

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

FINANCIAL STATEMENTS

December 31, 2008 and 2007

With Independent Auditors' Report

INDEPENDENT AUDITORS' REPORT

The Board of Directors and Members
New Hampshire Electric Cooperative, Inc.

We have audited the accompanying balance sheets of New Hampshire Electric Cooperative, Inc. (the Cooperative) as of December 31, 2008 and 2007, and the related statements of operations, changes in equities (deficit), 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 U.S. generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above, present fairly, in all material respects, the financial position of New Hampshire Electric Cooperative, Inc. as of December 31, 2008 and 2007, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Berry, Dunn, McNeil & Parker

Portland, Maine
March 20, 2009

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Balance Sheets

December 31, 2008 and 2007

ASSETS

	<u>2008</u> (000s)	<u>2007</u> (000s)
Utility plant		
Distribution and transmission	\$ 236,770	\$ 230,093
General and other	25,526	24,792
Construction work in progress	<u>4,929</u>	<u>2,905</u>
Total utility plant	267,225	257,790
Less accumulated depreciation and amortization	<u>110,122</u>	<u>102,959</u>
Net utility plant	<u>157,103</u>	<u>154,831</u>
Other assets		
Non-utility property, net	391	404
Investment in associated organizations, at cost	<u>10,422</u>	<u>10,068</u>
Total other assets	<u>10,813</u>	<u>10,472</u>
Current assets		
Cash and cash equivalents	822	926
Receivables from members - energy sales, net of allowance for doubtful accounts of \$601 in 2008 and \$493 in 2007	13,945	13,290
Other receivables, net of allowance for doubtful accounts of \$95 in 2008 and \$108 in 2007	2,977	1,278
Materials and supplies	1,868	1,733
Prepayments and other current assets	<u>1,293</u>	<u>1,376</u>
Total current assets	<u>20,905</u>	<u>18,603</u>
Deferred debits and other assets	<u>41,299</u>	<u>39,967</u>
	<u>\$ 230,120</u>	<u>\$ 223,873</u>

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

LIABILITIES AND EQUITIES

	<u>2008</u> (000s)	<u>2007</u> (000s)
Equities		
Patronage capital		
Assigned	\$ 53,729	\$ 48,515
Assignable	4,450	5,214
Accumulated deficit	(5,332)	(6,532)
Other capital	<u>300</u>	<u>300</u>
Total equities	<u>53,147</u>	<u>47,497</u>
Commitments and contingencies (Notes 5, 6, 8, and 11)		
Current liabilities		
Line of credit	5,439	6,882
Accounts payable	10,544	9,188
Accrued liabilities	3,868	2,009
Member deposits	976	1,055
Current portion of long-term obligations	<u>16,510</u>	<u>15,921</u>
Total current liabilities	<u>37,337</u>	<u>35,055</u>
Long-term obligations, excluding current portion	119,411	125,770
Deferred credits and other liabilities	<u>20,225</u>	<u>15,551</u>
-	<u>\$ 230,120</u>	<u>\$ 223,873</u>

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Statements of Operations

Years Ended December 31, 2008 and 2007

	<u>2008</u> (000s)	<u>2007</u> (000s)
Operating revenues	\$ 145,439	\$ 139,569
Operating expenses	<u>135,756</u>	<u>129,512</u>
Operating margins before interest and other deductions	9,683	10,057
Interest and other deductions, net	<u>5,233</u>	<u>4,843</u>
Net operating margins	<u>4,450</u>	<u>5,214</u>
Nonoperating margins		
Interest and patronage dividends	1,001	1,110
Other	<u>199</u>	<u>162</u>
Net nonoperating margins	<u>1,200</u>	<u>1,272</u>
Net margins	\$ <u>5,650</u>	\$ <u>6,486</u>

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

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Statements of Changes in Equities (Deficit)

Years Ended December 31, 2008 and 2007

	<u>Patronage Capital</u>		Accumulated <u>Deficit</u> (000s)	<u>Other Capital</u> (000s)	Total <u>Equities</u> (000s)
	<u>Assigned</u> (000s)	<u>Assignable</u> (000s)			
December 31, 2006	\$ 42,923	\$ 5,592	\$ (7,804)	\$ 300	\$ 41,011
2006 patronage capital assigned	5,592	(5,592)	-	-	-
Net operating margin	-	5,214	-	-	5,214
Net nonoperating margin	<u>-</u>	<u>-</u>	<u>1,272</u>	<u>-</u>	<u>1,272</u>
December 31, 2007	48,515	5,214	(6,532)	300	47,497
2007 patronage capital assigned	5,214	(5,214)	-	-	-
Net operating margin	-	4,450	-	-	4,450
Net nonoperating margin	<u>-</u>	<u>-</u>	<u>1,200</u>	<u>-</u>	<u>1,200</u>
December 31, 2008	<u>\$ 53,729</u>	<u>\$ 4,450</u>	<u>\$ (5,332)</u>	<u>\$ 300</u>	<u>\$ 53,147</u>

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

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Statements of Cash Flows

Years Ended December 31, 2008 and 2007

	<u>2008</u> (000s)	<u>2007</u> (000s)
Cash flows from operating activities		
Net margins	\$ 5,650	\$ 6,486
Adjustments to reconcile net margins to net cash provided by operating activities		
Depreciation and amortization	9,509	9,003
Net gain on sale of utility assets	(20)	(23)
Noncash patronage capital dividends	(1,003)	(1,011)
Change in deferred credits	(4,435)	(8,988)
Change in deferred debits	8,228	10,270
(Increase) decrease in		
Member and other accounts receivable	(2,354)	(689)
Materials and supplies	(135)	(32)
Prepayments and other current assets	83	(210)
Increase (decrease) in		
Accounts payable	1,356	3,414
Accrued liabilities	1,859	(89)
Member deposits	<u>(79)</u>	<u>141</u>
Net cash provided by operating activities	<u>18,659</u>	<u>18,272</u>
Cash flows from investing activities		
Retirement of capital certificates	853	888
Construction and acquisition of plant	(11,331)	(11,976)
Proceeds from sales of utility assets	20	23
Removal costs of retirements, net of materials salvaged	<u>(888)</u>	<u>(527)</u>
Net cash used by investing activities	<u>(11,346)</u>	<u>(11,592)</u>

(Continued next page)

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

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Statements of Cash Flows (Concluded)

Years Ended December 31, 2008 and 2007

	<u>2008</u> (000s)	<u>2007</u> (000s)
Cash flows from financing activities		
Net (repayments) advances on line of credit	\$ (1,443)	\$ 6,882
Principal payments of long-term obligations	(15,974)	(15,568)
Proceeds from long-term obligations	<u>10,000</u>	<u>-</u>
Net cash used by financing activities	<u>(7,417)</u>	<u>(8,686)</u>
Net decrease in cash and cash equivalents	(104)	(2,006)
Cash and cash equivalents, beginning of year	<u>926</u>	<u>2,932</u>
Cash and cash equivalents, end of year	\$ <u>822</u>	\$ <u>926</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for interest	\$ <u>7,813</u>	\$ <u>8,421</u>

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

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

Organization and Purpose

New Hampshire Electric Cooperative, Inc. (NHEC or the Cooperative) is a rural electric cooperative utility established under the laws of the state of New Hampshire (NH). The Cooperative is subject to regulation by the Federal Energy Regulatory Commission (FERC) and the New Hampshire Public Utilities Commission (NHPUC) for certain rates and other matters. NHEC is a distribution cooperative, providing electric power to its members in certain areas of New Hampshire. NHEC serves more than 78,000 accounts, spread over nine of New Hampshire's ten counties.

1. Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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 statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Regulatory Accounting

The Cooperative follows the accounting prescribed by the FERC Chart of Accounts, the NHPUC, and Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation," for its regulated services. This accounting recognizes the economic effects of rate regulation by recording costs and a return on investment, as such amounts are recovered through rates authorized by regulating authorities. The Cooperative annually reviews the continued applicability of SFAS No. 71 based on the current regulatory and competitive environment.

In accordance with New Hampshire statute, the Cooperative's members have the option to vote to reduce the level of NHPUC regulation that affects the Cooperative. The option to reduce NHPUC regulation was passed by a vote of the Cooperative's membership at its June 2000 annual meeting. Additional legislation became law during 2001 that further reduced the NHPUC's regulatory authority over the Cooperative such that its optional and default energy service (also known as "Co-op Power") is no longer subject to NHPUC regulation. The NHPUC retains regulatory control for all aspects of the Cooperative that pertain to the restructuring of the electric industry. Therefore, all regulatory assets and liabilities associated with stranded costs, default power service, energy efficiency, energy assistance and the restructuring efforts will continue to be regulated by the NHPUC. The Cooperative's Board of Directors regulates its other rate components.

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

Utility Plant and Depreciation

Utility plant is stated at cost including an allowance for funds used during construction. The provision for depreciation and amortization is computed on a straight-line method at rates based upon the estimated service lives of the assets. Utility plant depreciation was approximately \$9,947,000 in 2008 and \$9,451,000 in 2007, a portion of which is capitalized.

Maintenance and repairs of utility plant are charged to operations as incurred. Replacements and betterments are capitalized. At the time units of utility plant are retired, the cost of the property retired and costs of removal, less salvage, are charged to the allowance for depreciation.

Allowance for Funds Used During Construction

The allowance for funds used during construction represents the cost of borrowed funds used for construction of utility plant. The allowance is capitalized as a component of the cost of utility plant. The Cooperative capitalized \$216,461 and \$195,909 of interest in 2008 and 2007, respectively.

Operating Revenues

The Cooperative extends credit to its members at standard terms after appropriate review. Operating revenues are based on rates, most of which are authorized by the NHEC Board of Directors and the remainder of which are authorized by NHPUC. The rates are applied to members' utilization of electricity, which NHEC bills its members on a cycle basis throughout the month. NHEC records revenues as it provides service to its members.

Purchased Power Costs

NHEC's rates reflect estimates of the cost of purchased power, including contract power costs, spot market costs, cost of renewable energy credits, capacity costs, and the cost of ancillary services. Retail members who purchase their power from the Cooperative are billed a seasonally levelized power cost recovery charge based on projected data for the cost of wholesale power. NHEC's rates also include estimates of transmission and distribution access costs. NHEC rates also reflect estimates of cost associated with services and administration necessary for members to access energy services from competitive suppliers. To the extent that cost estimates differ from actual charges incurred, the differences are deferred and refunded or charged to members through periodic rate adjustments as approved by NHEC's Board of Directors in accordance with New Hampshire Statutes.

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

Derivative Instruments

NHEC evaluates purchase power contracts using guidance under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." For contracts assessed as derivatives, NHEC has marked these contracts to fair market value. As such, the Cooperative recognizes the gain or loss on the derivative instrument, as well as the offsetting loss or gain on the contract, as a regulatory asset or liability. For all other purchase power contracts, NHEC applies the normal purchase and normal sales exception or lease exception. If these contracts cease to meet this exception, the fair value of the contracts is recognized in the balance sheets and the contracts are accounted for using the mark to market (MTM) model. The Cooperative recognizes the MTM as a receivable from or a payable to members as allowed by SFAS No. 71.

Deferred Debits and Other Assets

Certain of the Cooperative's Deferred Debits and Other Assets have been designated as stranded costs. These costs are associated with the Cooperative's past purchased power and generation obligations for which the NHPUC has recognized the Cooperative's continued obligation. The Deferred Debits are related to the stranded cost debt. The interest and principal related to these obligations are reported in the financial statements as an amortization expense as approved by the NHPUC and are recoverable through a stranded cost charge. The NHPUC has also recognized that, as a member-owned cooperative without shareholders to absorb stranded costs, the Cooperative requires full recovery of its non-mitigated stranded costs. NHEC's retail rates reflect estimates of stranded costs. Retail members are billed a levelized stranded cost charge based on projected data for stranded costs. To the extent that cost estimates differ from actual charges incurred, the differences are deferred and refunded or charged to members through periodic rate adjustments under a tariff approved by the NHPUC.

Deferred Credits

NHEC establishes Deferred Credits for costs associated with the over-recovery of certain tariff rates that are deferred and refunded to members through periodic rate adjustments. Deferred Credits are regulatory in nature and are approved by either the Board of Directors or the NHPUC. Deferred Credits also include amounts related to pension and regulatory liabilities that are amortized over a defined period established at the inception of the credit.

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

Other Regulated Rates

NHEC's tariff rates also include an Energy Efficiency System Benefit Charge (EE-SBC) and an Energy Assistance Program System Benefit Charge (EAP-SBC) at rates set by the NHPUC for all New Hampshire jurisdictional utilities. The EE-SBC recovers the costs of NHEC's energy efficiency program services it provides to its members in accordance with NHPUC approval. The funds collected through NHEC's EAP-SBC are reconciled to the benefits provided to NHEC's income-qualified members; any under or over recovery of benefits paid to members is received from or submitted to, respectively, the State of New Hampshire which administers the pooled funds of all jurisdictional utilities.

Materials and Supplies

Inventories of materials and supplies are stated at average cost.

Income Tax Status

NHEC is exempt from United States income taxes pursuant to §501(c)(12) of the Internal Revenue Code, which requires that at least 85% of a cooperative's income be collected from its members.

The Company has elected to defer the application of Financial Accounting Standards Board Interpretation No. 48, "Accounting for Uncertainty in Income Taxes," to its first fiscal year beginning after December 15, 2008. The Company accounts for uncertain income tax positions based on management's best estimate of the amount that will ultimately be accepted by the applicable tax authority.

Patronage Capital

The bylaws of the Cooperative provide that operating revenues from the furnishing of electric energy in excess of operating costs and expenses, referred to as operating margins, shall be allocated as patronage capital. All other amounts received in excess of other expenses, referred to as non-operating margins, shall be used to offset any losses incurred during the current or any prior fiscal year and, to the extent not needed for that purpose, allocated to its patrons on the basis of their patronage, and any amount so allocated shall be included as part of the capital credited to the accounts of patrons.

NHEC may refund patronage capital within parameters set in the master loan agreement from the National Rural Utilities Cooperative Finance Corporation (CFC), its lender. In the event of the dissolution or liquidation of NHEC, after all outstanding indebtedness has been paid, outstanding capital credits shall be retired without priority on a pro rata basis.

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

Cash and Cash Equivalents

NHEC considers all highly liquid debt instruments with an original maturity of three months or less to be cash equivalents. The Cooperative maintains cash in bank deposit accounts which may exceed federally insured limits. The Cooperative has not experienced losses in such accounts, and management does not believe that it is exposed to any significant risk on cash and cash equivalents.

Receivables

Receivables are stated at the amount management expects to collect on outstanding balances. Management provides for probable uncollectable amounts through a charge to earnings and a credit to an allowance for doubtful accounts (allowance) based on its assessment of the collectability of outstanding accounts. Individual accounts that are still outstanding after management has used reasonable collection efforts are written off through a charge to the allowance and a credit to accounts receivable. Credit is extended without collateral.

Postretirement Benefit Plan

The Cooperative sponsors a defined benefit postretirement medical plan through National Rural Electric Cooperative Association (NRECA) that covers substantially all of its employees. The Cooperative has adopted SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106 and 132(R)." SFAS No. 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its balance sheet and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. The Cooperative recognizes changes in the funded status using a regulatory liability or regulatory asset as allowed under SFAS No. 71 because the changes in funded status will be recognized in future regulated rates.

Environmental Laws

The Cooperative has continuing requirements that must be met under environmental laws. Management believes that the Cooperative is in compliance with applicable laws in all material respects.

Taxes Collected from Consumers and Remitted to Governmental Authorities

The Cooperative reports certain taxes on a net basis. Accordingly, they are recorded as a liability when billed to consumers and excluded from revenue and expenses.

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

Recent Accounting Pronouncement

In December 2008, the Financial Accounting Standards Board (FASB) issued FASB Staff Position (FSP) No. FAS 132(R)-1, *Additional Disclosures Concerning Plan Assets of Defined Benefit Pension and Postretirement Plans*. FSP No. FAS 132(R)-1 amends SFAS No. 157, "Fair Value Measurements," to exclude plan assets of a defined benefit pension or other postretirement plan from the scope of SFAS No. 157 because the plan assets are subject to the disclosure requirements of SFAS No. 132(R), "Employers' Disclosures about Pension and Other Postretirement Benefits (as amended)." FSP No. FAS 132(R)-1 also expands disclosure requirements for plan assets, including the level within the fair value hierarchy, as identified above, in which fair value measurements are determined. Adoption of FSP No. FAS 132(R)-1 is required for fiscal years ending after December 15, 2009. Management plans to adopt FSP No. FAS 132(R)-1 for the year ending December 31, 2009.

2. Nuclear Utility Plant

NHEC had a 2.17391% undivided ownership interest in the Seabrook Nuclear Plant (Seabrook) until November 1, 2002, when the Cooperative sold its interest. As part of the NHPUC's approval of NHEC's stranded costs, NHEC reduced the carrying value of the Seabrook plant to \$3,750,000 and classified the excess of the book value of Seabrook as the Seabrook Regulatory Asset in Deferred Debits and Other Assets. The regulatory asset includes an amount to recognize NHEC's total debt obligation relative to the Seabrook plant (Note 1). The stranded cost charge has been approved by the NHPUC through 2009. The Cooperative will be required to get updated approval thereafter.

3. Investment in Associated Organizations

At December 31, investments in associated organizations, which are not marketable and are carried at cost, consisted of the following:

	<u>2008</u> (000s)	<u>2007</u> (000s)
Capital term certificates - CFC	\$ 5,369	\$ 5,374
Patronage capital credits - CFC	4,857	4,578
Other	<u>196</u>	<u>116</u>
Total	<u>\$ 10,422</u>	<u>\$ 10,068</u>

These assets are considered for impairment annually. There are no identified events or changes in circumstances that may have a significant adverse effect on fair value.

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

4. Deferred Debits and Other Assets

Deferred debits and other assets at December 31, 2008 and 2007 were as follows:

	<u>2008</u> <u>(000s)</u>	<u>2007</u> <u>(000s)</u>
Deferred debits		
Deferred Recoveries (Note 1)	\$ 2,154	\$ 244
Termination Payment Regulatory Asset (Note 6)	5,488	7,151
Seabrook Regulatory Asset (Note 2)	21,398	29,466
Regulatory asset - derivative power contracts (Note 6)	10,862	-
Past Service Cost Recovery	1,034	1,257
Other assets	363	722
Derivative Contracts - Power	<u>-</u>	<u>1,127</u>
 Total	 <u>\$ 41,299</u>	 <u>\$ 39,967</u>

5. Long-Term Obligations

As of December 31, 2008 and 2007, long-term obligations were as follows:

	<u>2008</u> <u>(000s)</u>	<u>2007</u> <u>(000s)</u>
General debt		
6% notes payable to CFC, payable in quarterly installments, including interest, through October 2012	\$ 1,034	\$ 1,257
4.25% - 5.80% notes payable to CFC, payable in quarterly installments, including interest, through November 2012	16,365	19,935
6.35% notes payable to CFC, payable in quarterly installments, including interest, through December 2012	1,554	1,869
4.60% - 6.85% notes payable to CFC, payable in quarterly installments, including interest, through November 2022	18,115	18,916
6.20% notes payable to CFC, payable in monthly installments, including interest, through November 2028	9,362	9,593
4.55% - 4.90% notes payable to CFC, payable in quarterly installments, including interest, through July 2030	14,922	15,309

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

	<u>2008</u> (000s)	<u>2007</u> (000s)
4.25% - 6.15% notes payable to CFC, payable in quarterly installments, including interest, through January 2034	\$ 22,077	\$ 22,490
6.20% notes payable to CFC, payable in quarterly installments, including interest, through April 2035	6,020	6,107
6.75% notes payable to CFC, payable in quarterly installments, including interest, through October 2038	7,797	7,875
6.55% - 6.80% notes payable to CFC, payable in quarterly installments, including interest, through October 2039	10,179	-
Stranded cost related debt		
5.74% - 6.20% notes payable to CFC, payable in quarterly installments, including interest, through October 2011	4,733	6,129
5.66% - 7.35% notes payable to CFC, payable in quarterly installments, including interest, through October 2011	22,741	29,588
Variable rate notes payable to CFC, payable in quarterly installments, interest only, principal due October 2011; interest rate varies monthly (5.00% at December 31, 2008)	<u>1,022</u>	<u>2,623</u>
Total long-term obligations	135,921	141,691
Less current portion	<u>16,510</u>	<u>15,921</u>
Total long-term obligations, excluding current portion	\$ <u>119,411</u>	\$ <u>125,770</u>

The mortgage agreements provide that all outstanding obligations to CFC are collateralized by substantially all assets and the rents, income, revenues, proceeds and benefits derived, received or had for any and all such assets.

Interest expense for long-term debt approximated \$7,707,000 in 2008 and \$8,419,000 in 2007. Based on an agreement reached in 2000 with the NHPUC regarding the termination payment (Note 6) and the Seabrook regulatory asset (Note 2), the Cooperative is classifying interest expense of approximately \$2.1 million in 2008 and \$2.9 million in 2007 from certain CFC notes in operating expenses, which are recovered through stranded costs.

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

The Cooperative must also comply with certain covenants which include restrictions on the Cooperative's ability to borrow additional monies, enter into specified transactions or pay dividends or distribute patronage capital without first seeking the mortgagee's approval. Additional covenants address insurance coverage, the sale of assets and other non-financial matters. CFC mortgage notes are subject to repricing periodically to reflect current market interest rates.

NHEC refinanced all its Rural Utilities Service debt through CFC in 1995 through 1997, resulting in discounts, net of refinancing fees, of approximately \$7,673,000. Accumulated amortization of these net discounts was approximately \$5,869,000 at December 31, 2008 and \$5,418,000 at December 31, 2007. The discounts are reflected as deferred credits which are being amortized over the remaining life of the reacquired debt maturing in 2012.

In 2004, NHEC signed an agreement with CFC for a four-year work plan loan of approximately \$48.9 million. The interest rate will be determined based on the CFC market rates at the time of each advance, and principal will be paid over a period not to exceed 35 years through November 2039. NHEC had taken advances of \$24,490,000 through 2008, including \$10,204,000 in 2008.

The financing agreement with CFC requires NHEC to purchase loan capital term certificates (LCTC) in an amount not to exceed 12.5% of the total principal amount borrowed from CFC. CFC calculates the amount of LCTC that are required to be purchased at the time of each loan advance. NHEC financed the acquisition of \$204,000 in LCTC's in 2008, in a non-cash transaction.

As a cooperative, CFC may pay capital dividends to its borrowers for their patronage. The total capital dividends NHEC received from CFC were \$929,000 during 2008 and \$992,000 in 2007, of which \$650,000 for 2008 and \$695,000 for 2007 was paid in cash with the remainder being patronage capital certificates in CFC to be retired at a later date.

The Cooperative has a perpetual revolving \$20 million line of credit from CFC. As of December 31, 2008, \$5,439,000, with interest at 5%, was outstanding on the line of credit. As of December 31, 2007, \$6,882,000, with interest at 6.4%, was outstanding on the line of credit. This line of credit is collateralized in the same manner as the other CFC debt obligations.

Principal payments to be made on long-term obligations, based on agreements currently in place, for the next five years are as follows:

	<u>General</u>	(000s) <u>Stranded</u> <u>Costs</u>	<u>Total</u>
2009	\$ 6,544	\$ 9,966	\$ 16,510
2010	6,821	9,652	16,473
2011	7,156	8,877	16,033
2012	7,591	-	7,591
2013	2,646	-	2,646

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Notes to Financial Statements

December 31, 2008 and 2007

6. Long-Term Power Supply and Sale Agreements

Prior to January 1, 2000, NHEC had a contract agreement to purchase nearly all of its power supply from Public Service of New Hampshire (PSNH). In September 1999, NHEC negotiated an agreement with PSNH to terminate this contract. The agreement provided the Cooperative's members with the opportunity to purchase competitively supplied power at retail. The Cooperative made a termination payment to PSNH of \$18 million pursuant to the agreement, after borrowing the funds from CFC. NHEC established a deferred debit relating to this payment (Note 4). As part of the settlement agreement, NHEC will purchase interconnection and delivery service from PSNH pursuant to a long-term contract which is FERC regulated, cost-based, and cancelable by either party with a seven-year notice.

On January 22, 1997, the Cooperative executed a Power Purchase Agreement with Waste Management of New Hampshire, Inc. for 100% of the energy and capacity output of a landfill gas fueled generating facility located at the Turnkey Recycling and Environmental Enterprises landfill in Rochester, NH, for fixed and inflation indexed prices through June 2014.

On October 27, 2006, the Cooperative executed a Unit Power Contract with Braintree Electric Light Department which gives the Cooperative a cost-based purchase entitlement in the new natural gas fired, oil capable Thomas A. Watson Power Plant to begin as of the date commercial operation commences, projected for May 1, 2009, for a term of 20 years, with additional five-year renewal options. The plant is a high efficiency peaking plant. The contract is expected to contribute to NHEC's capacity requirements and reduce NHEC's exposure to anticipated market energy prices. NHEC's purchase entitlement is 11.25%, or approximately 13 megawatts (MW), of the plant's expected capacity and associated energy and related products.

On December 24, 2007, the Cooperative executed a Unit Contingent Energy and Renewable Energy Certificate agreement with a biomass plant, which gives the Cooperative a fixed price to purchase 9.4% of the energy and renewable energy certificates from the biomass plant. Commercial operation is expected to occur in 2013.

On August 15, 2008, the Cooperative executed a Power Purchase Agreement with PSNH to purchase 10% of the energy and capacity produced by the Lempster Wind Project (a 24 MW wind farm in Lempster, NH) at a rate indexed to the ISO New England (ISO NE) real-time market prices and 10% of the Renewable Energy Certificates that PSNH retains following the expiration of Lempster Wind LLC's repurchase options pursuant to a separate contract between PSNH and Lempster Wind LLC, at fixed prices. The Project began operation in October 2008. The contract continues for 15 years.

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On June 12, 2008, the Cooperative entered a unit contingent agreement with Beaver Ridge Wind, LLC, for the purchase of 100% of the energy, capacity, ancillary services, renewable energy certificates, and environmental attributes produced by the Beaver Ridge Wind facility consisting of three 1.5 MW wind turbines located on Beaver Ridge in the Town of Freedom, Maine. The term of the contract is 15 years from the date the facility began commercial operation, which was November 1, 2008.

In 2006, the Cooperative executed a power supply agreement that provided fixed prices for load following energy service for approximately 28% of the Cooperative's January 1, 2007 through December 31, 2007 wholesale energy requirements. Also in 2006, the Cooperative executed an agreement for blocks of energy at fixed prices for the period January 1, 2007 through June 30, 2009, to serve approximately 40% of the Cooperative's wholesale energy requirement. In 2007, the Cooperative executed an additional power supply agreement to purchase blocks of energy at prices indexed to natural gas prices for the period January 1, 2008 through December 31, 2011. During 2008, NHEC locked in the natural gas price for all of this indexed contract purchased through March 2010. The total of the two energy block contracts provided approximately 75% of the Cooperative's energy needs for 2008 and are expected to provide a similar percentage for the first half of 2009. The Cooperative expects to purchase the remainder of its energy requirements through additional contracts and the ISO NE day ahead and real time markets.

Should a significant number of NHEC's members choose to purchase competitively supplied power instead of purchasing power from the Cooperative, NHEC would still have the obligation to purchase some of the contracted power per these agreements. Management expects that NHEC would then sell any excess power in the marketplace. However, management expects that the likelihood of this happening is remote, as all members currently purchase power from the Cooperative. Purchases from a competitive supplier were made for a brief period by only one member since retail competition became available on January 1, 2000.

As of December 2006, the New England wholesale power and energy markets administered by ISO NE under regulatory authority of the FERC introduced a new Forward Capacity Market that imposes an obligation on load serving entities to make payments for capacity. The Cooperative paid \$6.4 million for capacity in 2007 and \$7.9 million in 2008, which is included in Cooperative power rates.

To assist in meeting its capacity requirements for the Forward Capacity Market, on February 1, 2008, the Cooperative executed a fixed price, fixed quantity financial settlement contract for a portion of its capacity requirements for the period June 2010 through May 2012. Also on February 1, 2008, the Cooperative executed a fixed price, fixed quantity physically settled contract for another portion of its capacity requirements for the period June 2010 through May 2015.

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On January 1, 2008, an "Electric Renewable Portfolio Standard" (RPS) under New Hampshire Statute RSA 362 F:13 became effective. The law requires providers of electricity, including utilities and competitive providers, to acquire a specified percentage of their energy from four classes of renewable resources. By statute, some of the percentages increase over the effective period of the law. To facilitate the required energy acquisition, the law implements a program of "renewable energy credits" (RECs) that allow for the trading of the renewable attributes of energy independent of the energy itself. Finally, the law establishes standards for alternative compliance payments made by electricity providers in lieu of REC acquisition in certain circumstances. In addition to the two wind contracts described above which will provide some of the Cooperative's RPS obligation, the Cooperative has executed contracts with two small hydro units for a portion of its RPS obligation. These contracts continue for five years. The Cooperative has recorded a liability of approximately \$750,000 which it anticipates paying to the State of New Hampshire as alternative compliance payments for the portion of its RPS obligation which it has been unable to obtain through RECs.

The Cooperative is purchasing Regional Network transmission service through ISO NE. NHEC is also purchasing unbundled Local Network transmission service from Northeast Utilities, PSNH's parent company, from Central Vermont Public Service Corporation, and from National Grid. All of these services are priced based on FERC regulated tariffs.

NHEC has executed agreements with CFC for the issuance by CFC of letters of credit as collateral for the Cooperative's performance under certain power supply agreements, ISO NE requirements and other agreements. The total authority under these facilities is \$80,000,000. At December 31, 2008, there were twelve letters of credit totaling \$31,450,000 outstanding under these facilities. Annual fee expenses for issuance of these letters are approximately \$516,000.

7. Deferred Credits and Other Liabilities

Deferred credits and other liabilities at December 31, 2008 and 2007 were as follows:

	<u>2008</u> (000s)	<u>2007</u> (000s)
Deferred credits		
Regulatory liability - Seabrook	\$ 5,238	\$ 7,059
Co-op power and regional access over-recovery (Note 1)	117	2,856
Unamortized gain on refinanced debt (Note 5)	1,804	2,255
Regulatory liability - postretirement benefits (Note 9)	1,702	1,905
Regulatory liability - derivative power contracts	-	1,127
Other deferred credits and recoveries	458	349
Stranded cost over-recovery (Note 1)	44	-
Other liabilities	<u>10,862</u>	<u>-</u>
Total	<u>\$ 20,225</u>	<u>\$ 15,551</u>

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8. Pension and 401(k) Savings Plan

Substantially all of the employees of the Cooperative participate in the Electric Cooperative NRECA Retirement and Security Program, a multi-employer defined benefit pension plan. The Cooperative funds accrued pension costs on an annual basis. Pension costs totaled \$1,884,000 and \$1,752,000 for 2008 and 2007, respectively. Under the Program, accumulated benefits and net asset information are not determined or allocated separately by individual employer.

The Cooperative has established a tax qualified 401(k) savings plan for the benefit of its employees and their beneficiaries. During 2008, the Cooperative matched contributions by those participating employees who are part of the collective bargaining unit, International Brotherhood of Electrical Workers Local 1837, up to 4.5% of annual base pay; bonuses and overtime are excluded. Contributions by participating non-union employees were matched up to 4.5% of annual base pay; bonuses and overtime are excluded. The Cooperative's contribution was approximately \$541,000 and \$512,000 for 2008 and 2007, respectively.

9. Postretirement Benefit Plan

The Cooperative sponsors a defined benefit postretirement medical and life insurance plan. The plan is contributory, with contributions set as a percent of benefit costs plus deductibles and coinsurance. Retiree contributions were not significant in 2008 and 2007. The Cooperative established an irrevocable trust to fund the plan as was required by the NHPUC. The Cooperative plans to fund future pay-as-you-go expenses from this trust and not provide additional funds to the trust. The Cooperative expects the pay-as-you-go expenses will be approximately equal to the income from the trust for the next several years.

SFAS No. 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its balance sheet and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. The statement requires that an employer recognize the funded status of a benefit plan, measured as the difference between plan assets at fair value and the benefit obligation, in its balance sheet. For a postretirement benefit plan, the benefit obligation is the accumulated postretirement benefit obligation.

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The following sets forth the plan's funded status and amounts reported in the Cooperative's financial statements at December 31, 2008 and 2007, and for the years then ended:

	<u>2008</u> (000s)	<u>2007</u> (000s)
<u>Benefit obligation and funded status</u>		
Benefit obligation at December 31	\$ (726)	\$ (748)
Fair value of plan assets at December 31	<u>948</u>	<u>1,145</u>
Funded status of the plans	\$ <u>222</u>	\$ <u>397</u>
<u>Amounts recognized in the balance sheet</u>		
Plan assets included in other assets	\$ 222	\$ 397
Regulatory liability-postretirement benefits	(1,702)	(1,905)

At December 31, 2008 and 2007, the regulatory liability-postretirement benefits was comprised of approximately \$1,579,000 and \$1,746,000 actuarial gain and \$123,000 and \$159,000 of unrecognized prior service credits, respectively. The Cooperative expects to amortize approximately \$109,000 of the actuarial gain and \$35,000 of the prior service costs into income in 2009.

	<u>2008</u> (000s)	<u>2007</u> (000s)
Benefit cost	\$ 28	\$ 28
Benefits paid	\$ 42	\$ 43

Weighted-average assumptions as of and for years ended December 31:

	<u>2008</u>	<u>2007</u>
Discount rate to determine net periodic benefit costs	5.75 %	5.75 %
Discount rate to determine benefit obligation	6.50 %	5.75 %
Expected return on plan assets	6.00 %	8.00 %

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Estimated future benefit payments for the next ten years are as follows:

	<u>(000s)</u>
2009	\$ 50
2010	55
2011	67
2012	61
2013	60
2014-2018	305

Fund assets are managed in a manner which seeks to achieve the following long-term investment objectives:

- Exceed Inflation - Achieve investment returns that average in excess of the annualized inflation rate, defined as the average annualized compound rate of the Consumer Price Index.
- Meet Actuarial Assumptions - Realize a long-term rate of return that meets or exceeds the assumed actuarial rate as stated in the plan's actuarial report.
- Perform in Line with Benchmark Returns - Realize a long-term rate of return that is in line with appropriate benchmark returns on a risk-adjusted basis for each of the asset classes/funds.
- Fund Plan Operating Needs - Provide sufficient income and liquidity to pay monthly retiree benefits and other liquidity needs.

To develop the expected long-term rate of return on assets assumption, the Cooperative considered the current level of expected returns on risk-free investments (primarily government bonds), the historical level of risk premium associated with the other asset classes in which the portfolio is invested and the expectations for future returns of each asset class. The expected return for each asset class was then weighted based on the target asset allocations to develop the expected long-term rate of return on assets assumption for the portfolio. This resulted in the selection of the 6.0% assumption for fiscal 2008.

Asset allocation as of December 31 is as follows::

	<u>2008</u>	<u>2007</u>
Bond funds	70.1 %	60.0 %
Stock funds	29.9	40.0

The trustees' policy is to target 60% of assets to bond funds and 40% to stock funds.

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For measurement purposes, a 9.0% annual rate of increase in the per capita cost of covered health care benefits was assumed for 2009. The rate was assumed to decrease gradually to 5.0% per year by 2017 and remain level thereafter.

In December 2003, the President signed the federal Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) into law. The Act adds the following two features to Medicare (Medicare Part D) that could affect the measurement of the accumulated postretirement benefit obligation and net periodic postretirement benefit cost for the Plan:

- A subsidy to plan sponsors that is based on 28% of an individual beneficiary's annual prescription drug costs between \$250 and \$5,000.
- The opportunity for a retiree to obtain a prescription drug benefit under Medicare.

During 2004, the FASB Staff issued FSP No. FAS 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003." The FSP addresses employers' accounting for the effects of the Act and is effective for the Cooperative beginning in 2005. The accounting for the Act depends on the Cooperative's assessment as to whether the prescription drug benefits available under its plan are actuarially equivalent to Medicare Part D, among other factors. The Cooperative has not determined that the benefit it provides would be considered actuarially equivalent to the benefit provided under the Act because management does not believe the impact would be significant. Accordingly, the Cooperative has not applied the provisions of the FSP.

10. Fair Value

In September 2006, the Financial Accounting Standards Board issued SFAS No. 157. This Statement defines fair value, establishes a framework for measuring fair value in accordance with U.S. generally accepted accounting principles, and expands disclosures about fair value measurements. Although this Statement does not require any new fair value measurements, it has expanded fair value disclosures. This Statement is effective for financial statements issued for fiscal years beginning after November 15, 2007.

SFAS No. 157 defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. SFAS No.157 also establishes 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 (unadjusted) for identical assets or liabilities in active markets that the entity has the ability to access as of the measurement date

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- Level 2: Significant other observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, and other inputs that are observable or can be corroborated by observable market data
- Level 3: Significant unobservable inputs that reflect an entity's own assumptions about the assumptions that market participants would use in pricing an asset or liability

Assets that are measured at fair value on a recurring basis are summarized below:

		Fair value measurements at December 31, 2008, using:	
	<u>2008</u> (000s)	<u>(Level 1)</u> (000s)	<u>(Level 2)</u> (000s)
Postretirement plan assets	\$ 948	\$ 948	\$ -
Derivative instruments - power contracts	10,862	-	10,862

The Cooperative's other financial instruments consist of cash and cash equivalents, short-term trade receivables and payables, investments in non-traded stock, lines of credit, and long-term debt. The carrying value of all instruments, except long-term debt, approximates their fair value. Based on borrowing rates currently available to the Cooperative for loans with similar terms and average maturities, the fair value of long-term debt was approximately \$129,753,000 and \$134,077,000 as of December 31, 2008 and 2007, respectively. These estimates are not necessarily indicative of the amounts that the Cooperative could realize in the current market and different methodologies may have a material effect on the estimated fair value amounts.

11. Commitments and Contingencies

The Cooperative is involved in various legal proceedings incidental to the conduct of its normal business operations. In the opinion of management, these proceedings will not have a material adverse impact on the financial condition of the Cooperative.