

**POLK-BURNETT ELECTRIC COOPERATIVE
AND SUBSIDIARIES
CENTURIA, WI
CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009**

**and
REPORT OF INDEPENDENT
CERTIFIED PUBLIC ACCOUNTANTS**

**POLK-BURNETT ELECTRIC COOPERATIVE AND SUBSIDIARIES
CENTURIA, WISCONSIN**

CONTENTS

	<u>Page</u>
Report of Independent Certified Public Accountants	1
Financial Statements:	
Consolidated Balance Sheets	2
Consolidated Statements of Operations	3
Consolidated Statements of Members' Equity	4
Consolidated Statements of Cash Flows	5 – 6
Notes to Consolidated Financial Statements	7 – 23

Report of Independent Certified Public Accountants

Board of Directors
Polk-Burnett Electric Cooperative
Centuria, WI 54824-9020

We have audited the accompanying consolidated balance sheets of Polk-Burnett Electric Cooperative and Subsidiaries as of December 31, 2010 and 2009, and the related consolidated statements of operations, members' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Cooperative's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control over financial reporting. Accordingly, we express no such opinion. 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 consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Polk-Burnett Electric Cooperative and Subsidiaries as of December 31, 2010 and 2009 and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Bauman Associates, Ltd.

CERTIFIED PUBLIC ACCOUNTANTS

Eau Claire, Wisconsin
February 17, 2011

POLK-BURNETT ELECTRIC COOPERATIVE
CONSOLIDATED BALANCE SHEETS
December 31, 2010 and 2009

<u>ASSETS</u>	<u>2010</u>	<u>2009</u>
PLANT, PROPERTY, AND EQUIPMENT:		
Plant	\$ 76,783,190	\$ 74,117,440
Construction work in progress	883,758	940,590
Total	<u>77,666,948</u>	<u>75,058,030</u>
Less accumulated depreciation	<u>18,679,493</u>	<u>16,410,327</u>
Net plant, property, and equipment	<u>58,987,455</u>	<u>58,647,703</u>
INVESTMENTS:		
Investments in associated cooperatives	9,354,322	8,767,634
Other investments	19,868	17,948
Total investments	<u>9,374,190</u>	<u>8,785,582</u>
CURRENT ASSETS:		
Cash and cash equivalents	4,700,603	2,549,148
Accounts receivable (less accumulated provision for uncollectible accounts of \$82,999 in 2010 and \$82,454 in 2009)	2,756,333	1,999,890
Materials and supplies	800,832	787,863
Prepayments - other	790,763	1,660,511
Total current assets	<u>9,048,531</u>	<u>6,997,412</u>
DEFERRED DEBITS	<u>113,730</u>	<u>169,376</u>
DISCONTINUED OPERATION ASSETS	<u>-</u>	<u>162,000</u>
TOTAL ASSETS	<u>\$ 77,523,906</u>	<u>\$ 74,762,073</u>

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

<u>EQUITIES AND LIABILITIES</u>	<u>2010</u>	<u>2009</u>
EQUITIES:		
Patronage capital	\$ 26,048,785	\$ 24,943,396
Other equities	1,600,347	1,695,139
Total equities	<u>27,649,132</u>	<u>26,638,535</u>
LONG-TERM DEBT	<u>41,269,791</u>	<u>40,167,138</u>
CURRENT LIABILITIES:		
Current portion of long-term debt	256,664	433,769
Accounts payable	520,455	420,729
Accounts payable - billed power costs	1,757,023	1,704,659
Propane customer deposits	2,112,491	1,875,817
Other current liabilities	2,295,653	2,181,789
Total current liabilities	<u>6,942,286</u>	<u>6,616,763</u>
DEFERRED CREDITS	<u>1,662,697</u>	<u>1,339,916</u>
DISCONTINUED OPERATION LIABILITIES	<u>-</u>	<u>(279)</u>
TOTAL EQUITIES AND LIABILITIES	<u>\$ 77,523,906</u>	<u>\$ 74,762,073</u>

POLK-BURNETT ELECTRIC COOPERATIVE
CONSOLIDATED STATEMENTS OF OPERATIONS
Years Ended December 31, 2010 and 2009

	2010	2009
OPERATING REVENUES	\$ 35,395,986	\$ 34,894,543
LESS COST OF GOODS SOLD	19,474,615	20,413,547
GROSS MARGINS	15,921,371	14,480,996
OPERATING EXPENSES:		
Operations	1,752,028	1,862,981
Maintenance	2,337,693	2,361,980
Customer accounts	745,856	647,751
Customer service and information	466,006	256,418
Sales	52,422	60,845
Administrative and general	3,694,050	3,367,614
Depreciation	3,120,420	2,213,583
Other	486,058	433,773
Total operating expenses	12,654,533	11,204,945
OPERATING MARGINS BEFORE CAPITAL CREDITS	3,266,838	3,276,051
CAPITAL CREDITS FROM OTHER COOPERATIVES	824,809	693,261
OPERATING MARGINS	4,091,647	3,969,312
NON-OPERATING MARGINS:		
Interest income	82,103	86,274
Finance charges	7,933	7,282
Other non-operating income (expense)	4,598	24,283
Total non-operating margins	94,634	117,839
MARGINS BEFORE INTEREST AND INCOME TAX	4,186,281	4,087,151
INTEREST EXPENSE	2,381,638	2,337,685
INCOME TAX EXPENSE (BENEFIT)	12,889	(90,656)
INCOME FROM CONTINUING OPERATIONS	1,791,754	1,840,122
DISCONTINUED OPERATIONS:		
Income (loss) from operations of the discontinued segment	(5,553)	(104,597)
Income tax (expense) benefit	(172,000)	172,448
NET MARGINS	\$ 1,614,201	\$ 1,907,973

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

POLK-BURNETT ELECTRIC COOPERATIVE
CONSOLIDATED STATEMENTS OF MEMBERS' EQUITY
Years Ended December 31, 2010 and 2009

	<u>Patronage Capital</u>	<u>Accumulated Unallocated Non-operating Margins</u>	<u>Other Equities</u>	<u>Accumulated Margins of Subsidiaries</u>	<u>Total</u>
Balance, December 31, 2008	\$ 23,691,359	\$ (115,607)	\$ 297,577	\$ 1,395,887	\$ 25,269,216
Unallocated 2008 margins	(133,055)	133,055	-	-	-
Net margins (losses)	1,951,121	-	-	(43,148)	1,907,973
Retirement of capital credits	<u>(566,029)</u>	<u>-</u>	<u>27,375</u>	<u>-</u>	<u>(538,654)</u>
Balance, December 31, 2009	24,943,396	17,448	324,952	1,352,739	26,638,535
Unallocated 2009 margins	(84,738)	84,738	-	-	-
Net margins (losses)	1,816,128	-	-	(201,927)	1,614,201
Retirement of capital credits	<u>(626,001)</u>	<u>-</u>	<u>22,397</u>	<u>-</u>	<u>(603,604)</u>
Balance, December 31, 2010	<u>\$ 26,048,785</u>	<u>\$ 102,186</u>	<u>\$ 347,349</u>	<u>\$ 1,150,812</u>	<u>\$ 27,649,132</u>

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

POLK-BURNETT ELECTRIC COOPERATIVE
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2010 and 2009

	2010	2009
CASH FLOWS FROM CONTINUING OPERATIONS		
CASH FLOWS FROM OPERATING ACTIVITIES:		
Income from continuing operations	\$ 1,791,754	\$ 1,840,122
Adjustments to reconcile income from continuing operations to net cash provided by (used in) operating activities:		
Depreciation	3,412,778	2,482,954
Amortization of debt conversion fees	(40,684)	(40,684)
Non-cash portion of patronage capital received	(824,809)	(693,261)
Loss (gain) on asset disposal	(6,698)	(37,506)
Change in assets and liabilities:		
Decrease (increase) in accounts receivable	(756,443)	322,499
Decrease (increase) in materials and supplies	(12,969)	93,396
Decrease (increase) in other current assets	1,031,748	823,709
Increase (decrease) in deferred debits	55,646	54,906
Increase (decrease) in accounts payable	152,090	169,329
Increase (decrease) in propane customer deposits	236,674	(924,710)
Increase (decrease) in other current liabilities	113,864	1,718
Increase (decrease) in deferred credits	290,781	(102,893)
Increase (decrease) in deferred taxes	32,000	32,000
Net cash provided by (used in) operating activities	5,475,732	4,021,579
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from sale of property and equipment	87,901	31,687
Extension and replacement of plant	(4,547,350)	(5,193,692)
Contributions in aid of construction	713,617	683,342
Purchase of investments	(27,375)	(171,500)
Proceeds from investments	263,576	247,458
Net cash provided by (used in) investing activities	(3,509,631)	(4,402,705)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from long-term debt	2,950,000	-
Principal payments on long-term debt	(533,768)	(695,768)
Net borrowings (payments) on line of credit	(1,450,000)	700,000
Retirements of patronage capital, net of gain	(603,604)	(538,654)
Net cash provided by (used in) financing activities	362,628	(534,422)
Net increase (decrease) in cash and cash equivalents from continuing operations	2,328,729	(915,548)

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

POLK-BURNETT ELECTRIC COOPERATIVE
CONSOLIDATED STATEMENTS OF CASH FLOWS
Years Ended December 31, 2010 and 2009

	2010	2009
CASH FLOWS FROM DISCONTINUED OPERATIONS		
CASH FLOWS FROM OPERATING ACTIVITIES:		
Income from discontinued operations	\$ (177,553)	\$ 67,851
Adjustments to reconcile income from discontinued operations to net cash provided by (used in) operating activities:		
Depreciation	-	7,184
Loss (gain) on asset disposal	-	87,782
Change in assets and liabilities:		
Decrease (increase) in accounts receivable	-	519,550
Decrease (increase) in income tax receivable	-	(162,000)
Increase (decrease) in accounts payable	-	13,508
Increase (decrease) in income tax payable	-	(755,000)
Increase (decrease) in other current liabilities	279	(1,182)
Net cash provided by (used in) operating activities	(177,274)	(222,307)
Net increase (decrease) in cash and cash equivalents from discontinued operations	(177,274)	(222,307)
Total increase (decrease) in cash and cash equivalents	2,151,455	(1,137,855)
Cash and cash equivalents at beginning	2,549,148	3,687,003
Cash and cash equivalents at end	\$ 4,700,603	\$ 2,549,148
Supplemental disclosure of cash flow information:		
Cash payments during the year for:		
Interest paid	\$ 2,409,233	\$ 2,346,628
Income tax paid (received)	\$ (157,111)	\$ 694,937
Supplemental disclosure of non-cash investing and financing activities:		
The Cooperative and its subsidiaries record patronage capital allocations from associated organizations as revenue and as investments in associated organizations as follows:		
Patronage capital allocations	\$ 824,809	\$ 693,261

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

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1 NATURE OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Organization and Business

Polk-Burnett Electric Cooperative's (the Cooperative) principal line of business is providing electric service to residential and business customers residing in six rural counties in west central Wisconsin. The Cooperative, through its subsidiaries, sells propane and installed and monitored security systems through 2008 (see Note 13). Electric rates charged to customers are established by the Board of Directors.

Financial Statement Presentation

As a member-elected Board of Director regulated entity, the Cooperative accounts for the financial effects of regulation in accordance with the Financial Accounting Standards Board Accounting Standards Codification (FASB ASC). This statement allows for the recording of a regulatory assets or liability for amounts that will be collected or refunded through the rate-making process in the future. In accordance with regulatory treatment, the Cooperative deferred a debt redemption gain and amortizes such gain over the life of the new debt. The accounting policies followed by the Cooperative are subject to the Federal Energy Regulatory Commission's Uniform System of Accounts prescribed for Class A and B Electric Utilities. The accounting policies conform to accounting principles generally accepted in the United States of America as applied in the case of regulated electric utilities. The Cooperative uses the accrual method of accounting.

Principles of Consolidation

The consolidated financial statements include the accounts of Polk-Burnett Diversified Services, Inc. and its subsidiaries Polk-Burnett Propane Services, Inc. and Northwestern Wisconsin Security, Inc., as well as its affiliate Polk-Burnett Economic Development Corporation. All material intercompany transactions and accounts have been eliminated.

Concentrations of Credit Risk

Financial instruments which potentially subject the Cooperative to concentrations of credit risk consist principally of cash equivalents, accounts receivable and notes receivable. The Cooperative places its cash deposits and cash investment with high credit quality financial institutions and, by policy, generally limits the amount of credit exposure to any one financial institution. Concentrations of credit risk with respect to accounts receivable are limited due to the Cooperative's large number of customers. The Cooperative believes it is not exposed to any significant credit risks.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1 NATURE OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Use of Estimates

The presentation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant estimates in the financial statements are plant useful lives, self-funded medical insurance reserve, allowance for uncollectible accounts and deferred income tax allowances. Actual results could differ from those estimates.

Investments in Associated Cooperatives

Investments in associated cooperatives are recorded at cost plus undistributed allocated equities from other cooperatives. Patronage allocations are recognized in the year the allocation pertains to and are redeemable only at the option of the issuing cooperative.

Other Investments

Other investments are recorded at cost, which approximates fair market value.

General

The Cooperative maintains its books in conformance with the Uniform System of Accounts prescribed by the Rural Development Utilities Program (RDUP).

Cash and Cash Equivalents

The Cooperative considers all highly liquid cash instruments with a maturity of three months or less when purchased to be cash equivalents. Cash equivalents are stated at cost, which approximates fair market value.

Accounts Receivable

Receivables are stated at the amount the Cooperative expects to collect from outstanding balances. The Cooperative provides for probable uncollectible amounts through a charge to earnings and a credit to a valuation allowance based on its assessment of the current status of individual accounts. Balances that are still outstanding after the Cooperative has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to the receivable accounts. Changes in the valuation allowance have not been material to the financial statements.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1 NATURE OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Inventories

Electric materials and supplies are recorded at average unit cost and propane inventory is recorded at the lower of average unit cost or market. Balances as of December 31, 2010 and 2009 are:

	<u>2010</u>	<u>2009</u>
Electric materials and supplies	\$ 568,184	\$ 590,626
Propane inventory	<u>232,648</u>	<u>197,237</u>
Total	<u>\$ 800,832</u>	<u>\$ 787,863</u>

Plant, Maintenance and Depreciation

Plant, property, and equipment are recorded at cost. The cost of additions includes contracted work, direct labor, materials and allocable overheads. When units of property are retired, sold or otherwise disposed of in the ordinary course of business, their average book cost, less net salvage, is charged to accumulated depreciation. Included in accumulated depreciation are non-legal costs of removing plant. Repairs and the replacement and renewal of items determined to be less than units of property are charged to maintenance. Any gains or losses on utility and non-utility plant and equipment using individual unit depreciation are reflected in operations. Depreciation for electric distribution plant is computed on the straight-line composite rate method which expenses the cost of plant over their estimated useful lives. General plant depreciation rates have been applied on a straight-line unit basis which expenses the cost of plant over their estimated useful lives. Depreciation rates are adopted by the Board of Directors.

Asset Retirement Obligation

The FASB ASC requires entities to record the fair value of a liability for legal obligations associated with an asset retirement in the period in which the obligations are incurred. When the liability is initially recorded, the entity capitalizes the cost of the asset retirement obligation by increasing the carrying amount of the related long-lived asset. Over time, the liability is accrued to its present value each period, and the capitalized cost is depreciated over the useful life of the related asset. The Cooperative has determined it does not have a material legal obligation to remove long-lived assets as described by the FASB ASC, and accordingly has not recognized any asset retirement obligation costs in its financial statements for the years ended December 31, 2010 and 2009.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1 NATURE OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Long-Lived Assets

Long-lived assets to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the related carrying amount may not be recoverable. When required, impairment losses on assets to be held and used are recognized based on the fair value of the asset. Long-lived assets to be disposed of are reported at the lower of carrying amount or their fair value less cost to sell.

Patronage Capital

Amounts received from the furnishing of electric energy in excess of operating costs and expenses are assigned to patrons on a patronage basis. Certain amounts received by the Cooperative from its other operations in excess of costs and expenses are allocated to its patrons on a patronage basis to the extent they are not needed to offset current or prior deficits. Dividends paid from the Cooperative's subsidiaries may be allocated to electric patrons on a patronage basis.

Revenue Recognition

Revenues are recognized based on products and services provided to customers each month. Electric customer meters are read and billed on a cycle basis, and electric revenue is recorded for services provided from the monthly meter-reading dates to month-end. Any revenue between meter-reading dates and month-end is immaterial. The related power costs are recorded to the month-end.

Self-funded Health Insurance

The Cooperative has a self-funded health insurance plan which provides medical payments to employees and their dependents that are not covered by the high deductible insurance plan. The health care expense is based on actual claims paid, reinsurance premiums, administrative fees and unpaid claims at year end. All health care costs are expensed as incurred.

Advertising Costs

Advertising costs are expensed as incurred. Advertising expenses were \$48,429 and \$59,369 for the years ended December 31, 2010 and 2009, respectively.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 1 NATURE OF BUSINESS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes

The Cooperative has been granted tax exempt status by the Internal Revenue Service and the State of Wisconsin.

The Cooperative adopted Financial Accounting Standards Board (FASB) ASC 740, *Accounting for Uncertainty in Income Taxes* on January 1, 2009. The Cooperative will recognize any accrued interest and penalties related to unrecognized benefits in income tax, if incurred. The Cooperative's previous 3 tax years are open for examination by the Internal Revenue Service.

Polk-Burnett Diversified Services, Inc. and its subsidiaries Polk-Burnett Propane Services, Inc. and Northwestern Wisconsin Security, Inc. and Polk-Burnett Economic Development Corporation are taxable at the federal and state level, and a provision for income taxes is included in the financial statements. A deferred tax liability for Polk-Burnett Propane Services, Inc. is recorded for future tax consequences attributable to temporary differences between financial statement carrying amounts of assets and liabilities and their respective tax bases. Principally these differences relate to depreciation of property and equipment and operating loss carryforwards.

Derivative Instruments and Hedging Activities

The Cooperative's policy is to not use freestanding derivatives and to not enter into contracts with terms that cannot be designated as normal purchases or sales. Management has determined that the Cooperative has no freestanding or embedded derivatives.

Date of Management Review

In preparing these financial statement, the Company has evaluated events and transactions for potential recognition or disclosure through February 17, 2011, the date the financial statements were available to be issued.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 2 PLANT, PROPERTY, AND EQUIPMENT

The cost and composite depreciation rates for plant, property, and equipment are as follows.

	Composite Depreciation Rates %	2010	2009
Electric Utility Plant			
Intangible		\$ 348	\$ 348
Distribution	4.22%	57,944,763	55,812,653
General	5.80%	13,489,147	12,905,630
Total in service		<u>71,434,258</u>	<u>68,718,631</u>
Under construction		883,758	940,590
Less accumulated depreciation		<u>(16,737,273)</u>	<u>(14,613,692)</u>
Subtotal Electric Plant		<u>55,580,743</u>	<u>55,045,529</u>
Non-Utility Plant			
Non-Utility Plant	2.94%	1,048,812	1,048,812
Less accumulated depreciation		<u>(244,129)</u>	<u>(213,335)</u>
Total Non-Utility Plant		<u>804,683</u>	<u>835,477</u>
Total Electric Cooperative Plant		<u>56,385,426</u>	<u>55,881,006</u>
Propane Subsidiary Plant			
In service	4.54%	4,300,120	4,349,997
Less accumulated depreciation		<u>(1,698,091)</u>	<u>(1,583,300)</u>
Subtotal		<u>2,602,029</u>	<u>2,766,697</u>
Net plant, property, and equipment		<u>\$ 58,987,455</u>	<u>\$ 58,647,703</u>

The non-utility plant is held in the electric utility and is leased to the subsidiaries or held directly by the subsidiary. See note 13.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 3 INVESTMENTS IN ASSOCIATED COOPERATIVES

	<u>2010</u>	<u>2009</u>
Patronage Capital Credits		
Dairyland Power Cooperative (DPC)	\$ 6,790,949	\$ 6,367,693
National Rural Utilities Cooperative Finance Corporation (CFC)	793,376	675,598
Federated Rural Electric Insurance Exchange	278,991	272,238
Rural Electric Supply Cooperative (RESCO)	168,338	155,564
Subtotal	<u>8,031,654</u>	<u>7,471,093</u>
CFC member capital securities (matures 1/9/44, 7.50%)	<u>100,000</u>	<u>100,000</u>
Capital Term Certificates of the National Rural Utilities Cooperative Finance Corporation		
Capital term certificates - maturities 10/1/2070-2080; interest rate, 5.0%	532,131	532,131
Loan term certificates - maturities 10/1/2020 - 2025; interest rate, 3.0%	47,900	47,900
Loan capital certificates - maturities 8/1/2019 to 1/1/2035 non-interest bearing	590,406	564,778
Subtotal	<u>1,170,437</u>	<u>1,144,809</u>
Other	<u>52,231</u>	<u>51,732</u>
Total	<u>\$ 9,354,322</u>	<u>\$ 8,767,634</u>

The investment in DPC consists primarily of capital credits for the Cooperative's share of DPC's operating margins that have been allocated but not received and its share of unallocated operating losses. Operating margins and losses are recognized based on the Cooperative's percentage of DPC's power output sold to its members each year, which approximates the Cooperative's ownership in DPC. The Cooperative's investment in DPC is recorded on the equity method. During 2010 and 2009, the Cooperative recognized income of \$528,589 and \$420,816, respectively, related to its portion of DPC's margin.

Investments in CFC represent undistributed capital credits allocated to Polk-Burnett Electric Cooperative as well as loan and capital term certificates. The certificates represent investments made pursuant to CFC borrowing requirements. During 2010 and 2009 the Cooperative recognized income of \$235,557 and \$188,889, respectively, related to its portion of CFC's margins.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 3 INVESTMENTS IN ASSOCIATED COOPERATIVES (Continued)

The investments in Federated Rural Electric Insurance Exchange and Rural Electric Supply Cooperative represent undistributed capital credits allocated to Polk-Burnett Electric Cooperative. Polk-Burnett purchases insurance and material and supplies from these two Cooperatives. During 2010 and 2009 Polk-Burnett recognized income of \$26,737 and \$27,614, respectively, from Federated and \$27,321 and \$55,898, respectively, from RESCO related to its portion of these Cooperative's margins.

Note 4 DEFERRED DEBITS

	<u>2010</u>	<u>2009</u>
Past service pension costs	\$ 39,989	\$ 57,168
Loan conversion costs	73,741	112,273
Other	<u>-</u>	<u>(65)</u>
	<u>\$ 113,730</u>	<u>\$ 169,376</u>

In 2001, the Cooperative amended its pension plan effective October 1, 2001. The retirement age was reduced from age 62 to 62/30. The additional cost of \$178,476 is being amortized over twelve years, the average service life of the covered participants.

In 2003 and 2005, the Cooperative converted the interest rates on \$5.0 million of CFC notes to take advantage of lower rates. The conversion costs of \$444,284 are being amortized over ten years.

The past service pension costs and loan conversion costs have been deferred in accordance with the FASB ASC.

Note 5 MEMBERS' EQUITY

Patronage Capital

	<u>2010</u>	<u>2009</u>
Assignable	\$ 1,816,128	\$ 1,951,121
Assigned to date	<u>38,731,808</u>	<u>36,865,668</u>
Subtotal	40,547,936	38,816,789
Retired to date	<u>14,499,151</u>	<u>13,873,393</u>
Total	<u>\$ 26,048,785</u>	<u>\$ 24,943,396</u>

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 5 MEMBERS' EQUITY (Continued)

Patronage Capital (Continued)

The mortgage provisions restrict the retirement of patronage capital unless, after retirement, the total equity of the Cooperative equals at least 20% of the assets of the Cooperative. However, retirements (exclusive of any distributions to the estates of deceased patrons) can be made if such distributions do not exceed 30% of the preceding year's net consolidated margin. No distribution can be made if there is unpaid, when due, any installments of principal or interest on the notes.

Distributions to estates are made at the request of the estates. The retirement paid out is discounted, and the excess is retained by the Cooperative as a gain on retirement of capital credits. Patronage capital credits, arising from prior years' margins, are retired chronologically.

No interest shall be paid or payable to the patrons on any capital furnished by the patrons.

Other Equities

	2010	2009
Accumulated unallocated non-operating margins	\$ 102,186	\$ 17,448
Gain on early retirement of capital credits	347,349	324,952
Accumulated margins of subsidiaries	1,150,812	1,352,739
 Total	 \$ 1,600,347	 \$ 1,695,139

Accumulated Unallocated Non-Operating Margins

Accumulated unallocated non-operating margins consist of non-operating margins less deficits from operating divisions.

Gain on Early Retirements of Capital Credits

Gain on early retirement of capital credits consists of the discounted portion of capital credits paid to estates, due to early retirement.

Accumulated Margins of Subsidiaries

The accumulated margins of subsidiaries consist of the income, net of losses, from the wholly owned subsidiaries from their date of incorporation to December 31, 2010 and 2009.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 6 LONG-TERM DEBT AND LINE OF CREDIT

Long term debt is as follows:

	<u>2010</u>	<u>2009</u>
National Rural Utilities Cooperative Finance Corporation (CFC)		
Mortgage notes - interest rates of 3.60% to 7.60%, notes payable in quarterly installments with maturities at various dates from 2012 to 2038.	\$ 38,856,903	\$ 36,072,891
Farmer Mac notes serviced through CFC - interest rate of 6.028% payable in semi-annual installments with maturities at various dates from 2015 to 2037.	2,588,184	2,668,946
Line of credit - variable interest rate 4.25% at December 31, 2010	-	1,450,000
Interest rate differentials conversion fee	<u>81,368</u>	<u>122,051</u>
	41,526,455	40,313,888
National Cooperative Services Corporation (NCSC) mortgage note, interest rate 6.35%, payable in quarterly installments with final maturity 2010.	-	187,019
Line of credit - variable interest rate 4.25% at December 31, 2010	<u>-</u>	<u>100,000</u>
Subtotal	41,526,455	40,600,907
Less amount due within one year	<u>256,664</u>	<u>433,769</u>
Total long-term debt	<u>\$ 41,269,791</u>	<u>\$ 40,167,138</u>

Substantially all assets are pledged to CFC and NCSC as a security on the mortgage notes. The notes mature from 18 to 40 years from the date of issuance. The notes payable to CFC contain provisions for changing the rate of interest at specified future dates.

Approximate annual principal payments on the existing long-term debt for the next five years are:

2011	256,664
2012	255,938
2013	254,613
2014	270,410
2015	290,815

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 6 LONG-TERM DEBT AND LINE OF CREDIT (Continued)

In 2003 and 2005, the Cooperative converted the interest rates on approximately \$5.0 million of CFC notes to take advantage of lower rates. The new rates on the converted debt range from 6.0% to 6.3%. An interest rate differentials conversion fee of approximately \$444,284 was incurred in connection with the conversions and is payable on a quarterly basis over the remaining term of the notes which range from two to nine years.

Un-advanced loan funds of \$7,450,000 are available to the Cooperative from CFC.

The mortgage agreement with CFC requires, among other provisions, that the Cooperative maintain certain annual debt service coverage levels. The Cooperative was in compliance with the annual debt service coverage covenant at December 31, 2010. The CFC security agreement and mortgage restricts the Cooperative's debt limit to \$50 million.

Line of Credit

The Cooperative has a perpetual line of credit agreement with the National Rural Utilities Cooperative Finance Corporation providing the Cooperative with loans up to \$5.0 million on a revolving basis. Interest is payable quarterly at rates established by CFC, which are not to exceed the lowest prime rate as published in the "Money Rates" column of *The Wall Street Journal* plus 1% or lesser rate as fixed by CFC. The rate was 4.25% at December 31, 2010. The agreement provides that combined borrowing on this and any other line of credit shall not exceed \$5.0 million. Outstanding advances in any single calendar year may not exceed the prior calendar year's plant additions plus one-twelfth of annual operations and maintenance expenses. Any advances must be paid in full within 360 days of the advance or remain as long-term debt as the Cooperative can convert its line of credit to long-term at the discretion of the Board of Directors.

The Cooperative, through its propane subsidiary, has a perpetual line of credit agreement with the NCSC providing the Cooperative with loans up to \$2.0 million on a revolving basis. Interest is payable quarterly at rates established by NCSC, which are not to exceed the lowest prime rate as published in the "Money Rates" column of *The Wall Street Journal* plus 1% or lesser rate as fixed by NCSC. The rate was 4.25% at December 31, 2010. The agreement provides that combined borrowing on this and any other line of credit shall not exceed \$4.0 million. Outstanding advances in any single calendar year may not exceed the prior calendar year's plant additions plus one-twelfth of annual operations and maintenance expenses. Any advances must be paid in full within 360 days of the advance and remain at a zero balance for at least five consecutive business days.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 7 OTHER CURRENT LIABILITIES

Other current liabilities consist of the following:

	<u>2010</u>	<u>2009</u>
Electric customer deposits	\$ 381,097	\$ 341,373
Taxes other than income	338,255	92,918
Accrued interest	406,419	410,051
Accrued payroll	212,798	245,694
Self-funded health insurance	386,037	438,043
Accrued employee vacations	562,340	632,018
Income tax payable	8,707	9,818
Other	<u>-</u>	<u>11,874</u>
Total	<u>\$ 2,295,653</u>	<u>\$ 2,181,789</u>

Note 8 DEFERRED CREDITS

The balance of deferred credits consists of the following:

	<u>2010</u>	<u>2009</u>
Unclaimed patronage capital retirement refunds, and general fund checks	\$ 133,615	\$ (307)
Deferred gain on RDUP buy out, net of amortization	322,082	359,223
Deferred compensation	300,000	310,000
Deferred tax liability (See note 9)	<u>907,000</u>	<u>671,000</u>
Total	<u>\$ 1,662,697</u>	<u>\$ 1,339,916</u>

In 1995 and 1996, the Cooperative refinanced its RDUP debt of \$9.3 million with funds from CFC and RDUP discounting the debt \$1,396,538. The discount is being amortized over the remaining lives of the original notes using the effective interest rate amortization method. The amortization amounted to \$37,141 for 2010 and \$52,618 for 2009 and was credited to interest expense and the accumulated amortization is \$1,074,456 and \$1,037,315 at December 31, 2010 and 2009 respectively. The deferred gain on refinancing has been deferred in accordance with the FASB ASC.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 9 INCOME TAX (BENEFIT) AND DEFERRED INCOME TAX LIABILITY

The provision for income tax expense (benefit) includes the following components:

	<u>2010</u>	<u>2009</u>
Current expense (benefit)		
Federal	\$ (94,610)	\$ (254,931)
State	43,499	(40,173)
Deferred income tax		
Federal	23,000	46,000
State	<u>213,000</u>	<u>(14,000)</u>
 Total	 <u>\$ 184,889</u>	 <u>\$ (263,104)</u>

The components of deferred income tax liability are as follows:

	<u>2010</u>	<u>2009</u>	<u>2008</u>
Deferred tax assets:			
Net operating loss carryforwards	\$ 56,000	\$ 34,000	\$ 643,000
Valuation allowance	<u>-</u>	<u>(8,000)</u>	<u>(643,000)</u>
	56,000	26,000	-
Deferred tax liabilities:			
Depreciation	<u>963,000</u>	<u>697,000</u>	<u>639,000</u>
 Net deferred tax liability	 <u>\$ 907,000</u>	 <u>\$ 671,000</u>	 <u>\$ 639,000</u>

The Cooperative's net operating loss carryforwards begin to expire in 2014.

Note 10 SELF-FUNDED HEALTH INSURANCE

The Cooperative has a self-funded program for employee health insurance. Stop-loss insurance coverage limits the Cooperative's risk to a maximum of \$45,000 per insured individual and approximately \$750,000 for all insured in the aggregate. The plan is administered and claims are validated by a benefits management company. All claims are expensed on the accrual basis when the benefits management company becomes aware of their validity. A liability of \$386,037 and \$563,255 as of December 31, 2010 and 2009, respectively, has been recorded to cover potential claims that may have occurred but which the benefits management company has not yet become aware of at December 31, 2010 and 2009.

Actual medical claims paid by the cooperative for medical and prescription benefits was \$568,005 and \$576,713 in 2010 and 2009, respectively. The cooperative offered a low and high deductible plan in 2009 and through August of 2010. As of September 2010 the cooperative offers a high deductible plan with deductibles of \$2000 for single plans and \$4000 for family plans.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 11 EMPLOYEE BENEFITS

Multi-employer Defined Benefit Pension Plan

Pension benefits for substantially all employees of the Cooperative are covered by a multi-employer defined benefit plan sponsored by the National Rural Electric Cooperative Association (NRECA). The Cooperative made contributions to the plan of \$994,260 in 2010 and \$778,662 in 2009. Information relating to the Cooperative's portion of assets and accumulated benefits is not available as the plan assets are not determined or allocated separately by individual employers.

Defined Contributions Plan

The Cooperative has a NRECA 401(k) defined contribution savings plan for employees who meet certain age and service requirements. The Cooperative matches employee contributions up to 4.5% for union employees and 6.0% for non-union employees' compensation into the plan. Savings plan expense was \$233,932 in 2010 and \$242,291 in 2009.

Other Plans

The cooperative provides employees with access to other premium based benefits including, medical, dental and vision insurances, long and short term disabilities and life insurance. The cost of these benefits are funded by both the employee and the employer. The cooperative's cost relating to these benefits was \$198,958 and \$168,415 in 2010 and 2009, respectively.

Compensated Absences

The cost of compensated absences (vacation, sick leave taken, and holidays) was \$655,562 and \$525,949 in 2010 and 2009, respectively.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 12 RELATED PARTY TRANSACTIONS AND COMMITMENTS

Purchased Power Agreement

Polk-Burnett Electric Cooperative is a member of Dairyland Power Cooperative (DPC) which is an electric generation and transmission cooperative. The Cooperative obtained all of its purchased power from DPC for the years ended December 31, 2010 and 2009. In 2010 and 2009, the Cooperative's total purchased power was \$16,652,881 and \$16,450,121, respectively.

Under its wholesale power agreement, the Cooperative is committed to purchase its electric power and energy requirements from DPC until December 31, 2055. The rates paid to DPC are subject to periodic review.

Management Consulting, Accounting and Other Services to Propane and Security Subsidiaries

Effective January 1, 2006, Polk-Burnett Electric Cooperative has an agreement with the Propane subsidiary, whereby the Cooperative furnishes management consulting, accounting, building and office space, and bulk facility maintenance and other related products and services as may be required by them. Compensation for such services is at cost. The agreement is to continue in force for one year and is automatically renewable for successive one year terms unless, either party, sixty days prior to the expiration of any contract term notifies the other of its desire to renegotiate the substantial provisions of the agreement or terminate the contract. The total costs charged to the subsidiary under the agreements amounted to \$24,000 in 2010 and 2009, respectively. This activity has been eliminated in the consolidated financial statements.

Lease of Office and Bulk Plant Facilities to Propane and Security Subsidiaries

Effective January 1, 2006, the Cooperative entered into a lease whereby it leases office space, land and equipment to the Propane subsidiary. The annual base rent is \$12,000 for Propane. The lease for the bulk facilities is ten years and is automatically renewable for successive five year periods. The total costs charged to the subsidiary under the agreements amounted to \$12,000 in 2010 and 2009, respectively. This activity has been eliminated in the consolidated financial statements.

The Cooperative also charges interest to subsidiaries for the use of funds. No interest was charged in 2010 or 2009.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 12 RELATED PARTY TRANSACTIONS AND COMMITMENTS (Continued)

Substation Operating Lease Commitment

In August 2002 the Cooperative entered into an agreement to lease a substation from another rural electric cooperative under a non-cancelable operating lease agreement. The lease agreement currently requires a monthly base lease payment of \$1,439 and expires August 10, 2032.

The annual rent expense under this agreement was \$17,268 for 2010 and 2009. Scheduled future minimum lease payments under the lease agreement are as follows:

<u>Year Ending December 31,</u>	
2011	\$ 17,268
2012	17,268
2013	17,268
2014	17,268
2015	17,268
Thereafter	<u>293,556</u>
Total	\$ <u><u>379,896</u></u>

Deferred Compensation

The deferred compensation plan represents the Company's accrued liability to the former CEO for a \$310,000 deferred compensation package. In 2010 payments under this agreement totaled \$10,000 resulting in the remaining \$300,000 balance. The deferred compensation plan is unfunded and is shown in deferred credits.

Propane Contract Commitments

At December 31, 2010, Polk-Burnett Propane Services, Inc, has contracted for approximately 1,237,671 gallons of propane sales with customers and has not contracted any gallons of propane gas purchases with suppliers. No gains or losses on these contracts are included in the financial statements.

POLK-BURNETT ELECTRIC COOPERATIVE
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2010 and 2009

Note 13 DISCONTINUED OPERATIONS

On December 1, 2008 Polk-Burnett Security Services, Inc. sold substantially all of its business assets and related liabilities along with its naming rights. The Company changed its name to Northwestern Wisconsin Security, Inc effective with the sale. The following are details relating to the discontinued operations reported on the consolidated balance sheet and statement of operations:

	<u>ASSETS</u>	<u>2010</u>	<u>2009</u>
CURRENT ASSETS:			
Income tax receivable		\$ -	\$ 162,000
TOTAL ASSETS		<u>\$ -</u>	<u>\$ 162,000</u>
LIABILITIES			
Other current liabilities		\$ -	\$ (279)
Statement of Operations			
		<u>2010</u>	<u>2009</u>
Operating revenues		\$ -	\$ 130
Less cost of goods sold		-	2,528
Gross margins (loss)		-	(2,398)
Operating expenses		(6,315)	(17,637)
Operating loss		(6,315)	(20,035)
Other income (loss)		762	(84,562)
Income (loss) before income taxes		(5,553)	(104,597)
Income tax (expense) benefit		(172,000)	172,448
Net income (loss)		<u>\$ (177,553)</u>	<u>\$ 67,851</u>