

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**REPORT ON FINANCIAL STATEMENTS**  
**YEARS ENDED DECEMBER 31, 2017 AND 2016**

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**PRESQUE ISLE ELECTRIC & GAS CO-OP  
BOARD OF DIRECTORS  
DECEMBER 31, 2017**

John Brown	Chairperson
Allen Berg	Vice Chairperson
Sandra Borowicz	Secretary
Daryl Peterson	Treasurer
Kurt Krajniak	Director
Raymond Wozniak	Director
Sally Knopf	Director
Charles Arbour	Director
Brentt Lucas	Director

President & Chief Executive Officer

Tom Sobeck



**Independent Auditor's Report**

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

**Report on the Financial Statements**

We have audited the accompanying financial statements of Presque Isle Electric & Gas Co-op as of December 31, 2017 and 2016, which comprises the balance sheet, related statements of income, retained earnings, 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 accounting principles generally accepted in the United States of America; 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 auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free 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 risk 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 Presque Isle Electric & Gas Co-op 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 accounting principles generally accepted in the United States of America.

Traverse City, Michigan  
March 13, 2018

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**BALANCE SHEETS**  
**DECEMBER 31, 2017 AND 2016**

	2017	2016
<b>ASSETS</b>		
UTILITY PLANT:		
In-Service – at cost	\$ 140,239,665	\$ 136,797,878
Construction work in progress	32,344	172,012
SUBTOTAL	140,272,009	136,969,890
Less accumulated depreciation and amortization	63,737,119	60,747,421
NET UTILITY PLANT	76,534,890	76,222,469
OTHER ASSETS AND INVESTMENTS		
Investments on associated organizations	24,644,319	24,733,009
CURRENT ASSETS:		
Cash and temporary cash investments	2,971,080	3,494,617
Accounts Receivable, less allowance for possible losses of \$118,000 in 2017 and 2016.	4,648,383	4,645,458
Materials and supplies (at average cost)	1,460,638	1,508,895
Other current assets	347,401	397,673
TOTAL CURRENT ASSETS	9,427,502	10,046,643
DEFERRED DEBITS	236,795	221,082
TOTAL ASSETS	\$ 110,843,506	\$ 111,223,203

The accompanying notes are an integral part of these statements.

	<u>2017</u>	<u>2016</u>
<b>EQUITIES AND LIABILITIES</b>		
<b>EQUITIES:</b>		
Memberships	\$ 276,930	\$ 268,545
Patronage capital	50,165,119	49,647,759
Other equities	<u>2,836,466</u>	<u>1,234,718</u>
<b>TOTAL EQUITIES</b>	<u>53,278,515</u>	<u>51,151,022</u>
<b>LONG-TERM DEBT, NET OF CURRENT MATURITIES:</b>		
Mortgage notes to National Rural Utilities Cooperative Finance Corporation (CFC)	48,874,610	50,609,285
Accrued post – retirement benefits	<u>1,274,093</u>	<u>2,436,845</u>
<b>TOTAL LONG-TERM DEBT</b>	<u>50,148,703</u>	<u>53,046,130</u>
<b>CURRENT LIABILITIES:</b>		
Current maturities of long-term debt	1,731,000	1,618,000
Accounts payable, purchased energy	2,471,023	2,279,843
Accounts payable, other	847,569	432,531
Patronage capital payable	20,661	18,047
Customer deposits	544,851	533,947
Accrued property taxes	521,015	514,337
Accrued interest	259,442	261,976
Accrued sick and vacation pay	575,134	631,841
Accrued other	<u>416,349</u>	<u>408,634</u>
<b>TOTAL CURRENT LIABILITIES</b>	<u>7,387,044</u>	<u>6,699,156</u>
<b>DEFERRED CREDITS</b>	<u>29,244</u>	<u>326,895</u>
<b>TOTAL EQUITIES AND LIABILITIES</b>	<u>\$ 110,843,506</u>	<u>\$ 111,223,203</u>

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**STATEMENTS OF REVENUE**  
**FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016**

	<u>2017</u>	<u>2016</u>
OPERATING REVENUES	\$ 42,909,614	\$ 43,134,964
OPERATING EXPENSES:		
Cost of energy	24,003,855	24,382,270
Distribution – operation	1,678,316	1,848,171
Distribution – maintenance	3,841,955	3,919,474
Consumers accounts	1,781,925	1,890,613
Customer service and information expense	832,042	672,529
Administrative and general	1,871,995	1,865,636
Depreciation and amortization	3,748,845	3,679,291
Taxes – property	1,136,847	1,123,240
Taxes – other	1,052	1,678
TOTAL OPERATING EXPENSES	<u>38,896,832</u>	<u>39,382,902</u>
OPERATING MARGIN BEFORE FIXED CHARGES	<u>4,012,782</u>	<u>3,752,062</u>
FIXED CHARGES:		
Interest	2,464,041	2,442,927
Other deductions	1,000	220
TOTAL FIXED CHARGES	<u>2,465,041</u>	<u>2,443,147</u>
OPERATING MARGINS AFTER FIXED CHARGES	<u>1,547,741</u>	<u>1,308,915</u>
CAPITAL CREDITS:		
Generation and transmission capital credits	1,340,933	1,908,599
Other capital credits	271,253	257,415
TOTAL CAPITAL CREDITS	<u>1,612,186</u>	<u>2,166,014</u>
NET OPERATING MARGINS	<u>3,159,927</u>	<u>3,474,929</u>

The accompanying notes are an integral part of these statements.

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**STATEMENTS OF REVENUE**  
**FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016**  
**(Continued)**

	2017	2016
NET OPERATING MARGINS (from previous page)	\$ 3,159,927	\$ 3,474,929
NON-OPERATING MARGINS:		
Interest and dividend income	74,105	52,123
Other expenses	(88,479)	(233,530)
TOTAL NON-OPERATING MARGINS	(14,374)	(181,407)
NET MARGINS	\$ 3,145,553	\$ 3,293,522

The accompanying notes are an integral part of these statements.



**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**STATEMENT OF CHANGES IN PATRONAGE CAPITAL**  
**FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016**

	<u>Memberships</u>	<u>Patronage Capital</u>	<u>Other Equities</u>	<u>Accumulated Other Comprehensive Loss</u>	<u>Total</u>
Balance, January 1, 2016	\$ 261,005	\$ 48,581,114	\$ 2,240,981	\$ (1,319,079)	\$ 49,764,021
Capital credits retired		(1,237,688)			(1,237,688)
Memberships retired	7,540				7,540
Other equity transactions		(989,189)	312,816		(676,373)
Net margin		<u>3,293,522</u>			<u>3,293,522</u>
Balance, December 31, 2016	268,545	49,647,759	2,553,797	(1,319,079)	51,151,022
Capital credits retired		(2,628,193)			(2,628,193)
Memberships issued (retired)	8,385				8,385
Other equity transactions			535,751	1,065,997	1,601,748
Net margin		<u>3,145,553</u>			<u>3,145,553</u>
Balance, December 31, 2017	<u>\$ 276,930</u>	<u>\$ 50,165,119</u>	<u>\$ 3,089,548</u>	<u>\$ (253,082)</u>	<u>\$ 53,278,515</u>

The accompanying notes are an integral part of these statements.

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016**

	2017	2016
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Cash received from consumers	\$ 42,955,756	\$ 43,064,510
Cash paid to suppliers and employees	(34,458,481)	(34,323,485)
Interest received	74,105	52,123
Interest paid	(2,467,575)	(2,444,196)
Taxes paid	(1,103,791)	(1,095,749)
	<u>5,000,014</u>	<u>5,253,203</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Construction and acquisition of plant	(4,346,202)	(3,862,090)
(Increase) decrease in:		
Material inventory	48,257	(69,711)
Investments – associated organizations	1,700,876	1,882,834
	<u>(2,597,069)</u>	<u>(2,048,967)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Payment of debt	(1,621,675)	(1,500,368)
Advances of long term debt	-	5,600,000
Payments on line of credit - net	-	(5,000,000)
Memberships issued	8,385	7,540
Patronage capital retired	(2,628,193)	(1,237,688)
Adjustment to pension benefit obligation	1,065,997	-
Increased (decrease) in:		
Consumer deposits	10,904	9,754
Deferred credits	(297,651)	67,079
Other equities	535,751	312,816
	<u>(2,926,482)</u>	<u>(1,740,867)</u>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>(523,537)</b>	<b>1,463,369</b>
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<b>3,494,617</b>	<b>2,031,248</b>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<b>\$ 2,971,080</b>	<b>\$ 3,494,617</b>

The accompanying notes are an integral part of these statements.

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**STATEMENTS OF CASH FLOWS**  
**FOR THE YEARS ENDED DECEMBER 31, 2017 AND 2016**  
**(Continued)**

	2017	2016
RECONCILIATION OF NET MARGINS TO NET CASH PROVIDED BY OPERATING ACTIVITIES:		
Net Margins	\$ 3,145,553	\$ 3,293,522
Adjustments to reconcile net margins to net cash provided by Operating activities:		
Depreciation and amortization	3,931,664	3,838,364
(Gain) loss on disposition of assets	102,117	244,339
G&T and other capital credits	(1,612,186)	(2,166,014)
(Increase) decrease in:		
Customer and other accounts receivable	(2,925)	(95,403)
Other current assets	50,272	54,470
Deferred debits	(15,713)	30,928
Increase (decrease) in:		
Accounts payable	608,832	29,787
Accrued property taxes	6,678	19,896
Accrued interest payable	(2,534)	(1,049)
Current and accrued liabilities – other	(48,992)	(71,519)
Accrued post retirement benefits	(1,162,752)	75,882
Total Adjustments	1,854,461	1,959,681
NET CASH PROVIDED BY OPERATING ACTIVITIES	\$ 5,000,014	\$ 5,253,203
NON-CASH ITEMS – INVESTING & FINANCING		
Capital credits from associated organizations	\$ 1,612,186	\$ 2,166,014

The accompanying notes are an integral part of these statements.

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**NOTES TO FINANCIAL STATEMENTS**

**NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

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

Nature of Operations

Presque Isle Electric & Gas Co-op (Presque Isle) is a member-owned, not-for-profit corporation whose purpose is to provide retail energy services to its members. As a cooperative, all monies in excess of cost of providing electric service are capital, at the moment of receipt, and are credited to each member's capital account.

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

Utility Plant

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

Investments

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

Cash

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

Member Energy Prepayments and Unbilled Revenues

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

Accounts receivable

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

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**NOTES TO FINANCIAL STATEMENTS**

**NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued**

Regulation

Electric accounting and rate matters are subject to the Board of Directors and membership approval. Natural gas accounting and rate matters are either subject to Home Rule approval pursuant to the Michigan Home Rule Statute or subject to the approval of the Michigan Public Service Commission.

Materials and Supplies

Electrical and natural gas materials and supplies are valued at average cost. Merchandise held for resale is valued at average cost.

Retirement Plan

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

Contributions in Aid of Construction

Contributions in aid of construction are received from members on electrical and gas service requests and re-applied against the construction costs.

Income Taxes

The Cooperative is exempt from federal and state income taxes under Section 501(c)(12) of the Internal Revenue Code which provides, in part that the Cooperative derive at least 85 percent of its annual gross income from members to retain the exemption. The Cooperative expects to meet the requirements for the tax year ended December 31, 2017. Accordingly, no provision for income taxes has been made in the financial statements. The Cooperative's federal information returns for Calendar year 2011 and after are subject to examination by the Internal Revenue Service.

**NOTE 2: ASSETS PLEDGED**

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

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**NOTES TO FINANCIAL STATEMENTS**

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

Major classes of electric and gas plant as of December 31, 2017 and 2016 consisted of:

	2017	2016
Intangible plant	\$ 1,021,015	\$ 1,021,015
Distribution plant	129,447,361	127,183,640
General plant	9,771,289	8,593,222
	140,239,665	136,797,878
Construction work in progress	32,344	172,012
<b>TOTAL</b>	<b>\$ 140,272,009</b>	<b>\$ 136,969,890</b>

**NOTE 4: ELECTRIC AND GAS PLANT AND DEPRECIATION RATES AND PROCEDURES**

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

General plant depreciation rates have been applied on a straight-line basis as follows for the year ended December 31, 2017:

	Years
Structures and improvements	10-50
Office furniture equipment	1.5-7
Transportation equipment	4-7
Power operated equipment	3-16
Other	4-5

Depreciation and amortization of electric and gas plant in service was charged as follows for the years ended December 31, 2017 and 2016:

	2017	2016
Charged to:		
Classified as depreciation and amortization	\$ 3,748,845	\$ 3,679,291
Classified in other operating expenses	182,819	159,073
	3,931,664	3,838,364
Charged to construction	246,716	211,825
<b>TOTAL DEPRECIATION AND AMORTIZATION</b>	<b>\$ 4,178,380</b>	<b>\$ 4,050,189</b>

**PRESQUE ISLE ELECTRIC & GAS CO-OP  
NOTES TO FINANCIAL STATEMENTS**

**NOTE 5: INVESTMENTS IN ASSOCIATED ORGANIZATIONS**

Investments in associated organizations consisted of the following at December 31, 2017 and 2016:

	2017	2016
Wolverine Power Supply Coop. Inc. - capital credits	\$ 20,486,928	\$ 20,649,114
National Rural Utilities Cooperative Finance Corp.:		
Capital term certificates maturing October 1, 2020 through October 1, 2080 at interest rates between 3% and 5.0%	1,521,664	1,542,010
Patronage capital certificates	1,989,899	1,889,412
Other	645,828	652,473
 TOTAL	 \$ 24,644,319	 \$ 24,733,009

In 2016, Wolverine Power Supply Coop, Inc. restated its balance sheet for changes to methods of depreciation, the effect of this change was a reduction of the investment by \$989,189, this change is reflected as an equity transaction for 2016.

**NOTE 6: CASH AND INVESTMENTS**

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

	Per Institution	Per Book
Insured	\$ 1,065,104	\$ 1,065,104
Uninsured	1,930,960	1,904,476
Cash in banks and credit union	\$ 2,996,064	2,969,580
Working funds		1,500
Total per books		\$ 2,971,080

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**NOTES TO FINANCIAL STATEMENTS**

**NOTE 7: DEFERRED DEBITS**

The Cooperative has recorded deferred debits in the following amounts:

	<u>2017</u>	<u>2016</u>
Prepaid tap fees	\$ 55,386	\$ 57,382
Prepaid years of service	75,113	104,045
Other deferred debits	59,655	59,655
Consumer prepayments	<u>46,641</u>	<u>-</u>
<b>TOTAL</b>	<b><u>\$ 236,795</u></b>	<b><u>\$ 221,082</u></b>

**NOTE 8: MEMBERSHIPS**

The following is a summary of changes in memberships for the years ended December 31, 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Balance, beginning	\$ 268,545	\$ 261,005
Membership and subscriptions issued	<u>8,385</u>	<u>7,540</u>
<b>Balance, ending</b>	<b><u>\$ 276,930</u></b>	<b><u>\$ 268,545</u></b>

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

**NOTE 9: PATRONAGE CAPITAL**

Patronage capital balances as of December 31, 2017 and 2016 consisted of:

	<u>2017</u>	<u>2016</u>
Assignable	\$ 3,145,553	\$ 3,293,522
Adjustment-WPSC prior depreciation	-	(989,189)
Assigned to date	<u>61,860,704</u>	<u>59,556,371</u>
	65,006,257	61,860,704
Less retirements to date	<u>14,841,138</u>	<u>12,212,945</u>
<b>Balance</b>	<b><u>\$ 50,165,119</u></b>	<b><u>\$ 49,647,759</u></b>



**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**NOTES TO FINANCIAL STATEMENTS**

**NOTE 9: PATRONAGE CAPITAL - continued**

Under the provisions of the Mortgage Agreement, until the equities and margins equal or exceed twenty percent of the total assets of the Cooperative, the return to patrons of capital contributed by them is limited generally to twenty-five percent of the patronage capital or margins received by the Cooperative in the next preceding year. The equities and margins of Presque Isle represent 48.0% and 45.9% of the total assets for the years 2017 and 2016, respectively. There were capital credits retired of \$2,628,193 and \$1,237,688 during 2017 and 2016, respectively.

**NOTE 10: MORTGAGE NOTES**

Long-term debt is composed of 2.75 percent to 6.45 percent mortgage notes payable to the National Rural Utilities Cooperative Finance Corporation (CFC). All mortgage notes to CFC will be re-priced and the interest rate adjusted accordingly during the next 10 years in accordance with the policy and procedure governing such re-pricing. The notes are for 35 year periods each, with principal and interest installments due either quarterly or semiannually. The notes are scheduled to be fully repaid at various times from December, 2020 through November 2047.

There were unadvanced loan funds available at December 31, 2017 in the amount of \$9,900,000.

Detail of the long-term debt is as follows:

	<u>2017</u>	<u>2016</u>
National Rural Utilities Cooperative Finance Corporation mortgage notes bearing interest at 3.65% to 6.45% per annum for 2017 and 2016	\$ 50,605,610	\$ 52,227,285
	50,605,610	52,227,285
Less current maturities	<u>1,731,000</u>	<u>1,618,000</u>
<b>TOTAL LONG-TERM DEBT</b>	<u>\$ 48,874,610</u>	<u>\$ 50,609,285</u>

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

2018	\$	1,731,000
2019	\$	1,813,379
2020	\$	1,901,123
2021	\$	1,904,419
2022	\$	1,996,411

**PRESQUE ISLE ELECTRIC & GAS CO-OP  
NOTES TO FINANCIAL STATEMENTS**

**NOTE 11: LINE OF CREDIT**

Presque Isle had available a short-term line of credit from CFC for 2017 and 2016 of \$8,000,000, with a revolving credit and term of sixty months. The agreement requires that within 360 days of the first advance, the cooperative will reduce to zero for a period of at least five consecutive business days amounts outstanding. The Cooperative was in compliance with this provision during 2017 and 2016. Balance available at December 31, 2017 and 2016 was \$8,000,000. The outstanding balance at December 31, 2017 and 2016 was \$-0-.

Additionally, Presque Isle has a \$6,000,000 unsecured revolving line-of-credit agreement with CoBank. Interest on outstanding borrowings is payable monthly and is computed at 5.0% at December 31, 2017. Presque Isle had an outstanding balance of \$0 at December 31, 2017 and 2016.

**NOTE 12: DEFERRED CREDITS**

Following is a summary of the amounts recorded as deferred credits as of December 31, 2017 and 2016:

	2017	2016
Under-collection of 2016 WPSC PSCR Costs	\$ 29,244	\$ 281,835
Customer energy prepayments	-	45,060
<b>TOTAL</b>	<b>\$ 29,244</b>	<b>\$ 326,895</b>

**NOTE 13: RETIREMENT PLAN**

Retirement plan benefits for substantially all employees are provided through participation in a defined contribution SelectRE pension plan with 401k option with cash and deferred arrangement of the National Rural Electric Cooperative Association (NRECA) and its member systems. The income earned by funds while held under the plan is tax-exempt under Code Sections 401 and 501 of the Internal Revenue Code. Contributions to the savings program, which are based on a percentage of the employees' compensation, were \$515,800 in 2017 and \$437,149 in 2016.

**NOTE 14: POWER SUPPLY COST RECOVERY CLAUSE**

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

Wolverine Power Supply Cooperative, Inc. (Wolverine) and the member-distribution Cooperatives including Presque Isle, obtained authority to implement and apply PSCR clauses and monthly factors. Presque Isle's monthly factor may not exceed -1.31 mills per KWH for the current period.

**PRESQUE ISLE ELECTRIC & GAS CO-OP  
NOTES TO FINANCIAL STATEMENTS**

**NOTE 14: POWER SUPPLY COST RECOVERY CLAUSE - continued**

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

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

Presque Isle's balance sheets reflect an amount (due to)/from member-consumers for under/(over) collections in the amounts of \$(191,698) and \$67,491 at December 31, 2017 and 2016, respectively. These amounts are included in the accounts receivable balance.

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

The GCR mechanism includes provisions whereby gas cost recovery over-collections must be remedied by refunds and gas cost recovery under-collections must be remedied by additional collections. Presque Isle's balance sheet reflects an amount due (to)/from member-consumers for under collections in the amounts of \$80,306 and \$140,152 for the years ended December 31, 2017 and 2016, respectively. This amount is recorded in accounts receivable.

**NOTE 15: POST-RETIREMENT BENEFITS OTHER THAN PENSIONS**

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

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

At the end of 2017 there were no active participants and the accounting rules of the Financial Accounting Standards Board Statement No. 88 regarding curtailment must be recognized. The reconciliation of the funded status at December 31, 2017 is as follows:

**PRESQUE ISLE ELECTRIC & GAS CO-OP  
NOTES TO FINANCIAL STATEMENTS**

**NOTE 15: POST-RETIREMENT BENEFITS OTHER THAN PENSIONS - continued**

	2017	2016
(Accrued) post-retirement benefit costs, beginning	\$ (2,436,845)	\$ (2,360,963)
Net periodic post-retirement benefit (costs)	(47,967)	(183,835)
Contributions made	118,914	107,953
Valuation adjustment	1,091,805	-
(Accrued) post-retirement benefit cost, end of year	\$ (1,274,093)	\$ (2,436,845)

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

	2017	2016
Interest cost	\$ (37,692)	\$ 88,006
Net actuarial gain (loss)	(10,275)	95,829
	\$ (47,967)	\$ 183,835

For measurement purposes a 8.0% annual rate of increase in the per capita cost of covered health care benefits was assumed for 2017; the rate was assumed to decrease gradually to an ultimate rate of 5.0% per annum. The health care cost trend rate assumption has a significant effect on the amounts reported. To illustrate, increasing the assumed health care cost trend rates by 1 percentage point in each year would increase the accumulated post-retirement benefit obligation \$89,913. Decreasing the assumed health care cost trend rates by 1 percentage point in each year would decrease the accumulated post-retirement benefit obligation \$72,499.

The weighted-average discount rate used in determining the accumulated post-retirement benefit obligation was 3.08 percent.

**NOTE 16: FLEX BENEFIT PLAN - under Section 125 of the Internal Revenue Code**

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

**PRESQUE ISLE ELECTRIC & GAS CO-OP**  
**NOTES TO FINANCIAL STATEMENTS**

**NOTE 17: LETTERS OF CREDIT**

The Co-op has a letter of credit outstanding to CFC for \$1,500,000 at December 31, 2017. This letter of credit is required in order to mitigate counter party risk in natural gas purchase transactions. This also is a risk management tool for the Co-op with respect to mark to market issues.

**NOTE 18: RECLASSIFICATION OF AMOUNTS**

Certain amounts previously reported have been reclassified to conform to the 2017 presentation.

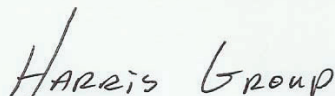
**NOTE 19: SUBSEQUENT EVENTS**

In preparing these financial statements, management has evaluated, for potential recognition or disclosure, significant events or transactions that occurred during the period subsequent to December 31, 2017, the most recent statement of financial position presented herein, through March 13, 2018, the issuance date of the accompanying financial statements. No significant such events or transactions were identified.



### AUDITORS' CERTIFICATION REGARDING LOAN FUND EXPENDITURES

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

A handwritten signature in dark ink that reads 'HARRIS GROUP' in a cursive, slightly slanted font.

Certified Public Accountants  
March 13, 2018