ONTINENTAL COOPERATIVE SERVICES

WO THOUSAND FOUR ANNUAL REPORT

2004

20

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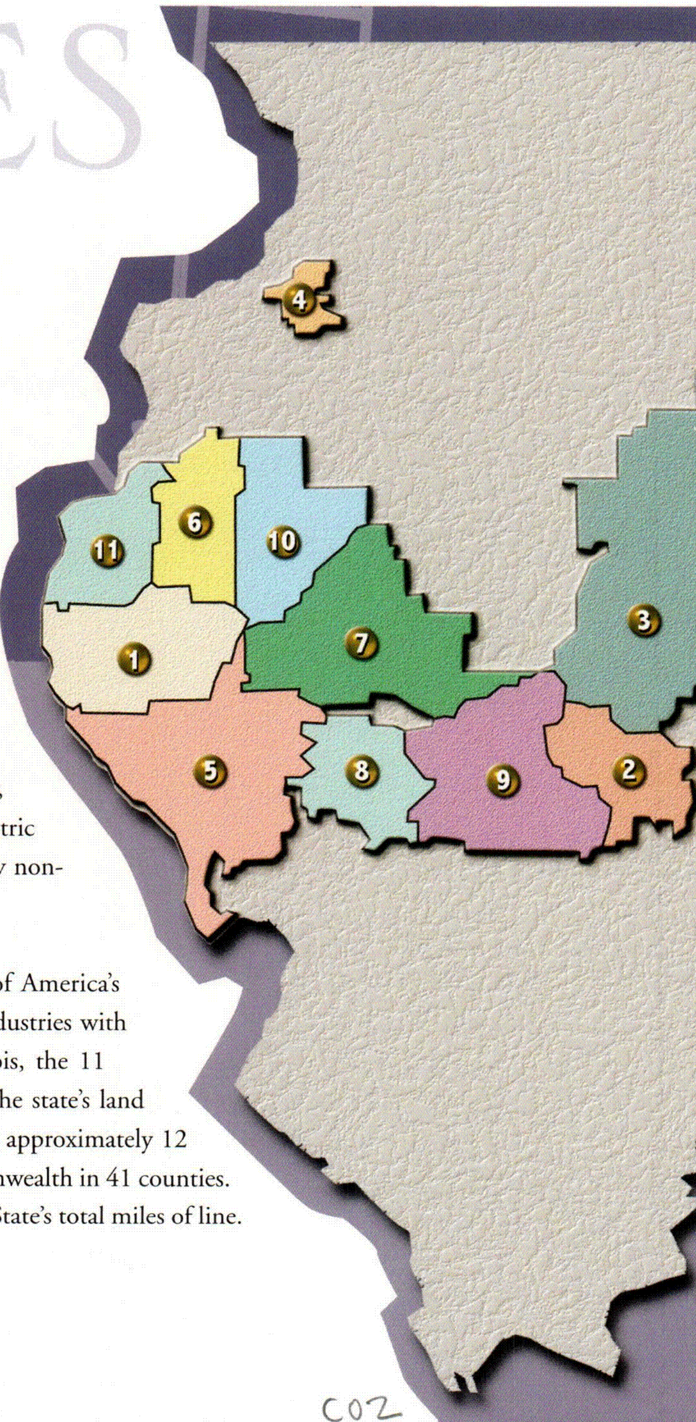
04 Annual Report

ABOUT CONTINENTAL COOPERATIVE SERVICES

ABOUT CONTINENTAL COPERATIVE SERVICES



A trusted energy partner, Continental Cooperative Services (CCS), ensures the delivery of reliable, affordable, and competitive wholesale power to 25 affiliated electric distribution cooperatives in Illinois, New Jersey, and Pennsylvania. CCS affiliated cooperatives, in turn, provide electric generation to nearly 1 million electric cooperative consumers.

CCS, based in Harrisburg, Pa., was created in March 2000, the result of a strategic alliance between two electric generation and transmission cooperatives (G&Ts) — Allegheny Electric Cooperative, Inc. (Allegheny), the wholesale power supplier to 14 electric distribution cooperatives in Pennsylvania and New Jersey, and Soyland Power Cooperative, Inc. (Soyland), which provides power to 11 electric distribution cooperatives in Illinois. CCS marks the first time two geographically non-contiguous G&Ts have joined forces in this fashion.

Cooperative electric systems comprising the CCS network are a critical part of America's rural infrastructure, dedicated to serving homes, farms, small businesses, and industries with integrity, accountability, innovation, and commitment to community. In Illinois, the 11 electric distribution cooperatives affiliated with CCS serve nearly one-third of the state's land area across 44 counties. The 13 CCS affiliated cooperatives in Pennsylvania own approximately 12 percent of the state's electric distribution lines, spanning one-third of the Commonwealth in 41 counties. New Jersey's lone electric cooperative maintains roughly 1 percent of the Garden State's total miles of line.

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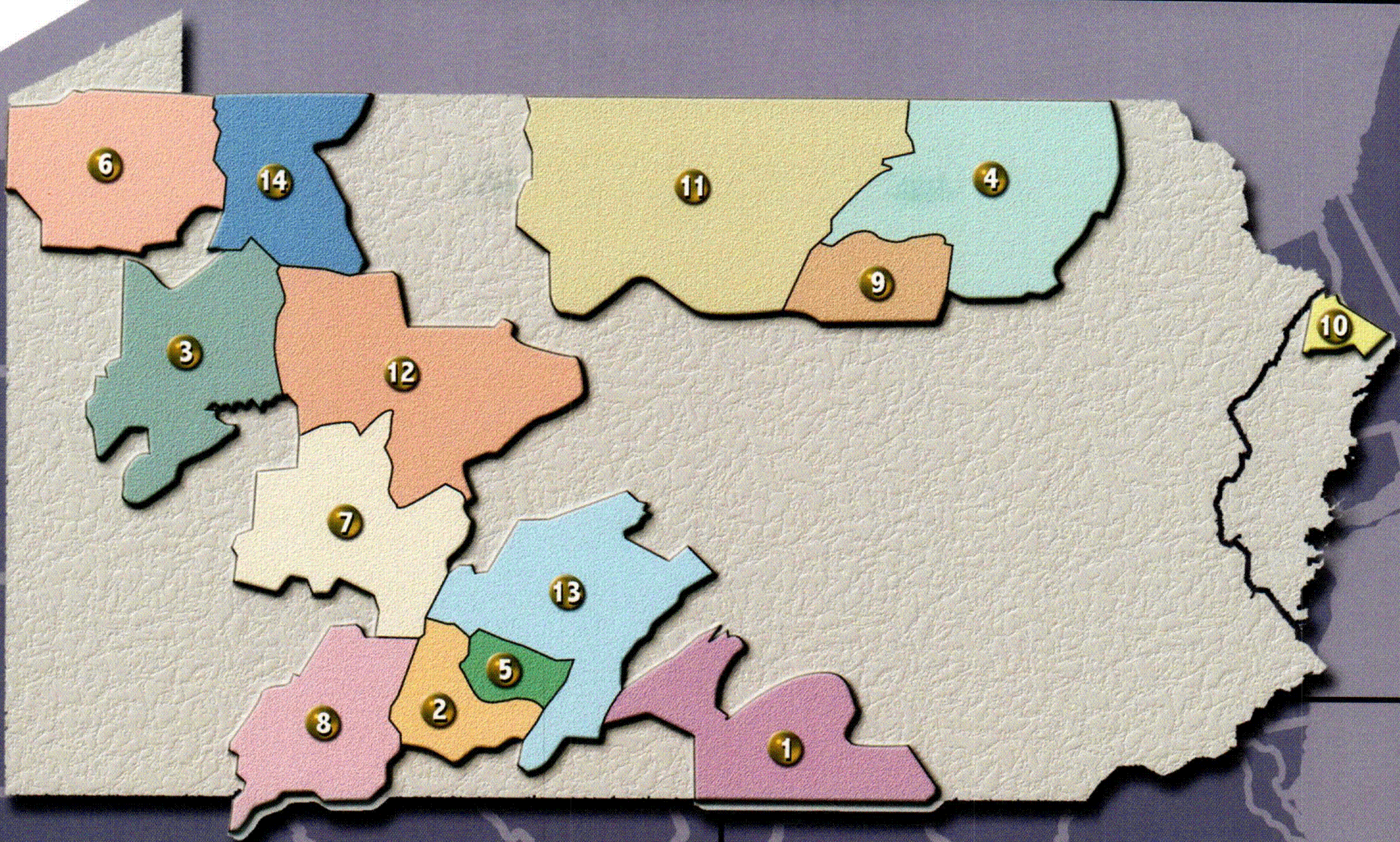


Allegheny Electric Cooperative, Inc. Territory

1. Adams Electric Cooperative, Inc.
2. Bedford Rural Electric Cooperative, Inc.
3. Central Electric Cooperative, Inc.
4. Claverack Rural Electric Cooperative, Inc.
5. New Enterprise Rural Electric Cooperative, Inc.
6. Northwestern Rural Electric Cooperative Association, Inc.
7. REA Energy Cooperative, Inc.
8. Somerset Rural Electric Cooperative, Inc.
9. Sullivan County Rural Electric Cooperative, Inc.
10. Sussex Rural Electric Cooperative, Inc.
11. Tri-County Rural Electric Cooperative, Inc.
12. United Electric Cooperative, Inc.
13. Valley Rural Electric Cooperative, Inc.
14. Warren Electric Cooperative, Inc.

Soyland Power Cooperative, Inc. Territory

1. Adams Electric Cooperative
2. Coles-Moultrie Electric Cooperative
3. Eastern Illini Electric Cooperative
4. Farmers Mutual Electric Company
5. Illinois Rural Electric Cooperative
6. McDonough Power Cooperative
7. Menard Electric Cooperative
8. Rural Electric Convenience Cooperative Company
9. Shelby Electric Cooperative
10. Spoon River Electric Cooperative, Inc.
11. Western Illinois Electrical Cooperative

CO3

A MESSAGE FROM THE EXECUTIVE COMMITTEE AND PRESIDENT & CEO

A MESSAGE FROM THE EXECUTIVE COMMITTEE AND PRESIDENT & CEO

Continental Cooperative Services (CCS) completed its fourth full year of operations in 2004 in strong fashion. To date, our unique and forward-thinking alliance has produced approximately $7 million in general and administrative cost savings. Even more importantly, the long-term rate prognosis for both CCS legacy organizations — Allegheny Electric Cooperative, Inc. (Allegheny) and Soyland Power Cooperative, Inc. (Soyland) — remains excellent. In just a few years, both Allegheny and Soyland will have reduced debt even further, providing the two organizations with substantial flexibility in today's competitive utility environment.

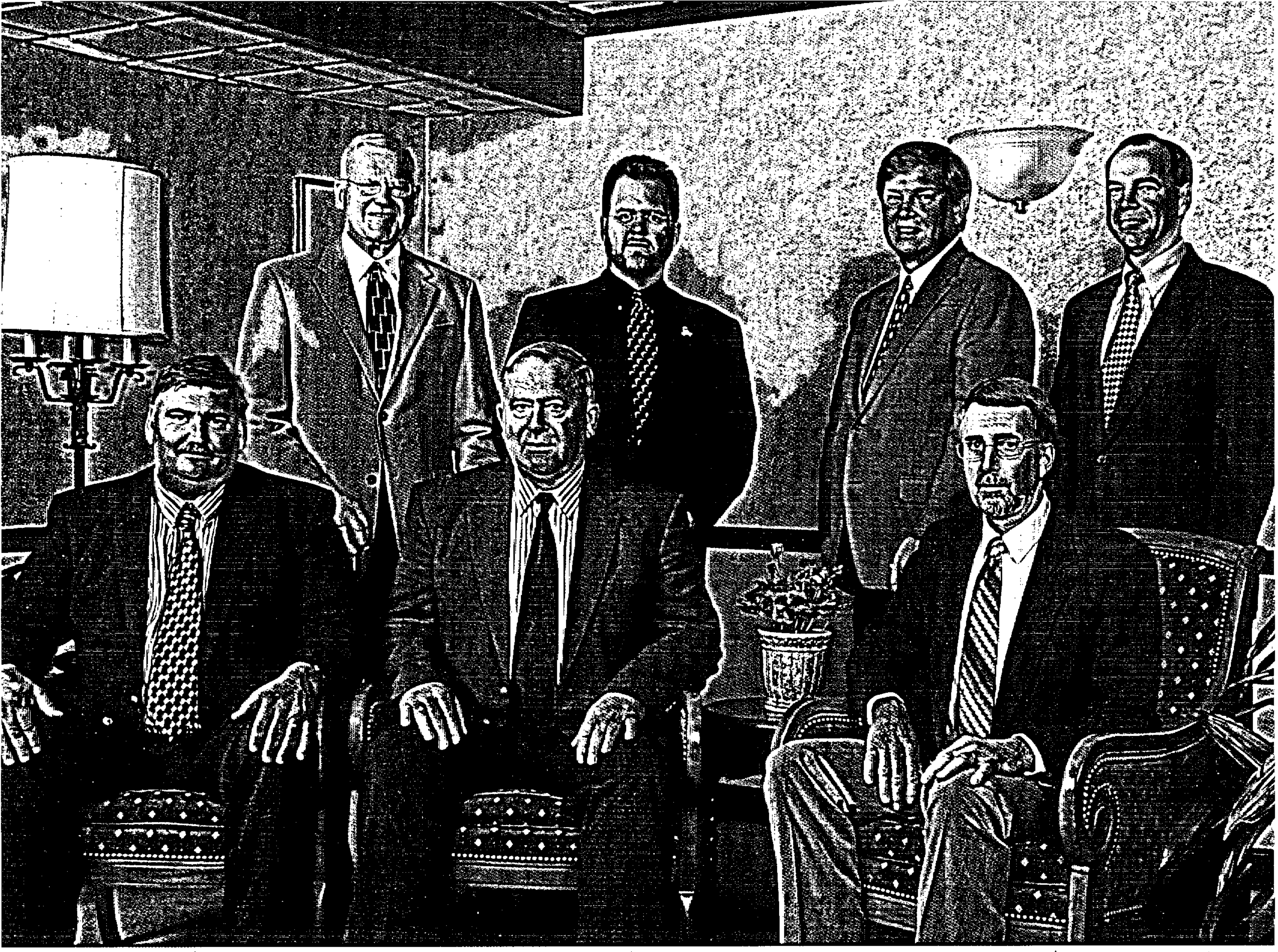
We also expect to see noticeable improvements in the reliability of delivery service provided to our affiliated electric distribution cooperatives, thanks to agreements reached late in the year with private power companies FirstEnergy/Penelec and FirstEnergy/Met-Ed in Pennsylvania and Ameren Corporation in Illinois.

The settlement with the FirstEnergy operating companies — which includes specific milestones and expenditures — culminates intense efforts by CCS and follows on the heels of private power company reliability regulations adopted by the Pennsylvania Public Utility Commission. In addition, the FirstEnergy companies are still mandated to spend roughly $49 million through 2009 repairing and building lines and equipment that feed electric cooperative delivery points. Taken together, these steps should yield more reliable service for Pennsylvania electric cooperative consumers well into the future.

On the Illinois side, CCS and Ameren Corporation have agreed to form a joint dispute resolution committee to resolve territorial conflicts before they reach the Illinois Commerce Commission. Ameren has also agreed to work with CCS on a regular basis to improve power supply reliability.

During 2004, all legal matters involving buyouts by former Soyland member cooperatives were resolved, allowing CCS to enter the new year free of such litigation.

CCS also took steps in 2004 to promote additional growth. Our original structure was created to accommodate generation and transmission cooperatives as members, but it did not provide a clear manner to bring smaller, single entities that could reasonably benefit from CCS into the fold.



As a result, CCS's bylaws were changed to create a new at-large member, or ALM group. The ALM structure will allow individual electric distribution cooperatives or other utilities that serve at retail, such as municipal electric systems and even private power companies, to join our alliance.

As 2005 dawned, CCS was evaluating options to secure its power supply future. Thanks to our existing favorable power purchase contracts, we will not need capacity until 2009.

The phrase, "In unity, there is strength," underscores why CCS continues on the path to success. In a deregulated energy marketplace, we continue to believe that CCS — embodying the basic electric cooperative operating principle of "cooperation among cooperatives" — represents the future of the rural electrification program. Along with our affiliated electric distribution cooperatives, we will push ahead to fulfill our primary mission: to provide a competitive and reliable supply of power for rural consumers in Illinois, New Jersey, and Pennsylvania.

THE CCS EXECUTIVE COMMITTEE: FRONT ROW, FROM LEFT TO RIGHT, CURTIN RAKESTRAW II, AT-LARGE MEMBER; DAVE TURNER, CHAIRMAN; AND MICHAEL CARLS, VICE CHAIRMAN. BACK ROW, FROM LEFT TO RIGHT, ROBERT HOLMES, SECRETARY; JAMES COLEMAN, TREASURER; MURRAY MADSEN, AT-LARGE MEMBER; AND FRANK BETLEY, PRESIDENT & CEO.

CCS AT A GLANCE

CCS AT A GLANCE

2004 FACT SHEET

Energy Sales

Soyland $1,402,798
Allegheny $2,749,040

Total Operating Revenue

Soyland $82,117,858
Allegheny $166,197,000

Net Margin

Soyland $3,375,304
Allegheny $14,877,000

Total Assets

Soyland $111,641,449
Allegheny $355,325,000

Budgeted System Rate

Soyland ....57.9 mills per kWh
Allegheny ....57.4 mills per kWh

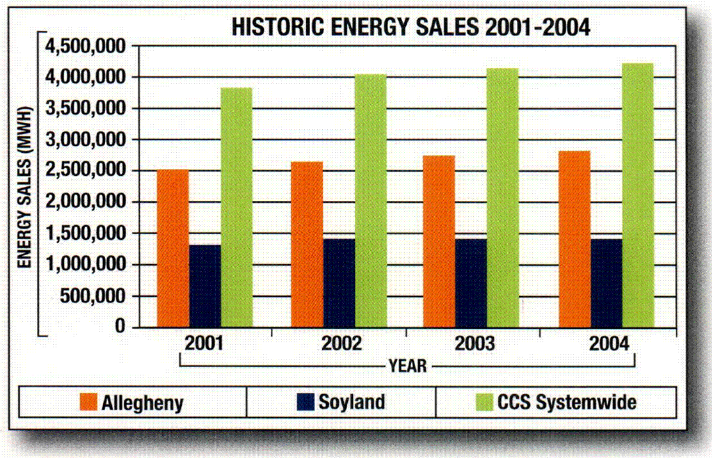
Member Distribution Systems..........................25

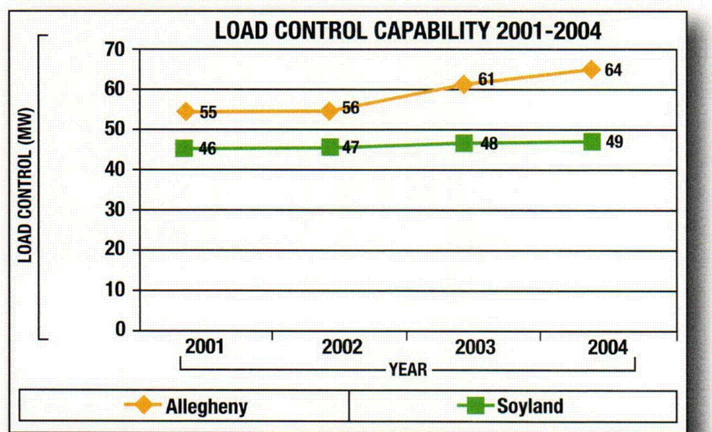
Total Retail Customers......................................296,736

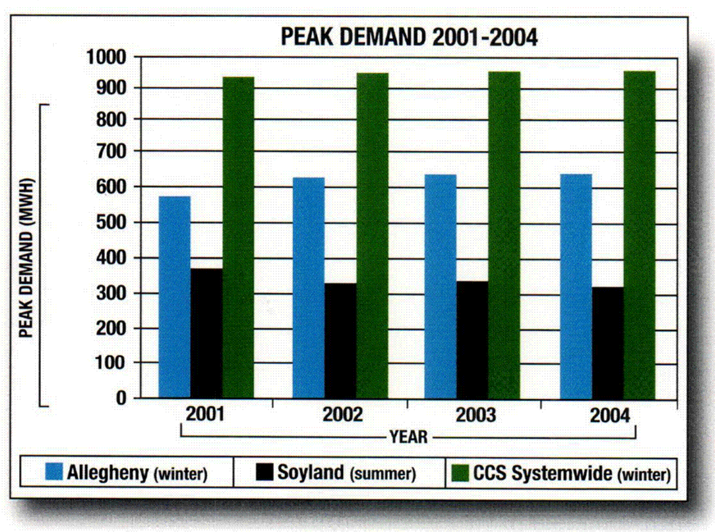
Pennsylvania 208,279
Illinois 77,131
New Jersey...11,326

2004 Peak Demand ....964 MW

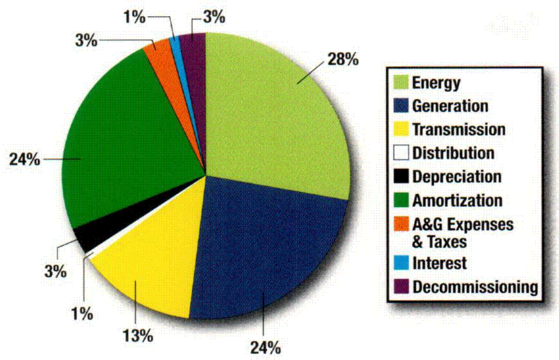
Miles of Transmission Line 670



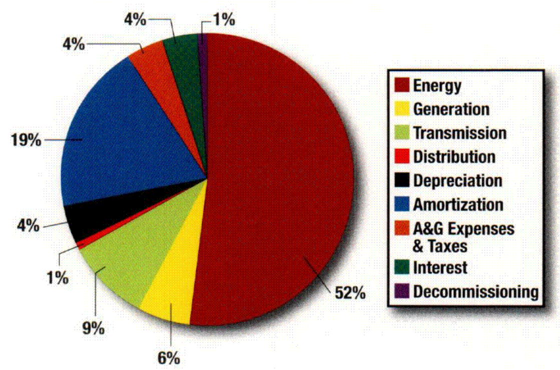




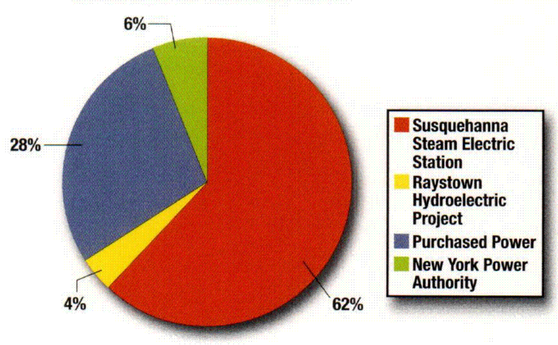
ALLEGHENY
2004 OPERATING EXPENSES



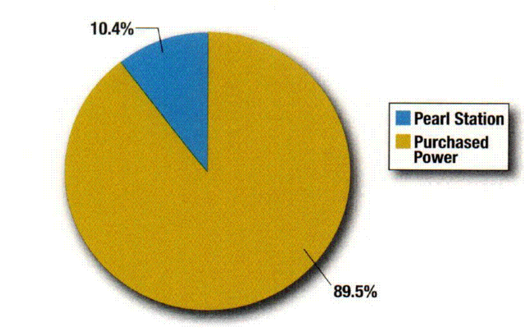
SOYLAND
2004 OPERATING EXPENSES



ALLEGHENY
SOURCES OF ENERGY 2004



SOYLAND SOURCES OF ENERGY 2004*
(Peaking facilities less than 1 percent)



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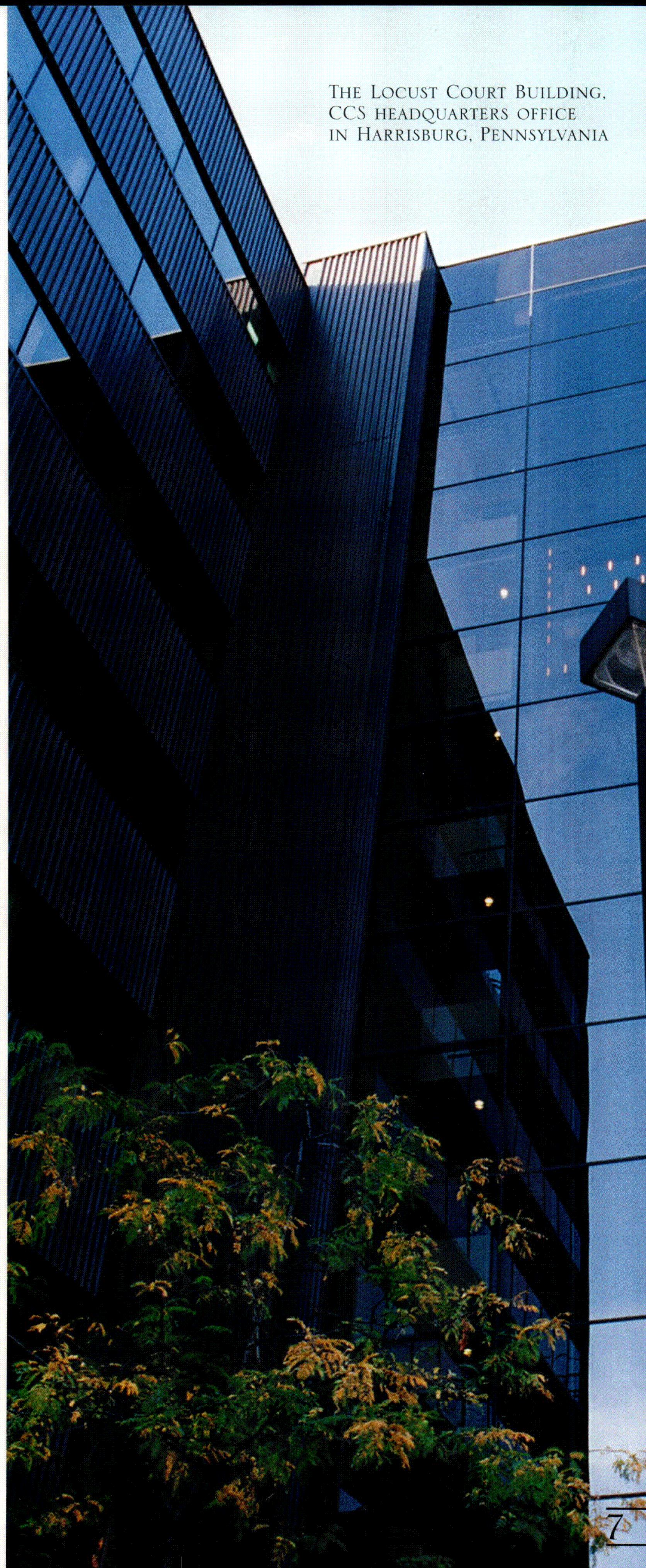


THE LOCUST COURT BUILDING, CCS HEADQUARTERS OFFICE IN HARRISBURG, PENNSYLVANIA

YEAR IN REVIEW

YEAR IN REVIEW

Power Supply

CCS continued to enjoy the benefits of advantageous power supply contracts with AmerenEnergy Marketing for the Illinois area and Williams Power Company for the Pennsylvania/New Jersey region. Both arrangements continue until the end of 2008, a move that brings all of the organization's supplemental power contracts into synch and secures a reasonable rate for power over a relatively long period.

Generation

A diverse mix of self-owned generation coupled with demand-side management capabilities provide the cornerstone for CCS to fulfill its core mission — achieving stable and affordable wholesale power rates for affiliated electric distribution cooperatives in Illinois, New Jersey, and Pennsylvania.

"Fuel diversity" affords CCS better balance and increased leverage in a competitive energy market easily shaped by national and global events. Crude oil prices, natural gas supplies, drought, even market jitters over regional power crises all affect how electricity markets operate and significantly impact power prices.

CCS's diversified generation portfolio played a key role in helping the organization negotiate attractive wholesale power supply contracts with AmerenEnergy Marketing and Williams Power Company. Here is a look at CCS's power plant portfolio:

Alsey Generating Station: Owned by Soyland and operated by CCS staff, the Alsey Generating Station is a five-unit, natural gas-fired peaking complex located in Scott County, Ill., near the village of Alsey. The facility entered service in July 1999 and has a nameplate rating of 125 megawatts. (The units can also operate on fuel oil, if necessary.)

Alsey Station operates in conjunction with a private power company when it is more cost-effective to run the combustion turbines than purchase power from other providers. It is designed to run during periods of peak electric use. Since air permits for the facility limit emissions to no more than 250 tons of nitrogen oxides annually, operation is capped at 937 hours per year. Alsey generated 1,216 megawatt-hours during 2004.

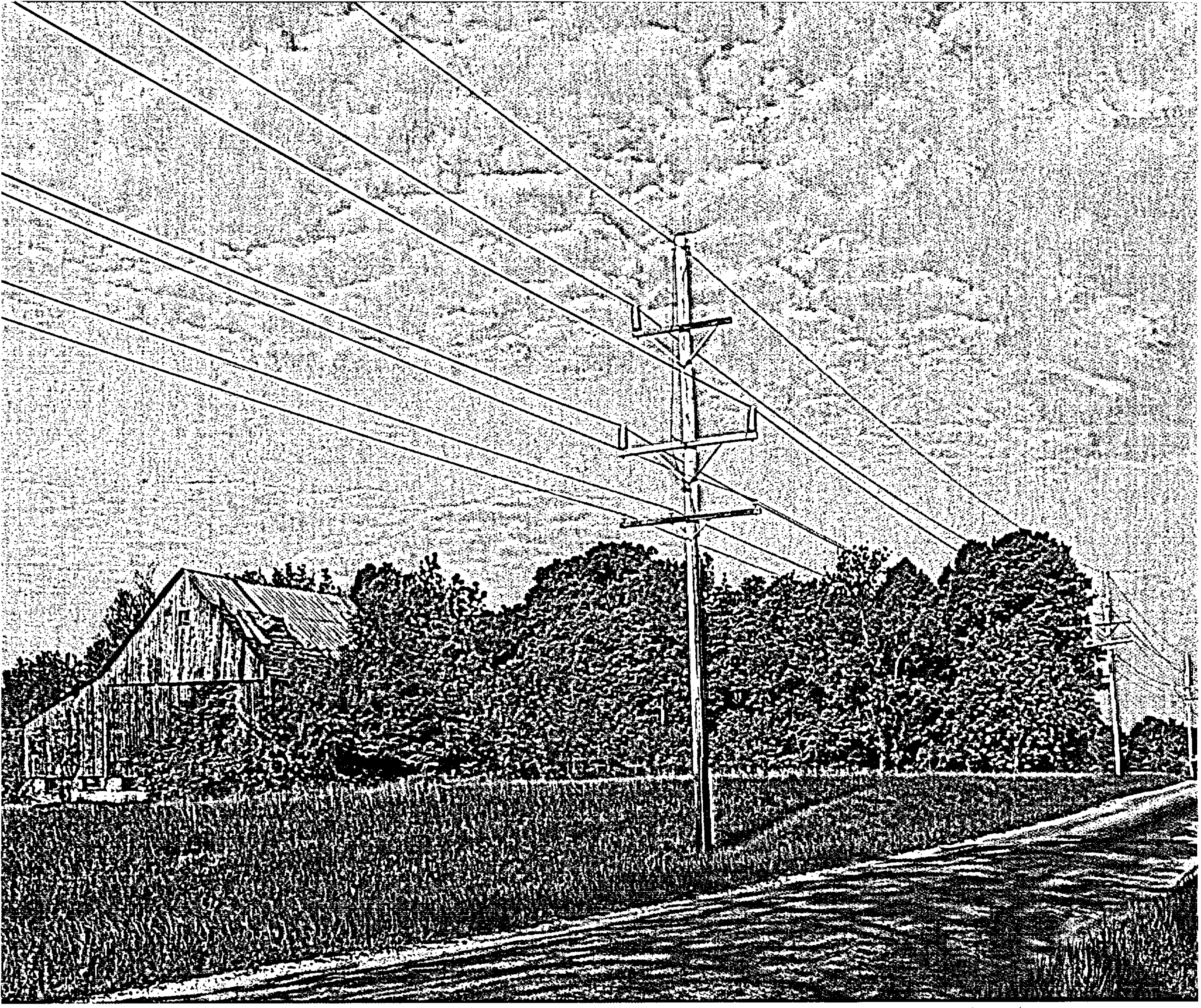
Pearl Station: A 22-megawatt, coal-fired baseload power plant located in Pike County, Ill., along the Illinois River, Pearl Station — owned by Soyland and operated by CCS staff — first went on-line in 1968. In fiscal 2004, Pearl produced nearly 147.6 million kilowatt-hours of electricity.

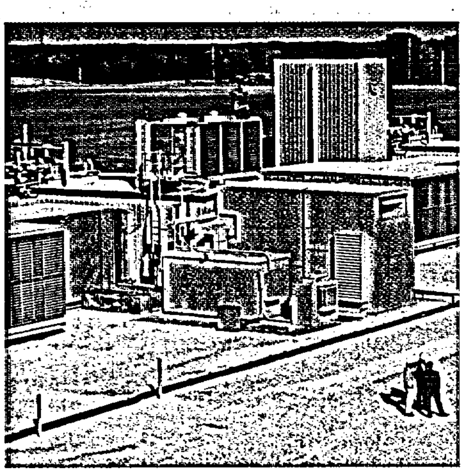
Other Illinois Peaking Plants: During times of peak electricity demand and system emergencies, Soyland can call on a 20-megawatt oil-fired combustion turbine based at Pearl Station and 9 megawatts from five diesel units located at Pittsfield in Pike County, Ill. Typically, both facilities run less than 200 hours per year.

New York Power Authority: Since 1966, Allegheny has purchased power generated by federal hydroelectric projects located along the Niagara and St. Lawrence rivers in upstate New York. Both facilities are operated by the New York Power Authority (NYPA).

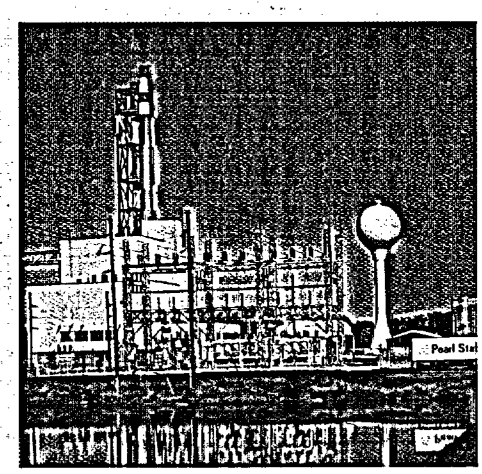
In 2004, Pennsylvania received an allocation of 38.7 megawatts (MW) from the 1,880-MW Niagara Power Project and 11.2 MW from the 912-MW St. Lawrence Power Project. Out of this, Allegheny and its member electric cooperatives in the Commonwealth received approximately 32 MW (31 MW from Niagara and nearly 0.5 MW from St. Lawrence). An additional 2 MW from both projects was allocated to Sussex REC, a CCS affiliated electric distribution cooperative in New Jersey.

Allegheny handles all contracts, billing, and transmission arrangements for Pennsylvania utilities that receive NYPA power in its role as state NYPA Bargaining Agent.

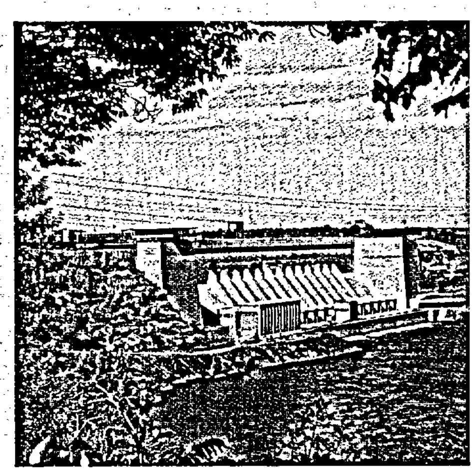




ALSEY GENERATING STATION



PEARL STATION



NIAGARA POWER PROJECT OPERATED BY THE NEW YORK POWER AUTHORITY

U R A N N U A L R E P O R T

YEAR IN REVIEW CONTINUED

Raystown Hydroelectric Project: Allegheny's Raystown Hydroelectric Project, William F. Matson Generating Station (Raystown) is a two-unit, 21-megawatt, run-of-river hydropower facility located at Raystown Lake and Dam in Huntingdon County, Pa. Buoyed by abundant rainfall across the Mid-Atlantic region, Raystown in 2004 provided more than 113.9 million kilowatt-hours at delivery — its second highest production level ever — exceeding projections by more than 33 percent.

CCS staff operates the hydro project in close cooperation with the Baltimore District of the U.S. Army Corps of Engineers. The Corps controls water releases from Raystown Lake, the largest man-made body of water in Pennsylvania.

Susquehanna Steam Electric Station: Allegheny owns 10 percent of the Susquehanna Steam Electric Station (SSES), a 2,355-megawatt, two-unit nuclear power plant located in Luzerne County, Pa. PPL Susquehanna, a division of Allentown, Pa.-based PPL Corporation, owns the remaining 90 percent and operates the boiling water reactor facility.

In 2004, this 10 percent share of SSES provided a record 1.8 billion kilowatt-hours of electricity at delivery to Pennsylvania and New Jersey electric cooperatives. The capacity factor of SSES Unit 1 was 78.2 percent; Unit 2 was 97 percent. This works out to an average annual composite capacity factor for the facility of 87.6 percent.

Both Unit 1 and Unit 2 run on a 24-month refueling cycle.

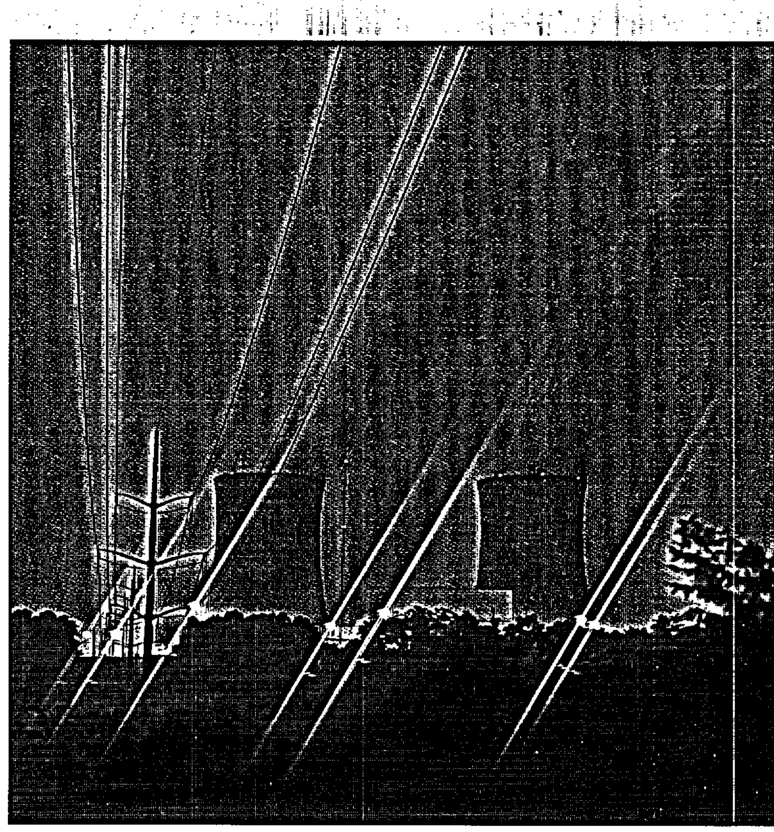
Load Management: In 1986, Allegheny, along with CCS affiliated electric distribution cooperatives in Pennsylvania and New Jersey, launched the Coordinated Load Management System (CLMS) to reduce electricity consumption during peak demand periods.

By shifting use of residential water heaters, electric thermal storage units, dual fuel home heating systems, and other special equipment in the homes of volunteer cooperative consumers to off-peak hours, CLMS improves system efficiency, cuts costly demand charges cooperatives must pay for purchased power, and reduces the need for new generating capacity. CLMS is also used during summer peaks to reduce CCS capacity obligations under procedures established by the PJM Interconnection.

In 2004, CLMS reduced cooperative purchased power costs by $4.5 million, bringing total net power cost savings achieved since December 1986 to more than $72.7 million. Currently, 183 substations are being utilized for load control with more than 45,500 load control receivers installed on appliances, mostly water heaters, in the homes of electric cooperative consumers.

Soyland employs a system control and data acquisition (SCADA) system to monitor load levels, transmission facilities, and generating plant performance. Through SCADA, real-time decisions about generation or purchased power requirements and consumer load reductions can be made based on forecasts, schedules, and actual system performance. This decision-making capability is key in today's market-based electric utility industry.

As part of energy supply agreements with local private power companies, remote terminal units installed on the cooperative's interconnection points are connected through the SCADA system, allowing Soyland to furnish real-time load signals from one control area to another. This helps CCS minimize energy imbalance costs incurred under transmission tariffs.



SUSQUEHANNA STEAM ELECTRIC STATION

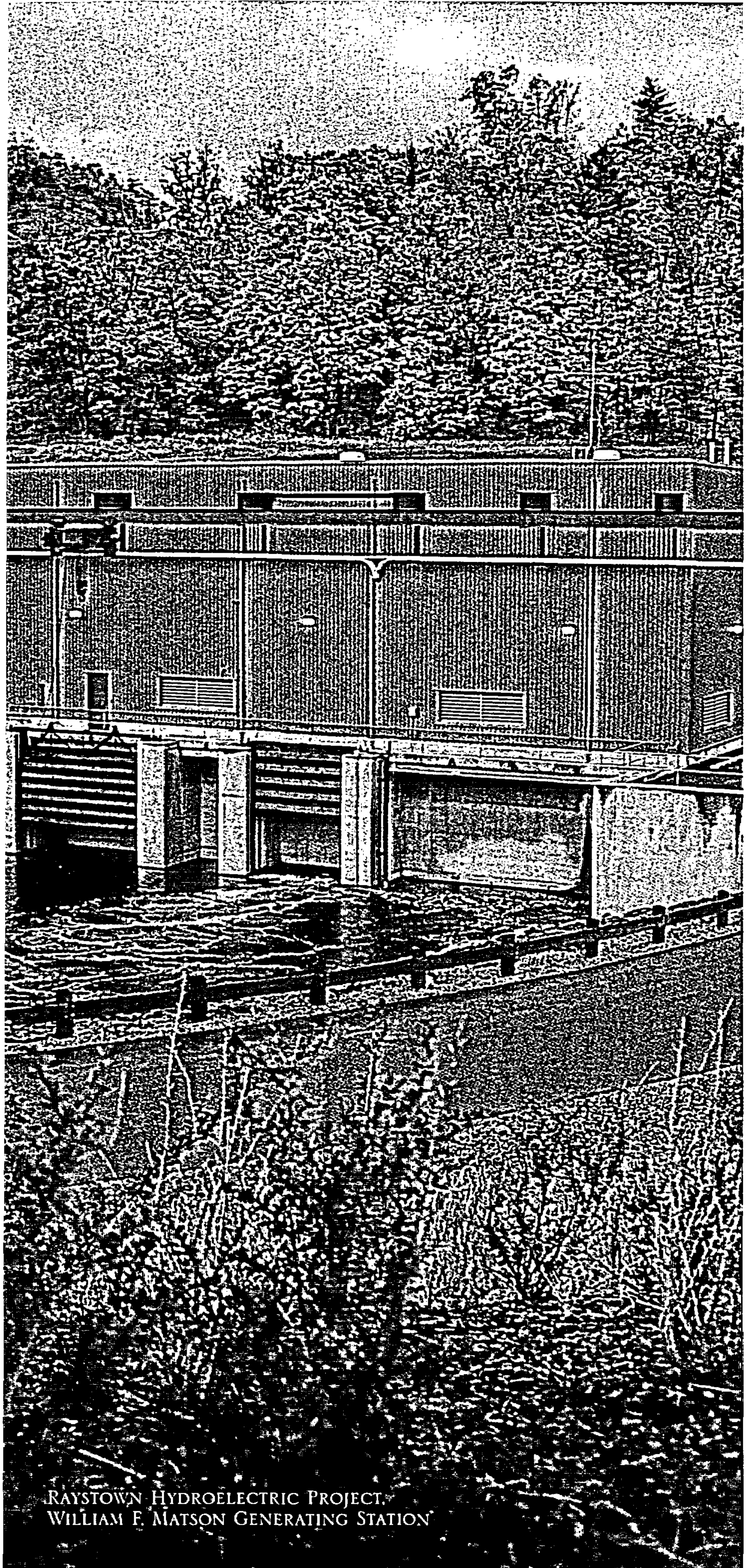
CLEAN POWER LAW RECOGNIZES ELECTRIC COOPERATIVE LOAD MANAGEMENT EFFORTS

Because Pennsylvania's electric cooperatives have promoted the benefits of energy conservation and "green" power for years, they became natural partners in helping shape Pennsylvania's renewable portfolio standard (RPS) law, enacted in 2004. Under RPS, private power companies and competitive electric generation suppliers across the state must include increasing amounts of green energy in their generation mix — up to 18 percent by 2020.

Electric cooperatives, on the other hand, must meet RPS requirements by offering a "voluntary program of energy efficiency and demand-side management." Pennsylvania electric cooperatives already do this through the Coordinated Load Management System (CLMS), which launched operations in December 1986.

The Pennsylvania General Assembly realized that imposing RPS on electric cooperatives would go against the historic legislative intent of cooperative self-regulation and unnecessarily raise costs for rural residents. As not-for-profit, consumer-owned and controlled utilities, electric cooperatives base decisions on economic, operational, and community impact, with the goal of providing a reliable supply of power at the lowest possible cost.

Electric cooperatives in the Commonwealth successfully demonstrated to legislators that they have always had an interest in renewable generation and energy efficiency, as reflected by their ownership of the 21-megawatt Raystown Hydroelectric Project. But more importantly, cooperatives also advanced the argument that the cleanest megawatt is the one not produced at all. Members of the legislature were impressed that CLMS — which essentially works like a power plant in reverse — lowers Allegheny power requirements by nearly 10 percent.



RAYSTOWN HYDROELECTRIC PROJECT, WILLIAM F. MATSON GENERATING STATION

COORDINATED LOAD MANAGEMENT SYSTEM

CCS BOARD OF DIRECTORS

CCS BOARD OF DIRECTORS

Dave Turner
Chairman
Warren Electric Cooperative, Inc.
Youngsville, Pa.

Michael Carls
Vice Chairman
Menard Electric Cooperative
Petersburg, Ill.

Robert Holmes
Secretary
Valley Rural Electric Cooperative, Inc.
Huntingdon, Pa.

James Coleman
Treasurer
Shelby Electric Cooperative
Shelbyville, Ill.

Curtin Rakestraw II
At-Large
Sullivan County Rural Electric
Cooperative, Inc.
Forksville, Pa.

Murray Madsen
At-Large
Farmers Mutual Electric Company
Geneseo, Ill.

Robert Willis
Adams Electric Cooperative
Camp Point, Ill.

David Cowan
Adams Electric Cooperative, Inc.
Gettysburg, Pa.

C. Robert Koontz
Bedford Rural Electric Cooperative, Inc.
Bedford, Pa.

Richard Weaver
Central Electric Cooperative, Inc.
Parker, Pa.

John McNamara
Claverack Rural Electric Cooperative, Inc.
Wysox, Pa.

Scott Uphoff
Coles-Moultrie Electric Cooperative
Mattoon, Ill.

Bradley Ludwig
Eastern Illini Electric Cooperative
Paxton, Ill.

Merton Pond
Illinois Rural Electric Cooperative
Winchester, Ill.

William Pollock
McDonough Power Cooperative
Macomb, Ill.

Robert Guyer
New Enterprise Rural Electric
Cooperative, Inc.
New Enterprise, Pa.

Kathryn Cooper-Winters
Northwestern Rural Electric
Cooperative Association, Inc.
Cambridge Springs, Pa.

Wayne Stiles
REA Energy Cooperative, Inc.
Indiana, Pa.

David White
Rural Electric Convenience
Cooperative Company
Auburn, Ill.

Lowell Friedline
Somerset Rural Electric
Cooperative, Inc.
Somerset, Pa.

Jack Clark
Spoon River Electric Cooperative, Inc.
Canton, Ill.

Thomas Webb
Sussex Rural Electric Cooperative, Inc.
Sussex, N.J.

James Davis
Tri-County Rural Electric Cooperative, Inc.
Mansfield, Pa.

Stephen Marshall
United Electric Cooperative, Inc.
DuBois, Pa.

Haven Vaughn
Western Illinois Electrical Cooperative
Carthage, Ill.

Each affiliated electric distribution cooperative has one seat on the CCS Board of Directors.

ALLEGHENY ELECTRIC COOPERATIVE, INC. BOARD OF DIRECTORS

ALLEGHENY ELECTRIC COOPERATIVE, INC.
BOARD OF DIRECTORS

Lowell Friedline
Chairman
Somerset REC
Director

Richard Weaver
Central Electric
Director

Thomas Webb
Sussex REC
Director

Kathryn Cooper-Winters
Vice Chairman
Northwestern REC
Director

John McNamara
Claverack REC
Director

James Davis
Tri-County
Rural Electric
Director

Robert Holmes
Secretary/Treasurer
Valley REC
Director

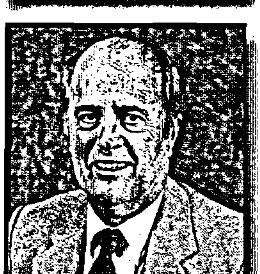
Robert Guyer
New Enterprise REC
Director

Stephen Marshall
United Electric
Director

David Cowan
Adams Electric
Director

Wayne Stiles
REA Energy
Director

Dave Turner
Warren Electric
Director



C. Robert Koontz
Bedford REC
Director

Curtin Rakestraw II
Sullivan County REC
Director

All Allegheny Electric Cooperative, Inc. directors also serve as CCS directors.

SOYLAND POWER COOPERATIVE, INC BOARD OF DIRECTORS

SOYLAND POWER COOPERATIVE, INC. BOARD OF DIRECTORS

Lynn Frasco, P.E.
Chairman
Menard Electric
Manager

Bruce Giffin
Assistant Secretary-Treasurer
Illinois Rural
Manager

Jon Miles
At-Large
McDonough Power
Manager

Robert Willis*
Vice Chairman
Adams Electric
Director

M.L. (Chris) Christman
At-Large
Coles-Moultrie Electric
Manager

Jim Thompson
Adams Electric
Manager

Bradley Ludwig*
Secretary-Treasurer
Eastern Illini Electric
Director

Jack Clark*
At-Large
Spoon River Electric
Director

Scott Uphoff*
Coles-Moultrie Electric
Director

Wm. David Champion Jr.
Eastern Illini Electric
Manager

Michael Carls*
Menard Electric
Director

William Dodds
Spoon River Electric
Manager

Murray Madsen*
Farmers Mutual Electric
Director

David White*
RE Convenience Cooperative
Director

Haven Vaughn*
Western Illinois Electrical
Director

Robert Delp
Farmers Mutual Electric
Manager

David Stuva
RE Convenience Cooperative
Manager

Paul Dion
Western Illinois Electrical
Manager

Merton Pond*
Illinois Rural
Director

Richard Boggs
Shelby Electric
Director

** Denotes CCS director*

William Pollock*
McDonough Power
Director

James Coleman*
Shelby Electric
Manager

at continental cooperative services (ccs), the delivery of reliable, affordable, and competitive power is mission one. a dedicated and experienced team of board members, management, and employees make certain that wholesale electricity is provided round-the-clock to 25 affiliated electric distribution cooperatives in illinois, new jersey, and pennsylvania. ccs-affiliated cooperatives, in turn, provide electric generation to nearly one million ultimate consumers.

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2004 Financial Contents

2004 Financial Contents

04 Annual Report

Allegheny Electric Cooperative, Inc.

Allegheny Electric Cooperative, Inc.
Accountants' Report and Financial Statements

December 31, 2004 and 2003

Contents

Financial Statements

Independent Accountants' Report

Board of Directors
Allegheny Electric Cooperative, Inc.
Harrisburg, Pennsylvania

We have audited the accompanying balance sheets of Allegheny Electric Cooperative, Inc. (Cooperative) as of December 31, 2004 and 2003, and the related statements of income, members' equities (deficits), 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. 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 Allegheny Electric Cooperative, Inc. as of December 31, 2004 and 2003, 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.

As discussed in Note 8 to the financial statements, during 2003, the Cooperative changed its method of accounting for its asset retirement obligation to comply with Financial Accounting Standard 143 (FAS 143).

BKD, LLP

March 4, 2005

ALLEGHENY ELECTRIC COOPERATIVE, INC.

BALANCE SHEETS
DECEMBER 31, 2004 AND 2003 (IN THOUSANDS)

Assets

	2004	2003
Electric Utility Plant, at cost		
In service (see Note 2)	$ 781,139	$ 778,438
Less accumulated depreciation	(673,172)	(677,589)
	107,967	100,849
Construction work in progress	2,862	7,692
Nuclear fuel in process (see Note 1 and 3)	15,334	14,918
Net electric utility plant (see Note 1, 2 and 3)	126,163	123,459
Investments and Other Assets		
Investments in associated organizations (see Note 4)	739	841
Other investments (see Note 1 and 6)	47,828	44,065
Notes receivable, members, less current portion (see Note 5)	68	88
Non-utility property, at cost (net of accumulated depreciation of $4,754 in 2004 and $4,422 in 2003)	4,150	4,332
Other non-current assets	126	158
	52,911	49,484
Current Assets		
Cash and cash equivalents	35,781	17,889
Accounts receivable, members (see Note 1)	14,030	13,439
Accounts receivable, affiliated organizations	58	—
Other receivables	2,882	358
Inventories (see Note 1)	6,350	5,865
Other current assets	1,397	2,594
Total current assets	60,498	40,145
Restricted Investments (see Note 1)	15,837	15,777
Deferred Charges (see Note 1 and 7)		
Capital retirement asset	98,953	135,422
Other	963	1,290
	99,916	136,712
	$ 355,325	$ 365,577

See Notes to Financial Statements

Members' Equities (Deficits) and Liabilities

	2004	2003
Members' Equities (Deficits) (see Note 1)		
Membership fees	$ 3	$ 3
Patronage capital	34,122	34,122
Donated capital	38	38
Retained deficits	(52,911)	(67,788)
Members' deficits	(18,748)	(33,625)
Accumulated other comprehensive income	2,905	2,405
Total deficits	(15,843)	(31,220)
Asset Retirement Obligation (see Note 8)	112,505	108,178
Long-Term Debt (see Note 9)	196,904	232,083
Current Liabilities		
Current installments of long-term debt	38,833	30,214
Accounts payable and accrued expenses	17,307	21,097
Accounts payable to affiliated organizations	—	310
Total current liabilities	56,140	51,621
Other Liabilities and Deferred Revenue		
Accrued decontamination and decommissioning of nuclear fuel	308	617
Deferred income tax obligation from safe harbor lease (see Note 13)	2,423	2,748
Other deferred revenue (see Note 14)	2,888	1,550
	5,619	4,915
	$ 355,325	$ 365,577

ALLEGHENY ELECTRIC COOPERATIVE, INC.

STATEMENTS OF INCOME
YEARS ENDED DECEMBER 31, 2004 AND 2003
(IN THOUSANDS)

	2004	2003
Operating Revenues	$ 166,197	$ 154,786
Operating Expenses		
Operations		
Purchased capacity and energy costs	44,128	47,300
Transmission		
Operation	19,427	20,785
Maintenance	126	196
Production		
Operation	21,050	16,693
Maintenance	8,837	8,576
Fuel	7,584	7,021
	101,152	100,571
Depreciation	5,066	4,695
Accretion of asset retirement obligation	4,327	4,161
Amortization of capital retirement asset	36,469	31,867
Administrative and general	5,286	5,033
Property and other taxes	457	442
	152,757	146,769
Operating Margin Before Interest and Other Expenses	13,440	8,017
Other Expenses		
Interest expense	966	924
Other deductions, net	1,265	1,202
	2,231	2,126
Operating Margin	11,209	5,891
Non-operating Margins		
Net non-operating rental income	1,275	1,220
Interest income	2,294	2,436
Other income	99	768
Net income before cumulative effect of adoption of FAS 143	14,877	10,315
Cumulative Effect of Adoption of FAS 143 (see Note 8)	—	(51,136)
Net Income (Loss)	14,877	(40,821)
Other Comprehensive Income		
Unrealized appreciation in investments	500	856
Comprehensive Income (Loss)	$ 15,377	$ (39,965)

See Notes to Financial Statements

Allegheny Electric Cooperative, Inc.

Statements of Members' Equities (Deficits) Years Ended December 31, 2004 and 2003
(In thousands)

	Membership Fees	Donated Capital	Patronage Capital
Balance, January 1, 2003	$ 3	$ 38	$ 34,122
Comprehensive income			
Net loss	—	—	—
Change in unrealized appreciation on investments	—	—	—
Balance, December 31, 2003	3	38	34,122
Comprehensive income			
Net income	—	—	—
Change in unrealized appreciation on investments	—	—	—
Balance, December 31, 2004	$ 3	$ 38	$ 34,122

See Notes to Financial Statements

Retained Deficits	Total Members' Deficits	Accumulated Other Comprehensive Income	Total Deficits
$ (26,967)	$ 7,196	$ 1,549	$ 8,745
(40,821)	(40,821)	—	(40,821)
—	—	856	856
(67,788)	(33,625)	2,405	(31,220)
14,877	14,877	—	14,877
—	—	500	500
$ (52,911)	$ (18,748)	$ 2,905	$ (15,843)

Allegheny Electric Cooperative, Inc.

Statements of Cash Flows
Years Ended December 31, 2004 and 2003
(In thousands)

	2004	2003
Operating Activities		
Net income (loss)	$ 14,877	$ (40,821)
Items not requiring cash		
Depreciation and fuel amortization	9,840	9,604
Amortization of deferred charges and deferred revenue	36,469	31,867
Accretion of asset retirement obligation	4,327	4,161
Cumulative effect of adoption of FAS 143	—	51,136
Change in		
Accounts receivable, members	(591)	897
Other receivables	(2,524)	677
Inventories	(485)	(1,004)
Other current and non-current assets	1,336	848
Accounts payable and accrued expenses	(3,790)	(1,123)
Accounts (receivable) payable, affiliated organizations	(368)	250
Other liabilities and deferred credits	1,031	(36,240)
Asset retirement obligation	—	36,001
Net cash provided by operating activities	60,122	56,253
Investing Activities		
Additions to electric utility plant and non-utility property, net	(12,362)	(18,765)
Payments received on notes receivable, members	15	22
Purchase of restricted investments	(60)	(462)
Purchase of other investments	(3,263)	(3,824)
Net cash used in investing activities	(15,670)	(23,029)
Financing Activity		
Principal payments on long-term debt	(26,560)	(32,326)
Net cash used in financing activity	(26,560)	(32,326)
Net Increase in Cash and Cash Equivalents	17,892	898
Cash and Cash Equivalents, Beginning of Year	17,889	16,991
Cash and Cash Equivalents, End of Year	$ 35,781	$ 17,889
Supplemental Cash Flows Information		
Interest paid	$ 941	$ 940
Income tax paid	354	250

See Notes to Financial Statements

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2004 AND 2003

Note 1: Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Allegheny Electric Cooperative, Inc. (Cooperative) is a rural electric cooperative corporation established under the laws of the Commonwealth of Pennsylvania. Financing assistance has been provided by the U.S. Department of Agriculture, Rural Utilities Service (RUS) formerly known as the Rural Electrification Administration (REA) and, therefore, the Cooperative is subject to certain rules and regulations promulgated for rural electric borrowers by RUS. The Cooperative is a generation and transmission cooperative. The member cooperatives' primary service areas are rural areas throughout much of rural Pennsylvania and a portion of New Jersey. The Cooperative extends unsecured credit to its members. The Cooperative's primary operating asset is its 10% undivided interest in the Susquehanna Steam Electric Station (SSES), a 2,250-megawatt, two-unit nuclear power plant, co-owned by a subsidiary of PPL Corporation (PPL).

The Board of Directors of the Cooperative, appointed by its members, has full authority to establish electric rates subject to approval by RUS. Rates are established on a cost of service basis.

Basis of Accounting

The Cooperative maintains its accounting records in accordance with the Federal Energy Regulatory Commission's (FERC) uniform system of accounts as modified and adopted by RUS.

In accordance with FERC guidelines, the Cooperative also maintains its accounts in accordance with Statement of Financial Accounting Standards Board (FASB) No. 71, *Accounting for the Effects of Certain Types of Regulations.*

Deregulation

Pennsylvania retail electric customers have the choice of selecting the power supplier, or generator, from which they buy electricity. The ability to choose alternative energy suppliers has not significantly affected the Cooperative's operations or ability to recover its costs through future rates charged to members.

On a regular basis, the Cooperative reevaluates its application of FASB Statement No. 71, *Accounting for the Effects of Certain Types of Regulation,* and No. 101, *Regulated Enterprises – Accounting for the Discontinuation of Application of FASB Statement No. 71.* The Cooperative has determined that regulatory assets and liabilities should continue to be accounted for under the provisions of FASB No. 71 because it is reasonable to assume that the Cooperative will continue to be able to charge and collect its cost of service-based rates.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of financial report and the reported amounts of revenues and expenses during the years then ended. Actual results could differ from those estimates.

Electric Utility Plant

Electric utility plant is carried at cost. Depreciation of electric utility plant is provided over the estimated useful lives of the respective assets on the straight-line basis, except for nuclear fuel, as follows:

Nuclear Utility Plant	
Production	39 years
Transmission	2.75%
General plant	3% - 12.5%
Nuclear fuel	Units of heat production
Non-Nuclear Utility Plant	3% - 33%

Maintenance and repairs of property and replacements and renewals of items determined to be less than units of property are charged to expense. Replacements and renewals of items considered to be units of property are charged to the property accounts. At the time properties are disposed of, the original cost, plus cost of removal less salvage of such property, is charged to accumulated depreciation.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2004 AND 2003

Nuclear Fuel

Nuclear fuel is charged to fuel expense based on the quantity of heat produced for electric generation. Under the Nuclear Waste Policy Act of 1982, the U.S. Department of Energy (DOE) is responsible for the permanent storage and disposal of spent nuclear fuel removed from nuclear reactors. The Cooperative currently pays to PPL its portion of DOE fees for such future disposal services.

Other Investments

Debt and equity securities for which the Cooperative has no immediate plan to sell but that may be sold in the future are classified as available for sale and carried at fair value. Unrealized gains and losses are recorded in members' equities (deficits).

Realized gains and losses, based on the specifically identified cost of the security, are included in net income.

Cash Equivalents

Cash and cash equivalents consist of bank deposits in federally insured accounts and temporary investments.

The Cooperative places its cash and temporary investments with high quality financial institutions. Such cash and temporary investments may be in excess of FDIC insurance limits. For purposes of the statements of cash flows, the Cooperative considers all highly liquid investments with an original maturity of three months or less when purchased to be cash equivalents. Cash equivalents are carried at cost.

The Cooperative's cash and investments are in a variety of financial instruments. The related values as presented in the financial statements are subject to various market fluctuations, which include changes in the equity markets, interest rate environment and the general economic conditions. The Cooperative's credit losses have historically been minimal and within management's expectations.

Accounts Receivable and Notes Receivable

Accounts receivable are stated at the amount billed to members. Accounts receivable are due in accordance with approved policies. An allowance for doubtful accounts has not been recorded because all accounts receivable are considered fully collectible.

Notes receivable are stated at their outstanding principal amount. An allowance for uncollectible notes has not been recorded because all notes receivable are considered fully collectible.

Inventories

The Cooperative accounts for certain power plant spare parts using a deferred inventory method. Under this method, purchases of spare parts under inventory control are included in an inventory account and then charged to the appropriate capital or expense accounts when the parts are used or consumed. Inventories are carried at cost, with cost determined on the average cost method.

Restricted Investments

The Cooperative was required by RUS to establish a trust account for the proceeds from the settlement of litigation with a former power supply provider. RUS is a named beneficiary of the trust fund and RUS requires that the Cooperative seek prior approval to utilize any of the amounts from this account. Such uses to date have consisted of providing collateral for financial obligations and for capital expenditures. Restricted investments consist of interest bearing sweep accounts and are stated at market.

Patronage Capital and Other Margins and Equities (Deficiencies)

The Cooperative has established an unallocated equity account, Retained Deficits, as a result of charges against income. These charges against income were recorded as deficits in an unallocated equity account because the amount is not allocable to the Cooperative's members. RUS requires that subsequent net income recognized by the Cooperative must be used to reduce the deficits.

Income Taxes

Deferred tax assets and liabilities are recognized for the tax effects of differences between the financial statement and tax bases of assets and liabilities. A valuation allowance is established to reduce deferred tax assets if it is more likely than not that a deferred tax asset will not be realized.

Revenue Recognition

Revenue from the sale of electricity to members is recorded based on contracted power usage.

Impairment of Long-Lived Assets

The Cooperative reviews the carrying amount of an asset for possible impairment whenever events or changes in circumstances indicate that such amount may not be recoverable. For the years ended 2004 and 2003, no such circumstances were noted.

Note 2: Electric Utility Plant in Service

	2004	2003
	(In thousands)	
Nuclear Utility Plant		
Production	$ 577,381	$ 580,031
Transmission	41,589	41,555
General plant	580	1,298
Nuclear fuel	148,636	142,700
	768,186	765,584
Non-Nuclear Utility Plant	12,953	12,854
Total	$ 781,139	$ 778,438

Note 3: Susquehanna Steam Electric Station

The Cooperative owns a 10% undivided interest in SSES. PPL owns the remaining 90%. Both participants provide their own financing. The Cooperative's portion of SSES's gross assets, which includes electric utility plant in service, construction and nuclear fuel in progress, totaled $781 million and $778 million as of December 31, 2004 and 2003, respectively. The Cooperative's share of anticipated costs for ongoing construction and nuclear fuel for SSES is estimated to be approximately $73.8 million over the next five years. The Cooperative receives a portion of the total SSES output equal to its percentage ownership. SSES accounted for approximately 62% and 66% of the total kilowatt hours sold by the Cooperative during the years ended December 31, 2004 and 2003, respectively. The balance sheets and statements of income reflect the Cooperative's respective share of assets, liabilities and operations associated with SSES.

Note 4: Investments in Associated Organizations

	2004	2003
	(In thousands)	
National Rural Utilities Cooperative Finance Corporation (CFC) Subordinated Term Certificates, bearing interest from 0% to 5%, maturing January 1, 2014 through October 1, 2080	$ 427	$ 471
Other	312	370
	$ 739	$ 841

The Cooperative is required to maintain these investments pursuant to certain loan and guarantee agreements. Such investments are carried at cost.

Note 5: Notes Receivable from Members

Notes receivable from members arise from the lease of load management equipment to the member cooperatives. Such notes bear interest at a variable rate (4.35% and 2.60% as of December 31, 2004 and 2003, respectively) and mature on March 31, 2009. Notes receivable from members were $90,000 and $105,000 as of December 31, 2004 and 2003, respectively.

Note 6: Other Investments

Other investments consist of the following as of December 31, 2004 and 2003:

	December 31, 2004			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
Decommissioning Trust Fund A:				
Cash	$ 246	$ —	$ —	$ 246
U.S. Government securities	9,229	19	(114)	9,134
Corporate bonds	5,974	149	(42)	6,081
Other obligations	740	2	(4)	738
Corporate stocks	3,145	1,002	(275)	3,872
	19,334	1,172	(435)	20,071
NRC mandated Decommissioning Trust Fund B:				
Cash	380	—	—	380
U.S. Government securities	10,421	19	(174)	10,266
Corporate bonds	6,706	109	(40)	6,775
Other obligations	791	9	(9)	791
Common stocks	5,454	2,441	(187)	7,708
	23,752	2,578	(410)	25,920
Debt Service Reserve Fund — U.S. Government securities	1,837	—	—	1,837
	$ 44,923	$ 3,750	$ (845)	$ 47,828

	December 31, 2003			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
	(In thousands)			
Decommissioning Trust Fund A:				
Cash	$ 94	$ —	$ —	$ 94
U.S. Government securities	10,455	78	(78)	10,455
Corporate bonds	4,670	221	(25)	4,866
Other obligations	288	—	—	288
Corporate stocks	3,085	645	(262)	3,468
	18,592	944	(365)	19,171
NRC mandated Decommissioning Trust Fund B:				
Cash	208	—	—	208
U.S. Government securities	10,133	38	(87)	10,084
Corporate bonds	4,428	194	(16)	4,606
Other obligations	1,544	37	(26)	1,555
Common stocks	4,919	1,843	(157)	6,605
	21,232	2,112	(286)	23,058
Debt Service Reserve Fund — U.S. Government securities	1,836	—	—	1,836
	$ 41,660	$ 3,056	$ (651)	$ 44,065

Certain investments in debt and equity securities are reported in the financial statements at an amount less than their historical cost. Total fair value of these investments at December 31, 2004 and 2003, was $22.9 million and $15.9 million, respectively. These declines primarily resulted from increases in market interest rates prior to the balance sheet date and the failure of certain investments to meet projected earnings targets, which management believes is temporary. The gross unrealized losses at December 31, 2004 for a period of less than 12 months was $250,000 and for a period greater than 12 months was $595,000. The gross unrealized losses at December 31, 2003 for a period of less than 12 months was $152,000 and for a period greater than 12 months was $499,000.

Note 7: Deferred Charges

Deferred charges consist of the following regulatory assets as of December 31, 2004 and 2003.

	2004	2003
	(In thousands)	
Capital retirement asset	$ 98,953	$ 135,422
Accrued decontamination and decommissioning of nuclear fuel	867	1,181
Safe harbor lease closing costs	96	109
	$ 99,916	$ 136,712

Based on membership agreements signed by the 14 member distribution cooperatives on March 29, 1999, with an effective date of January 1, 1999, a portion of the SSES impairment writedown, which took place in 1998, has been recognized as a regulatory asset, referred to as the capital retirement asset. Under this agreement, the Cooperative will recover from members certain financing costs related primarily to the Cooperative's investment in SSES in the amount of $311 million over a nine-year period.

Note 8: Asset Retirement Obligation

The Cooperative adopted Financial Accounting Standard 143 (FAS 143), "Accounting for Asset Retirement Obligations," effective January 1, 2003. FAS 143 addresses the accounting for obligations associated with the retirement of tangible long-lived assets. In connection with the adoption of FAS 143, the Cooperative recorded a cumulative effect of adoption that decreased net income by $51.1 million.

Amounts collected from the Cooperative's members for decommissioning, less applicable taxes, are deposited in external trust funds for investment and can only be used for future decommissioning costs. The fair value of the nuclear decommissioning trust was $46.0 million and $42.2 million for the years ended December 31, 2004 and 2003, respectively.

The changes in the carrying amounts of asset retirement obligations were as follows (in thousands):

	2004	2003
	(In thousands)	
Beginning balance	$ 108,178	$ 104,017
Accretion expense	4,327	4,161
Ending balance	$ 112,505	$ 108,178

The amount of actual obligation could differ materially from the estimates reflected in these financial statements.

Note 9: Long-Term Debt

	2004	2003
	(In thousands)	
Debt settlement note payable to RUS at an interest rate varying from 0.0% to 7.18%, due in varying amounts through 2007	$ 211,663	$ 236,354
6.00% replacement notes payable to RUS due in varying amounts through 2007	1,439	1,864
Pollution Control Revenue Bonds, payable semiannually, including interest through 2014. Variable rates ranged from 0.9% to 2.18% in 2004 and 1.15% to 1.0% in 2003	18,000	19,100
5.00% mortgage notes payable to RUS due in varying amounts through 2019	4,635	4,979
	235,737	262,297
Less current installments	38,833	30,214
	$ 196,904	$ 232,083

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2004 AND 2003

Long-term debt consisted principally of advances under mortgage notes payable for electric utility plant to RUS and to the United States of America acting through the Federal Financing Bank (FFB) and guaranteed by RUS. Substantially all of the assets of the Cooperative are pledged as collateral.

The Cooperative made application for a FFB loan, guaranteed by RUS, in May 2003 in the amount of approximately $50 million to finance system improvements and new construction of existing generating facilities.

Pursuant to the provisions set forth in 7 CFR Part 1717, *Settlement of Debt Owed by Electric Borrowers*, the Cooperative entered into a restructuring agreement with RUS on March 29, 1999, with an effective date of January 1, 1999. Under the restructuring, the original advances under the mortgage notes to FFB were replaced with a new RUS note in the amount of $406 million. The new note has a final maturity date on January 1, 2008, with an option for early termination on January 1, 2006 and January 1, 2007. Interest on the new note is 7.18%. The Cooperative, however, can receive an interest credit up to the amount of total interest expense based on the number of participating members. All of the Cooperative's members are currently participating.

Long-term Pollution Control Revenue Bonds (Bonds) were issued by an industrial development authority on the Cooperative's behalf. The Bonds are subject to purchase on demand of the holder and remarketing on a "best efforts" basis until the Bonds are converted to a fixed interest rate at the Cooperative's option. If a fixed interest rate is established for the Bonds, the Bonds will cease to be subject to purchase by the remarketing agent or the trustee. The indenture agreement contains various redemption provisions with redemption prices ranging from 100% to 103%. Included in other investments, at December 31, 2004 and 2003, respectively, are $1,837,000 and $1,836,000 of investments which relate to a debt service reserve fund required under the Bond Indenture.

In the event that the Bonds are called and cannot be remarketed, the Bonds are collateralized by irrevocable letters of credit from Rabobank Nederland (Rabobank). The trustee may draw on the letters of credit to make required payments to the bondholders. If Rabobank draws on such letters of credit and the Cooperative does not reimburse Rabobank for such draws under the terms of the agreements, the letters of credit are converted into a one-year term loan, with payments of principal and interest due quarterly.

The letters of credit and respective reimbursement agreements were amended as of July 21, 2003 and the stated termination date of each of the agreements is on October 31, 2006 or such later date as may be determined by Rabobank.

Future maturities of all long-term debt are as follows (in thousands):

2005	$ 38,833
2006	37,023
2007	36,696
2008	106,571
2009	1,832
Thereafter	14,782

The Cooperative is required by mortgage covenants to maintain certain levels of interest coverage and annual debt service coverage. The Cooperative represents that it was in compliance with the applicable mortgage covenants as of December 31, 2004 and 2003.

Certain of the Cooperative's long-term debt is at variable interest rates and is therefore subject to various market and interest rate fluctuations.

During 2004 and 2003, the Cooperative incurred interest costs of $966,000 and $924,000, respectively.

Note 10: Income Taxes

There was no provision for federal income taxes at December 31, 2004 and 2003. The Cooperative is not subject to state income taxes.

At December 31, 2004, the Cooperative had available nonmember net operating loss carryforwards of approximately $77 million for tax reporting purposes expiring in 2004 through 2021, and alternative minimum tax credit carryforwards of approximately $300,000 which carry forward indefinitely.

Temporary differences that give rise to deferred tax balances are principally attributable to fixed asset basis, safe harbor lease treatment, gain on installment sale, and financial statement accruals. Deferred tax assets also include the effect of net operating loss carryforwards. The temporary differences and the carryforward items produce a net deferred tax asset at year end. Realization of the net deferred tax asset is contingent upon the Cooperative's future earnings. A valuation allowance had been established against the asset since it has been determined that it is more likely than not that the net deferred tax asset will not be realized.

Note 11: Pennsylvania Public Utility Realty Taxes

In December of 1998, the Pennsylvania Department of Revenue issued, pursuant to the Pennsylvania Public Utility Realty Tax Act (PURTA), additional assessments to PURTA taxpayers in order to cover the shortfall between PURTA tax revenues and the distributions. The Cooperative's additional assessment was $1,868,000, which was recorded as of October 1998. The Cooperative satisfied the 1997 reassessment by applying 1998 prepaid taxes against the assessment.

In 1999, approximately 20 utilities and the Cooperative filed suits against the Commonwealth of Pennsylvania challenging provisions of PURTA. The state later amended the PURTA statute and the way in which the tax is calculated retroactive to 1998. The Cooperative subsequently received and paid a 1998 PURTA tax bill of approximately $380,000.

In 2000, the Commonwealth removed electric generation assets from the PURTA tax base and effectively returned those assets to local real estate tax jurisdiction with liability calculations based on assessed values. During 2001, PPL settled the 2000 liability for county, municipality, and school district real estate taxes on the full value of the jointly owned SSES property. Also during 2001, the Cooperative's portion of these real estate taxes was billed by and paid to PPL.

Although the final resolution of 1998 and 1999 PURTA issues remains unknown, the Cooperative believes that it has recorded appropriate liabilities for any remaining PURTA taxes. At December 31, 2004, the Cooperative had letters of credits totaling $355,000 to secure the unpaid tax liability billed by the Commonwealth of Pennsylvania.

Note 12: Related Party Transactions

The Cooperative has arrangements with two affiliated organizations, the Pennsylvania Rural Electric Association (PREA) and Continental Cooperative Services (CCS). Both organizations have provided the Cooperative with certain management, general, and administrative services on a cost reimbursement basis. The costs for the services provided by PREA were $510,541 and $252,928 for the years ended December 31, 2004 and 2003, respectively. The costs for services provided by CCS were $5,408,307 and $5,628,271 for the same two comparative periods, respectively.

CCS was incorporated in March 2000, the result of a strategic alliance between the Cooperative, based in Harrisburg, Pennsylvania, and Soyland Power Cooperative, Inc. (Soyland), formerly based in Decatur, Illinois. CCS is organized as a Non-Profit Electric Cooperative Corporation in the Commonwealth of Pennsylvania.

CCS is governed by a board of directors, composed of one representative from each affiliated distribution cooperative in Pennsylvania, New Jersey, and Illinois. Included in the Cooperative's investment in associated organizations is $100,000 for its membership in CCS.

Note 13: Commitments and Contingencies

Power Supply and Transmission Agreements

The Cooperative has entered into power supply and transmission agreements with approximately 45 service providers. A significant amount of these agreements are umbrella type agreements and do not bind the Cooperative to enter into any type of transaction. As of December 31, 2004, there were no significant transactions under these agreements.

The Cooperative has a number of power supply agreements under which it currently purchases capacity and power. These agreements contain no minimum purchase or take-or-pay provisions. Power supply agreements are as follows:

New York Power Authority

This contract meets a portion of the Cooperative's base load requirements and its delivered cost to the Cooperative's members is below market. The current contract terminates in August 2007 for the Niagara Project. A new contract for the St. Lawrence Project expires in 2017.

Williams Energy Marketing & Trading, Inc.

Effective on April 1, 2001, the Cooperative entered into an arrangement with Williams Energy Marketing & Trading, Inc. (Williams). The arrangement provides that Williams receives the output of all power from the Cooperatives' owned and controlled resources and in turn supplies all of the Cooperatives' load requirements in certain geographic areas. The agreement with Williams is scheduled to terminate on December 31, 2008.

The Williams agreement contains certain hourly and monthly energy caps. Energy provided above these thresholds is purchased at market prices. The Williams agreement also contains thresholds related to output from the Cooperative's resources. If the Cooperative fails to provide energy sufficient to meet the thresholds, the balance is purchased from Williams at market prices. Transmission service for this load is provided under the appropriate PJM Open Access Transmission Tariff (OATT) or the GPU WASP agreement as explained below.

The Williams Agreement requires the Cooperative to provide credit support in the amount of $9 million. The National Rural Utilities Cooperative Finance Corporation (CFC) issued an irrevocable standby letter of credit on behalf of the Cooperative in the amount of $9 million in favor of Williams. The letter of credit is valid until June 1, 2006. In a related agreement to facilitate the transmission of power received from Williams, the Cooperative executed a Load Serving Entity Agreement with PJM LLC (PJM). The terms of the agreement required the Cooperative to provide $2 million of credit support for activities with PJM. To provide for the credit support, the Cooperative has an irrevocable standby letter of credit from CFC for $2 million in favor of PJM. This standby letter of credit is also valid until June 1, 2006.

SSES Replacement Power Insurance Policy

The Cooperative mitigated a portion of the economic risk of an outage by purchasing a Replacement Power Insurance Policy for XL Specialty Insurance Company. Under the terms of the policy, if SSES had a forced outage event, the Cooperative would have been reimbursed the cost of replacement power for the insured quantity of 230 MW. Replacement power cost is the total of the loss, in dollars, as calculated by subtracting the insured price of $50/MWh from the market price index (PJM Western Hub LMP) and multiplying that difference by the insured quantity. The policy stipulates that the outage limit for each such forced outage is 90 consecutive days, the effective policy period is calendar year 2004, and the aggregate coverage limit is $25 million. For this coverage, the Cooperative paid XL a total premium of $861,000. Effective on January 1, 2005, the Cooperative entered into a similar insurance arrangement. Under the new policy, the Cooperative will pay a total premium of $926,400 for the policy period ending on December 31, 2005.

Pennsylvania Electric Company

The Cooperative terminated its supplemental generation portion of its Wheeling and Supplemental Power (WASP) agreement with Pennsylvania Electric Company (Penelec) on March 31, 2001. However, the Cooperative continues to purchase transmission service in the Penelec, Metropolitan Edison Company (Met-Ed), and Jersey Central Power & Light (JCP & L) zones from Penelec under the WASP agreement and the PJM OATT. Beginning April 1, 2001, the Cooperative became the sole Load Serving Entity (LSE) for the Cooperatives' load in the Penelec, Met-Ed, and JCP & L zones. Consequently, the Cooperative executed a LSE agreement with PJM, which outlines the responsibilities of each party with respect to the revised transmission and power supply arrangement. As part of its new LSE status, it was also necessary to take Network Integrated Transmission Service (NITS) under the PJM OATT. Penelec reimburses the Cooperative for most of the PJM NITS charges to prevent double billing for NITS.

Insurance

PPL, as the 90% owner and sole operator of SSES, and the Cooperative, as owner of a 10% undivided interest in SSES, are members of certain insurance programs which provide coverage for property damage to SSES nuclear generation plant. Under these programs, the plant, as a whole, has property damage coverage for up to $2.75 billion. Additionally, there is coverage for the cost of replacement power during prolonged outages of nuclear units caused by certain specified conditions. Under the property and replacement power insurance programs, PPL and the Cooperative could be assessed retrospective premiums in the event the insurers' losses exceed their reserves. At December 31, 2004, the maximum amount PPL and the Cooperative could jointly be assessed under these programs ranged from $20 million to $40 million annually.

PPL and the Cooperative's public liability for claims resulting from a nuclear incident is currently limited to $11.0 billion under provisions of the Price-Anderson Amendment Acts of 1988.

In the event of a nuclear incident at any of the reactors covered by the Act, PPL and the Cooperative could be assessed up to $100.6 million per reactor per incident, payable at $20 million per year.

Safe Harbor Lease

The Cooperative previously sold certain investment and energy tax credits and depreciation deductions pursuant to a safe harbor lease. The proceeds from the sale, including interest earned thereon, have been deferred and are being recognized on the statements of operations over the 30-year term lease. The deferred gain was $2.4 million and $2.7 million as of December 31, 2004 and 2003, respectively. The net proceeds and related interest were required by RUS to be used to retire outstanding FFB debt.

Under the term of the safe harbor lease, the Cooperative is contingently liable in varying amounts in the event the lessor's tax benefits are disallowed and in the event of certain other occurrences. The maximum amount for which the Cooperative was contingently liable as of December 31, 2004 was approximately $7.7 million. Payment of this contingent liability has been guaranteed by CFC.

Purchased Power

For years preceding 2004, the Cooperative accrued amounts as a contingency for certain purchased power related costs. In accordance with Financial Accounting Standard 5 (FAS 5), the contingency was reversed during 2004 after the Cooperative received additional information suggesting the imposition of such costs unlikely. Accordingly, the reversal was treated as a credit against purchased capacity and energy costs in the amount of $7.7 million.

Litigation

The Cooperative may be subject to claims and lawsuits that arise primarily in the ordinary course of business. At December 31, 2004, no such claims or lawsuits existed.

Note 14: Sale/Leaseback Arrangement

The Cooperative previously completed a sale and leaseback of its hydroelectric generation facility at the Raystown Dam (the Facility). The Facility was sold to a trustee bank representing Ford Motor Credit Company (Ford) for $32.0 million in cash. During 1996, Ford transferred its interest in the Facility to a third party. Under terms of the arrangement, the Cooperative is leasing the Facility for an initial term of 30 years. Payments under the lease are due in semi-annual installments which commenced January 10, 1989. At the end of the 30-year term, the Cooperative will have the option to purchase the Facility for an amount equal to the Facility's fair market value or for a certain amount fixed by the transaction documents.

The Cooperative also has the option to renew the lease for a five-year fixed rate renewal and three fair market renewal periods, each of which may not be for a term of less than two years. Payments during the fixed rate renewal period are 30% of the average semi-annual installments during the initial lease term. The Cooperative will retain co-licensee status for the Facility throughout the term of the lease. The gain of $1.9 million related to the sale is being recognized over the lease term. The unrecognized gain is recorded in other deferred revenue and was $1.11 million and $1.15 million as of December 31, 2004 and 2003, respectively.

The payments by the Cooperative under this lease were determined in part on the assumption that Ford, or its successor, will be entitled to certain income tax benefits as a result of the sale and leaseback of the Facility. In the event that Ford, or its successor, were to lose all or any portion of such tax benefits, the Cooperative would be required to indemnify Ford, or its successor, for the amount of the additional federal income tax payable to Ford, or its successor, as a result of any such loss.

The leaseback of the Facility is accounted for as an operating lease by the Cooperative. As of December 31, 2004, future minimum lease payments under this lease, which can vary based on the interest paid on the debt used to finance the transaction, are estimated as follows (in thousands):

2005	$	1,932
2006		1,932
2007		1,932
2008		1,932
Thereafter		21,677
Total minimum lease payments	$	29,405

The future minimum lease payments shown above are for the initial lease term and the five-year renewal period. These payments are based on an assumed interest rate of 8.8% and may fluctuate based on differences between the future interest rate and the assumed interest rate. Rental expense for this lease totaled $1.4 million and $2.2 million in years ended December 31, 2004 and 2003, respectively.

Note 15: Government Regulations

The Energy Policy Act of 1992 established, among other things, a fund to pay for the decontamination and decommissioning of three nuclear enrichment facilities operated by DOE. A portion of the fund is to be collected from electric utilities that have purchased enrichment services from DOE and will be in the form of annual special assessments for a period not to exceed more than 15 years. The special assessments are based on a formula that takes into account the amount of enrichment services purchased by the utilities in past periods.

The Cooperative has previously recorded its share of the liability in connection with PPL's recognition of the liability in the accounts of SSES. The Cooperative's share of the liability is $4.4 million. The Cooperative recorded its share of the liability as a deferred charge which is being amortized to expense and paid over 15 years, consistent with the ratemaking treatment. The remaining liability to be amortized was $0.9 million and $1.2 million as of December 31, 2004 and 2003, respectively.

Note 16: Fair Value of Financial Instruments

The estimated fair value amounts have been determined by the Cooperative using available market information and appropriate valuation methodologies. However, considerable judgment is required in interpreting market data to develop the estimates of fair value.

Accordingly, the estimates presented herein are not necessarily indicative of the amounts that the Cooperative could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Assets

- *Cash and Restricted Investments* – The carrying amounts of these items are a reasonable estimate of their fair value due to the short-term nature of the instruments.
- *Other Investments and Investments in Associated Organizations* – The fair value of other investments are estimated based on quoted market prices. Fair values of investments in associated organizations approximate their carrying amount.
- *Notes Receivable from Members* – The carrying amount of the Cooperative's notes receivable from members, which primarily relate to sales-type leases, approximates fair value because the notes bear a variable rate of interest which is reset on a frequent basis.

Liabilities

- *Long-term debt* – The fair value of the Cooperative's fixed rate long-term debt is estimated using discounted cash flows based on current rates offered to the Cooperative for similar debt of the same remaining maturities.

The estimated fair values of the Cooperative's financial instruments at December 31, 2004 and 2003, are as follows (in thousands):

	2004		2003	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Cash and cash equivalents	$ 35,781	$ 35,781	$ 17,889	$ 17,887
Restricted investments	15,837	15,837	15,777	15,777
Other investments	47,828	47,828	44,065	44,065
Investment in associated organizations	739	739	841	841
Notes receivable from members	68	68	88	88
Long-term debt	235,737	201,334	262,297	212,457

Soyland Power Cooperative, Inc.

Soyland Power Cooperative, Inc.
Accountants' Report and Financial Statements

December 31, 2004 and 2003

Contents

Financial Statements

Independent Accountants' Report

Board of Directors
Soyland Power Cooperative, Inc.
Harrisburg, Pennsylvania

We have audited the accompanying balance sheets of Soyland Power Cooperative, Inc. (Cooperative) as of December 31, 2004 and 2003, and the related statements of income, members' 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. 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 Soyland Power Cooperative, Inc. as of December 31, 2004 and 2003, 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.

As discussed in Note 6 to the financial statements, during 2003, the Cooperative changed its method of accounting for its asset retirement obligation to comply with Financial Accounting Standard 143 (FAS 143).

BKD, LLP

February 18, 2005

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SOYLAND POWER COOPERATIVE, INC.

BALANCE SHEETS
DECEMBER 31, 2004 AND 2003

Assets

	2004	2003
Electric Utility Plant, at cost		
In service (See Note 2)	$ 83,867,826	$ 79,746,905
Less accumulated depreciation	(43,603,437)	(40,396,666)
	40,264,389	39,350,239
Construction work in progress	2,118,413	4,069,097
Plant site held for future use	3,921,195	3,921,195
Net electric utility plant	46,303,997	47,340,531
Investments (See Notes 3 and 9)	12,600,849	12,312,894
Current Assets		
Cash and temporary investments	8,659,101	2,906,326
Accounts receivable, members	7,804,069	7,902,362
Other receivables	690,330	710,270
Inventories	2,475,348	2,401,370
Prepayments and other assets	358,153	322,813
Advance energy payments	—	249,050
Total current assets	19,987,001	14,492,191
Deferred Charges (See Note 4)		
Deferred loss on asset write-down	4,288,368	16,018,977
Deferred opt-out fee	20,191,245	23,047,005
Deferred recoverable energy	8,269,989	9,196,620
	32,749,602	48,262,602
	$ 111,641,449	$ 122,408,218

See Notes to Financial Statements

SOYLAND POWER COOPERATIVE, INC.

BALANCE SHEETS
DECEMBER 31, 2004 AND 2003

Members' Equities and Liabilities

	2004	2003
Members' Equities		
Membership fees	$ 1,675	$ 1,675
Patronage capital	1,815,155	1,638,736
Retained earnings	13,078,811	9,879,926
Total members' equities	14,895,641	11,520,337
Long-Term Debt (See Notes 5 and 9)	58,392,950	71,674,548
Asset Retirement Obligation (See Note 6)	6,134,354	5,679,957
Current Liabilities		
Current installments of long-term debt	13,226,066	12,522,838
Line of credit	—	1,000,000
Accounts payable	6,329,117	5,093,220
Member prepayments	2,459,087	1,780,315
Accrued interest	282,618	353,342
Accrued expenses	476,496	533,068
Total current liabilities	22,773,384	21,282,783
Deferred Revenue (See Note 1)	9,445,120	12,250,593
	$ 111,641,449	$ 122,408,218

STATEMENTS OF INCOME
YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004	2003
Operating Revenues		
Electric energy sales	$ 81,043,224	$ 80,098,503
Distribution revenue	1,007,522	922,002
Rent of electric property	67,112	65,740
	82,117,858	81,086,245
Operating Expenses		
Operations		
Purchased capacity and energy costs	47,611,185	46,625,105
Production-other	4,141,788	4,599,587
Transmission	1,102,854	712,441
Distribution	290,998	217,522
	53,146,825	52,154,655
Maintenance	1,219,281	891,479
Administrative and general	3,185,468	2,551,100
Depreciation and amortization	18,832,705	17,506,768
Accretion	454,397	420,737
Property and other taxes	479,887	480,858
	77,318,563	74,005,597
Net Operating Margin	4,799,295	7,080,648
Other Revenue		
Interest and other patronage capital income	843,080	653,906
Litigation settlement (see Note 7)	1,532,613	—
Net Margin Before Interest Charges	7,174,988	7,734,554
Interest Charges		
Interest on long-term debt	3,708,100	4,479,230
Other	91,584	339,985
	3,799,684	4,819,215
Net Income Before Cumulative Effect of Adoption of FAS 143	3,375,304	2,915,339
Cumulative Effect of Adoption of FAS 143 (see Note 6)	—	(1,066,041)
Net Income	$ 3,375,304	$ 1,849,298

See Notes to Financial Statements

Soyland Power Cooperative, Inc.

Statements of Members' Equities
Years Ended December 31, 2004 and 2003

	Membership Fees	Patronage Capital	Retained Earnings	Total Members' Equities
Balance, January 1, 2003	$ 1,675	$ 1,638,736	$ 8,030,628	$ 9,671,039
Net income	—	—	1,849,298	1,849,298
Balance, December 31, 2003	1,675	1,638,736	9,879,926	11,520,337
Patronage capital allocation	—	176,419	(176,419)	—
Net income	—	—	3,375,304	3,375,304
Balance, December 31, 2004	$ 1,675	$ 1,815,155	$ 13,078,811	$ 14,895,641

See Notes to Financial Statements

STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2004 AND 2003

	2004	2003
Operating Activities		
Net income	$ 3,375,304	$ 1,849,298
Items not requiring cash		
Depreciation of electric utility plant	3,319,705	3,149,768
Amortization of deferred charges	15,513,000	14,357,000
Accretion of asset retirement obligation	454,397	420,737
Loss on equity investment	—	40,871
Cumulative effect of adoption of FAS 143	—	1,066,041
Change in		
Accounts and other receivables	578,720	542,665
Inventories	(73,978)	60,645
Prepayments and other assets	213,710	(58,481)
Accounts payable and accrued expenses	1,108,601	(4,331,772)
Deferred revenue	(2,805,473)	(2,952,774)
Asset retirement obligation	—	3,656,017
Net cash provided by operating activities	21,683,986	17,800,015
Investing Activities		
Additions to electric utility plant, net	(2,743,658)	(1,576,371)
Additions to investments	(1,086,170)	(2,103,881)
Proceeds from investments	798,215	835,967
Net cash used in investing activities	(3,031,613)	(2,844,285)
Financing Activities		
Net payments on line of credit	(1,000,000)	(8,846,615)
Principal payments on long-term debt	(12,578,370)	(13,428,017)
Proceeds from long-term debt	—	8,529,463
Change in member prepayments	678,772	(456,072)
Net cash used in financing activities	(12,899,598)	(14,201,241)
Net Increase in Cash and Cash Equivalents	5,752,775	754,489
Cash and Cash Equivalents, Beginning of Year	2,906,326	2,151,837
Cash and Cash Equivalents, End of Year	$ 8,659,101	$ 2,906,326
Supplemental Cash Flows Information		
Cash paid for interest	$ 3,870,408	$ 4,780,058
Transfer of construction in progress to other receivables	460,487	—

See Notes to Financial Statements

SOYLAND POWER COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

Note 1: Nature of Operations and Significant Accounting Policies

Nature of Operations

Soyland Power Cooperative, Inc. (Cooperative) is a not-for-profit organization engaged in the generation and transmission of wholesale electric service to its eleven members located throughout Illinois. The Cooperative extends unsecured credit to its members. The Cooperative has entered into wholesale power agreements with each of its members which require the members to buy and receive from the Cooperative all of their power and energy requirements and require the Cooperative to sell and deliver power and energy in satisfaction of such requirements. The wholesale power agreements with members extend to various dates from years 2015 to 2017.

The Cooperative has a formal buyout policy under which a member who seeks to buy out of the wholesale power agreement is required to reimburse the Cooperative for all liabilities, including any related to Cooperative's power supply and transmission agreements, incurred in connection with such buyout, in accordance with a predetermined formula.

The Cooperative's wholesale power rate charged to members is established by the Board of Directors. Such wholesale power rate charged to members is determined based on annual cash requirements, including debt service requirements. The formula for determining the rate is subject to the approval of the Federal Energy Regulatory Commission (FERC), which approval has been received. The Cooperative is not subject to the regulatory authority of the Illinois Commerce Commission.

Deregulation

In 1997, the State of Illinois passed Public Act 90-561, Electric Service Customer Choice and Rate Relief Law of 1997 (Act). The Act was intended to bring competition to the electric industry in the State of Illinois and ultimately lead to market-based pricing of electric generation services. The Cooperative is exempt from the Act and management believes the Act will not significantly affect the Cooperative's operation or ability to recover its costs through future rates charged to members.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial report, as well as the reported amounts of revenues and expenses during the years then ended. Actual results could differ from those estimates.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2004 AND 2003

Basis of Accounting

The accounting records of the Cooperative are maintained in accordance with the Uniform System of Accounts prescribed by FERC. In accordance with FERC guidelines, the Cooperative also maintains its accounts in accordance with Statement of Financial Accounting Standards No. 71, *Accounting for the Effects of Certain Types of Regulation.*

Electric Utility Plant

Electric utility plant is carried at cost. Depreciation of electric utility plant in service is provided over the estimated useful lives of the respective assets on the straight-line basis at rates as follows:

Production Plant		
Steam		3.1% - 4.0%
Gas turbine and diesel	6.7%	
Transmission Plant	2.8%	
Distribution Plant	3.0%	
General Plant		2.5% - 20.0%

Maintenance and repairs of property and replacements and renewals of items determined to be less than units of property are charged to expense. Replacement and renewals of items considered to be units of property are charged to the property accounts. At the time properties are disposed of, the original cost, plus cost of removal less salvage of such property, is charged to accumulated depreciation.

Cash and Cash Equivalents

Cash and cash equivalents consist of bank deposits in federally insured accounts and temporary investments. Temporary investments consist of an interest bearing sweep account, which investments are stated at market. The Cooperative has one banking arrangement which requires the maintenance of a compensating balance. The Cooperative places its cash and temporary investments with high quality financial institutions. Such cash and temporary investments may be in excess of the FDIC insurance limit.

For purposes of the statement of cash flows, the Cooperative considers all highly liquid debt instruments, if any, purchased with an original maturity of three months or less to be cash equivalents.

Accounts Receivable

Accounts receivable are stated at the amount billed to members. Accounts receivable are due in accordance with approved policies. An allowance for doubtful accounts has not been recorded because all accounts receivable are considered fully collectible.

Inventories

Inventories consist of fuel, materials and supplies and are stated at moving average cost.

Deferred Charges

Deferred charges consist of amounts that are expected to be recovered through future rates.

Member Prepayments

Member prepayments represent cash advances from members. The Cooperative uses these advances to reduce borrowings. The Cooperative pays interest on member advances at a rate lower than that on outstanding debt. Such interest payments on member advances totaled $89,900 and $71,604 for the years ended December 31, 2004 and 2003, respectively.

Power Supply Payments

Payments made under power supply agreements are classified as purchased capacity and energy costs in the statement of income.

Income Taxes

The Cooperative is exempt from income taxes under Section 501 of the Internal Revenue Code and a similar provision of state law. However, the Cooperative is subject to federal income tax on any unrelated business taxable income. No income taxes were due or paid in 2004 and 2003.

Deferred Revenue

Deferred revenue consists of payments received from members that have bought out of the wholesale power agreement and regulatory asset prepayments. Deferred revenue is being amortized over the period during which it would have been earned (through 2007).

	2004	2003
Member buyout payments	$ 7,886,768	$ 10,515,691
Regulatory asset prepayments	1,558,352	1,734,902
Total	$ 9,445,120	$ 12,250,593

Revenue Recognition

Revenue from the sale of electricity to members is recorded based on contracted power use.

Note 2: Electric Utility Plant in Service

	2004	2003
Steam and other production plant	$ 40,964,798	40,075,298
Transmission plant	30,315,564	27,503,218
Distribution plant	8,770,929	8,741,571
General plant	3,816,535	3,426,818
Total	$ 83,867,826	$ 79,746,905

Note 3: Investments

	2004	2003
National Rural Utilities		
Cooperative Finance Corporation (CFC)		
Membership fees	$ 1,000	$ 1,000
Patronage capital	3,846,488	3,982,639
Subscription capital term certificates	2,252,049	2,252,049
Loan capital term certificates	5,698,062	5,799,881
Total	11,797,599	12,035,569
Debt securities	503,362	—
Other associated organizations	203,158	180,595
Investments in economic development organizations	96,730	96,730
Total	$ 12,600,849	$ 12,312,894

The Cooperative considers CFC capital term certificates to be a condition of borrowing and patronage capital to be directly related to borrowing.

Loan capital term certificates mature at various intervals in the years 2006 through 2022 and bear interest at rates ranging from 0% to 4.92%.

Subscription capital term certificates at December 31, 2004, bear interest at 5% and mature at various dates from years 2070 to 2080.

Note 4: Deferred Charges

The amount of the deferred loss on asset write-down relates to an interest in the Clinton nuclear generating facility. The regulatory asset will be amortized to operations as the amounts are collected in the rate charged to members, and is anticipated to be fully amortized by December 31, 2005.

The remaining amount of the Opt-Out Fee paid to AmerenIP, formerly Illinois Power, is expected to be recovered in future rates charged to members and has, therefore, been recorded as a regulatory asset at December 31, 2004 and 2003.

The recoverable energy amount is also expected to be recovered in future rates charged to members and has, therefore, been recorded as a regulatory asset at December 31, 2004 and 2003.

Amortization of regulatory assets totaled $15,513,000 and $14,357,000 in 2004 and 2003, respectively.

Note 5: Long-Term Debt

	2004	2003
CFC — fixed rates (ranging between 4.90% and 6.95%) promissory notes payable, due in quarterly installments through 2022	$ 25,354,882	$ 26,157,711
CFC — variable rate (3.05% at December 31, 2004) mortgage note payable, due in various quarterly installments through 2006	6,594,976	12,781,183
CFC — fixed rate (5.95%) capital addition loan note payable, due in quarterly installments through 2014	17,900,000	19,300,000
CFC — fixed rate (5.25%) promissory notes payable, due in quarterly installments through 2007 [1]	6,944,340	9,558,058
CFC — variable rate (3.05% at December 31, 2004) promissory note payable, due in quarterly installments through 2011 [1]	6,894,455	7,870,971
CFC – variable rate (3.10% at December 31, 2004) capital addition loan note, payable, due in quarterly installments through 2015	6,927,909	7,463,000
CFC – fixed rate (6.15%) promissory note payable, due in quarterly installments through 2015	1,002,454	1,066,463
Total long-term debt	71,619,016	84,197,386
Less current installments	13,226,066	12,522,838
Long-term debt, excluding current installments	$ 58,392,950	$ 71,674,548

[1] Certain Promissory Notes (Notes) to CFC are partially guaranteed by the members of the Cooperative. All Notes are secured by a mortgage on the assets of the Cooperative.

Annual maturities of long-term debt at December 31, 2004 are as follows: 2005, $13,226,066; 2006, $6,937,750; 2007, $5,864,165; 2008, $4,624,037; 2009, $4,965,943; and thereafter, $36,001,055.

The Cooperative has an $18,000,000 operating line of credit with CFC that expires December 31, 2005. The line of credit had an outstanding balance of $1,000,000 as of December 31, 2003, and no outstanding balance as of December 31, 2004. The interest rate on the line of credit fluctuates monthly based on CFC's cost of funds (3.10% at December 31, 2004).

During 2003, the Cooperative borrowed $7,463,000 that was used to fund 2002 and estimated 2003 capital additions. During 2004 and in agreement with CFC, the Cooperative reduced the amount available for advance by $1,923,629, the amount borrowed in excess of actual 2003 capital additions. No additional amounts were borrowed for 2004 capital additions. As of December 31, 2004, the Cooperative has approximately $8,546,000 available from long-term loans approved by CFC for capital additions.

All assets of the Cooperative are pledged to secure the CFC debt.

Note 6: Asset Retirement Obligation

The Cooperative adopted Financial Accounting Standard 143 (FAS 143), "Accounting for Asset Retirement Obligations," effective January 1, 2003. FAS 143 addresses the accounting for obligations associated with the retirement of tangible long-lived assets. In connection with the adoption of FAS 143, the Cooperative recorded a cumulative effect of adoption that decreased net income by $1,066,041.

The changes in the carrying amounts of asset retirement obligations were as follows:

	2004	2003
Beginning balance	$ 5,679,957	$ 5,259,220
Accretion expense	454,397	420,737
Ending balance	$ 6,134,354	$ 5,679,957

The amount of actual obligation could differ materially from the estimates reflected in these financial statements.

Note 7: Litigation Settlement

In October 2004, the Cooperative received $2,511,026 from a former member cooperative as final settlement of a Federal Energy Regulatory Commission (FERC) order. The payment reflected a total and complete settlement of all claims between the Cooperative and that former member. Of the $2,511,026 received, the Cooperative recorded income of $1,532,613 and refunded $978,413 to other former member cooperatives that elected to participate in the litigation. The amount paid to other former member cooperatives represents their respective share of legal costs and settlement proceeds.

NOTES TO FINANCIAL STATEMENTS
DECEMBER 31, 2004 AND 2003

Note 8: Related Parties

The Cooperative has an arrangement with an affiliated organization, Continental Cooperative Services (CCS). The organization provides the Cooperative with certain management, general, and administrative services on a cost reimbursement basis. The costs for services provided by CCS were $4,942,363 and $4,204,011 for the years ended December 31, 2004 and 2003, respectively. The Cooperative had accounts payable to CCS of $307,844 as of December 31, 2004, and accounts receivable from CCS of $328,060 as of December 31, 2003.

CCS was incorporated in March 2000, the result of a strategic alliance between Allegheny Electric Cooperative, Inc. (Allegheny), based in Harrisburg, Pennsylvania, and the Cooperative which is now based in Harrisburg, Pennsylvania. CCS is organized as a Non-Profit Electric Cooperative Corporation in the Commonwealth of Pennsylvania.

CCS is governed by a board of directors, composed of one representative from each affiliated distribution cooperative in Pennsylvania, New Jersey, and Illinois. Included in the Cooperative's investments is $100,000 for its membership in CCS.

Note 9: Disclosures About Fair Value of Financial Instruments

The estimated fair value amounts have been determined by the Cooperative using available market information and appropriate valuation methodologies. However, considerable judgment is necessarily required in interpreting market data to develop the estimates of fair value.

Accordingly, the estimates presented herein are not necessarily indicative of the amounts that the Cooperative could realize in a current market exchange. The use of different market assumptions and/or estimation methodologies may have a material effect on the estimated fair value amounts.

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2004 AND 2003

The following methods and assumptions were used to estimate the fair value of each class of financial instruments:

Assets

- *Investments* — The investment balances comprise the following:

	2004	2003
CFC capital term certificates (1)		
Subscription certificates	$ 2,252,049	$ 2,252,049
Loan certificates	5,698,062	5,799,881
	7,950,111	8,051,930
Patronage capital certificates		
Other patronage (1)	3,846,488	3,982,639
Memberships and miscellaneous patronage (2)	204,158	181,595
Debt securities (4)	503,362	—
Other associated organizations (3)	96,730	96,730
Total	$ 12,600,849	$ 12,312,894

Fair value for investments is estimated as follows:

1) The Cooperative considers CFC capital term certificates to be a condition of borrowing and patronage capital to be directly related to borrowing. As such, Cooperative management believes the fair value of these items is not determinable and they are reflected at their carrying amount.
2) Management was not able to estimate the fair value of instruments that represent the Cooperative's investment in memberships and miscellaneous patronage and they remain at their carrying value.
3) Management was not able to estimate the fair value of instruments that represent the Cooperative's investment in economic development instruments and they remain at their carrying amount.
4) Fair value is based on quoted market prices, if available. If a quoted market price is not available, fair value is estimated using quoted market prices for similar securities.

- *Cash and Temporary Investments* — The carrying amounts of these items are a reasonable estimate of their fair value due to the short-term nature of the instruments.

Liabilities

- *Long-Term Debt* — Due to the current market interest rates and/or short-term maturities of the Cooperative's debt, carrying amount approximates fair value.

	2004		2003	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Assets				
Investments	$ 12,600,849	(see above)	$ 12,312,894	(see above)
Cash and temporary investments	8,659,101	8,659,101	2,906,326	2,906,326
Liabilities				
Long-term debt (including current maturities)	71,619,016	71,619,016	84,197,386	84,197,386

Note 10: Commitments

Power Supply

The Cooperative owns generating capacity of 176 MW. Currently, all additional energy requirements are being furnished through a power supply agreement with AmerenEnergy Marketing Company.

Effective January 2003, the Cooperative contracted with AmerenEnergy Marketing Company to purchase energy at varying monthly minimum and maximum quantities of energy through December 2008. The contract commits the Cooperative to purchase an annual minimum of $39,716,270. The members guarantee performance under this contract.

Patronage Capital Allocation

In accordance with the Cooperative's bylaws, a patronage capital allocation will be made during 2005. The patronage capital allocation shall be all amounts in excess of operating costs and expenses offset for losses incurred during the current fiscal years. All non-operating revenues in excess of expenses are considered contributions to capital and are not allocated.

Patronage capital retirements are restricted by the terms of the CFC mortgage and the Cooperative's bylaws.

Note 11: Contingencies

The Cooperative may be subject to claims and lawsuits that arise primarily in the ordinary course of business. At December 31, 2004, no such claims or lawsuits existed.

Note 12: Subsequent Event

In February 2005, six of the eleven members of the Cooperative initiated a process for the Cooperative to become a minority owner of the proposed Prairie State Power Project planned for Washington County, Illinois. The Cooperative's investment for the 50 MW share of the two unit 1,500 MW coal plant will be approximately $100 million. The plant is scheduled for commercial operation during 2009.

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CONTINENTAL
COOPERATIVE
SERVICES

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