative has elected to offer to eligible employees the following Benefit Plans and Policies subject to the terms and conditions of the plan: (1) Disability Income - Short-Term (A&S); (2) Cancer Insurance; (3) Intensive Care Insurance; (4) Accident Insurance; and (5) Medical Care Expense Reimbursement, not to exceed $1,200 per plan year. The maximum Pre-Tax Premiums a participant can contribute via the Salary Redirection Agreement is the aggregate cost of the applicable Benefit Plans or Policies selected minus any Nonelective Contributions made by the employer. It is intended that such Pre-Tax Premium accounts shall, for tax purposes, constitute an employer contribution.

NOTE 18: LETTERS OF CREDIT

The Co-op has a letter of credit outstanding to the Sequent Energy for $1,500,000 at December 31, 2011. This letter of credit is required in order to mitigate counter party risk in natural gas purchase transactions. This also is a risk management tool for the Co-op with respect to mark to market issues.

NOTE 19: RECLASSIFICATION OF AMOUNTS

Certain amounts previously reported have been reclassified to conform to the 2011 presentation.

NOTE 20: SUBSEQUENT EVENTS

In preparing these financial statements, management has evaluated, for potential recognition or disclosure, significant events or transactions that occurred during the period subsequent to December 31, 2011, the most recent statement of financial position presented herein, through March 15, 2012 the issuance date of the accompanying financial statements. No significant such events or transactions were identified.

AUDITORS' CERTIFICATION REGARDING LOAN FUND EXPENDITURES

During the period of this audit, Presque Isle Electric & Gas Co-op received $0 in long-term loan fund advances from CFC on loans controlled by the 100% CFC Mortgage and Loan Agreement. Based on our review of construction work orders and other plant accounting records created during the audit period, it is our opinion that these CFC loan funds were expended for purposes contemplated in the Loan Agreements on such loans.

Harris Group

Certified Public Accountants
March 15, 2012