

NEW APPLICATION

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BEFORE THE ARIZONA CORPORATION COMMISSION

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Arizona Corporation Commission

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FEB 26 2009

AZ CORP COMMISSION
DOCKET CONTROL

COMMISSIONERS

- KRISTIN K. MAYES, Chairman
- GARY PIERCE
- PAUL NEWMAN
- SANDRA D. KENNEDY
- BOB STUMP

DOCKETED BY	AP
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E-01749A-09-0087

IN THE MATTER OF THE APPLICATION OF)
 GRAHAM COUNTY ELECTRIC ,)
 COOPERATIVE, INC. APPROVAL OF A LOAN)
 GUARANTEE)
 _____)

DOCKET NO. E-01749A-09-_____
 FINANCE APPLICATION

Pursuant to A.R.S. § 40-285 et seq., Graham County Electric Cooperative, Inc. ("GCEC"), hereby files with the Arizona Corporation Commission ("Commission") an Application ("Finance Application") for authorization to guarantee a loan for Graham County Utilities, Inc. ("GCU"). If approved, GCU will borrow \$1,050,000 (\$800,000 for GCU Gas Division, \$250,000 for GCU Water Division) from the National Cooperative Finance Corporation ("CFC Loan") to finance prior construction of plant in accordance with GCU's construction work plan. In support of its Finance Application, GCEC states as follows:

1. GCEC is a non-profit corporation and public service corporation.
 GCEC holds a Certificate of Convenience and Necessity, to provide Electric Distribution Service to its member-customers in Graham County, Arizona.
2. The Commission has jurisdiction over GCEC and the subject matter of this Finance Application.
3. GCEC currently provides electric service to approximately 6,065 members.

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1 4. GCEC manages the operations of GCU's Gas and Water Divisions pursuant to an
2 operations and management agreement. GCEC and GCU Gas and Water are operated as separate
3 and distinct entities from each other. Nevertheless, the same members (6 out of 9) serve on the
4 Boards of Directors of both GCU and GCEC.

5 5. On January 29, 2009, GCU filed separate applications with the Commission for
6 approval of a loan from the National Rural Utilities Cooperative Finance Corporation ("CFC") in
7 the approximate amount of \$1,050,000 (\$800,000 for GCU Gas Division in Docket No.
8 G-02527A-09-0032, \$250,000 for GCU Water Division in Docket No. W-02527A-09-0033), to
9 finance prior construction of plant.
10

11 6. On January 7, 2009, GCU's Board of Directors approved separate Resolutions for
12 the Gas and Water Divisions to make application to the National Rural Utilities Cooperative
13 Finance Corporation ("CFC") for a loan in the approximate amount of \$1,050,000 (\$800,000 for
14 GCU Gas Division, \$250,000 for GCU Water Division, to finance prior construction of plant.
15

16 7. Among other things, GCU Gas Division expended funds on new gas mains,
17 services, meters and regulators and miscellaneous distribution equipment to improve and work on
18 the gas distribution system. GCU Water Division has expended funds on structures and
19 improvements, wells, pumping equipment, mains, services, hydrants and meters.
20

21 8. GCEC has provided temporary financing to GCU for these gas and water plant
22 additions. GCU will be using the CFC Loan to repay GCEC for funds that it has advanced to
23 GCU.

24 9. GCU submitted an application for long-term financing to CFC in the amount of
25 \$1,050,000 (\$800,000 for GCU Gas Division, \$250,000 for GCU Water Division), with a
26

1 maturity date to cover a period of thirty (30) years, to fund the construction of the facilities
2 identified in GCU's schedules of net plant additions for the Gas and Water Division. On January
3 12, 2009, GCU received a conditional commitment letter (attached) from CFC to finance up to
4 \$1,050,000 contingent upon and subject to the following condition among five others:

5 * a guaranty from Graham County Electric Cooperative Inc., in the amount of the
6 total credit facility extended to Graham County Utilities, secured by a first
7 mortgage lien on Graham County Utilities' assets and revenues.
8

9 10. A copy of the Graham County Electric Cooperative Inc. Board of Directors'
10 Resolution approving the guarantee of the CFC Loan Application is attached here to.

11 11. GCU intends to repay, in substantial part, the cost of the CFC Loan
12 over a thirty (30) year period through the use of its general funds. GCU intends to file an
13 application for a rate case within the next month for both the Gas and Water Division.
14

15 12. GCEC believes its guarantee of the GCU loan will have no impact on its members
16 due to the fact that its guarantee of the GCU loan would only be exercised if GCU were unable to
17 repay the CFC loan.

18 13. As evidenced by its attached audited financials, GCEC is financially able to repay
19 the GCU CFC loan if in the unlikely event that GCU were unable to do so.

20 21 14. GCU's CFC Loan request is: (1) for lawful purpose; (2) within
22 GCU's corporate powers; (3) compatible with the public interest; (4) within sound financial
23 practices; and (5) within the proper performance of the Cooperative as a public service
24 corporation. The CFC Loan will improve GCU's ability to continue to provide safe and reliable
25 gas distribution and water service to its member-customers.
26

1 15. GCEC's guarantee of the GCU CFC loan is: (1) for lawful purpose; (2) within
2 GCEC's corporate powers; (3) compatible with the public interest; (4) within sound financial
3 practices; and (5) within the proper performance of the Cooperative as a public service
4 corporation.

5 16. The CFC Loan and GCEC's guarantee of such loan is dependant upon
6 authorization by this Commission.

7 17. The aggregate amount of securities outstanding, and proposed to be
8 outstanding, will not exceed the fair value of GCEC's properties and business. A copy of
9 GCEC's audited financial statements for the years ended September 30, 2008 and 2007 is also
10 attached here to.
11

12 18. GCEC requests that the Commission act on this application as soon as possible to
13 assist GCU financially to maintain reliable gas distribution and water service.
14

15 19. GCEC and GCU further request that the Commission consolidate this Docket No.
16 with Docket No. G-02527A-09-0032 and Docket No. W-02527A-09-0033 since these
17 applications are interrelated.

18 20. All correspondence with regard to this Finance Application should be
19 sent to:
20

21 John V. Wallace
22 Grand Canyon State Electric Cooperative Association, Inc.
23 120 N. 44th Street, Suite 100
24 Phoenix, Arizona 85034
25 E-mail: jwallace@gcseca.coop
26

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With a copy to:

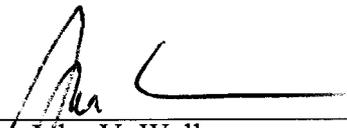
Russ Barney
GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
P. O. Drawer B
Pima, Arizona 85543
Email: russb@gce.coop

WHEREFORE, GCEC, having fully stated its Application and showing that it is in the public interest for the Cooperative to guarantee the GCU CFC Loan to obtain the to fund prior construction of facilities to serve GCU's member-customers, hereby requests that the Commission:

1. Accept GCEC's Application to Guarantee the GCU CFC Loan for filing.
2. Authorize GCEC to Guarantee the GCU CFC Loan to borrow \$1,050,000 (\$800,000 for GCU Gas Division, \$250,000 for GCU Water Division) for the lawful purposes set forth in this application, and to authorize the Cooperative to take such actions necessary and appropriate to execute a mortgage to secure the CFC Loan;
3. Consolidate this Docket No. with Docket No. G-02527A-09-0032 and Docket No. W-02527A-09-0033 since these applications are interrelated; and
4. Grant such other relief as may be in the public interest.

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RESPECTFULLY SUBMITTED this 26th day of February, 2009.

By 
John V. Wallace
Grand Canyon State Electric Cooperative Association, Inc.
120 N. 44th Street, Suite 100
Phoenix, Arizona 85034

Original and thirteen (13) copies of
GCEC's Application
filed this 26th day of February, 2009
with:

DOCKET CONTROL
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

**GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
BOARD RESOLUTION GUARANTEEING GRAHAM COUNTY UTILITIES,
INC. REQUEST FOR LONG TERM FINANCING**

WHEREAS, the Board of Directors of Graham County Electric Cooperative, Inc., agrees to guarantee a new loan request from Graham County Utilities, Inc. (Water Division), to borrow from NRUCFC for prior new water construction.

Total Financing Requested: \$250,000.00

NOW, THEREFORE BE IT RESOLVED, that this guarantee is based upon approval from the Arizona Corporation Commission.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of Graham County Electric Cooperative, Inc., this 7th day of January, 2009.



M. Max Peck, Secretary

CORPORATE SEAL

**GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
BOARD RESOLUTION GUARANTEEING GRAHAM COUNTY UTILITIES,
INC. REQUEST FOR LONG TERM FINANCING**

WHEREAS, the Board of Directors of Graham County Electric Cooperative, Inc., agrees to guarantee a new loan request from Graham County Utilities, Inc. (Gas Division), to borrow from NRUCFC for prior new gas construction.

Total Financing Requested: \$800,000.00

NOW, THEREFORE BE IT RESOLVED, that this guarantee is based upon approval from the Arizona Corporation Commission.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of Graham County Electric Cooperative, Inc., this 7th day of January, 2009.



M. Max Peck, Secretary

CORPORATE SEAL

ARIZONA 17 GRAHAM

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

PIMA, ARIZONA

FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION

FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

**CERTIFIED PUBLIC ACCOUNTANTS
LUBBOCK, TEXAS**

ARIZONA 17 GRAHAM

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

PIMA, ARIZONA

FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION

FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

AND

REPORT OF CERTIFIED PUBLIC ACCOUNTANTS

**ARIZONA 17 GRAHAM
GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.
PIMA, ARIZONA**

**FINANCIAL STATEMENTS WITH ACCOMPANYING INFORMATION
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007**

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BOLINGER, SEGARS, GILBERT & MOSS, L.L.P.

CERTIFIED PUBLIC ACCOUNTANTS

PHONE: (806) 747-3806

FAX: (806) 747-3815

8215 NASHVILLE AVENUE

LUBBOCK, TEXAS 79423-1954

INDEPENDENT AUDITORS' REPORT

Board of Directors
Graham County Electric Cooperative, Inc.
Pima, Arizona

We have audited the accompanying balance sheets of Graham County Electric Cooperative, Inc. as of September 30, 2008 and 2007, and the related statements of income and patronage capital, 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 audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Graham County Electric Cooperative, Inc. as of September 30, 2008 and 2007, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

November 3, 2008

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

Exhibit A

BALANCE SHEET
SEPTEMBER 30, 2008 AND 2007

ASSETS

	September 30,	
	2008	2007
UTILITY PLANT AT COST		
Electric Plant in Service	\$ 32,457,427	\$ 31,307,758
Construction Work in Progress	1,555,334	(146,118)
	\$ 34,012,761	\$ 31,161,640
Less: Accumulated Provision for Depreciation	11,906,120	10,931,571
	\$ 22,106,641	\$ 20,230,069
OTHER PROPERTY AND INVESTMENTS AT COST OR STATED VALUE		
Investments in Associated Organizations	\$ 4,095,966	\$ 2,137,714
Notes Receivable Less Current Portion	17,947	56,335
	\$ 4,113,913	\$ 2,194,049
CURRENT ASSETS		
Cash - General	\$ 580,635	\$ 689,357
Current Portion of Notes Receivable	41,728	38,761
Accounts Receivable (Less allowance for uncollectibles of \$108,030 in 2008 and \$66,733 in 2007)	1,717,569	1,641,010
Accounts Receivable - Graham County Utilities, Inc.	817,698	
Under Recovered Fuel Cost	153,234	122,336
Materials and Supplies	1,002,336	399,241
Other Current and Accrued Assets	39,713	45,918
	\$ 4,352,913	\$ 2,936,623
DEFERRED CHARGES	\$ 356,519	\$ 336,175
	\$ 30,929,986	\$ 25,696,916
EQUITIES AND LIABILITIES		
EQUITIES		
Memberships	\$ 30,322	\$ 30,020
Patronage Capital	10,749,123	7,901,285
Other Equities	1,364	(18,268)
Accumulated Other Comprehensive Income (Loss)	(934,010)	(1,227,489)
	\$ 9,846,799	\$ 6,685,548
LONG-TERM DEBT		
CFC Mortgage Notes Less Current Maturities	\$ 16,731,708	\$ 14,986,632
NRECA Past Service Retirement Cost Less Current Maturities	128,295	146,958
	\$ 16,860,003	\$ 15,133,590
POST RETIREMENT BENEFITS OTHER THAN PENSIONS	\$ 1,193,944	\$ 1,442,711
CURRENT LIABILITIES		
Current Maturities of Long-Term Debt	\$ 266,263	\$ 234,980
Accounts Payable - Purchased Power	1,091,092	1,060,243
Accounts Payable - Other	664,627	138,423
Accounts Payable - Graham County Utilities		26,193
Accrued Taxes	341,691	379,833
Accrued Interest	24,976	24,819
Consumer Deposits and Prepayments	174,787	161,897
Accrued Compensated Absences	346,135	306,814
Other Current and Accrued Liabilities	111,888	94,651
	\$ 3,021,459	\$ 2,427,853
DEFERRED CREDITS	\$ 7,781	\$ 7,214
	\$ 30,929,986	\$ 25,696,916

See accompanying notes to financial statements.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

Exhibit B

STATEMENT OF INCOME AND PATRONAGE CAPITAL
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

	Years Ended September 30,				Increase (Decrease)
	2008		2007		
	Amount	%	Amount	%	
OPERATING REVENUES					
Residential	\$ 8,772,976	50.8	\$ 7,800,396	47.9	\$ 972,580
Irrigation	1,524,173	8.8	1,626,523	10.0	(102,350)
Commercial and Industrial	6,478,565	37.5	5,884,934	36.1	593,631
Pub Post-retirement Benefits	13,345	0.1	12,275	0.1	1,070
Power Cost - Under (Over) Billed	30,898	0.2	546,997	3.4	(516,099)
Rent from Electric Property	123,543	0.7	148,629	0.9	(25,086)
Other Operating Revenues	323,645	1.9	267,667	1.6	55,978
Fuel Costs Over Recovered	\$ 17,267,145	100.0	\$ 16,287,421	100.0	\$ 979,724
OPERATING EXPENSES					
Purchased Power	\$ 11,736,801	68.0	\$ 11,330,034	69.6	\$ 406,767
Operation	591,612	3.4	581,729	3.6	9,883
Maintenance	1,457,094	8.4	1,495,928	9.2	(38,834)
Customer Accounts	425,405	2.5	399,683	2.5	25,722
Administrative and General	957,634	5.5	942,982	5.8	14,652
Depreciation and Amortization	940,139	5.4	899,353	5.5	40,786
Other Interest and Deductions	21,226	0.1	22,533	0.1	(1,307)
Total Operating Expenses	\$ 16,129,911	93.3	\$ 15,672,242	96.3	\$ 457,669
OPERATING MARGINS - Before					
Fixed Charges	\$ 1,137,234	6.7	\$ 615,179	3.7	\$ 522,055
FIXED CHARGES					
Interest on Long-Term Debt	1,037,979	6.0	1,004,064	6.2	33,915
OPERATING MARGIN (LOSS) - After					
Fixed Charges	\$ 99,255	0.7	\$ (388,885)	(2.5)	\$ 488,140
Other Capital Credits	2,006,274	11.6	118,818	0.7	1,887,456
NET OPERATING MARGIN (LOSS)	\$ 2,105,529	12.3	\$ (270,067)	(1.8)	\$ 2,375,596
NONOPERATING MARGINS					
Interest Income	\$ 66,772	0.4	\$ 87,932	0.5	\$ (21,160)
Nonoperating Income	695,169	4.0	16,064	0.1	679,105
	\$ 761,941	4.4	\$ 103,996	0.6	\$ 657,945
NET MARGINS (LOSS)	\$ 2,867,470	16.7	\$ (166,071)	(1.2)	\$ 3,033,541
OTHER COMPREHENSIVE INCOME (LOSS)					
Adjustment for Application of FASB Statement No. 158	\$ 293,479		\$ (1,227,489)		
COMPREHENSIVE INCOME (LOSS)	\$ 3,160,949		\$ (1,393,560)		
FASB Statement No. 158	(293,479)		1,227,489		
PATRONAGE CAPITAL - BEGINNING OF YEAR	7,901,285		8,047,724		
Offset Prior Year Losses with Current Margins	(19,632)				
Transfer Operating Loss to Other Equities			19,632		
PATRONAGE CAPITAL - END OF YEAR	\$ 10,749,123		\$ 7,901,285		

See accompanying notes to financial statements.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

Exhibit C

STATEMENT OF CASH FLOWS
FOR THE YEARS ENDED SEPTEMBER 30, 2008 AND 2007

	September 30,	
	2008	2007
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Margins (Loss)	\$ 2,867,470	\$ (166,071)
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities		
Depreciation and Amortization	1,101,637	1,035,252
Post-retirement Benefits	140,346	180,688
Capital Credits - Non Cash	(1,923,896)	(38,411)
Deferred Charges	(20,344)	34,261
Deferred Credits	567	454
Fuel Costs Over Recovered	(30,898)	(546,997)
Accounts Receivable	(76,559)	(583,317)
Accounts Receivable/ Payable - Graham County Utilities	(843,891)	101,959
Inventories and Prepaid Expenses	(596,890)	(81,360)
Payables and Accrued Expenses	588,514	440,545
Net Cash Provided by Operating Activities	<u>\$ 1,206,056</u>	<u>\$ 377,003</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to Utility Plant	\$ (2,998,636)	\$ (1,380,071)
Cost of Removal (in Excess of)/Less Than Salvage Value and Other Credits	20,427	(7,576)
Investments in Associated Organizations	(34,356)	(35,616)
Notes Receivable	35,421	36,004
Net Cash Used in Investing Activities	<u>\$ (2,977,144)</u>	<u>\$ (1,387,259)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
CFC Loan Proceeds	\$ 2,000,000	\$ 500,000
Payments on Long-Term Debt to CFC	(225,022)	(204,014)
Payments on Other Long-Term Debt	(17,280)	(16,000)
Payments on Behalf of Retirees	(95,634)	(98,087)
Memberships	302	1,255
Net Cash Provided by Financing Activities	<u>\$ 1,662,366</u>	<u>\$ 183,154</u>
DECREASE IN CASH EQUIVALENTS	\$ (108,722)	\$ (827,102)
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	689,357	1,516,459
CASH AND CASH EQUIVALENTS - END OF YEAR	<u>\$ 580,635</u>	<u>\$ 689,357</u>
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION		
Cash Paid During the Year for:		
Interest on Long-Term Debt	\$ 1,048,603	\$ 1,012,077
Federal Income Tax	<u>\$ 0</u>	<u>\$ 0</u>

SUPPLEMENTAL DISCLOSURE OF NON CASH FLOW INFORMATION

The Cooperative adopted the recognition and disclosure provisions of SFAS No. 158 for the year ending September 30, 2007. The adjustment for the initial application of this statement increased the accrued post-retirement benefit liability by \$1,227,489 and reduced equities by the same amount. During the year ended September 30, 2008, application of SFAS No. 158 resulted in a decrease in accrued post-retirement benefit liability and equities by \$293,479.

See accompanying notes to financial statements.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

1. Nature of Operations and Summary of Significant Accounting Policies

Nature of Operations

Graham County Electric Cooperative, Inc. (the Cooperative) is a non-profit company organized to provide electric service at the retail level to primarily residential and commercial accounts in a designated service area. Power delivered at retail is purchased wholesale from Arizona Electric Power Cooperative, Inc. of which Graham County Electric Cooperative is a member/owner. Any revenues earned in excess of costs incurred are allocated to members of Graham County Electric Cooperative, Inc. and are reflected as patronage capital equity in the balance sheet.

System of Accounts

The accounting records of the Cooperative are maintained in accordance with the Uniform System of Accounts as prescribed by the Federal Energy Regulatory Commission for Class A and B electric utilities modified for electric borrowers of the National Rural Utilities Cooperative Finance Corporation (CFC).

Electric Plant, Maintenance, and Depreciation

Electric plant is stated at the original cost of construction which includes the cost of contracted services, direct labor, materials, and overhead items. Contributions from others toward the construction of electric plant are credited to the applicable plant accounts.

When property which represents a retirement unit is replaced or removed, the estimated cost of such property is credited to electric plant and such cost, together with cost of removal less salvage, is charged to the accumulated provision for depreciation.

Maintenance and repairs, including the renewal of minor items of plant not comprising a retirement unit, are charged to the appropriate maintenance accounts, except that repairs of transportation and service equipment are charged to clearing accounts and redistributed to operating expense and other accounts.

Inventories

Materials and supplies inventories are valued at average unit cost.

Electric Revenues

The Cooperative's operating revenues are under the jurisdiction of the Arizona Corporation Commission.

The Cooperative records electric revenues as billed to customers on a monthly basis. Revenue is not accrued for power delivered but not billed at the end of each month. The unbilled revenue was estimated to be \$531,894 and \$498,074 at September 30, 2008 and 2007, respectively.

The Cooperative's tariffs for electric service include fuel adjustment clauses under which electric rates charged to consumers are adjusted to reflect changes in the cost of fuel included in purchased power. The power cost to be billed in subsequent periods is recognized as Under-Recovered Fuel Costs and power cost billed in advance is reflected as Over-Recovered Fuel Cost.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Group Concentration of Credit Risk

The Cooperative headquarters facilities are located in Pima, Arizona. The service area includes members located in Graham County, Arizona. The Cooperative records a receivable for electric revenues as billed on a monthly basis. The Cooperative requires a deposit from some consumers upon connection. The deposit is applied to any unpaid bills and fees in the event of default. The deposit accrues interest annually and is refunded after an established history of prompt payments. Deposits on hand totaled \$174,787 and \$161,897 at September 30, 2008 and 2007, respectively.

Graham County Electric Cooperative, Inc. is the guarantor of the mortgage notes executed by Graham County Utilities, Inc. (an affiliated company) to CFC in the amount of \$3,193,711 payable over 25 years with a maturity date of September 30, 2014, June 30, 2026, and September 30, 2031. At September 30, 2008, the principal balance owed on the mortgage note was \$1,690,299. Payments on the note are being made when due.

The Cooperative maintains its cash balances in various financial institutions in Safford, Arizona. The balance is insured at each location by the Federal Deposit Insurance Corporation up to \$100,000. Deposits, at times, exceed insured amounts.

Patronage Capital Certificates

Patronage capital from associated organizations is recorded at the stated amount of the certificate.

Federal Income Tax Status

The Cooperative qualifies for exempt status under Internal Revenue Code section 501(c)(12) which requires that 85% or more of income consists of amounts collected from members.

Allowance for Uncollectible Accounts

The Cooperative uses the aging method to allow for uncollectible receivable. During the year, management makes an evaluation of past due accounts to determine collectability. The accounts deemed uncollectible are written off upon approval by the Board of Directors.

Use of Estimates in the Preparation of Financial Statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

2. Electric Plant

The major classes of electric plant are as follows:

	September, 30,	
	2008	2007
Intangible Plant	\$ 3,060	\$ 3,060
Transmission Plant	2,551,563	2,551,563
Distribution Plant	26,419,057	25,473,673
General Plant	3,483,747	3,279,462
Total Electric Plant in Service	\$ 32,457,427	\$ 31,307,758
Construction Work in Progress	1,555,334	(146,118)
Total Electric Plant	\$ 34,012,761	\$ 31,161,640

Provision for depreciation of electric plant is computed using straight-line composite rates as follows:

Transmission Plant	2.75%
Distribution Plant	2.94%

Straight-line composite depreciation rates are applied to all general plant accounts, except the transportation equipment which is depreciated on an item by item basis. Depreciation rates are selected for the general plant account, based upon the estimated useful life of the asset and are as follows:

Buildings	2.0%
Transportation	20.0%
Office Equipment	6.0%
Laboratory and Tools	4.8%
Communication	6.5%

Depreciation and amortization for the years ended September 30, 2008 and 2007, was \$1,101,637 and \$1,035,252, respectively, of which \$940,139 and \$899,353 was charged to depreciation expense and \$161,498 and \$135,899 allocated to other accounts, respectively.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

3. Investments in Associated Organizations

Investments in associated organizations consisted of the following:

	September 30,	
	2008	2007
CFC		
Patronage Capital	\$ 247,905	\$ 213,657
Capital Term Certificates	493,202	457,670
Membership	1,000	1,000
	<u>\$ 742,107</u>	<u>\$ 672,327</u>
Arizona Electric Power Cooperative, Inc.		
Patronage Capital	\$ 3,289,621	\$ 1,408,128
Membership	5	5
	<u>\$ 3,289,626</u>	<u>\$ 1,408,133</u>
Graham County Utilities, Inc.		
Membership	\$ 5,000	\$ 5,000
Federated Rural Electric Insurance Corporation		
Common Stock	\$ 59,133	\$ 52,154
Other	\$ 100	\$ 100
	<u>\$ 4,095,966</u>	<u>\$ 2,137,714</u>

4. Notes Receivable

Notes receivable consisted of the following:

	September 30,	
	2008	2007
Due from Graham County Utilities, Inc.	<u>\$ 59,675</u>	<u>\$ 95,096</u>

During 1998, the Cooperative converted an account receivable from Graham County Utilities, Inc. into a note receivable with interest at 7.4%. The original term of the note was for five years. In 2001, the note was extended to 10 years with approval from the Arizona Corporation Commission.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

5. Inventories

Inventories consisted of construction materials and supplies and totaled \$430,526 and \$399,241, at September 30, 2008 and 2007, respectively. In addition, the Cooperative has a spare substation transformer in inventory valued at \$571,810.

6. Deferred Charges

Deferred charges consisted of the following:

	September 30,	
	2008	2007
NRECA Retirement Plan Past Service Cost	\$ 146,958	\$ 164,238
Rate Filing Expenses	25,734	
Engineering Costs (Maintenance Review, Long Range Plan, Sectionalizing Study, and Work Plan)	27,637	9,393
Computer Software	2,946	4,306
Right of Way Lease	51,507	54,941
City of Safford Project	100,000	100,000
Other	1,737	3,297
	<u>\$ 356,519</u>	<u>\$ 336,175</u>

Deferred charges applicable to NRECA retirement plan past service pension costs represent charges incurred to recognize employees' prior service. This cost is to be paid and amortized over a 30-year period. The Cooperative is applying the provisions of FASB Statement No. 71 to defer these costs and to include them as cost of service in the next rate filing with the Arizona Corporation Commission.

7. Return of Capital

Under the provisions of the mortgage agreements, until the equities and margins equal or exceed 30% of the total assets of the Cooperative, the return to patrons of capital contributed by them is limited generally to 25% of the patronage capital or margins received by the Cooperative in the prior calendar year. The equities and margins of the Cooperative represent 31.8% (after adjustment for accumulated Other Comprehensive Income) or 34.9% (before adjustment for Accumulated Other Comprehensive Income) of the total assets at balance sheet date. No capital credit retirements were made during the years ended September 30, 2008 and 2007.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

8. Patronage Capital

	September 30,	
	<u>2008</u>	<u>2007</u>
Assignable (9 months ended September 30)	\$ 1,763,738	\$ (27,756)
Assigned	<u>9,734,944</u>	<u>8,678,600</u>
	\$ 11,498,682	\$ 8,650,844
Less: Retired	<u>749,559</u>	<u>749,559</u>
	<u>\$ 10,749,123</u>	<u>\$ 7,901,285</u>

9. Other Equities

	September 30,	
	<u>2008</u>	<u>2007</u>
Retired Capital Credits Gain	\$ 1,364	\$ 1,364
Operating Loss		<u>(19,632)</u>
	<u>\$ 1,364</u>	<u>\$ (18,268)</u>

The prior year operating loss was offset by using 2007 margins.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

10. Long-Term Debt – CFC

Following is a summary of long-term debt due CFC maturing at various times from 2029 to 2038:

Note No.	Interest Rate	Maturity Date	Purpose	September 30,	
				2008	2007
9002 - 2&4	7.45%	05/24/29	Construction	\$ 437,336	\$ 446,124
9003	7.45%	07/20/30	Construction	433,530	441,281
9004	7.70%	07/20/30	Construction	445,953	453,653
9005	7.45%	07/20/30	Construction	433,530	441,281
9006	7.45%	01/20/32	Construction	443,800	451,734
9007	7.35%	09/04/32	Construction	591,187	601,904
9008 - 1&2	7.40%	09/04/32	Construction	763,513	774,984
9009 - 1&2	6.85%	09/03/33	Construction	1,817,617	1,844,923
9009 - 3	7.90%	09/03/33	Construction	1,851,575	1,875,061
9009 - 4&5	5.00%	06/30/33	Construction	1,779,011	1,814,636
9009 - 6	7.10%	06/30/33	Construction	364,060	369,316
9009 - 7	6.70%	06/30/33	Construction	319,434	324,349
90010 - 1	6.90%	12/31/38	Construction	966,564	975,799
90010 - 2	7.10%	09/30/34	Construction	2,872,658	2,909,965
90010 - 3	6.40%	06/30/38	Construction	970,023	980,656
90010 - 4	6.75%	03/31/37	Construction	493,102	498,666
90010 - 5&6	4.90%	12/31/38	Construction	1,996,415	
				\$ 16,979,308	\$ 15,204,332
Less: Current Maturities				247,600	217,700
				\$ 16,731,708	\$ 14,986,632

Except for note number 90010 – 5&6 which is a variable rate note all other notes have a fixed interest rate.

The Cooperative has unadvanced loan funds available of \$3,313,368.

As of September 30, 2008, annual maturities of long-term debt due CFC for the next five years are as follows:

2008	\$ 247,600
2009	264,800
2010	283,100
2011	302,800
2012	323,800

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Substantially all assets are pledged as security for the long-term debt due CFC.

11. Other Long-Term Debt

The cooperative has elected to finance the cost of NRECA Retirement and Security Plan prior service benefits. The total cost, \$283,080 (including a 1997 tiered benefit buy-back of \$206,520), is to be paid over 30 years in annual payments including interest at the rate of eight percent. The balance outstanding at September 30, 2008 and 2007, is \$146,958 and \$164,238, respectively. Annual maturities due NRECA for the next five years are as follows:

2008	\$ 18,663
2009	20,156
2010	21,768
2011	23,510
2012	25,390

12. Short-Term Borrowing

The Cooperative had a \$1,100,000 line of credit for short-term financing with CFC at an interest rate of one percent above the prime interest rate. The Cooperative had not borrowed any funds under the agreement at September 30, 2008 or 2007.

The Cooperative has a \$50,000 business line of credit with Bank One, N.A. No funds had been borrowed under this agreement at September 30, 2008 and 2007.

13. Deferred Credits

Deferred credits consisted of the following:

	September 30,	
	2008	2007
Unclaimed Memberships and Deposit Refunds	\$ 7,781	\$ 7,214

14. Litigation

There is no litigation pending against the Cooperative at September 30, 2008, that would have a material effect on the financial statements.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

15. Pension Benefits and Benefits to Retirees

Pension Benefits

Substantially all employees of the Cooperative participate in the National Rural Electric Cooperative Association (NRECA) Retirement & Security Program (a defined benefit plan) and the 401(K) Savings' Plan (a defined contribution plan). The plans are qualified and tax exempt under the Internal Revenue Code. In these multi-employer plans, which are available to all NRECA member cooperatives, the accumulated benefits and plan assets are not determined or allocated separately by individual employer.

The Cooperative makes monthly contributions to the retirement and security plan equal to the amounts accrued for pension expense. The pension cost for the Cooperative for the plan for the years ended September 30, 2008 and 2007, was \$412,999 and \$293,633, respectively.

The pension cost for the 401(K) Savings Plan was \$92,423 and \$66,211 for the years ended September 30, 2008 and 2007, respectively.

Benefits to Retirees

The Cooperative provides post-retirement medical and life insurance benefits for eligible employees and their dependents through a plan with NRECA (National Rural Electric Cooperatives Association). For purposes of this statement, the written plan in effect is the substantive plan, and is considered a defined benefit plan.

Summary of the Plan

The retiree medical plan is a Preferred Provider Organization. Eligibility for retirement benefits are currently retired, surviving spouse, or an active employee age 55 with 10 years of service by July 1, 2001. Active directors and spouses of future retirees will not become eligible for postretirement benefits.

The retiree contributes to the benefit plan based on the following schedule of years of service:

<u>Service</u>	<u>Contributions</u>
0-9	100.00%
10-14	66.67%
15-19	33.33%
20+	0.00%

The Cooperative contributes the same amount for the retiree's dependent or surviving spouse as for the retiree.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Effective October 1, 1995, the Cooperative adopted FASB Statement No. 106 "Employers' Accounting for Post-retirement Benefits Other Than Pension." Statement 106 requires that the cost of post-retirement medical benefits be recognized on the accrual basis as employees render service to earn the benefit. In addition, a transition obligation which reflects the accumulated liability up to the date of adoption of FASB 106 has been calculated and totals \$283,008. The Cooperative has elected to amortize and recognize this liability over 20 years resulting in an annual charge of \$18,868.

Net periodic post-retirement medical care costs for years ending September 30, 2008 and 2007, consisted of the following components:

	September 30,	
	2008	2007
I) Net Post-retirement Benefit Cost		
Interest Cost	\$ 70,493	\$ 87,997
Amortization of Transition Obligation	18,868	18,868
Amortization of Actuarial Loss	50,985	73,823
Total Expense	<u>\$ 140,346</u>	<u>\$ 180,688</u>
II) Accumulated Post-retirement Benefit Obligation (APBO) Reconciliation:		
APBO Balance at Beginning of Year	\$ 1,442,711	\$ 132,621
Total Expense	140,346	180,688
Amount Recognized as Accumulated Other Comprehensive Loss	(293,479)	1,227,489
Benefits Paid	<u>(95,634)</u>	<u>(98,087)</u>
Net Post-retirement Benefit Liability at Year End	<u>\$ 1,193,944</u>	<u>\$ 1,442,711</u>
III) Reconciliation of Funded Status		
APBO	\$ 259,934	\$ 215,222
Unrecognized Transition Obligation	132,064	150,932
Unrecognized Actuarial Loss	801,946	1,076,557
Accrued Post-retirement Benefit Cost	<u>\$ 1,193,944</u>	<u>\$ 1,442,711</u>
IV) Amounts Recognized as Accumulated Other Comprehensive Income		
Unamortized Actuarial Loss	\$ 132,064	\$ 1,076,557
Unrecognized Transition Obligation	801,946	150,932
Other Comprehensive Loss	<u>\$ 934,010</u>	<u>\$ 1,227,489</u>

The information is based on the most recent USI Consulting Group valuation calculated as of October 1, 2007.

The Cooperative funds the retiree health care premiums on a cash basis and in 2008 and 2007 paid \$95,634 and \$98,087, respectively, for retirees' health care coverage.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

The weighted-average discount rate used to develop the accumulated post-retirement benefit obligation was 6.17%. The assumed health care cost trend rate is eight percent for 2008. If health care cost trend rate assumptions were increased by one percent, the accumulated post-retirement benefit obligation would be increased by approximately \$112,545. The effect of this change on the sum of the service cost and interest cost components for the first year would be an increase of approximately \$9,040.

The estimated actuarial loss for the post-retirement medical benefit plan that will be amortized from accumulated other comprehensive income into net post-retirement benefit cost over the next fiscal year is a credit of \$75,357. The amount of the transition obligation that will be amortized from accumulated other comprehensive income into net post-retirement benefit cost over the next fiscal year is an expense of \$18,868.

On September 29, 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 158, *Employers' Accounting for Defined Benefit Pension and Other Post-retirement Plans – an amendment of FASB Statements No. 87, 88, 106, and 132(R)*. SFAS No. 158 requires an employer that sponsors a defined benefit post-retirement plan to report the current economic status (the overfunded or underfunded status) of the plan in its balance sheet, to measure the plan assets and plan obligations as of the balance sheet date, and to include enhanced disclosures about the plan. The Cooperative adopted the recognition and disclosure provisions of SFAS No. 158 for the fiscal year ending September 30, 2008. The Cooperative will be required to adopt the measurement date provision for the fiscal year ending September 30, 2009.

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

2008	\$98,598
2009	99,778
2010	98,686
2011	96,342
2012	93,061

16. Related Parties

The Cooperative is represented on the Board of Directors of Arizona Electric Power Cooperative, Inc. (AEPCO) and purchases all of its electric power from AEPCO. Margins earned by AEPCO have been allocated to Graham County Electric Cooperative, Inc., and are reflected under investment in associated organizations on the balance sheet.

In addition, Graham County Electric Cooperative, Inc. (GCEC) is related by having almost identical Boards of Directors with Graham County Utilities, Inc. (GCU). GCEC is a Class "A" Member of GCU, having paid a membership fee of \$5,000.

GCEC provides administrative and general, management, operations, consumer accounting, and construction services to GCU under an operating and management agreement signed by both parties on June 20, 1989. Services are billed and accounted for under the terms of the agreement.

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

NOTES TO FINANCIAL STATEMENTS

Intercompany balances between the two cooperatives are summarized as follows:

	September 30,	
	<u>2008</u>	<u>2007</u>
Graham County Electric Cooperative, Inc.		
Accounts Payable	\$	\$ (26,193)
Accounts Receivable	817,698	
Note Receivable	<u>59,675</u>	<u>95,096</u>
Net Due from Affiliated Cooperative	<u>\$ 877,373</u>	<u>\$ 68,903</u>
Graham County Utilities, Inc.		
Accounts Receivable	\$	\$ 26,193
Accounts Payable	(817,698)	
Note Payable	<u>(59,675)</u>	<u>(95,096)</u>
Net Due to Affiliated Cooperative	<u>\$ (877,373)</u>	<u>\$ (68,903)</u>

17. Commitments and Contingencies

As previously mentioned in Note 1, Graham County Electric Cooperative is the guarantor of Graham County Utilities, Inc. mortgage note payable to CFC.

The Cooperative has executed a contract to purchase all of its electric power requirements from Arizona Electric Power Cooperative, Inc. (AEPCO). The contract is effective through December 31, 2050.

The Cooperative with other Class "A" members of AEPCO has guaranteed to provide its share of power to Salt River Project in the event that AEPCO cannot perform under its firm power agreement.

ACCOMPANYING INFORMATION

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**INDEPENDENT AUDITORS' REPORT ON
ACCOMPANYING INFORMATION**

Our audits of the basic financial statements presented in the preceding section of this report were made for the purpose of forming an opinion on such financial statements taken as a whole. The accompanying information shown on pages 18 through 21 is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

November 3, 2008

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

Schedule 1

ELECTRIC PLANT
FOR THE YEAR ENDED SEPTEMBER 30, 2008

	Balance 10/1/2007	Additions and Transfers	Retirements	Balance 9/30/2008
Intangible Plant	\$ 3,060	\$	\$	\$ 3,060
Transmission Plant				
Land and Land Rights	\$ 7,253	\$	\$	\$ 7,253
Station Equipment	144,717			144,717
Poles and Fixtures	1,643,066			1,643,066
Overhead Conductors and Devices	756,527			756,527
Total	<u>\$ 2,551,563</u>	<u>\$ 0</u>	<u>\$ 0</u>	<u>\$ 2,551,563</u>
Distribution Plant				
Land and Land Rights	\$ 47,810	\$	\$	\$ 47,810
Station Equipment	5,634,888			5,634,888
Poles, Towers, and Fixtures	6,510,663	250,018	66,343	6,694,338
Overhead Conductors and Devices	3,525,806	141,560	38,655	3,628,711
Underground Conductors	542,955			542,955
Underground Conductors and Devices	690,464	39,100		729,564
Line Transformers	6,023,764	507,711	26,214	6,505,261
Services	1,228,773	69,351	12,033	1,286,091
Meters	1,059,526	84,624	2,010	1,142,140
Installations on Consumers' Premises	209,024	533	2,260	207,297
Total	<u>\$ 25,473,673</u>	<u>\$ 1,092,897</u>	<u>\$ 147,515</u>	<u>\$ 26,419,055</u>
General Plant				
Land and Land Rights	\$ 50,394	\$ 7,200	\$	\$ 57,594
Structures and Improvements	324,366			324,366
Office Furniture and Equipment	37,802	11,357		49,159
Office Furniture and Equipment - Computer	180,958	35,210		216,168
Transportation	1,961,368	102,875		2,064,243
Store Equipment	2,587			2,587
Tools, Shop, and Garage Equipment	174,921	40,439		215,360
Laboratory Equipment	78,788	3,485		82,273
Power Operated Equipment	183,406			183,406
Communications Equipment	281,720	3,721		285,441
Miscellaneous Equipment	3,152			3,152
Total	<u>\$ 3,279,462</u>	<u>\$ 204,287</u>	<u>\$ 0</u>	<u>\$ 3,483,749</u>
Total Classified Plant in Service	\$ 31,307,758	\$ 1,297,184	\$ 147,515	\$ 32,457,427
Construction Work in Progress	(146,118)	1,701,452		1,555,334
	<u>\$ 31,161,640</u>	<u>\$ 2,998,636</u>	<u>\$ 147,515</u>	<u>\$ 34,012,761</u>

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC

Schedule 2

ACCUMULATED PROVISION FOR DEPRECIATION AND AMORTIZATION
FOR THE YEAR ENDED SEPTEMBER 30, 2008

	<u>Balance 10/1/2007</u>	<u>Depreciation Accruals</u>	<u>Retirements</u>	<u>Balance 9/30/2008</u>
Transmission Plant	\$ 733,717	\$ 69,968	\$ 125,154	\$ 678,531
Distribution Plant	\$ 7,869,996	\$ 766,260	\$ _____	\$ 8,636,256
General Plant	\$ 2,350,726	\$ 265,409	\$ _____	\$ 2,616,135
Total Classified Electric Plant in Service	\$ 10,954,439	\$ 1,101,637	\$ 125,154	\$ 11,930,922
Retirement Work in Progress	<u>(22,868)</u>	<u>_____</u>	<u>1,934</u>	<u>(24,802)</u>
Total Utility Plant	<u>\$ 10,931,571</u>	<u>\$ 1,101,637</u>	<u>\$ 127,088</u>	<u>\$ 11,906,120</u>

(1)

(2)

(1) Charged to Depreciation and Amortization Expense
Charged to Clearing and Other Accounts

\$ 940,139

161,498

\$ 1,101,637

(2) Cost of Units Retired
Less: Salvage and Other Credits in Excess of Cost of Removal

\$ 147,515

(20,427)

\$ 127,088

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

Schedule 3

ADMINISTRATIVE AND GENERAL EXPENSES
SEPTEMBER 30, 2008 AND 2007

	September 30,		Increase
	<u>2008</u>	<u>2007</u>	<u>(Decrease)</u>
Administrative and General Salaries	\$ 267,289	\$ 295,052	\$ (27,763)
Office Supplies and Expense	152,321	129,730	22,591
Outside Services Employed	77,907	83,423	(5,516)
Property Insurance	9,705	10,784	(1,079)
Injuries and Damages	50,911	56,562	(5,651)
Employee Pension and Benefits	125,996	119,440	6,556
Regulatory Commission Expense	27,151	28,232	(1,081)
Miscellaneous General Expense	145,832	149,577	(3,745)
Rents	11,058	15,192	(4,134)
Maintenance of General Plant	<u>89,464</u>	<u>54,990</u>	<u>34,474</u>
Total	<u>\$ 957,634</u>	<u>\$ 942,982</u>	<u>\$ 14,652</u>

GRAHAM COUNTY ELECTRIC COOPERATIVE, INC.

Schedule 4

FIVE YEAR COMPARATIVE STATEMENT OF REVENUES AND EXPENSES

	Years Ended September 30,				
	2008	2007	2006	2005	2004
OPERATING REVENUES	\$ 17,267,145	\$ 16,287,421	\$ 13,962,428	\$ 11,364,581	\$ 11,406,541
OPERATING EXPENSES					
Purchased Power	\$ 11,736,801	\$ 11,330,034	\$ 9,359,803	\$ 7,123,301	\$ 7,228,900
Operation	591,612	581,729	504,795	478,522	455,830
Maintenance	1,457,094	1,495,928	1,273,325	949,046	1,148,745
Customer Accounts	425,405	399,683	357,972	307,294	341,966
Administrative and General	957,634	942,982	813,419	830,542	744,927
Depreciation and Amortization	940,139	899,353	853,484	728,601	686,753
Other Interest and Deductions	21,226	22,533	21,932	20,864	21,875
Total Operating Expenses	\$ 16,129,911	\$ 15,672,242	\$ 13,184,730	\$ 10,438,170	\$ 10,628,996
OPERATING MARGINS - Before Fixed Charges	\$ 1,137,234	\$ 615,179	\$ 777,698	\$ 926,411	\$ 777,545
Interest - Long-Term Debt	1,037,979	1,004,064	989,919	901,884	670,341
OPERATING MARGINS (LOSS) - After Fixed Charges	\$ 99,255	\$ (388,885)	\$ (212,221)	\$ 24,527	\$ 107,204
Other Capital Credits	2,006,274	118,818	117,853	81,524	65,829
NET OPERATING MARGINS (LOSS)	\$ 2,105,529	\$ (270,067)	\$ (94,368)	\$ 106,051	\$ 173,033
NONOPERATING MARGINS	761,941	103,996	95,430	65,915	47,112
NET MARGINS (LOSS)	\$ 2,867,470	\$ (166,071)	\$ 1,062	\$ 171,966	\$ 220,145

COMPLIANCE AND INTERNAL CONTROL SECTION

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**LETTER TO BOARD OF DIRECTORS REGARDING POLICIES
CONCERNING AUDITS OF CFC BORROWERS**

Board of Directors
Graham County Electric Cooperative, Inc.
Pima, Arizona

We have audited, in accordance with auditing standards generally accepted in the United States of America, the financial statements of Graham County Electric Cooperative, Inc., for the year ended September 30, 2008, and have issued our report thereon dated [Date].

In connection with our audits, nothing came to our attention that caused us to believe that the Cooperative failed to comply with the terms of Article V of the National Rural Utilities Finance Corporation Loan Agreement insofar as they relate to accounting matters. However, our audits were not directed primarily toward obtaining knowledge of such noncompliance.

The Cooperative's accounting and reporting procedures were considered adequate in all material respects. The records were maintained in accordance with the prescribed Uniform System of Accounts. The procedures used in accounting for material, transportation, labor, and overhead costs provide a fair distribution of these costs to construction, retirement, and maintenance or other expense accounts. However, certain items were noted as explained below:

- Continuing property records have not been established for transmission and distribution plant accounts. Retirements from plant are recorded at estimated cost.
- Subsidiary detail records have not been established and maintained for all general plant accounts.
- Patronage capital subsidiary records have not been reconciled with the appropriate general ledger control accounts for several prior years.

During the year ended September 30, 2008, the Cooperative was advanced \$2,000,000 in loan funds for construction purposes.

This report is intended solely for the information and use of the Board of Directors and management of Graham County Electric Cooperative, Inc. and the National Rural Utilities Cooperative Finance Corporation and is not intended to be and should not be used by anyone other than these specified parties.

Bolinger, Segars, Gilbert & Moss LLP

Certified Public Accountants

November 3, 2008