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Reaching  
**MILESTONES**

ALLEGHENY ELECTRIC COOPERATIVE, INC

2010 ANNUAL REPORT





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**Allegheny Electric Cooperative, Inc. in 2010 achieved a number of significant milestones in establishing itself as a leader in a changing energy environment.**

Taking a look back often provides a nice perspective on things. Like markers on a timeline, we can see events and decisions that have shaped us over time. In the past year, we can see several accomplishments that have established 2010 as a “milestone” year for Allegheny Electric Cooperative, Inc. (Allegheny). More importantly, we can see how these individual pieces – all tied together in a “Patchwork Quilt” design – help Allegheny continue to successfully fulfill its mission of providing a reliable supply of electricity at a competitive price.

In having this opportunity to look back, we are pleased to report that 2010 has been a successful and productive year for Allegheny. The power provider for 14 electric distribution cooperatives in Pennsylvania and New Jersey recorded another year of excellent operating performance and positive financial results. Highlighted by better-than-expected margins, Allegheny’s strong financial position allowed the retirement of more than \$3 million in patronage capital to its members in 2010, bringing the total retired since 2006 to more than \$17 million. Further, Allegheny assigned over \$6 million to members as patronage capital for 2010.

In 2010, Allegheny’s strong financial position allowed the retirement of more than \$3 million in patronage capital to its members.

In recording a solid year financially and operationally, Allegheny delivered wholesale rates that were lower than they were in 1987, and marked some significant achievements along the way.

Most notably, Allegheny ended 2010 by positioning itself to have the lowest generation rate in the region – and the timing could not have been better. The remaining caps on electric generation rates – initiated under the electric restructuring process that began in the mid-1990s in Pennsylvania – were lifted at the close of 2010. With the rate caps off, generation



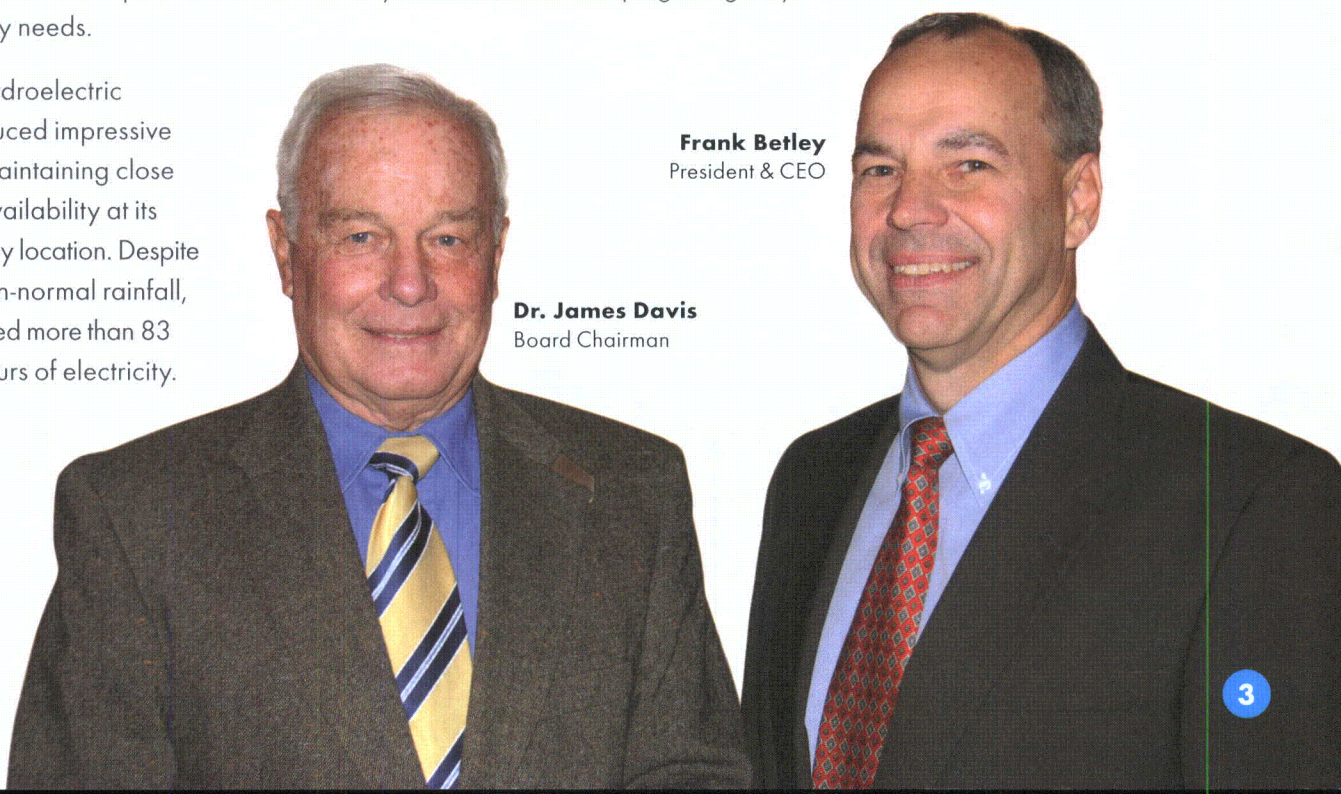
suppliers have had to prepare for a fully competitive marketplace. As investor-owned utilities (IOUs) suddenly had to contend with market-influenced rate increases, Allegheny members enjoyed continued rate stability – with generation prices that were the lowest in Pennsylvania and New Jersey. Given the volatility of the energy market today, this is a striking achievement, and one in which our cooperative program can take great pride.

Unlike the IOUs, who sold off or transferred ownership of their generation assets under electric restructuring, Allegheny held onto its power resources. Today, this strong foundation in self-owned, baseload generation resources provides approximately two-thirds of our energy needs, leaving Allegheny and its member cooperatives not nearly as affected by market volatility as the IOUs. This foundation also gives us tremendous flexibility both in securing other power needs and in long-range planning.

In 2010, Allegheny's self-owned resources enjoyed an exceptional year. Following a generation record set in 2009, the Susquehanna Steam Electric Station, the nuclear plant we co-own with PPL Corporation, achieved another note of distinction. With equipment and system upgrades completed in 2010, the facility's Unit 1 reactor is now the largest boiling water reactor in terms of thermal power and generating capacity in the United States, according to the Nuclear Regulatory Commission (NRC).

This milestone achievement comes on the heels of the NRC's renewal of the operating licenses for the plant's two units for an additional 20 years, thanks to the plant's record of safe and reliable operation. Together, both units at the Luzerne County, Pa., facility generated close to 2 billion kilowatt-hours of electricity for Pennsylvania and New Jersey cooperatives in 2010. The license renewal extends production at the facility to 2044, further helping Allegheny meet future energy needs.

Our Raystown Hydroelectric Project also produced impressive results in 2010, maintaining close to 100 percent availability at its Huntingdon County location. Despite receiving less-than-normal rainfall, the facility provided more than 83 million kilowatt-hours of electricity.



**Frank Betley**  
President & CEO

**Dr. James Davis**  
Board Chairman

Raystown plays an important role in bringing more renewable generation into the cooperative power supply mix, while providing other significant benefits. Recognized in 2009 as a Tier 1 renewable generation resource, the Raystown Project allows Allegheny to market renewable energy certificates (RECs) generated by the plant. Revenue from the sale of these RECs provides funding for our Renewable Energy Assistance Program (REAP), which has assisted member cooperatives and their consumers with the costs associated in the interconnection of consumer-owned renewable energy units to cooperative systems.

In June 2010, Allegheny achieved another milestone by interconnecting the 100th consumer-owned renewable energy project in the Pennsylvania-New Jersey electric cooperative service area. These interconnections, which include a mix of wind turbines, solar arrays and anaerobic digesters, reached 140 by the end of 2010. Programs like REAP – tied to our Raystown facility – help boost the supply of clean energy resources and further enhance our ability to better serve our members.

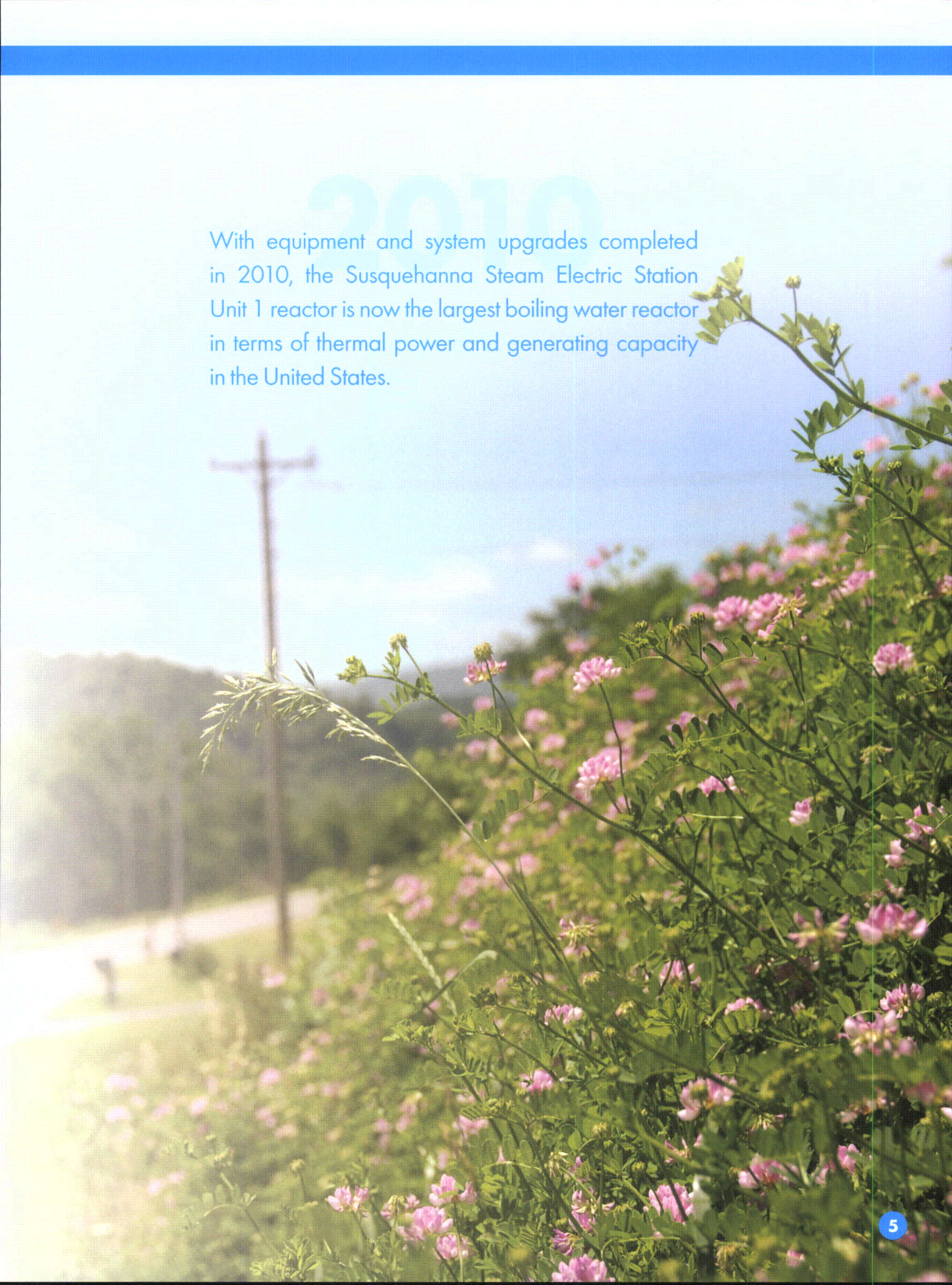
**In June 2010, Allegheny achieved another milestone by interconnecting the 100th consumer-owned renewable energy project in the Pennsylvania-New Jersey electric cooperative service area.**

Working with our member cooperatives, Allegheny achieved a major Coordinated Load Management System (CLMS) milestone in November 2010. Developed in 1986 with our distribution cooperatives, CLMS is a demand-response program that works by shifting electricity use of residential electric water heaters and other special equipment

in the homes of volunteer consumers from times of peak demand (when prices are higher) to times of lesser demand. Reducing the amount of power used during these periods has been a significant factor in stabilizing electric costs. Last November, the program reached the \$100 million mark for gross power cost savings.

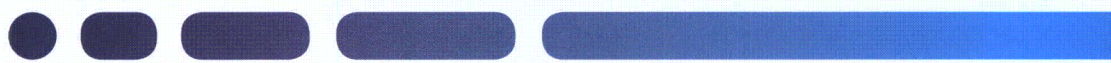
This achievement comes at a time when more attention is being focused on energy efficiency and conservation measures. In fact, Allegheny's CLMS has been touted by legislators and governmental officials as the model for demand-side management systems. Many IOUs are now being mandated to develop similar programs. Our CLMS is currently undergoing an enhancement project, with equipment upgrades that will continue to improve its capabilities.

All tied together, these milestone achievements exemplify Allegheny's Patchwork Quilt design: different pieces working together in an overall strategy that has proved highly successful for the organization and its members. Looking back on those achievements provides a nice perspective on Allegheny's progress. It also serves as a nice vantage point from which to view Allegheny's future course – a course moving in a very positive direction.



2010

With equipment and system upgrades completed in 2010, the Susquehanna Steam Electric Station Unit 1 reactor is now the largest boiling water reactor in terms of thermal power and generating capacity in the United States.



## THE YEAR IN REVIEW

Marked by solid financial and operational performance, Allegheny in 2010 continued to show the strength of its innovative Patchwork Quilt strategy of power supply management. The strategy involves securing power in different amounts, from different sources, for different periods of time. Developed over the past several years, the plan helps further diversify Allegheny's power resources – all the more prudent, given the volatility of the energy market and difficult economic climate of the past few years.

The Patchwork Quilt plan adds complementary pieces to a solid foundation of Allegheny-owned or -controlled power resources, helping us achieve our core mission of stable and affordable wholesale power rates for our member cooperatives in Pennsylvania and New Jersey.

Here is a look at Allegheny's 2010 power supply portfolio:

### RAYSTOWN HYDROELECTRIC PROJECT

Allegheny's Raystown Hydroelectric Project is a two-unit, 21-megawatt, run-of-river hydropower facility located at Raystown Lake and Dam in Huntingdon County, Pa. In 2010, Raystown provided 83.2 million kilowatt-hours, equating to 2.6 percent of Allegheny's requirements for the year. The plant maintained a 99.5 percent availability.

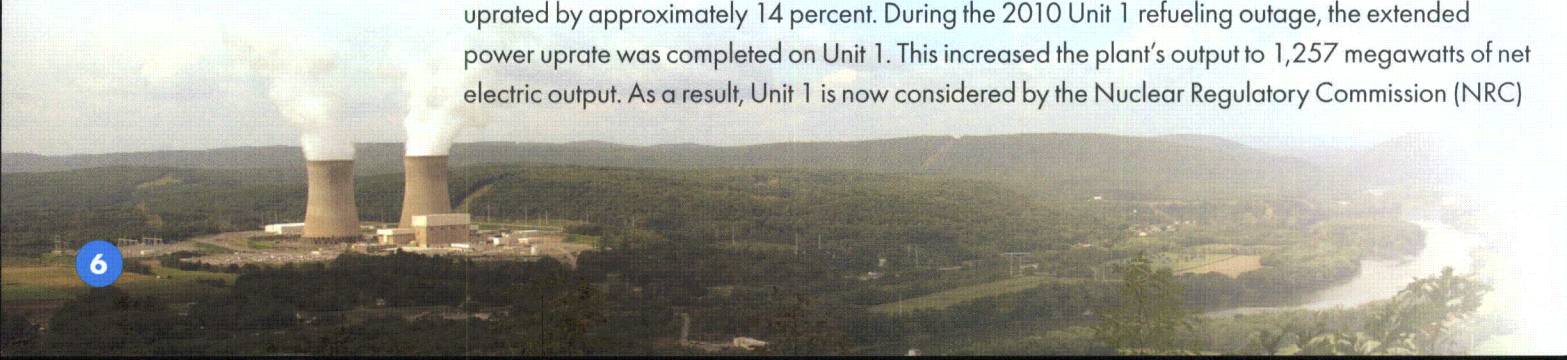
Allegheny staff operates the hydroelectric project in close cooperation with the Baltimore District of the U.S. Army Corps of Engineers, which controls water releases from Raystown Lake, the largest man-made body of water in Pennsylvania.

### SUSQUEHANNA STEAM ELECTRIC STATION

Allegheny owns 10 percent of the Susquehanna Steam Electric Station (SSES), a 2,450-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 2010, this 10 percent share of SSES provided 1.85 billion kilowatt-hours of electricity to Pennsylvania and New Jersey electric cooperatives. Considering a refueling outage, the capacity factor of Unit 1 was 75.1 percent; Unit 2 achieved a calendar year capacity factor of 95.3 percent. This corresponds to an average annual composite capacity factor for the facility of 85.2 percent.

Both Unit 1 and Unit 2 operate on a 24-month refueling cycle, and both are in the process of being uprated by approximately 14 percent. During the 2010 Unit 1 refueling outage, the extended power uprate was completed on Unit 1. This increased the plant's output to 1,257 megawatts of net electric output. As a result, Unit 1 is now considered by the Nuclear Regulatory Commission (NRC)





to be the United States' largest boiling water reactor in terms of thermal power and generating capacity. Completion of the extended power uprate for Unit 2 is scheduled for spring of 2011.

In November 2009, the NRC officially renewed the operating licenses for Susquehanna units 1 and 2 for an additional 20 years, extending operation to 2042 for Unit 1 and 2044 for Unit 2.

## NEW YORK POWER AUTHORITY

Since 1966, Allegheny has purchased power generated by 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 2010, Allegheny received an allocation of 31 megawatts from the projects for the benefit of its 14 member cooperatives. Since 1966, it is estimated that NYPA generation has saved our electric distribution cooperatives more than \$347 million (\$10.2 million in 2010), compared to the cost of purchasing the same amount of electricity from other sources.

## LOAD MANAGEMENT

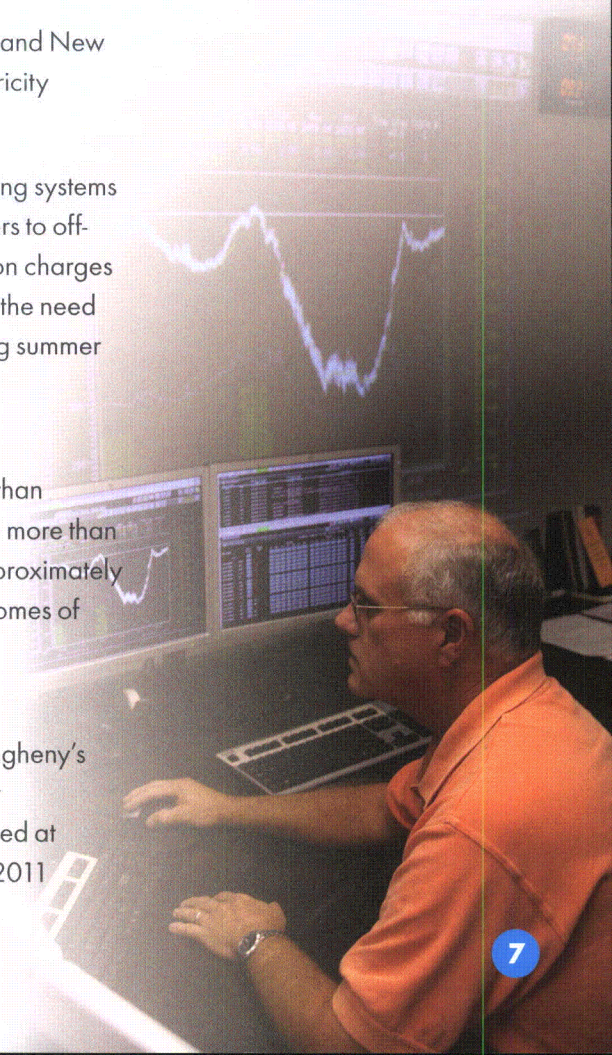
In 1986, Allegheny and its member electric distribution cooperatives in Pennsylvania and New Jersey launched the Coordinated Load Management System (CLMS) to reduce electricity consumption during peak demand periods.

By shifting use of residential water heaters, electric thermal units, dual fuel home heating systems and other special equipment in the homes of volunteer cooperative consumer-members to off-peak hours, the CLMS improves system efficiency, cuts costly demand and transmission charges Allegheny and its member cooperatives must pay for purchased power, and reduces the need for new generating capacity. The system reduces transmission zone peaks and, during summer peaks, reduces Allegheny's capacity obligation under procedures established by the PJM Interconnection.

Over the past year, the CLMS reduced cooperative purchased power costs by more than \$5.3 million, bringing total net power cost savings achieved since December 1986 to more than \$100.7 million. Currently, 203 substations are being utilized for load control with approximately 48,500 load control receivers installed on appliances (mostly water heaters) in the homes of electric cooperative consumer-members.

Beginning in 2007, Allegheny took steps to update the system. New CLMS-related equipment was placed on-line beginning in 2008 and by the end of 2009, 12 of Allegheny's 14 member cooperatives were in the process of installing new field equipment in their respective substations. At the end of 2010, field equipment installations were completed at 43 of the 203 substations. Further implementation of the CLMS upgrade throughout 2011 will provide even greater system efficiencies.

In 2010, Allegheny's share of the Susquehanna Steam Electric Station provided 1.85 billion kilowatt-hours of electricity to Pennsylvania and New Jersey electric cooperatives.



## CLEAN POWER COMMITMENT

Allegheny and its 14 member cooperatives continue to be very active in meeting consumer-members' desire to support energy efficiency, clean and renewable energy generation, and a secure energy future for electric cooperatives. In addition to Allegheny's investments in clean and carbon-free nuclear and hydropower resources, and our demand-side efficiency measures, here are some of our other initiatives for a better environment:

## INTERCONNECTED PROJECTS

Allegheny and its member distribution cooperatives actively worked with cooperative consumer-members who were considering the addition of renewable energy projects to their homes or businesses. By the end of 2010, there were 140 consumer-member-owned renewable energy projects that had been interconnected, including six digesters, 44 wind turbines, 89 solar photovoltaic arrays, and one small hydroelectric facility. We expect to interconnect additional projects on a regular basis. See map next page, foldout.

## RENEWABLE ENERGY ASSISTANCE PROGRAM

As a positive partner in the Commonwealth's alternative energy initiatives, Allegheny provides a program to assist cooperative consumer-members who want to install a clean energy generation system at their home, farm or business. The Renewable Energy Assistance Program (REAP) provides grants to electric distribution cooperatives to help cover various interconnection costs, such as metering equipment and distribution transformers. The program also pays for certain transitional costs to help ensure that other electric cooperative consumer-members do not subsidize the operation or installation of small renewable energy generation systems – such as anaerobic digesters, wind turbines or solar units. In many ways, REAP reflects the electric cooperative tradition of members helping members, and adds a new chapter to Allegheny's history of addressing environmental and energy challenges in a cost-effective and fair way.

## RAYSTOWN EARNS TIER 1 STATUS

In July 2009, our Raystown Hydroelectric Project was recognized as a Pennsylvania Tier 1 renewable generation resource by the Commonwealth's Alternative Energy Program Administrator. The certification as a Tier 1 resource allows Allegheny to market renewable energy certificates (RECs) generated by the plant to other load-serving entities in the Commonwealth. Allegheny can also market Raystown RECs as Class II resources in New Jersey. Revenue from the sale of Raystown Hydroelectric Project RECs provides funding for our Renewable Energy Assistance Program. This follows the plant's 2007 certification as a low-impact hydroelectric facility by the Low Impact Hydropower Institute. Raystown is the first and remains the only hydro plant in Pennsylvania to earn this distinction for environmental stewardship.

By the end of 2010, there were 140 interconnected consumer-member-owned renewable energy projects.

ABOUT ALLEGHENY ELECTRIC COOPERATIVE, INC.

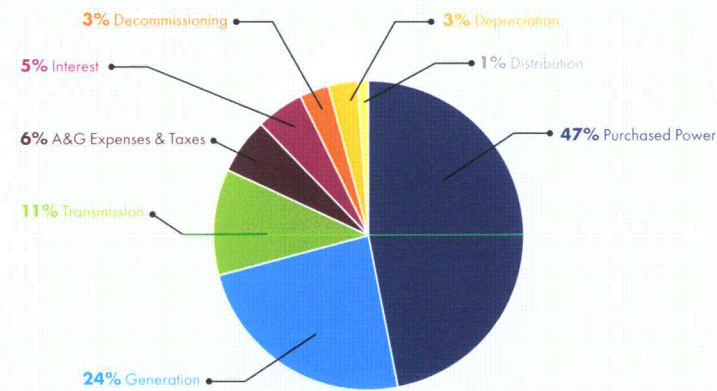
Electricity – powering our lives each day with heat, light, sound and motion. At Allegheny Electric Cooperative, Inc., a dedicated and experienced team of board members, management, and employees makes certain that wholesale electricity is provided round-the-clock to 14 member electric distribution cooperatives in Pennsylvania and New Jersey. In turn, those 14 member distribution cooperatives own and control Allegheny.

The cooperative electric systems comprising the Allegheny “family” maintain approximately 12.5 percent of all electric distribution lines in Pennsylvania, spanning one-third of the Commonwealth in 42 counties. New Jersey’s lone electric cooperative maintains roughly 1 percent of the Garden State’s total miles of line. Through these facilities, Allegheny member cooperatives deliver electricity to more than 230,000 homes, farms, small businesses, and industries with a combination of integrity, accountability, innovation, and commitment to community.

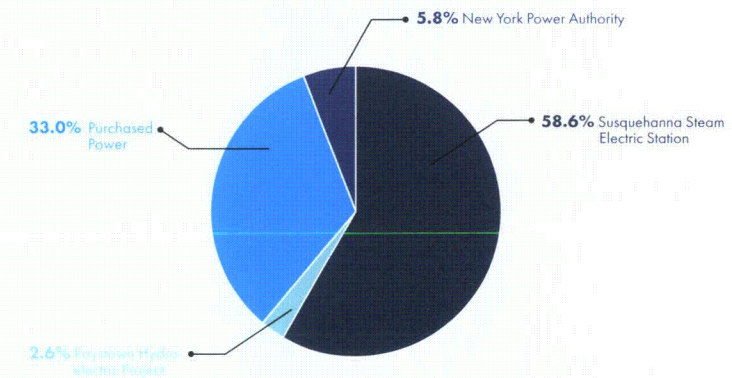
2010 FACT SHEET

Energy Sales . . . . .	3,262,980 MWh	System Rate . . . . .	5.66 cents per kWh
Total Consolidated Operating Revenue . . . . .	\$204,921,000	Total Retail Customers . . . . .	230,805
Net Margins . . . . .	\$9,123,000	2010 Peak Demand . . . . .	685 MW
Total Assets . . . . .	\$497,347,000	Miles of Transmission Line . . . . .	85

ALLEGHENY 2010 OPERATING EXPENSES

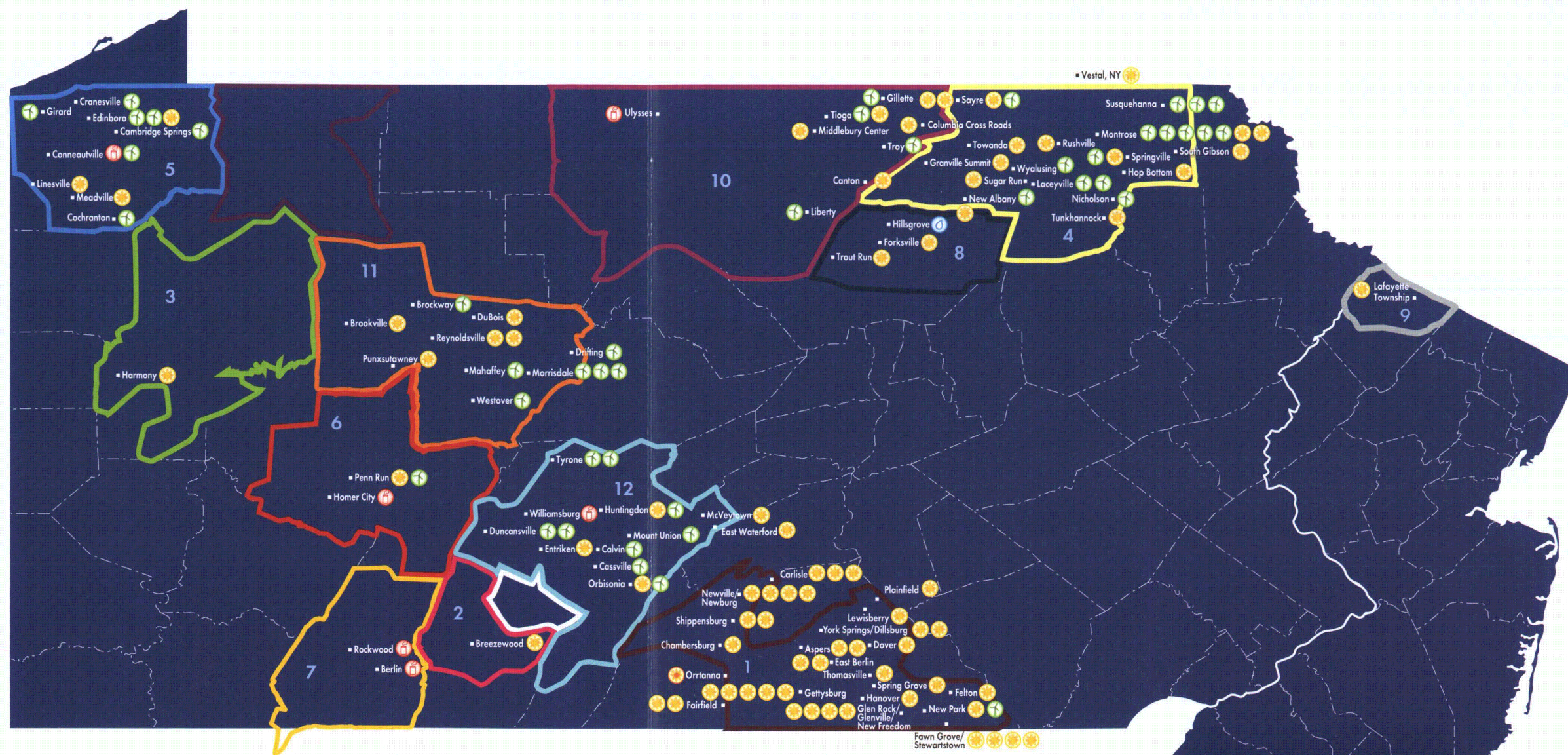


ALLEGHENY 2010 SOURCES OF ENERGY



# interconnections

- 1 Adams Electric Cooperative, Inc.  
**51 solar, 1 wind**  
**319.2 total kW**
- 2 Bedford Rural Electric Cooperative, Inc.  
**1 solar**  
**3.5 total kW**
- 3 Central Electric Cooperative, Inc.  
**1 solar**  
**1.9 total kW**
- 4 Claverack Rural Electric Cooperative, Inc.  
**13 solar, 15 wind**  
**157.17 total kW**
- 5 Northwestern Rural Electric Cooperative Association, Inc.  
**3 solar, 7 wind, 1 digester**  
**659.3 total kW**
- 6 REA Energy Cooperative, Inc.  
**1 solar, 1 wind, 1 digester**  
**92 total kW**
- 7 Somerset Rural Electric Cooperative, Inc.  
**2 digesters**  
**470 total kW**
- 8 Sullivan County Rural Electric Cooperative, Inc.  
**3 solar, 1 hydro**  
**125.34 total kW**
- 9 Sussex Rural Electric Cooperative, Inc.  
**1 solar**  
**5.1 total kW**
- 10 Tri-County Rural Electric Cooperative, Inc.  
**5 solar, 4 wind, 1 digester**  
**210.7 total kW**
- 11 United Electric Cooperative, Inc.  
**5 solar, 7 wind**  
**44.7 total kW**
- 12 Valley Rural Electric Cooperative, Inc.  
**5 solar, 9 wind, 1 digester**  
**261.76 total kW**

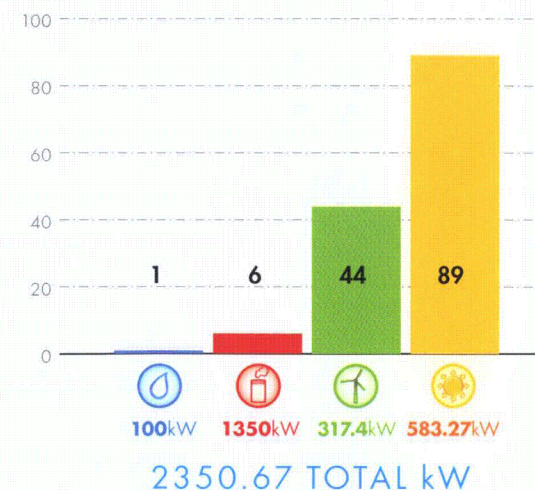


This interconnection map illustrates for each participating cooperative the various types of interconnections and total kW of power produced.

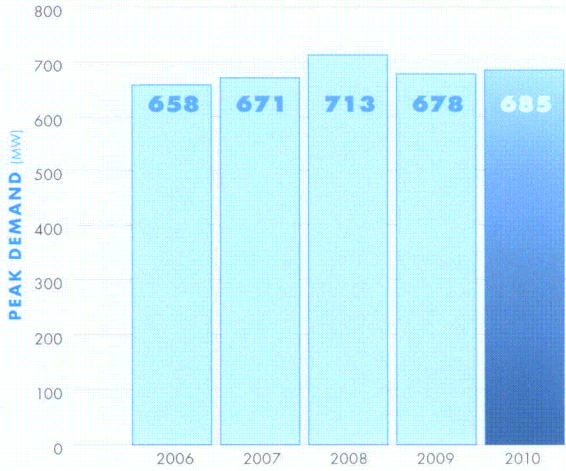
## LEGEND



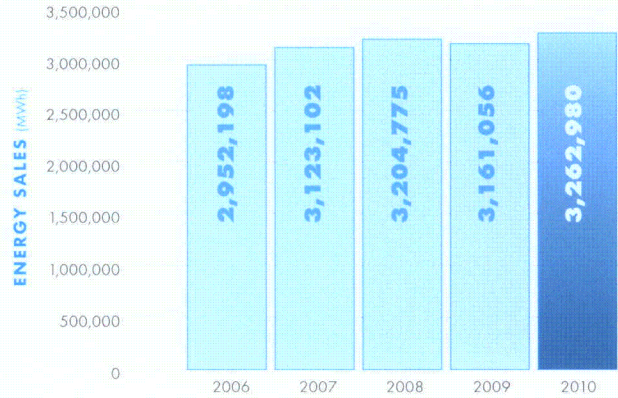
## TOTAL INTERCONNECTED PROJECTS (END 2010): 140



PEAK DEMAND 2006-2010



HISTORIC ENERGY SALES 2006-2010



ALLEGHENY ELECTRIC COOPERATIVE, INC. TERRITORY



- |  |   |   |  |   |
|--|---|---|--|---|
| 1 Adams Electric Cooperative, Inc.<br>Gettysburg, Pa.      | 4 Claverack Rural Electric Cooperative, Inc.<br>Wysox, Pa.                            | 7 REA Energy Cooperative, Inc.<br>Indiana, Pa.                        | 10 Sussex Rural Electric Cooperative, Inc.<br>Sussex, N.J.       | 13 Valley Rural Electric Cooperative, Inc.<br>Huntingdon, Pa. |
| 2 Bedford Rural Electric Cooperative, Inc.<br>Bedford, Pa. | 5 New Enterprise Rural Electric Cooperative, Inc.<br>New Enterprise, Pa.              | 8 Somerset Rural Electric Cooperative, Inc.<br>Somerset, Pa.          | 11 Tri-County Rural Electric Cooperative, Inc.<br>Mansfield, Pa. | 14 Warren Electric Cooperative, Inc.<br>Youngsville, Pa.      |
| 3 Central Electric Cooperative, Inc.<br>Parker, Pa.        | 6 Northwestern Rural Electric Cooperative Association, Inc.<br>Cambridge Springs, Pa. | 9 Sullivan County Rural Electric Cooperative, Inc.<br>Forksville, Pa. | 12 United Electric Cooperative, Inc.<br>DuBois, Pa.              |   |

# allegheny

board of directors & senior management team



## ALLEGHENY ELECTRIC COOPERATIVE, INC. 2010 BOARD OF DIRECTORS

**Top row, left to right:** Thomas Webb, Director, Sussex REC; Thomas Elliott, Director, Claverack REC; Lowell Friedline, Director, Somerset REC; Herman Blakley, Director, REA Energy; Stephen Marshall, Director, United EC; C. Robert Koontz, Director, Bedford REC; Robert Holmes, Director, Valley REC; Richard Weaver, Director, Central EC.

**Bottom row, left to right:** Dave Turner, Director, Warren EC; Robert Guyer, Director, New Enterprise REC; Kathryn Cooper-Winters, Allegheny Board Treasurer, Director, Northwestern RECA; Dr. James Davis, Allegheny Board Chairman, Director, Tri-County REC; Jay Grove, Allegheny Board Secretary, Director, Adams EC; Curtin Rakestraw II, Allegheny Board Vice Chairman, Director, Sullivan County REC.



ALLEGHENY ELECTRIC COOPERATIVE, INC. **SENIOR MANAGEMENT TEAM**



**Frank Betley**  
President & CEO



**Laurence Bladen**  
Vice President  
Strategic & Corporate  
Services



**David Dulick**  
General Counsel



**Kenneth Kammeier**  
Vice President  
Finance & Accounting



**William Logan**  
Vice President  
Public Affairs &  
Member Services



**Todd Sallade**  
Vice President  
Power Supply &  
Engineering



# 2010 financial statements

DECEMBER 31, 2010 AND 2009

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## Independent Accountants' Report

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

We have audited the accompanying consolidated balance sheets of Allegheny Electric Cooperative, Inc. (Cooperative) as of December 31, 2010 and 2009, and the related consolidated statements of margin, 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Allegheny Electric Cooperative, Inc. as of December 31, 2010 and 2009, 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.

*BKD, LLP*

April 26, 2011

# consolidated balance sheets

<b>ASSETS</b>	<b>2010</b>	<b>2009</b>
<b>Electric Utility Plant, at cost</b>		
In service (see Note 2)	\$ 868,151	\$ 837,703
Less accumulated depreciation	<u>(710,597)</u>	<u>(697,804)</u>
	157,554	139,899
Construction work in progress	10,940	14,620
Nuclear fuel in process (see Notes 1 and 3)	<u>29,235</u>	<u>27,236</u>
Net electric utility plant (see Notes 1, 2 and 3)	<u>197,729</u>	<u>181,755</u>
<b>Investments and Other Assets</b>		
Investments in associated organizations (see Note 4)	27,556	27,568
Nuclear Decommissioning Trust (NDT) (see Notes 1 and 5)	73,080	63,455
Non-utility property, at cost (net of accumulated depreciation of \$6,254 in 2010 and \$6,102 in 2009)	4,171	3,623
Assets of consolidated variable interest entity		
Non-utility property, at cost (net of accumulated depreciation of \$1,052 in 2010 and \$1,068 in 2009)	21	34
Deferred tax assets, net (see Note 10)	12,927	11,858
Other noncurrent assets	<u>11,435</u>	<u>7,028</u>
	<u>129,190</u>	<u>113,566</u>
<b>Current Assets</b>		
Cash and cash equivalents	31,345	38,180
Investments (see Note 1 and 4)	57,167	74,837
Derivative investments (see Note 6)	40,764	29,170
Accounts receivable, members (see Note 1)	16,560	16,491
Accounts receivable, affiliated organization	4	-
Other receivables	825	467
Inventories (see Note 1)	8,516	11,218
Other current assets	2,582	5,147
Assets of consolidated variable interest entities		
Cash and cash equivalents	543	608
Accounts receivable, affiliated organization	174	-
Other receivables	10	9
Other current assets	<u>755</u>	<u>732</u>
Total current assets	<u>159,245</u>	<u>176,859</u>
<b>Deferred Charges (see Note 7)</b>		
Capital retirement asset	957	1,010
Deferred asset plan - NDT investments	3,315	3,845
Deferred asset plan - forward swaps	6,886	9,170
Other	25	37
	<u>11,183</u>	<u>14,062</u>
<b>Total assets</b>	<b><u>\$ 497,347</u></b>	<b><u>\$ 486,242</u></b>

<b>MEMBERS' EQUITIES AND LIABILITIES</b>	<b>2010</b>	<b>2009</b>
<b>Members' Equities</b> (see Note 1)		
Membership fees	\$ 3	\$ 3
Patronage capital	54,369	49,462
Donated capital	38	38
Unrestricted net assets	100	100
Retained earnings	9,123	7,917
Members' equities	63,633	57,520
Accumulated other comprehensive income	14,158	9,826
Total equities	77,791	67,346
<b>Asset Retirement Obligation</b> (see Note 8)	142,355	136,880
<b>Long-Term Debt</b> (see Note 9)	152,401	158,508
<b>Current Liabilities</b>		
Current installments of long-term debt	5,858	5,219
Derivative liability - forward swaps (see Note 6)	34,621	25,287
Accounts payable and accrued expenses	18,734	17,140
Accounts payable, affiliated organization	3	38
Liabilities of consolidated variable interest entities		
Accounts payable and accrued expenses	1,996	1,718
Accrued postretirement benefit cost	216	-
Accounts payable, affiliated organization	88	175
Total current liabilities	61,516	49,577
<b>Other Liabilities and Deferred Revenue</b>		
Deferred income tax obligation from safe harbor lease (see Note 15)	617	926
Financial transmission rights (see Note 6)	13,030	13,053
Deferred credits (see Note 16)	49,637	59,952
	63,284	73,931
<b>Total liabilities and members' equities</b>	<b>\$ 497,347</b>	<b>\$ 486,242</b>

# consolidated statements

## of margin

	<b>2010</b>	<b>2009</b>
<b>Operating Revenues</b>	<u>\$ 204,921</u>	<u>\$ 202,922</u>
<b>Operating Expenses</b>		
Operations		
Purchased capacity and energy costs	97,160	95,865
Transmission		
Operation	23,871	22,501
Maintenance	255	251
Production		
Operation	25,177	23,088
Maintenance	13,160	9,784
Fuel	10,586	9,982
Depreciation	5,822	4,895
Accretion of asset retirement obligation	5,475	5,265
Amortization of capital retirement asset	54	9,280
Administrative and general	11,676	10,888
Property and other taxes	728	686
<b>Total Operating Expenses Before Interest</b>	<u>193,964</u>	<u>192,485</u>
<b>Operating Margin Before Interest Expense</b>	<u>10,957</u>	<u>10,437</u>
<b>Interest Expense</b>	<u>(10,467)</u>	<u>(9,391)</u>
<b>Operating Margin</b>	<u>490</u>	<u>1,046</u>

	<b>2010</b>	<b>2009</b>
<b>Non-operating Margins</b>		
Non-operating rental income	1,399	1,531
Non-operating rental expense	(1,367)	(1,431)
Interest income	6,061	5,987
Capital Credits and Other income	<u>2,540</u>	<u>784</u>
	<u>8,633</u>	<u>6,871</u>
<b>Net Margin</b>	9,123	7,917
<b>Other Comprehensive Margin</b>		
Postretirement benefit plan	17	-
Unrealized appreciation in investments	<u>4,444</u>	<u>6,745</u>
<b>Comprehensive Margin</b>	<u><b>\$ 13,584</b></u>	<u><b>\$ 14,662</b></u>



# consolidated statements

of members' equities



	MEMBERSHIP FEES	DONATED CAPITAL	PATRONAGE CAPITAL
<b>Balance, January 1, 2009</b>	\$ 3	\$ 38	\$ 43,781
Patronage capital retirement	-	-	(3,478)
Patronage capital assignment	-	-	10,000
Patronage capital - NDT (earnings) losses	-	-	841
Comprehensive margin			
Net margin	-	-	-
Change in unrealized depreciation on investments	-	-	-
<b>Balance, December 31, 2009</b>	<u>3</u>	<u>38</u>	<u>49,462</u>
Patronage capital retirement	-	-	(3,010)
Patronage capital assignment	-	-	7,058
Patronage capital - NDT (earnings) losses	-	-	859
Comprehensive margin			
Net margin	-	-	-
Transfer of postretirement benefit obligation	-	-	-
Net change in postretirement plan arising during period	-	-	-
Change in unrealized appreciation on investments	-	-	-
<b>Balance, December 31, 2010</b>	<u><u>\$ 3</u></u>	<u><u>\$ 38</u></u>	<u><u>\$ 54,369</u></u>

UNRESTRICTED NET ASSETS	RETAINED EARNINGS	TOTAL MEMBERS' EQUITIES	ACCUMULATED OTHER COMPREHENSIVE MARGIN	TOTAL EQUITIES
\$ 100	\$ 9,159	\$ 53,081	\$ 3,081	\$ 56,162
-	-	(3,478)	-	(3,478)
-	(10,000)	-	-	-
-	841	-	-	-
-	7,917	7,917	-	7,917
-	-	-	6,745	6,745
<u>100</u>	<u>7,917</u>	<u>57,520</u>	<u>9,826</u>	<u>67,346</u>
-	-	(3,010)	-	(3,010)
-	(7,058)	-	-	-
-	(859)	-	-	-
-	9,123	9,123	-	9,123
-	-	-	(129)	(129)
-	-	-	17	17
-	-	-	4,444	4,444
<u>\$ 100</u>	<u>\$ 9,123</u>	<u>\$ 63,633</u>	<u>\$ 14,158</u>	<u>\$ 77,791</u>

# consolidated statements

## of cash flows

	2010	2009
<b>Operating Activities</b>		
Net margin	\$ 9,123	\$ 7,917
Items not requiring cash		
Depreciation and fuel amortization	14,498	12,763
Amortization of capital retirement asset	53	9,280
Accretion of asset retirement obligation	5,475	5,265
Deferred income taxes	(1,069)	4,512
Loss on disposal of equipment	9	3
Other than temporary losses	-	(160)
Change in		
Investments in associated organizations	12	(9,835)
Accounts receivable, members	(69)	2,707
Other receivables	(359)	(63)
Inventories	2,702	(3,497)
Derivative investments	(11,594)	(21,930)
Other current and non-current assets	(1,865)	(1,367)
Accounts payable and accrued expenses	1,872	5,528
Accounts payable, affiliated organizations	(196)	141
Derivative liability - forward swaps	9,334	25,287
Other liabilities and deferred charges	(7,821)	(17,580)
	<u>20,105</u>	<u>18,971</u>
Net cash provided by operating activities	<u>20,105</u>	<u>18,971</u>



	<b>2010</b>	<b>2009</b>
<b>Investing Activities</b>		
Additions to electric utility plant and non-utility property, net	(31,016)	(33,036)
Proceeds from investments, net	18,325	1,630
Purchase of other investments	<u>(5,836)</u>	<u>(2,717)</u>
Net cash used in investing activities	<u>(18,527)</u>	<u>(34,123)</u>
<b>Financing Activities</b>		
Principal payments on long-term debt	(5,468)	(4,458)
Proceeds from issuance of long-term debt	-	40,000
Patronage capital retirement	<u>(3,010)</u>	<u>(3,478)</u>
Net cash provided by (used in) financing activities	<u>(8,478)</u>	<u>32,064</u>
<b>Net Increase (Decrease) In Cash and Cash Equivalents</b>	<b>(6,900)</b>	<b>16,912</b>
<b>Cash and Cash Equivalents, Beginning of Year</b>	<b><u>38,788</u></b>	<b><u>21,876</u></b>
<b>Cash and Cash Equivalents, End of Year</b>	<b><u>\$ 31,888</u></b>	<b><u>\$ 38,788</u></b>
<b>Supplemental Cash Flows Information</b>		
Interest paid	\$ 10,521	\$ 9,038
Income tax paid	375	-

## 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. The Cooperative extends unsecured credit to its members, with credit extended to one member of 18% and 22% of accounts receivable at December 31, 2010 and 2009, respectively. The Cooperative finances 100 percent of its outstanding debt with the National Rural Utilities Cooperative Finance Corporation (CFC).

The Cooperative is a generation and transmission cooperative. The member cooperatives' primary service areas are rural areas throughout much of Pennsylvania and a portion of New Jersey. The Cooperative extends unsecured credit to its members. The Cooperative's primary operating asset is its 10 percent undivided interest in the Susquehanna Steam Electric Station (SSES), a 2,450-megawatt, two-unit nuclear power plant, co-owned by a subsidiary of PPL Corporation (PPL).

The Board of Directors of the Cooperative, elected by its members, has full authority to establish electric rates to its member cooperatives. Rates are established on a cost of service basis. The Cooperative's Board of Directors has established a deferred revenue account to offset future increases in power supply costs.

### Principles of Consolidation

The financial statements include the accounts of the Cooperative and a variable interest entity, Continental Electric Cooperative Services, Inc. (CCS), of which the Cooperative has determined it is the primary beneficiary. All significant intercompany accounts and transactions have been eliminated in consolidation.

### Variable Interest Entity and Change in Accounting Principle

A legal entity is referred to as a variable interest entity (VIE) if any of the following conditions exist, which are outlined in the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) variable interest accounting guidance (ASC 810-10-15-04): (1) the total equity investment at risk is insufficient to permit the legal entity to finance its activities without additional subordinated financial support from other parties, or (2) the entity has equity investors who cannot make significant decisions about the entity's operations or who do not absorb their proportionate share of the expected losses or receive the expected returns of the entity.

On January 1, 2010, the Cooperative adopted ASU 2009-17, Consolidations (Topic 810): Improvements to Financial Reporting by Enterprises Involved with Variable Interest Entities, which amended the consolidation guidance applicable to variable interest entities. ASU 2009-17 identifies a VIE's primary beneficiary as the entity that has the power to direct the VIE's significant activities and has an obligation to absorb losses or the right to receive benefits that could be potentially significant to the VIE.

A VIE must be consolidated by the Cooperative if it is deemed to be the primary beneficiary of the VIE.

All facts and circumstances are taken into consideration when determining whether the Cooperative has variable interests that would deem it the primary beneficiary and, therefore, require consolidation of the related VIE or otherwise rise to the level where disclosure would provide useful information to the users of the Cooperative's financial statements. In many cases, it is qualitatively clear whether the Cooperative is obligated to absorb significant losses of or has a right to receive significant benefits from the VIE.

In other cases, a more detailed qualitative analysis and possibly a quantitative analysis are required to make such a determination.

The Cooperative monitors the consolidated VIE to determine if any reconsideration events have occurred that could cause it to no longer be a VIE. The Cooperative reconsiders whether it is the primary beneficiary of a VIE on an ongoing basis. A previously consolidated VIE is deconsolidated when the Cooperative ceases to be the primary beneficiary or the entity is no longer a VIE.

Initial adoption of ASU 2009-17 resulted in continuing to consolidate the VIE previously included in the consolidated financial statements and did not cause consolidation of any additional VIEs.

Continental Electric Cooperative Services, Inc. (CCS) is considered to be a variable interest entity and the Cooperative is determined to be the primary beneficiary of CCS. As such, the assets, liabilities, and results of operations have been consolidated into these financial statements.

### 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 the U.S. Department of Agriculture, Rural Utilities Service (RUS).

In accordance with FERC guidelines, the Cooperative also maintains its accounts in accordance with Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Topic 980, *Regulated Operations*.

### 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 ASC Topic 980, *Regulated Operations*, and Topic 980-20, *Discontinuation of Rate Regulated Accounting*. The Cooperative has determined that regulatory assets and liabilities should continue to be accounted for under the provisions of Topic 980 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 the 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 a straight-line basis, except for nuclear fuel, as follows:

Nuclear Utility Plant	
Production	Remaining License Life (Extended to 2044)
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.

### Non-utility Property

Non-utility property acquisitions are stated at cost less accumulated depreciation and amortization. Depreciation and amortization is charged to expense on a straight-line basis over the estimated useful life of each asset.

The estimated useful lives of non-utility property range from 3 to 50 years.

### 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 PPL for its portion of DOE fees for such future disposal services.

### Investments

Investments are classified as "available for sale" and recorded at fair value, with unrealized gains and losses excluded from earnings and reported in other comprehensive income. Purchase premiums and discounts are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are recorded on the trade date and are determined using the specific identification method.

For debt securities with fair value below carrying value when the Cooperative does not intend to sell a debt security, and it is more likely than not, the Cooperative will not have to sell the security before recovery of its cost basis, it recognizes the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income.

The Cooperative's consolidated statement of margin as of December 31, 2010, reflects the full impairment (that is, the difference between the security's amortized cost basis and fair value) on debt securities that the Cooperative intends to sell, or would more likely than not be required to sell before the expected recovery of the amortized cost basis. For available-for-sale debt securities that management has no intent to sell and believes that it more likely than not will not be required to sell prior to recovery, only the credit loss component of the impairment is recognized in earnings, while the noncredit loss is recognized in other comprehensive income. The credit loss component recognized in earnings is identified as the amount of principal cash flows not expected to be received over the remaining term of the security as projected based on cash flow projections.

For equity securities, when the Cooperative has decided to sell an impaired available-for-sale security and the entity does not expect the fair value of the security to fully recover before the expected time of the sale, the security is deemed other-than-temporarily impaired in the period in which the decision to sell is made. The Cooperative recognizes an impairment loss when the impairment is deemed other than temporary even if a decision to sell has not been made.

### Cash and Cash Equivalents

Cash and cash equivalents consist of bank deposits in federally insured accounts, temporary investments, money market funds and commercial paper.

The Cooperative places its cash and temporary investments with high quality financial institutions. 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.

One or more of the financial institutions holding the Cooperative's cash accounts are participating in the FDIC's Transaction Account Guarantee Program. Under that program through December 31, 2010, all noninterest-bearing transaction accounts at these institutions were fully guaranteed by the FDIC for the entire amount in the account.

For financial institutions opting out of the FDIC's Transaction Account Guarantee Program or interest-bearing cash accounts, the FDIC's insurance limits were permanently increased to \$250,000, effective July 21, 2010. At December 31, 2010, the Cooperative's cash accounts exceeded federally insured limits by approximately \$9,519,000, which was held at the following institutions:

Wells Fargo	
Sweep and money market	\$ 7,755,000
BB&T Capital Markets	
Repurchase agreement	897,000
M&T Bank	
Money market and commercial paper	867,000
	<u>\$ 9,519,000</u>

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

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.

### Derivatives

Derivatives are recognized as assets and liabilities on the consolidated balance sheet and measured at fair value. For exchange-traded contracts, fair value is based on quoted market prices. For nonexchange-traded contracts, fair value is based on dealer quotes, pricing models, discounted cash flow methodologies, or similar techniques for which the determination of fair value may require significant management judgment or estimation.

### 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.

### Patronage Capital

Current and future margins (excluding earnings from the Nuclear Decommissioning Trust), will be assigned as patronage capital.

### Income Taxes

The Cooperative accounts for income taxes in accordance with income tax accounting guidance (ASC 740, Income Taxes). The income tax accounting guidance results in two components of income tax expense: current and deferred. Current income tax expense reflects taxes to be paid or refunded for the current period by applying the provisions of the enacted tax law to the taxable income or excess of deductions over revenues. The Cooperative determines deferred income taxes using the liability (or balance sheet) method. Under this method, the net deferred tax assets or liabilities, and enacted changes in tax rates and laws are recognized in the period in which they occur.

Deferred tax assets and liabilities are recognized for the tax effects of differences between the financial statement and tax bases of assets and liabilities. Deferred tax assets are reduced by a valuation allowance if, based on the weight of evidence available, it is more likely than not that some portion or all of a deferred tax asset will not be realized.

Uncertain tax positions are recognized if it is more likely than not, based on the technical merits, that the tax position will be realized or sustained upon examination. (The term more-likely-than-not means a likelihood of more than 50 percent; the terms examined and upon examination also include resolution of the related appeals or litigation processes, if any.) A tax position that meets the more-likely-than-not recognition threshold is initially and subsequently measured as the largest amount of tax benefit that has a greater than 50 percent likelihood of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The determination of whether or not a tax position has met the more-likely-than-not recognition threshold considers the facts, circumstances and information available at the reporting date and is subject to management's judgment. At December 31, 2010 and 2009, no uncertain tax positions have been identified.

The Cooperative would recognize interest and penalties on income taxes, if any, as a component of income tax expense.

### Revenue Recognition

Revenue from the sale of electricity to members is recorded based on contracted power usage billed under the Cooperative's current rate schedule.

### Comprehensive Margin

Comprehensive margin consists of net margin and other comprehensive margin, net of applicable income taxes. Other comprehensive margin includes unrealized appreciation (depreciation) on available-for-sale securities, unrealized appreciation (depreciation) for which a portion of an other-than-temporary impairment has been recognized in margin, and changes in the funded status of the postretirement plan.

### Impairment of Long-Lived Assets

The Cooperative evaluates the recoverability of the carrying value of long-lived assets whenever events or circumstances indicate that carrying amount may not be recoverable. If a long-lived asset is tested for recoverability and the undiscounted estimated future cash flows is expected to result from the use and eventual disposition of the asset is less than the carrying amount of the asset, the asset cost is adjusted to fair value and an impairment loss is recognized as the amount by which the carrying amount of a long-lived asset exceeds its fair value. No asset impairment was recognized during the years ended December 31, 2010 and 2009.

### Reclassifications

Certain reclassifications have been made to the 2009 financial statements to conform to the 2010 financial statement presentation. These reclassifications had no effect on net margins.

**Note 2: Electric Utility Plant in Service**

	2010	2009
	(in thousands)	
Production	\$ 604,190	\$ 592,770
Transmission	41,232	41,232
General plant	3,842	3,394
Nuclear fuel	198,608	186,151
Other	20,279	14,156
<b>Total</b>	<b>\$ 868,151</b>	<b>\$ 837,703</b>

**Note 3: Susquehanna Steam Electric Station**

The Cooperative owns a 10 percent undivided interest in SSES. PPL owns the remaining 90 percent. 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 \$643 million and \$633 million as of December 31, 2010 and 2009, respectively. The Cooperative's share of anticipated costs for ongoing construction and nuclear fuel for SSES is estimated to be approximately \$115 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 59% and 62% of the total kilowatt hours sold by the Cooperative during the years ended December 31, 2010 and 2009, 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****Associated Organizations**

	2010	2009
	(in thousands)	
National Rural Utilities Cooperative Finance Corporation (CFC) Subordinated Term Certificates, bearing interest at 5.8%, maturing January 1, 2026 <sup>1</sup>	\$ 15,569	\$ 16,101
National Rural Utilities Cooperative Finance Corporation (CFC) Subordinated Term Certificates, bearing interest from 0% to 5%, maturing January 1, 2014 <sup>1</sup>	128	172
National Rural Utilities Cooperative Finance Corporation (CFC) Member Capital Securities, bearing interest at 7.5%, maturing March 24, 2044 <sup>1</sup>	10,000	10,000
Other	1,859	1,295
<b>Total</b>	<b>\$ 27,556</b>	<b>\$ 27,568</b>

<sup>1</sup> The Cooperative is required to maintain these investments pursuant to certain loan and guarantee agreements. Such investments are carried at cost.

# notes

## to consolidated financial statements

### Investments

The Cooperative makes temporary investments of excess corporate funds in investment accounts managed by qualified registered investment advisors. The amortized cost, which includes any premiums or discounts at acquisition, and approximate fair values of these investments are as follows:

	2010	2009
	(in thousands)	
Certificates of deposit		
Amortized cost	\$-	\$ 997
Unrealized gains	-	2
	<u>-</u>	<u>999</u>
Debt securities		
Amortized cost	50,061	60,308
Unrealized gains	2,078	1,546
Unrealized losses	(233)	(167)
	<u>51,906</u>	<u>61,687</u>
Equity securities		
Amortized cost	2,447	1,575
Unrealized gains	314	249
	<u>2,761</u>	<u>1,824</u>
Total investments at fair value	<u>54,667</u>	<u>64,510</u>
Investments, at cost with National Rural Utilities Cooperative Finance Corporation		
Medium term notes	2,500	10,000
Commercial paper	-	327
	<u>\$ 57,167</u>	<u>\$ 74,837</u>



Maturities of investments at December 31, 2010:

	<b>Amortized Cost</b>	<b>Approximate Fair Value</b>
	(in thousands)	
One year or less	\$ 23,914	\$ 23,921
After one through five years	31,561	33,246
	<b>\$ 55,475</b>	<b>\$ 57,167</b>

No other-than-temporary impairment has been recorded for 2010 and 2009.

### Note 5: Nuclear Decommissioning Trust

The Nuclear Decommissioning Trust consists of the following as of December 31, 2010 and 2009:

	<b>Cost</b>	<b>Gross Unrealized Gains</b>	<b>2010 Gross Unrealized Losses</b>	<b>Realized Losses</b>	<b>Fair Value</b>
	(in thousands)				
Decommissioning Trust Fund A:					
Money market funds	\$ 759	\$ -	\$ -	\$ -	\$ 759
U.S. Government securities	8,725	30	(130)	-	8,625
Corporate bonds	4,542	249	(37)	-	4,754
Other obligations	201	15	-	-	216
Common stocks	7,200	3,949	(48)	-	11,101
	<u>21,427</u>	<u>4,243</u>	<u>(215)</u>	<u>-</u>	<u>25,455</u>
NRC mandated Decommissioning Trust Fund B:					
Money market funds	444	-	-	-	444
U.S. Government securities	12,900	105	(208)	-	12,797
Corporate bonds	8,276	378	(61)	-	8,593
Other obligations	875	27	(14)	-	888
Common stocks	17,164	7,863	(124)	-	24,903
	<u>39,659</u>	<u>8,373</u>	<u>(407)</u>	<u>-</u>	<u>47,625</u>
<b>Total</b>	<b><u>\$ 61,086</u></b>	<b><u>\$ 12,616</u></b>	<b><u>\$ (622)</u></b>	<b><u>-</u></b>	<b><u>\$ 73,080</u></b>

# notes

## to consolidated financial statements

	Cost	Gross Unrealized Gains	2009 Gross Unrealized Losses	Realized Losses	Fair Value
(in thousands)					
Decommissioning Trust Fund A:					
Money market funds	\$ 173	\$ -	\$ -	\$ -	\$ 173
U.S. Government securities	7,248	21	(72)	-	7,197
Corporate bonds	5,467	307	(14)	-	5,760
Other obligations	254	13	-	-	267
Common stocks	7,000	2,591	(37)	(39)	9,515
	<u>20,142</u>	<u>2,932</u>	<u>(123)</u>	<u>(39)</u>	<u>22,912</u>
NRC mandated Decommissioning Trust Fund B:					
Money market funds	307	-	-	-	307
U.S. Government securities	12,795	62	(135)	-	12,722
Corporate bonds	7,154	401	(18)	-	7,537
Other obligations	642	22	(7)	-	657
Common stocks	14,379	5,137	(75)	(121)	19,320
	<u>35,277</u>	<u>5,622</u>	<u>(235)</u>	<u>(121)</u>	<u>40,543</u>
<b>Total</b>	<b><u>\$ 55,419</u></b>	<b><u>\$ 8,554</u></b>	<b><u>\$ (358)</u></b>	<b><u>\$ (160)</u></b>	<b><u>\$ 63,455</u></b>

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, 2010 and 2009, was \$21.4 million and \$19.8 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. The gross unrealized losses at December 31, 2010 for a period of less than 12 months were \$549,000 and for a period of greater than 12 months were \$73,000. Gross unrealized losses of \$358,000 at December 31, 2009 were for a period of less than 12 months.

For 2009, the Cooperative recorded other-than-temporary impairments on equity securities and specific debt securities in the amount of \$160,000. The cost-basis of these investments has been adjusted to reflect the recognition of these impairments. No other-than-temporary impairment has been recorded for 2010.

Under ASC Topic 980, *Regulated Operations*, the Cooperative has elected to defer these losses and pass them on to members through the future rate structure. As of December 31, 2010 and 2009, total deferred charges for the Nuclear Decommissioning Trust other-than-temporary impairment were \$3,315,000 and \$3,845,000.

### Note 6: Derivatives and Hedging

ASC Topic 815-10 seeks to improve financial reporting for derivative instruments and hedging activities by requiring enhanced disclosures regarding the impact on financial position, financial performance, and cash flows. To achieve this increased transparency, the additional guidance requires (a) the disclosure of the fair value of derivative instruments and gains and losses in a tabular format; (b) the disclosure of derivative features that are credit risk-related;

and (c) cross-referencing within the footnotes. The Cooperative adopted this Topic as of January 1, 2009.

The Cooperative does not engage in speculative derivative transactions, however, the Cooperative engages in hedging activities that are a natural part of power supply and transmission activities.

The Cooperative uses hedging instruments, including forwards, futures, financial transmission rights, and options, to manage power market price risks. In addition, substantial reliance on the purchase of energy from other power suppliers exposes the Cooperative to the risk that counterparties will default. Therefore, an assessment is performed on the creditworthiness of counterparties and other credit issues related to these purchases, which may require the counterparties to post collateral. Defaults, however, may still occur. If a default occurs, the Cooperative may be forced to enter into alternative contractual arrangements or purchase energy in the forward, short-term or spot markets at then-current market prices that could vary from the prices previously agreed upon with the defaulting counterparty. The Cooperative has never had a counterparty default or fail to perform, but past performance is no guarantee of future results.

### Financial Transmission Rights

The Cooperative is issued Financial Transmission Rights (FTRs) by PJM Interconnection LLC, (PJM). These FTRs have been found to meet the FASB ASC Topic 815, *Derivatives and Hedging*, definition of a derivative, and therefore must have special derivative accounting procedures applied to them.

The Cooperative received an entitlement of FTRs. FTRs are defined from a "source" node to a "sink" node (path) for a specific amount of megawatts of electric power. The holder of an FTR is entitled to receive whole or partial offsets of transmission congestion charges that arise when that specific path is congested. The purpose of the FTR mechanism is to act as a hedge against volatile congestion charges.

Market values of FTRs are only observable based on the clearing prices of the FTRs in multi-year, annual, seasonal and monthly auctions. The expected value of FTRs fluctuates based on seasonal expectations of the supply and demand of energy for each specific path. Significant assumptions and modeling projections are necessary to value FTRs. The expected FTR values are considered in the rate-making process and therefore the fair value of FTRs are recognized on the balance sheet and recorded as deferred income under ASC Topic 980, *Regulated Operations*. The fair value of FTRs was \$13,030,000 and \$13,053,000 as of December 31, 2010 and 2009 for the remainder of the current PJM planning periods that end May 31, 2011 and 2010 and beyond.

	2010	2009
	(in thousands)	
Fair value of FTRs	\$ 13,030	\$ 13,053
Balance sheet locations	Current assets	Current assets
	Noncurrent liabilities	Noncurrent liabilities

### Forward Swaps

The Cooperative is exposed to market purchases of power and natural gas to meet the power supply needs of the member distribution cooperatives that are not met by Cooperative owned generation. While the Cooperative does not engage in speculative practices, the Cooperative utilizes derivative contracts to manage this exposure. Power is purchased under both long-term and short-term physically-delivered and financially-settled forward contracts to supply power to member cooperatives. These forward purchase contracts meet the accounting definition of a derivative; however, a majority of the forward purchase derivative contracts qualify for the normal purchases/normal sales exception under previously issued

guidance. As a result, these contracts are not recorded at fair value and are not subject to the disclosure requirements. Purchased power is expensed when the power under the forward contract is delivered.

The Cooperative purchases natural gas futures contracts to hedge the price of natural gas for use as a basis in determining the price of power in certain forward power purchase agreements. The Cooperative also purchases capacity swap forward contracts in order to lock in capacity pricing prior to the completion of capacity auctions. These derivatives do not qualify for the normal purchases/normal sales exception; however, the Cooperative has opted out of the cash flow hedge accounting as allowed under previously issued guidance. For these derivative contracts that do not qualify for the normal purchases/normal sales exception, the Cooperative defers all gains and losses on a net basis as a regulatory asset or liability in accordance with ASC Topic 980, *Regulated Operations*. These amounts are subsequently reclassified as purchased power in the consolidated statements of margin as the power is delivered and/or the contract settles.

Generally, derivatives are reported on the consolidated balance sheet at fair value. The measurement of fair value is based on actively quoted market prices, if available. Otherwise, indicative price information is sought from external sources, including broker quotes and industry publications. For individual contracts, the use of differing assumptions could have a material effect on the contract's estimated fair value.

Changes in the fair value of the derivative instruments are recorded as a regulatory asset or regulatory liability. The change in these accounts is included in the operating section of the statement of cash flows.

As of December 31, 2010 and 2009, the Cooperative had the following outstanding derivative futures contracts:

<b>Commodity</b>	<b>Unit of Measure</b>	<b>Quantity 2010</b>	<b>Quantity 2009</b>
Natural gas	MMBTU	30,000	150,000
Capacity swap	MW	197,585	130,390

As of December 31, 2010 and 2009, the fair value of the derivative instruments, excluding contracts accounted for as a normal purchase/normal sale, were as follows:

<b>2010</b>	<b>Remaining Cost (in thousands)</b>	<b>Fair value (in thousands)</b>
Natural gas futures contracts	\$ 157	\$ 91
Capacity swap forward contracts	34,464	27,643
<b>Total</b>	<b>\$ 34,621</b>	<b>\$ 27,734</b>
Balance sheet locations	Current liabilities	Current assets

<b>2009</b>	<b>Remaining Cost (in thousands)</b>	<b>Fair value (in thousands)</b>
Natural gas futures contracts	\$ 966	\$ 716
Capacity swap forward contracts	24,321	15,401
<b>Total</b>	<b>\$ 25,287</b>	<b>\$ 16,117</b>
Balance sheet locations	Current liabilities	Current assets

As of December 31, 2010 and 2009, the Cooperative has deferred the following losses on a net basis as a regulatory asset in accordance with ASC Topic 980, *Regulated Operations*.

	<b>Location of Loss in the Statement of Margin at Settlement</b>	<b>Amount of Deferred Loss at December 31, 2010 (in thousands)</b>
Natural gas futures contracts	Purchased Power	\$ (65)
Capacity swap forward contracts	Purchased Power	(6,821)
<b>Total</b>		<b>\$ (6,886)</b>

	<b>Location of Loss in the Statement of Margin at Settlement</b>	<b>Amount of Deferred Loss at December 31, 2009 (in thousands)</b>
Natural gas futures contracts	Purchased Power	\$ (250)
Capacity swap forward contracts	Purchased Power	(8,920)
<b>Total</b>		<b>\$ (9,170)</b>

## Note 7: Deferred Charges

Deferred charges consist of the following regulatory assets as of December 31, 2010 and 2009.

	<b>2010</b>	<b>2009</b>
	(in thousands)	
Capital retirement asset	\$ 957	\$ 1,010
Deferred asset plan - NDT investments	3,315	3,845
Deferred asset plan - forward swaps	6,886	9,170
Safe harbor lease closing costs	25	37
	<b>\$ 11,183</b>	<b>\$ 14,062</b>

Based on agreements signed by the 14 member distribution cooperatives on March 29, 1999, with an effective date of January 1, 1999, and amended in 2004 and 2006, a portion of the SSES impairment writedown that took place in 1998 has been recognized as a regulatory asset and is referred to as the capital retirement asset. Under these agreements, the Cooperative was to recover from members certain financing costs related primarily to the Cooperative's investment in SSES in the amount of \$311 million no later than December 31, 2009. During 2009, certain members elected to extend repayment under these agreements to 2011.

### Note 8: Asset Retirement Obligation

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 \$73.1 million and \$63.5 million for the years ended December 31, 2010 and 2009, respectively.

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

	2010	2009
	(in thousands)	
Beginning balance	\$ 136,880	\$ 131,615
Accretion expense	5,475	5,265
<b>Ending balance</b>	<b>\$ 142,355</b>	<b>\$ 136,880</b>

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



**Note 9: Long-Term Debt**

	2010	2009
	(in thousands)	
Note payable CFC, payable in varying quarterly installments beginning April 2008, plus interest at 6.8%, final payment January 2014	\$ 12,775	\$ 16,225
Note payable CFC, payable in varying quarterly installments beginning April 2014, plus interest at 6.9%, final payment January 2021	38,600	38,600
Note payable CFC, payable in varying quarterly installments beginning April 2021, plus interest at 7.0%, final payment April 2025	39,700	39,700
Note payable CFC, payable in varying quarterly installments beginning July 2006, plus interest at 6.8%, final payment January 2014	1,925	2,425
Note payable CFC, payable in varying quarterly installments beginning April 2014, plus interest at 6.9%, final payment January 2021	5,800	5,800
Note payable CFC, payable in varying quarterly installments beginning April 2021, plus interest at 7.0%, final payment April 2025	6,200	6,200
Note payable CFC, payable in varying quarterly installments beginning July 2006, plus interest at 7.25%, final payment October 2025	12,507	12,956
Note payable CFC, payable in varying quarterly installments beginning July 2006, plus interest at 7.25%, final payment October 2025	2,002	2,071
Note payable CFC, payable in varying quarterly installments beginning October 2009, plus interest ranging from 4.05% to 6.65%, final payment October 2025	38,750	39,750
Total long-term debt	158,259	163,727
Less current installments	5,858	5,219
<b>Long-term debt, net of current installments</b>	<b>\$ 152,401</b>	<b>\$ 158,508</b>

The Cooperative has an additional available borrowing balance with CFC totaling \$40,716,000 at December 31, 2010.

Included in the above, the Cooperative has a \$35,000,000 operating line of credit with CFC that expires on March 31, 2011. Subsequent to December 31, 2010, the Cooperative renewed the operating line of credit through March 31, 2016 at \$50,000,000 under the same basic terms. There were no outstanding borrowings against this line as of December 31, 2010 and 2009. The interest rate on the line of credit fluctuates as established by CFC.

Additionally, the Cooperative has a commitment from CFC to provide unsecured letters of credit of up to \$25,000,000. Under this commitment, the Cooperative has an unsecured letter of credit facility for \$5,000,000 which expires November 30, 2011. As of December 31, 2010 and 2009, no funds have been drawn against this facility.

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

2011	\$ 5,858
2012	6,074
2013	6,494
2014	7,292
2015	7,668
Thereafter	124,873

The Cooperative is required to maintain certain covenants including an annual debt service coverage ratio. The Cooperative was in compliance with the applicable covenant as of December 31, 2010 and 2009, respectively.

During 2010 and 2009, the Cooperative incurred interest costs of \$10,467,000 and \$9,391,000, respectively.

## Note 10: Income Taxes

As of December 31, 2010 and 2009, the Cooperative had available nonmember net operating loss carryforwards of approximately \$22 and \$26 million, respectively for tax reporting purposes expiring in 2011 through 2019, and alternative minimum tax credit carryforwards of approximately \$1,008,000 and \$1,130,000 respectively, which carry forward indefinitely.

There was no provision for federal income taxes at December 31, 2010 and 2009. The Cooperative is not subject to state income taxes. The Cooperative is no longer subject to federal income tax examinations by tax authorities for years before 2007.

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 deferred tax asset at December 31, 2010 and 2009, of approximately \$18 and \$17 million, respectively. Realization of the net deferred tax asset is contingent upon the Cooperative's future earnings. A valuation allowance of approximately \$5 million has been established against this asset because it has been determined that this portion of the deferred tax asset more likely than not will be unrealized. The Cooperative will include the utilization of the net deferred tax asset of approximately \$13 million and \$12 million at December 31, 2010 and 2009, respectively, in future rates charged to members. Therefore, a deferred credit has been recorded equal to the net deferred tax asset under FASB ASC Topic 980, *Regulated Operations*.

## Note 11: Related Party Transaction

A related organization, the Pennsylvania Rural Electric Association (PREA) has provided the Cooperative with certain management, general, and administrative services on a cost reimbursement basis. The costs for services provided by PREA were \$891,000 and \$921,000 for the years ended December 31, 2010 and 2009, respectively.

## Note 12: Consolidated Variable Interest Entity

As the primary beneficiary, the Cooperative consolidates CCS. The general creditors of CCS have no recourse against the general credit of the Cooperative.

The following table summarizes the carrying amount of the assets and liabilities of CCS included in the Cooperative's consolidated balance sheets at December 31, 2010 and 2009:



	<b>2010</b>	<b>2009</b>
	(in thousands)	
Current assets		
Cash and cash equivalents	\$ 543	\$ 608
Accounts receivable, affiliated organization	174	-
Other receivables	10	9
Other current assets	755	732
Non-utility property	21	34
<b>Total assets</b>	<b>\$ 1,503</b>	<b>\$ 1,383</b>
Current liabilities		
Accounts payable and accrued expenses	\$ 1,996	\$ 1,718
Accrued postretirement benefit cost	216	-
Accounts payable, affiliated organization	88	175
<b>Total liabilities</b>	<b>\$ 2,300</b>	<b>\$ 1,893</b>

### Note 13: Postretirement Benefits

During 2010, the administration of the postretirement benefit plan, including the obligation liability and all accounting for it, was transferred from PREA to CCS. As of November 1, 1995 (the effective date), PREA eliminated postretirement medical benefits to all of its employees except for grandfathered employees. There were two different levels of benefits for those grandfathered retirees. For each retiree over the age of 62 on the effective date, PREA, and now CCS, pays the full premium for the appropriate medical insurance for the remainder of the retiree's life. For those that were over the age of 55 but younger than 62 on the effective date, PREA, and now CCS, pays a maximum premium for medical insurance equal to the policy premium on November 1, 1995. In this second group, the retiree is responsible for any increases above this amount. On December 31, 2010, there were seven retirees covered under this plan. CCS expects to contribute \$27,000 to the plan in 2011. This amount will be allocated to the Cooperative and PREA based on historical payroll allocations of the retirees covered under the plan.

CCS uses a December 31 measurement date for the plan. Information about the plan's funded status follows:

	<b>2010</b>
	(in thousands)
Benefit obligation, projected	\$ 216
Fair value of plan assets	-
<b>Funded status</b>	<b>\$ (216)</b>

Amounts recognized in the statements of financial position:

	<b>2010</b>
	(in thousands)

**Accrued postretirement benefit cost liability**

**\$ 216**

Amounts recognized in accumulated other comprehensive income not yet recognized as components of net periodic benefit cost consist of:

	<b>2010</b>
	(in thousands)
Net loss	\$ 30
Transition obligation	82
	<b>\$ 112</b>

The accumulated benefit obligation for the plan was \$104,000 at December 31, 2010.

Other significant balances and costs are:

	<b>2010</b>
	(in thousands)
Employer contributions	\$ 6
Benefits paid	6
Benefit cost	9

The following amounts have been recognized in the consolidated statement of margins for the year ended December 31, 2010:

	<b>2010</b>
	(in thousands)
Amounts arising during the period:	
Net loss	\$ -
Net transition obligation	17

The estimated net loss and transition obligation for the plan that will be amortized from accumulated other comprehensive income into net periodic benefit cost over the next fiscal year are \$0 and \$17,000, respectively.

The discount rate used to determine the benefit obligation was 5.75% for 2010.

For measurement purposes, a 6% annual rate of increase in the per capita cost of covered health care benefits was assumed for 2010 and should remain at that level.

As of December 31, 2010, the expected future payments, which reflect expected future service, are as follows:

2011	\$ 27
2012	26
2013	25
2014	24
2015 and thereafter	114

#### Note 14: Employee Benefit Plans

All employment relationships are through CCS, the consolidated variable interest entity of the Cooperative. CCS's leave policies provide for payment of unused leave after the end of each calendar year for 2010 and 2009. A provision has been recorded for this liability.

The Cooperative through CCS, participates in a multi-employer defined-benefit pension plan and a 401(k) defined-contribution plan (Plans) covering substantially all of its employees. The Cooperative makes annual contributions to the Plans equal to the amount accrued for pension expense. Total pension expense for both plans amounted to \$2,203,000 and \$1,586,000 for the years ended December 31, 2010 and 2009, respectively.

The Cooperative, through CCS, has an employment agreement, that contains a funded deferred compensation agreement, with its President and CEO.

#### Note 15: Commitments and Contingencies

##### Power Supply and Transmission Agreements

The Cooperative has entered into power supply and transmission agreements with various service providers. A significant number of these agreements are umbrella type agreements and do not bind the Cooperative to enter into any type of transaction.

Since June 2007, the Cooperative has issued periodic Requests for Proposal (RFP) for energy and/or capacity products for varying quantities and terms between one and five years with delivery beginning in 2009 or later.

As of December 31, 2010, there were several significant capacity and energy transactions under these umbrella agreements with some energy deliveries beginning as early as 2009 and extending through 2013. Additional arrangements were made in 2009 and 2010 for energy deliveries beginning in 2012 and extending through 2014.

The Cooperative also purchased capacity for 2009 through June 2014, in a series of transactions. These transactions contained specific quantities of capacity, all of which were or will be needed to serve the Cooperative's load.

A summary of the power supply agreements are as follows:

##### New York Power Authority

This contract meets a portion of the Cooperative's base load and peaking requirements and its delivered cost to the Cooperative's members is below market. The current contract terminates in 2025 for the Niagara Project. The current contract for the St. Lawrence Project expires in 2017.

##### 2010 Energy Provider

The Cooperative entered into an arrangement in October 2009 to provide the Cooperative's remaining unmet load requirements beginning in January 2010. The agreement requires the Cooperative to supply monthly a predetermined minimum amount of energy from its generation resources and power purchase agreements and purchase any remaining requirements to meet its load pursuant to the contract. If it does not supply the minimum amount of generation required in

any given month, the Cooperative is required to purchase replacement energy for any shortfalls at a market-based price. The transition to the new supplier occurred on January 1, 2010. The agreement expires in December 2011.

### **Future Power Supply**

Using the RFP process, the Cooperative had entered into power purchase agreements in 2009 with various counterparties for a combination of around-the-clock, on-peak and off-peak energy and call option products that would meet approximately 95 percent of its projected energy requirements in 2010.

Various purchased power agreements require the Cooperative to post collateral deposits for exposure exceeding specified thresholds. As of December 31, 2010, collateral deposits totaled \$11,407,000. Additionally, one agreement requires the Cooperative to provide additional credit support in the form of an irrevocable standby letter of credit in the amount of \$5,000,000. The letter of credit is provided by CFC and is valid until November 30, 2011.

### **SSES Replacement Power Insurance Policy**

The Cooperative mitigated a portion of the economic risk of an outage at SSES by purchasing a Replacement Power Insurance Policy from Arrow Syndicate 1910. Under the terms of the policy, if SSES had a forced outage event, the Cooperative would have been reimbursed for the cost of replacement power for the insured quantity of 250 MW. The policy stipulates that the outage limit for each such forced outage is 90 consecutive days, and the aggregate coverage limit is \$15 million. For this coverage, the Cooperative purchased a two-year policy terminating December 31, 2012.

### **Transmission Service**

Transmission service for the Cooperative's load is provided through a hybrid arrangement consisting of the PJM Open Access Transmission Tariff (OATT) and the pre-existing Wheeling and Supplemental Power Agreement with Pennsylvania Electric Company.

## **Insurance**

PPL, as the 90 percent owner and sole operator of SSES, and the Cooperative, as owner of a 10 percent undivided interest in SSES, are members of certain insurance programs which provide coverage for property damage to the 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, 2010, the maximum amount PPL and the Cooperative jointly could be assessed under these programs was \$40 million annually.

PPL and the Cooperative's public liability for claims resulting from a nuclear incident is currently limited to \$12.6 billion under provisions of the Price-Anderson Act Amendments of 2005.

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 \$235 million per incident, payable at \$35 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 \$0.7 million and \$1.0 million as of December 31, 2010 and 2009, respectively.

Under the terms 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, 2010 was approximately \$2.6 million. Payment of this contingent liability has been guaranteed by CFC.

### Litigation

The Cooperative may be subject to claims and lawsuits that arise primarily in the ordinary course of business. At December 31, 2010, no such claims or lawsuits existed.

## Note 16: Deferred Credits

### 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 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 beginning June 1988. 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 percent 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 \$632,000 and \$711,000 as of December 31, 2010 and 2009, 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 by 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, 2010, 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):

2011	\$ 2,361
2012	2,361
2013	2,361
2014	2,361
2015	2,361
Thereafter	7,082
<b>Total minimum lease payments</b>	<b>\$ 18,887</b>

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 percent and may fluctuate based on differences between the future interest rate and the assumed interest rate.

Rental expense for this lease totaled \$1.9 and \$1.8 million in years ended December 31, 2010 and 2009, respectively.

### Deferred Revenue Plan

The Board has established a Deferred Revenue Plan, which seeks to stabilize members' rates for 2011 and as long as possible thereafter to mitigate the effects of expected increases in rates. The deferral of revenue for 2010 was determined as any amount above \$500,000 operating margins, and for 2009 was determined as any amount above the budgeted assignable margins, after excluding earnings from the Nuclear Decommissioning Trust. Deferred revenue additions and deletions are recorded in operating revenues in the consolidated statements of margin. At December 31, 2010 and 2009, deferred revenues associated with the Deferred Revenue Plan were \$35,732,000 and \$46,943,000, respectively. The changes in deferred revenues in 2010 and 2009 were as follows:

	2010	2009
	(in thousands)	
Beginning balance	\$ 46,943	\$ 57,980
Additions	3,079	10,276
Deletions	(14,290)	(21,313)
Ending balance	<u>\$ 35,732</u>	<u>\$ 46,943</u>

### Deferred Credit

With the establishment of a deferred tax asset to record the effect of the temporary differences related to net operating loss carryforwards, fixed asset basis, safe harbor lease treatment, gain on installment sale and financial statement accruals, the Cooperative established a deferred credit of \$13 and \$12 million for 2010 and 2009, respectively, under FASB ASC Topic 980, *Regulated Operations*. The value of the deferred tax asset is considered in the rate making process as required by Topic 980.

### Note 17: Disclosures About Fair Value of Assets and Liabilities

ASC Topic 820, *Fair Value Measurements*, defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Topic 820 also specifies a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The standard describes three levels of inputs that may be used to measure fair value:

- Level 1** Quoted prices in active markets for identical assets or liabilities
- Level 2** Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in active markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities
- Level 3** Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

Following is a description of the valuation methodologies and inputs used for instruments measured at fair value on a recurring basis and recognized in the accompanying balance sheet, as well as the general classification of such instruments pursuant to the valuation hierarchy.

### Nuclear Decommissioning Trust and Investments (Available-for-sale Securities)

Where quoted market prices are available in an active market, securities are classified within Level 1 of the valuation hierarchy. Level 1 securities include highly liquid government bonds and exchange-traded equities. If quoted market prices are not available, then fair values are estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. For these investments, the inputs used by the pricing service to determine fair value may include, one, or a combination of: observable inputs such as benchmark yields, reported trades, broker/dealer quotes, benchmark securities, bids, offers, and reference data market research publications and are classified within Level 2 of the valuation hierarchy. Level 2 securities include certain collateralized mortgage and debt obligations and certain municipal securities. In certain cases where Level 1 or Level 2 inputs are not available, securities are classified within Level 3 of the hierarchy and include auction rate securities. Inputs include quoted market prices, benchmark securities, bids, offers and broker/dealer quotes.

### Derivatives

The fair value is estimated using inputs that are observable or that can be corroborated by observable market data and, therefore, are classified within Level 2 of the valuation hierarchy. For financial transmission rights, inputs include clearing prices of the FTRs at multi-year, annual, seasonal and monthly auctions adjusted for seasonal expectations of the supply and demand of energy. For forward swaps, inputs include actively quoted market prices, broker quotes and industry publications.

The following table presents the fair value measurements of assets recognized in the accompanying consolidated balance sheet measured at fair value on a recurring basis and the level within the fair value hierarchy in which the fair value measurements fall at December 31, 2010 and 2009:

#### 2010 FAIR VALUE MEASUREMENTS USING

	Fair Value	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
(in thousands)				
Available-for-sale securities				
Nuclear Decommissioning Trust	\$ 73,080	\$ 56,970	\$ 16,110	\$ -
Investments	54,667	4,733	46,656	3,278
Derivatives				
Financial transmission rights	13,030	-	13,030	-
Forward swaps	27,734	-	27,734	-

**2009 FAIR VALUE MEASUREMENTS USING**

	<b>Fair Value</b>	<b>Quoted Prices in Active Markets for Identical Assets (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Significant Unobservable Inputs (Level 3)</b>
(in thousands)				
Available-for-sale securities				
Nuclear Decommissioning Trust	\$ 63,455	\$ 45,079	\$ 18,376	\$ -
Investments	64,510	1,824	59,108	3,578
Derivatives				
Financial transmission rights	13,053	-	13,053	-
Forward swaps	16,117	-	16,117	-

The following is a reconciliation of the beginning and ending balances of recurring fair value measurements recognized in the accompanying balance sheet using significant unobservable (Level 3) inputs:

	<b>Debt Security</b>
(in thousands)	
Balance, January 1, 2009	\$ 4,078
Total realized and unrealized gains and losses	
Included in net margin	-
Included in other comprehensive margin	-
Purchases, issuances and settlements	(500)
Transfers in and/or out of Level 3	-
Balance, December 31, 2009	3,578
Total realized and unrealized gains and losses	
Included in net margin	-
Included in other comprehensive margin	-
Purchases, issuances and settlements	(300)
Transfers in and/or out of Level 3	-
<b>Balance, December 31, 2010</b>	<b>\$ 3,278</b>

During 2010 and 2009, there were no realized and unrealized gains and losses for items reflected in the table above included in net margin in the accompanying consolidated statements of margin.

The following methods were used to estimate the fair value of all other financial instruments not recognized in the accompanying balance sheet.



### Cash and Cash Equivalents

The carrying amount approximates fair value.

### Investments in Associated Organizations

Management was not able to estimate the fair value of investments that represent the Cooperative's investment in memberships and other associated organizations and they remain at their carrying value.

### Long-term Debt

Due to the current market interest rates and/or short-term maturities of the Cooperative's debt, carrying amounts approximate fair value.

The estimated fair values of the Cooperative's financial instruments at December 31, 2010 and 2009 are as follow (in thousands):

	2010		2009	
	Carrying Amount	Estimated Fair Value	Carrying Amount	Estimated Fair Value
Cash and cash equivalents	\$ 31,888	\$ 31,888	\$ 38,788	\$ 38,788
Investments	57,167	57,167	74,837	74,837
Nuclear Decommissioning Trust	73,080	73,080	63,455	63,455
Investment in associated organizations	27,556	27,556	27,568	27,568
Derivative investments	40,764	40,764	29,170	29,170
Long-term debt	158,259	158,259	163,727	163,727

### Note 18: Realty Taxes

The Cooperative's portion of local real estate taxes related to SSES are billed by and paid to PPL. The Cooperative is billed and pays directly to various local tax jurisdictions local real estate taxes on other property that is exclusively owned by the Cooperative.

### Note 19: Current Economic Condition

The current protracted economic decline continues to present electric cooperatives with difficult circumstances and challenges, which in some cases have resulted in large and unanticipated declines in the fair value of investments and other assets. The financial statements have been prepared using values and information currently available to the Cooperative.

Current economic conditions have put additional pressure on many cooperatives and affiliated organizations to meet their financing and liquidity needs. A significant decline in operating revenues could have an adverse impact on the Cooperative's future operating results.

In addition, given the volatility of current economic conditions, the values of assets and liabilities recorded in the financial statements could change, resulting in material future adjustments in investment values, allowances for receivables, etc. All known impairments and changes to fair value have been recorded in these financial statements.

**Note 20: Subsequent Events**

Subsequent to December 31, 2010, the Board of Directors of the Cooperative authorized the submission of a \$100 million request for long-term financing with CFC for future construction and utility plant additions.

Subsequent events have been evaluated through April 26, 2011, which is the date the financial statements were available to be issued.



