NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

FINANCIAL STATEMENTS

December 31, 2017 and 2016

With Independent Auditor's Report

BerryDunn

INDEPENDENT AUDITOR'S REPORT

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

Report on the Financial Statements

We have audited the accompanying financial statements of New Hampshire Electric Cooperative, Inc. (the Cooperative), which comprise the balance sheets as of December 31, 2017 and 2016, and the related statements of operations, changes in equities, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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. These standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Cooperative as of December 31, 2017 and 2016, and the results of its operations and its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

Berry Dunn McNeil & Parker, LLC

Portland, Maine
April 4, 2018

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Balance Sheets

December 31, 2017 and 2016

ASSETS

	2017 **(000s)**	2016 (000s)
Utility plant		
Distribution and transmission	**$ 318,732**	$ 312,562
General and other	**42,887**	42,165
Construction work in progress	**12,565**	3,719
Total utility plant	**374,184**	358,446
Less accumulated depreciation and amortization	**170,195**	159,923
Net utility plant	**203,989**	198,523
Other assets		
Temporary investments	**1,000**	3,000
Intangible assets	**1,375**	1,375
Non-utility property, net	**274**	283
Investment in associated organizations, at cost	**11,563**	11,418
Total other assets	**14,212**	16,076
Current assets		
Cash and cash investments	**12,118**	9,235
Restricted cash	**3,064**	1,000
Receivables from members - energy sales, net of allowance for doubtful accounts of $504 in 2017 and $532 in 2016	**13,968**	12,529
Other receivables, net of allowance for doubtful accounts of $44 in 2017 and $45 in 2016	**6,470**	1,816
Materials and supplies	**2,893**	2,943
Prepayments and other current assets	**2,735**	2,704
Total current assets	**41,248**	30,227
Deferred debits and other assets	**10,062**	7,233
	$ 269,511	$ 252,059

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

LIABILITIES AND EQUITIES

	2017 (000s)	2016 (000s)
Equities		
Patronage capital		
Assigned	**$ 120,982**	$ 112,202
Assignable	**6,806**	8,780
Other capital	**300**	300
Total equities	**128,088**	121,282
Current liabilities		
Lines of credit	**3,751**	292
Accounts payable	**14,663**	8,063
Accrued liabilities	**4,017**	2,797
Member deposits	**1,842**	1,820
Current portion of long-term obligations	**6,127**	6,327
Total current liabilities	**30,400**	19,299
Long-term obligations, excluding current portion	**104,231**	105,335
Deferred credits and other liabilities	**6,792**	6,143
	$ 269,511	$ 252,059

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Statements of Operations

Years Ended December 31, 2017 and 2016

	2017 (000s)	2016 (000s)
Operating revenues	**$ 139,471**	$ 128,869
Operating expenses	**128,810**	115,901
Operating margins before interest and other deductions	**10,661**	12,968
Interest and other deductions, net	**4,569**	4,832
Net operating margins	**6,092**	8,136
Nonoperating margins		
Interest and patronage dividends	**665**	602
Other	**49**	42
Net nonoperating margins	**714**	644
Net margins	**$ 6,806**	$ 8,780

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

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Statements of Changes in Equities

Years Ended December 31, 2017 and 2016

	Patronage Capital Assigned (000s)	Patronage Capital Assignable (000s)	Other Capital (000s)	Total Equities (000s)
December 31, 2015	$ 102,685	$ 9,517	$ 300	$ 112,502
2015 patronage capital assigned	9,517	(9,517)	-	-
Net operating margins	-	8,136	-	8,136
Net nonoperating margins	-	644	-	644
December 31, 2016	112,202	8,780	300	121,282
2016 patronage capital assigned	**8,780**	**(8,780)**	**-**	**-**
Net operating margins	**-**	**6,092**	**-**	**6,092**
Net nonoperating margins	**-**	**714**	**-**	**714**
December 31, 2017	**$ 120,982**	**$ 6,806**	**$ 300**	**$ 128,088**

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

NEW HAMPSHIRE ELECTRIC COOPERATIVE, INC.

Statements of Cash Flows

Years Ended December 31, 2017 and 2016

	2017 (000s)	2016 (000s)
Cash flows from operating activities		
Net margins	**$ 6,806**	$ 8,780
Adjustments to reconcile net margins to net cash provided by operating activities		
Depreciation and amortization	**13,127**	12,733
Cash restricted for operations	**(2,064)**	(500)
Noncash patronage capital dividends	**(431)**	(428)
Change in deferred credits	**649**	(26)
Change in deferred debits	**(2,829)**	(258)
Decrease (increase) in		
Member and other accounts receivable	**(6,093)**	166
Materials and supplies	**50**	(38)
Prepayments and other current assets	**(31)**	63
Increase (decrease) in		
Accounts payable	**4,317**	(2,836)
Accrued liabilities	**788**	(502)
Member deposits	**22**	(52)
Net cash provided by operating activities	**14,311**	17,102
Cash flows from investing activities		
Retirement of capital certificates	**286**	400
Construction and acquisition of plant	**(14,885)**	(14,250)
Removal costs of retirements, net of materials salvaged	**(984)**	(1,096)
Net transfer of temporary investments to cash investments	**2,000**	700
Net cash used by investing activities	**(13,583)**	(14,246)
Cash flows from financing activities		
Net advances (repayments) on lines of credit	**3,459**	(8,181)
Principal payments of long-term obligations	**(6,304)**	(5,982)
Proceeds from long-term obligations	**5,000**	13,800
Net cash provided (used) by financing activities	**2,155**	(363)
Net increase in cash and cash investments	**2,883**	2,493
Cash and cash investments, beginning of year	**9,235**	6,742
Cash and cash investments, end of year	**$ 12,118**	$ 9,235
Supplemental disclosures of cash flow information:		
Cash paid during the year for interest, net of capitalized interest	**$ 4,712**	$ 4,924
Construction and acquisition of plant included in accounts payable	**$ 2,283**	$ -
Construction and acquisition of plant included in accrued liabilities	**$ 432**	$ -

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

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 currently subject to limited regulation by the NH Public Utilities Commission (NHPUC). NHEC is a distribution cooperative, providing electric power to its members in certain areas of NH. NHEC serves more than 83,000 accounts throughout nine of NH'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 Federal Energy Regulatory Commission's Uniform System of Accounts, the NHPUC, and Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 980, *Regulated Operations*, 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 ASC 980 based on the current regulatory and competitive environment.

In accordance with NH 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 energy service (also known as "Co-op Power") is not subject to NHPUC regulation. The NHPUC retains limited regulatory jurisdiction for some aspects of the Cooperative's operations that pertain to the restructuring of the electric industry. All regulatory assets and liabilities associated with default power service, energy efficiency, energy assistance and some aspects of restructuring will continue to be regulated by the NHPUC. The Cooperative's Board of Directors regulates its other rate components.

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 $13,118,000 in 2017 and $12,722,000 in 2016, 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 $127,000 and $162,000 of interest in 2017 and 2016, respectively.

Temporary Investments

Temporary investments are made up of investments in National Rural Utilities Cooperative Finance Corporation (CFC) Medium-Term Notes, with maturities greater than twelve months, and interest rates ranging from 1.77% to 1.87%. As the maturities of these investments fall below twelve months, the investments are transferred to cash investments.

Intangible Assets

Intangible assets consists of radio frequency licenses. As there is an observable market for radio frequency licenses, the Cooperative believes that these licenses qualify as indefinite life intangibles. Radio frequency licenses are tested for impairment annually, or more frequently if events or changes in circumstances indicate that the radio frequency licenses may be impaired.

Cash and Cash Investments

NHEC considers all highly liquid debt instruments with an original maturity of twelve months or less to be cash equivalents, which are reported as cash investments. 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 investments.

Restricted Cash

The Board of Directors has approved and authorized the Company's President/Chief Executive Officer to designate amounts as restricted cash to pay for future storm costs. At December 31, 2017 and 2016, the Cooperative had designated $1,000,000 for future storm costs. At December 31, 2017, the Cooperative also had $2,064,000 as restricted cash related to a bond issuance as discussed in Note 4.

Receivables

Receivables are stated at the amount management expects to collect on outstanding balances. Management provides for probable uncollectible amounts through a charge to earnings and a credit to an allowance for doubtful accounts (allowance) based on its assessment of the collectibility 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 reduction in accounts receivable. Credit may be extended without collateral.

Other receivables include amounts due for goods or services that are not related to delivery of electricity. During 2017, two storms that covered significant portions of NHEC's service territory were declared major disasters by the NH Department of Homeland Security. NHEC is allowed to recover a portion of these storm costs through the Federal Emergency Management Agency (FEMA). At December 31, 2017, NHEC had completed the submission of recoverable costs of approximately $1,4000,000 for the first storm, but has not received approval from FEMA. At December 31, 2017, NHEC has not completed the submission of recoverable costs of approximately $3,100,000 for the second storm. These estimated receivables are included in other receivables in the balance sheet at December 31, 2017.

Materials and Supplies

Inventories of materials and supplies are stated at average cost.

Deferred Debits and Other Assets

NHEC establishes deferred debits for costs associated with the under-recovery of certain tariff rates that are deferred and collected from members through periodic rate adjustments. Deferred debits are regulatory in nature and are approved by either the Board of Directors or the NHPUC. Deferred debits also include amounts related to the National Rural Electric Cooperative Association (NRECA) Retirement Security Program (RS Plan) that are amortized over a defined period established at the inception of the debit. Other assets include amounts related to postretirement benefits.

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 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.

Purchased Power Costs

NHEC's "Co-op Power" energy service rates reflect estimates of the cost of purchased power, including contract power costs, spot market costs, cost of renewable energy credits, capacity costs, cost of ancillary services and related administrative costs. Retail members who purchase their energy from the Cooperative are billed a seasonally levelized power cost recovery charge based on projected data for the cost of wholesale power. NHEC's "Regional Access Charge" rates include estimates of wholesale transmission and distribution interconnection service costs. These rates also reflect estimates of costs associated with services and administration necessary for

members to access energy services from NHEC or competitive suppliers. To the extent that actual costs incurred for a rate period differ from estimates used in setting rates for the period, the differences are deferred and refunded or charged to members in subsequent periods through the periodic rate adjustments as approved by NHEC's Board of Directors in accordance with NH Statutes.

Derivative Instruments

NHEC evaluates purchase power contracts, used to manage power costs over various periods, using guidance issued in FASB ASC 815, *Derivatives and Hedging.* Power contracts that are determined to be derivatives that do not meet the normal purchase and normal sales exclusion of FASB ASC 815, if any, are recorded at fair value. At December 31, 2017 and 2016, the Cooperative determined that all significant power contracts meet the normal purchase and normal sales exclusion and therefore are not recorded at fair value.

Deferred Credits and Other Liabilities

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 postretirement benefits and regulatory liabilities that are amortized over a defined period established at the inception of the credit.

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.

Other Regulated Rates

NHEC's tariff rates 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 NH jurisdictional utilities. The EE SBC recovers the costs of those NHEC energy efficiency program services that are subject to NHPUC approval. The funds collected through NHEC's EAP SBC are reconciled to the benefits provided to NHEC's income qualified members and any under- or over-recovery of benefits paid to members is received from or submitted to, respectively, the State of NH which administers the pooled funds of all jurisdictional utilities.

Income Tax Status

NHEC is exempt from United States income taxes pursuant to Section 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 Cooperative follows guidance for uncertainty in income taxes which is part of FASB ASC 740, *Income Taxes*. The guidance prescribes a recognition threshold and measurement attributes for financial statement recognition of a tax position taken or expected to be taken on a tax return.

Postretirement Benefit Plan

The Cooperative sponsors a defined benefit postretirement medical plan through NRECA that covers substantially all of its employees. The Cooperative applies FASB ASC 715, *Compensation-Retirement Benefits*, that 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 ASC 980, 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.

Subsequent Events

Subsequent events were evaluated through April 4, 2018, which is the date the financial statements were available for issuance, and no subsequent events occurred requiring recognition or disclosure.

2. Investment in Associated Organizations

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

	2017 (000s)	2016 (000s)
Capital term certificates - CFC	**$ 4,005**	$ 4,082
Patronage capital credits - CFC	**7,054**	6,861
Other	**504**	475
Total	**$ 11,563**	$ 11,418

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.

3. Deferred Debits and Other Assets

Deferred debits and other assets at December 31, 2017 and 2016 were as follows:

	2017 (000s)	2016 (000s)
Deferred debits		
Deferred Recoveries (Note 1)	$ 5,859	$ 2,072
Renewable Energy Certificates	127	579
Regulatory asset - Regional Greenhouse Gas Initiative (RGGI)	238	119
RS Plan Prepayment (Note 7)	3,676	4,354
Other assets	162	109
Total	$ 10,062	$ 7,233

4. Long-Term Obligations

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

	2017 (000s)	2016 (000s)
General debt		
2.05% notes payable to CFC, payable in quarterly installments, including interest, through April 2018	$ 735	$ 2,184
3.65% - 6.60% notes payable to CFC, payable in quarterly installments, including interest, through November 2022	8,307	9,724
6.20% notes payable to CFC, payable in monthly installments, including interest, through November 2028	6,524	6,893
3.50% - 5.05% notes payable to CFC, payable in quarterly installments, including interest, through July 2030	10,408	11,013
4.00% - 4.65% notes payable to CFC, payable in quarterly installments, including interest, through January 2034	6,831	7,118
6.20% notes payable to CFC, payable in quarterly installments, including interest, through April 2035	4,935	5,088
6.75% notes payable to CFC, payable in quarterly installments, including interest, through October 2038	6,797	6,940

	2017 **(000s)**	2016 (000s)
4.00% - 5.00% notes payable to CFC, payable in quarterly installments, including interest, through October 2039	**17,517**	17,941
4.20% notes payable to CFC, payable in quarterly installments, including interest, through July 2042	**5,000**	-
4.35% notes payable to CFC, payable in quarterly installments, including interest, through October 2044	**7,615**	7,760
4.10% notes payable to CFC, payable in quarterly installments, including interest, through January 2046	**13,432**	13,681
4.10% notes payable to CFC, payable in quarterly installments, including interest, through April 2048	**4,697**	4,773
Loans under CFC management		
3.99% notes payable to Federal Agricultural Mortgage Corporation (Farmer Mac) payable in semi-annual installments, including interest, through May 2034	**9,400**	9,969
4.09% notes payable to Farmer Mac, payable in semi-annual installments, including interest, through May 2037	**8,160**	8,578
Total long-term obligations	**110,358**	111,662
Less current portion	**6,127**	6,327
Total long-term obligations, excluding current portion	**$ 104,231**	$ 105,335

The mortgage agreements provide that all outstanding obligations to CFC and Farmer Mac 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 $4,645,000 in 2017 and $4,827,000 in 2016.

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 nonfinancial matters. CFC mortgage notes are subject to repricing periodically to reflect current market interest rates.

In March 2017, NHEC received New Clean Renewable Energy Bonds (CREB) Issuance authority from the Department of Treasury for up to $5,300,000 for the construction of a Solar Energy Facility that consists of a 2MW (DC) / 1.75 – 2.15 MW (AC) utility scale solar array. In August 2017, NHEC obtained the bond issuance through a note payable to CFC in the amount of $5,000,000.

In December 2012, NHEC signed an agreement with CFC for a new five-year work plan loan of approximately $50,000,000. In October 2017, NHEC received an extension of the draw period to December 2022. The interest rate will be determined based on the CFC market rate at the time of each advance and principal will be paid over a period not to exceed 40 years through December 18, 2052. The Cooperative has $23,200,000 of remaining availability as of December 31, 2017.

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. CFC will review the need for additional LCTC purchases when needed, at its discretion. Since the Cooperative met its requirement for purchasing LCTCs, the Cooperative has not been required to purchase LCTCs since 2009.

As a cooperative, CFC may pay capital dividends to its borrowers for their patronage. The total capital dividends NHEC received from CFC were $386,000 during 2017 and $373,000 in 2016, of which $193,000 for 2017 and $187,000 for 2016 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 $20,000,000 line of credit from CFC. The amount outstanding at December 31, 2017 was $3,751,434 (interest at 2.75%) and at December 31, 2016 was $292,396 (interest at 2.50%). This line of credit is collateralized in the same manner as the other CFC debt obligations.

The Cooperative has an agreement with National Cooperative Services Corporation for an unsecured revolving line of credit of $20,000,000 through August 2018, with interest based on the seven-day London Interbank Offered Rate plus 190 basis points. There were no outstanding balances at December 31, 2017 or 2016. Management expects to renew this agreement.

Scheduled maturities on long-term obligations for the next five years, based on agreements currently in place, are as follows:

	(000s)
2018	$ 6,127
2019	5,557
2020	5,746
2021	5,935
2022	6,126

5. Long-Term Power Supply and Sale Agreements

NHEC procures wholesale energy, capacity, ancillary services and renewable energy credits (together, “bundled energy service”) from a variety of resources in New England’s deregulated competitive wholesale capacity, energy, ancillary services and renewable attributes markets to meet the needs of its members who elect, or default to, NHEC’s “Co-op Power” bundled energy service option rather than choosing to purchase bundled energy service from retail competitive suppliers.

NHEC’s wholesale procurement arrangements include bilateral purchase agreements of various term lengths, with various suppliers, for various products or combinations of products. The contract terms are from several months up to 20 years. These products may include daily, weekly, monthly, seasonal, or annual, on-peak and off-peak fixed volume or load following energy. Bilateral contract pricing may be fixed or indexed, and indexed contracts may include provisions to allow NHEC the option to swap future period index pricing for a fixed, capped or collared price. NHEC may also meet a portion of its wholesale requirements through contract arrangements tied to the output of specific generating plants or demand resources and may engage in ownership of such resources. NHEC uses competitive bidding and direct negotiation to establish terms, conditions and pricing of its bilateral wholesale procurements. NHEC may participate with other entities in joint or group procurement.

To the extent NHEC’s wholesale requirements are not fully met through bilateral contract arrangements or ownership, they are met through NHEC’s participation in the New England Power Pool markets administered by ISO-New England (ISO-NE), such as the day-ahead and real-time energy markets and the forward capacity market that imposes an obligation on load serving entities to provide or make payments for capacity.

Should a significant number of NHEC's members choose to purchase competitively supplied power instead of purchasing Co-op Power from the Cooperative, NHEC would still have the obligation to purchase the power contracted for bilaterally. Management expects that, if such contracted volumes exceed NHEC's needs, NHEC would then sell any excess contracted power in the marketplace. However, management does not anticipate the likelihood of this happening and if so, would not be long in duration, as the volume of members who do not purchase Co-op Power from the Cooperative has been relatively limited and consistent, and NHEC manages its bilateral procurements taking into account members' use of competitive suppliers as it changes over time.

The Cooperative is subject to New Hampshire Statute RSA Chapter 362 F, an "Electric Renewable Portfolio Standard" (RPS). 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 time. To facilitate the renewable energy production, 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, and provides for final settlement of annual REC obligations by mid-June of the following year. Finally, the law establishes standards for alternative compliance payments (ACP) made by electricity providers in lieu of REC acquisition in certain circumstances. The Cooperative met 98.2% of its total 2016 RPS obligations through unit contracts and REC purchases, and made an ACP payment of $26,522. This ACP payment was due to a shortfall of “Class IV” RECs which are provided by

hydroelectric facilities. The year 2016 was an unusually dry year and less than expected Class IV RECs were produced in the region. NHEC met 89.6% of its Class IV obligation through unit contracts and RECs purchases. Final renewable energy certificate transactions for 2017 are not required to be completed until June 16, 2018, as a function of the relevant RPS rules, but the Cooperative anticipates meeting 100% of its 2017 obligations through unit contracts and REC purchases.

To deliver energy from the New England regional wholesale markets to NHEC's retail distribution network, NHEC purchases Regional Network transmission service through ISO-NE, unbundled Local Network transmission service provided by Eversource Energy (formerly Northeast Utilities), Vermont Electric Power Company, Green Mountain Power and National Grid as well as interconnection and delivery service from Eversource Energy pursuant to FERC regulated contracts and tariffs.

NHEC has a Standard and Poor's Rating A+ issuer credit rating with an outlook of positive. Many of NHEC's power supply contract counterparties rely on NHEC's investment grade rating as primary performance credit support. NHEC has also executed agreements with CFC for the issuance by CFC of letters of credit as primary or back-up collateral for the Cooperative's performance under certain power supply and other agreements. The total authority under these facilities is $30,000,000. As of December 31, 2017 and 2016, letters of credit outstanding under these facilities totaled $4,000,000 and $2,000,000, respectively. Annual fee expenses for issuance of these letters are approximately $135,000 for 2017 and $120,000 for 2016, and are recovered through the Co-op Power rate.

6. Deferred Credits and Other Liabilities

Deferred credits and other liabilities at December 31, 2017 and 2016 were as follows:

	2017 (000s)	2016 (000s)
Deferred credits		
Co-op power and regional access over-recovery (Note 1)	**$ 5,171**	$ 4,610
Regulatory liability - postretirement benefits (Note 8)	**678**	324
Other deferred credits and recoveries	**943**	764
Postretirement obligation (Note 8)	**-**	445
Total	**$ 6,792**	$ 6,143

7. Pension and 401(k) Savings Plan

The RS Plan sponsored by the NRECA is a defined benefit pension plan qualified under Section 401 and tax-exempt under Section 501(a) of the Internal Revenue Code. It is a multi-employer plan under the accounting standards. The plan sponsor's Employee Identification Number is 53-0116145 and the Plan Number is 333. The RS Plan covers all employees, including those employees subject to the provisions of the Cooperative's Collective Bargaining agreements that expire April 30, 2018. Management expects a new agreement to be reached upon expiration.

A unique characteristic of a multi-employer plan compared to a single employer plan is that all plan assets are available to pay benefits of any plan participant. Separate asset accounts are not maintained for participating employers. This means that assets contributed by one employer may be used to provide benefits to employees of other participating employers.

The Cooperative funds accrued pension costs on an annual basis. Pension costs totaled $2,410,000 and $2,320,000 for 2017 and 2016, respectively, which represented less than 5% of the total contributions made to the plan by all participating employers.

For the RS Plan, a "zone status" determination is not required, and therefore not determined, under the Pension Protection Act (PPA) of 2006. In addition, the accumulated benefit obligations and plan assets are not determined or allocated separately by individual employer. In total, the Retirement Security Plan was over 80% funded at January 1, 2017 and 2016 based on the PPA funding target and PPA actuarial value of assets on those dates. Because the provisions of the PPA do not apply to the RS Plan, funding improvement plans and surcharges are not applicable. Future contribution requirements are determined each year as part of the actuarial valuation of the plan and may change as a result of plan experience.

At the December 2012 meeting of the Insurance and Financial Services Committee of the NRECA Board of Directors, the Committee approved an option to allow participating cooperatives in the RS Plan to make a contribution prepayment and reduce future required contributions. The prepayment amount is a cooperative's share, as of January 1, 2013, of future contributions required to fund the RS Plan's unfunded value of benefits earned to date using RS Plan actuarial valuation assumptions. The prepayment amount typically equaled approximately 2.5 times a cooperative's annual RS Plan required contribution as of January 1, 2013. After making the prepayment, for most cooperatives the billing rate was reduced by approximately 25%, retroactive to January 1, 2013. The 25% differential in billing rates is expected to continue for approximately 15 years. However, changes in interest rates, asset returns and other plan experiences different from expected, plan assumption changes and other factors may have an impact on the differential in billing rates and the 15-year period.

In 2013, the Cooperative made a lump-sum prepayment of $6,786,000 to the NRECA RS Plan to reduce future required contributions. The Cooperative is amortizing this amount over ten years. The amount amortized to pension costs was approximately $678,000 for both 2017 and 2016.

The Cooperative has established a tax qualified 401(k) savings plan (Plan) for the benefit of its employees and their beneficiaries. The Cooperative matches contributions of annual base pay for participating employees. In 2017 and 2016, employees who are part of the collective bargaining unit, International Brotherhood of Electrical Workers (IBEW) Local 1837 had a match of up to 2.5%. Warehouse employees who are members of IBEW Local 1837 had a match of up to 2.5% in 2017 and 2016, and employees who participated in the Plan and are not part of the collective bargaining unit had a match of up to 4.5% in 2017 and 2016. The Cooperative's contribution was approximately $534,000 and $533,000 for 2017 and 2016, respectively.

8. 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 2017 and 2016. The Cooperative established an irrevocable trust to fund the plan as was required by the NHPUC. At this time, the Cooperative plans to fund future pay-as-you go expenses (benefits paid) 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.

ASC 715 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. As allowed by ASC 980, the Cooperative reports the accumulated change as a regulatory liability or regulatory asset. ASC 715 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.

The following sets forth the plan's funded status and amounts reported in the Cooperative's financial statements at December 31, 2017 and 2016, and for the years then ended:

	2017 **(000s)**	2016 (000s)
Benefit obligation and funded status		
Benefit obligation at December 31	**$ (1,817)**	$ (2,135)
Fair value of plan assets at December 31	**1,849**	1,690
Funded status of the plans	**$ 32**	$ (445)
Amounts recognized in the balance sheet		
Plan assets included in other assets	**$ 32**	$ -
Plan obligation included in deferred credits and other liabilities	**-**	(445)
Regulatory liability-postretirement benefits	**(678)**	(324)

The regulatory liability-postretirement benefits were comprised of approximately $678,000 and $324,500 of actuarial gains at December 31, 2017 and 2016, respectively. The Cooperative expects to amortize approximately $48,100 of the actuarial gain in the regulatory liability in 2018.

	2017 **(000s)**	2016 (000s)
Benefit cost	**$ 84**	$ 97
Benefits paid	**$124**	$146

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

	2017	2016
Discount rate to determine net periodic benefit costs	**4.55 %**	4.20 %
Discount rate to determine benefit obligation	**4.05 %**	4.55 %
Expected return on plan assets	**4.70 %**	4.70 %

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

	(000s)
2018	$ 131
2019	153
2020	118
2021	138
2022	162
2023 - 2027	777

For measurement purposes, a 7.5% annual rate of increase in the per capita cost of covered healthcare benefits was assumed for 2018. The rate was assumed to decrease gradually to 5.0% by 2027 and remain level thereafter.

Plan Assets

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, 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.

Asset allocation as of December 31 is as follows:

	2017	2016
Bond funds	**57 %**	56 %
Stock funds	**43**	44

Investment Strategy

The Trustees of NHEC's postretirement plan assets meet semi-annually to review the performance of the funds. The overall objective is to maintain a balance of 60% in bond funds and 40% in stock funds with investments in a high quality portfolio which:

- Preserves the principal value of the investment portfolio
- Maintains liquidity to meet anticipated cash flows
- Achieves the best available yields consistent with capital preservation and liquidity requirements
- Avoids inappropriate concentrations of investments through diversification

ASC 820 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. ASC 820 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.

- 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, 2017, Using:	
	2017	**(Level 1)**
	(000s)	**(000s)**
Postretirement plan assets:		
Bond Funds:		
Short-Term Government Securities Fund (a)	**$ 351**	**$ 351**
Short-Term Bond Fund (b)	**707**	**707**
Stock Funds:		
Stock Index Fund (c)	**192**	**192**
Value Fund (d)	**403**	**403**
Small-Company Stock Fund (e)	**120**	**120**
International Value Fund (f)	**76**	**76**
Total	**$ 1,849**	**$ 1,849**

	Fair Value Measurements at December 31, 2016, Using:	
	2016	(Level 1)
	(000s)	(000s)
Postretirement plan assets:		
Bond Funds:		
Short-Term Government Securities Fund (a)	$ 315	$ 315
Short-Term Bond Fund (b)	636	636
Stock Funds:		
Stock Index Fund (c)	194	194
Value Fund (d)	383	383
Small-Company Stock Fund (e)	93	93
International Value Fund (f)	69	69
Total	$ 1,690	$ 1,690

All of the funds listed are managed by NRECA's Homestead Funds Inc.

(a) 80% of the assets in this category are invested in fixed-income securities whose principal and interest payments are guaranteed by the U.S. Government.
(b) At least 80% of assets are invested in the three highest credit categories as ranked by a nationally recognized statistical rating organization – for example, securities rated AAA, AA, and A by Standard & Poor's Corp. (S&P).
(c) This fund invests all of its assets in the S&P 500 Index Master Portfolio.
(d) The Value Fund seeks capital growth over the long term and secondarily, income. Investments are in stocks of established companies.
(e) The Small-Company Fund seeks capital growth over the long term by investing in stocks of small companies that advisors believe are undervalued with market capitalization similar to companies represented by the Russell 2000 Index.
(f) The International Value Fund seeks long-term capital appreciation by investing primarily in equity securities traded principally on markets outside the U.S.

9. 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 are not expected to have a material adverse impact on the financial condition of the Cooperative.