

ONE
MISSION | CO-OP

2014

**ANNUAL
REPORT**



Homer Electric
Association, Inc.

MESSAGE from the President & General Manager

On behalf of the Board of Directors and staff at Homer Electric Association (HEA), we would like to thank the members of Homer Electric Association for their on-going support as HEA transitions into a new era of independent power generation.

On January 1, 2014, HEA took a historic step forward, moving from a distribution cooperative to a full-fledged distribution, generation and transmission cooperative. This momentous occasion was accomplished through several years of study, planning, construction and implementation. The end result of all this work is a fully integrated cooperative that is committed to providing excellent service to its members.

When HEA “flipped the switch” on January 1, 2014, we were fully confident that the decision to construct and operate power plants on the Kenai Peninsula was the right decision. After a year of experience, we are more assured than ever that being independent is the best option for HEA and its members.

On the generation side of the cooperative, the Nikiski Combined Cycle Plant is operational and supplying Homer Electric Association with the majority of its power generation needs. The plant features a steam turbine in conjunction with a natural gas turbine that can produce a total of 80 megawatts of power. It’s important to note that the steam turbine is able to use waste heat to produce 18 megawatts of power without using any additional natural gas.

The Soldotna Combustion Turbine Plant was completed in the summer of 2014 and is now on line to provide additional power to the system when it’s needed. The plant features a very efficient natural gas fired LM 6000 turbine that can produce 48 megawatts of power.

Our third generation asset is the Bernice Lake Power Plant in Nikiski. This plant, purchased from Chugach Electric in 2011, has been overhauled and all three natural gas turbines are now operational. The 80 megawatt plant is available to provide peaking and reserve capacity for Homer Electric Association.

The challenges and opportunities in front of us are exciting. Homer Electric Association will continue to seek out potential natural gas contracts that will meet our long term needs and provide rate stability. At the same time, we are investigating an array of renewable energy possibilities

that will help us reach the goal of producing 22% of HEA’s power from renewable resources by 2018.

While we have spent a great deal of time and effort on the power generation side of the cooperative, our day-to-day operations continue to be a key component of Homer Electric Association. Exemplary customer service, whether it’s with a member in our lobby, on the phone, or in the field, is one of our top priorities. Each and every interaction we have with our membership is valued and we are committed to providing the best service possible.

At Homer Electric Association, we are always prepared for the unexpected and in 2014 that came about in the form of the Funny River Fire. The fire destroyed over 200,000 acres of land and burned right up to HEA’s transmission lines. Throughout the event, HEA worked closely with all the agencies involved in the response effort. The ability to use HEA’s improved transmission system and new power plants was instrumental in maintaining electric service and providing a high level of safety to the crews fighting the fire. While the fire could have had a devastating impact on the communities, it was an opportunity for Kenai Peninsula residents to come together and support each other. HEA was proud to be part of that community effort.

In the following pages, you will read in more detail about the projects and accomplishments of 2014. We look forward to another exciting year in 2015, with our goals focused on providing safe, reliable and reasonably priced electric service.

Thank you for being an involved and active member of Homer Electric Association.



Brad Janorschke
General Manager



Dick Waisanen
President



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ONE MISSION

This past year has been a year of transformation for your local, member-owned electric cooperative. It has brought together a diversity of departments, professionals, and industry experts to complete one mission – to provide safe, reliable electric service as a fully integrated electric cooperative.

ONE CO-OP

It is that mission which motivates Homer Electric's board of directors, management, and employees to embrace the cooperative spirit and work together as one cohesive team.

Following is a recap of significant projects and highlights from 2014.

2014 Year in Review

A TURNING POINT IN POWER PRODUCTION

A major historical milestone occurred on January 1, 2014, when Homer Electric began producing and supplying Homer Electric's members with its own generated electricity. The integration of a complex system of power generation, a transmission system, and a distribution system had come to fruition.

The Nikiski Combined Cycle Plant, the cornerstone of our generation, provides the majority of our power generation needs. Moreover, by utilizing a steam turbine, coupled with the natural gas turbine, the plant can produce 18 MW of power without using additional gas. Tours of the Nikiski plant were hosted throughout 2014 to commemorate the

event and inform members.

Also in 2014, many departments worked together to complete the Soldotna Combustion Turbine Plant which provides a valuable, economical source of back-up power. The completion of this project signified the achievement of many interdepartmental goals. Homer Electric hosted a tour of this new facility in conjunction with its area meeting in Sterling last October.

Last, but not least, the other generation component is the Bernice Lake Power Plant in Nikiski which provides up to 80 megawatts for peaking and reserve capacity. Tours of this plant were also conducted in 2014 in conjunction with the Nikiski Plant tours.



Soldotna Substation Upgrades

Located at the heart of HEA's transmission system, completion of this critical project was imperative to improving HEA's ability to reliably transfer power both across and off the Kenai Peninsula. This project included the replacement of outdated system protection equipment, the retirement of a 69 kilovolt (kV) transmission system, the installation of a new 115/25 kV power transformer, and an expansion of the previous facility to accommodate the newly constructed

115 kV transmission line from Soldotna to Nikiski. Perhaps the most tedious and complex part of the substation project was the successful reconstruction of the protection and control system – all accomplished without taking the substation out of service. New equipment utilizing modern microprocessor-based equipment replaced some of the existing equipment dating back to the 1960s.



Renewable Energy

A portion of Homer Electric's power generation portfolio comes from our 12 percent share of the output from the Bradley Lake Hydroelectric plant located 27 miles from Homer at the head of Kachemak Bay. The State owned facility is the largest hydroelectric facility in Alaska and serves six electric utilities, from Homer north to Fairbanks. Homer Electric has a contract with the State of Alaska to operate and maintain the facility which serves over 70 percent of the state's population. This hydro power source has been a clean and affordable component of Homer Electric's power portfolio.

Homer Electric and its subsidiary Kenai Hydro, LLC, continue to work toward licensing of a five megawatt hydroelectric project at Grant Lake near Moose Pass on the Kenai Peninsula. The proposed project will produce up to 19.5 gigawatt hours of electricity. After six years of evaluation, researching and studies (including aquatic, water, terrestrial, cultural, visual, and recreational), an engineering analysis, and collaboration with stakeholders, Kenai Hydro wrapped up most of the required research in 2014. Presently we are on track to file a final license application to the Federal Energy Regulatory Commission (FERC) late in 2015.

Homer Electric continues to investigate opportunities in other renewable ventures such as landfill gas, solar, and tidal projects to reduce our dependence on natural gas.

ENGINEERING & OPERATIONS: SYSTEM UPGRADES & MAINTENANCE

Homer Electric is committed to providing safe, reliable electric service to its members on a daily basis. With the power generation milestones achieved over the last few years, Homer Electric has worked to maintain, upgrade or replace its aging core systems. The following are highlights of this past year's efforts toward those accomplishments.

Transmission Line Upgrade Improves Reliability

Homer Electric completed its transmission line upgrade project in 2014. This new, single transmission line results in a significant reduction in outage time or, at best, no outage impact to the north end of our service territory. The upgraded 69 kV transmission line to 115 kV from Nikiski to Soldotna will improve reliability. In 2014, Homer Electric crews installed new poles and wires, as well as a new fiber optic line, along the 7.3 mile segment from the Beaver Creek Substation to the Soldotna Substation. The route of the project traversed challenging wetlands which required non-traditional means of setting poles during the winter months.

East End Road Relocation Project

This project consisted of relocating approximately two miles of three-phase overhead power lines to accommodate the rebuilding and expansion of the East End Road in Homer. New poles and wires replaced the aging equipment. In addition, the wire size was upgraded to support future power load growth along East End Road.

Cable Injection

Homer Electric has made good progress addressing the million feet of aging underground cable throughout the cooperative's system. In its seventh year, the cable injection project has been a great success. Injecting the cable increases its reliability and extends the life of the underground cable an additional 40 years. In 2014, Homer Electric injected almost as much footage, at the lowest cost to date, than in previous six years combined. Prior to 2014, Homer Electric injected 174,976 feet of underground cable. Last year alone, 155,162 feet of cable was injected.



Rights-of-Way Clearing

Homer Electric has a proactive right-of-way clearing program to protect our power lines and keep power flowing safely to your homes and businesses. If not cleared, inclement weather can cause outages and create safety hazards. In addition, a well cleared right-of-way provides safe and quick access for line crews to respond to outages.

The value of a well cleared right-of-way was evident in the Funny River Fire that encompassed over 200,000 acres of land last summer. The fire came very close to Homer Electric's transmission lines, but there was no significant damage to utility structures. Your

cooperative's diligent clearing of these corridors over the years has paid off – the well-maintained rights-of-ways near HEA transmission lines provided a natural fire break. In addition, the corridors served as a safe passage for fire crews to continue to fight the fire on the ground.

Furthermore in 2014, Homer Electric worked to re-clear and re-establish access to 18 miles of right-of-way in the Kenai Mountains that had been neglected for many years due to terrain and permitting difficulties.

Online Outage Map

Homer Electric now provides a real-time outage map on the cooperative website as a courtesy to keep our members informed. The map provides a visual snapshot of the affected outage area(s), the approximate number of affected customers, and the

duration of the latest outage. The outage map is also available on HEA's mobile app on iPhone and Android devices. The viewable map is for reviewing information only and not used to report outages. To report an outage, call 1-888-8OUTAGE.



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MEMBER RELATIONS: CONTINUED CALIBER OF CUSTOMER SERVICE

Homer Electric has come a long way since first energizing in 1950 and serving 56 members of the cooperative. Today Homer Electric serves almost 23,000 members and employs 150 employees. The management and staff at your local electric cooperative are not only committed to the core business of providing electric service, but also to foster positive experiences and relationships when supporting the member – whether it's in the field, over the phone, in the office, or at a cooperative sponsored event.



Old Fashioned Connections at Community Meetings, Energy Fairs

While the Digital Revolution has simplified and provided ease in business transactions, HEA still values the one-on-one time spent with its members. Each year Homer Electric hosts several events throughout the Kenai Peninsula and looks forward to the personal connections with its members at the annual community meetings and Energy & Conservation Fairs. The community meetings are an opportunity to visit with members in an informal setting, provide a family-style dinner, and present a recap of current projects and activities. These meetings

have been very popular with members and they provide the Homer Electric Board of Directors and management staff the opportunity to shake hands and visit with our members up close and personal.

Homer Electric's Energy & Conservation Fairs were hosted in Homer and Kenai for the seventh consecutive year and offered members a one-stop information venue for energy efficiency and conservation programs, services, and products. Energy experts were on hand for demonstrations, resource information, and advice.



Commitment to Community and Education

Homer Electric takes pride in providing several community outreach programs for our local youth each year to promote higher education, cooperative principles, energy conservation, and electrical safety. These programs include academic scholarship awards, an all-expense paid trip to the Idaho Youth Rally, an Energy Efficiency & Conservation student contest, and an

Electrical Safety Poster student contest.

In addition to providing educational opportunities to our local youth, one of Homer Electric's goals is to keep our members informed and educated on key industry and cooperative topics. Whether it's through our community outreach programs, area-wide meetings, newsletters, advertisements, the website or through our day-to-day conversation with members, HEA is committed to providing up-to-date and timely communications to its members. HEA was honored to be acknowledged for its communications efforts by the Northwest Public Power Association (NWPPA).

- 2014 Northwest Public Power Association (NWPPA) Excellence in Communications Awards:
 - o 1st place for the Kilowatt Courier, HEA's member newsletter
 - o 1st place in advertising campaign
 - o 3rd place in photography
 - o 2014 Tom Hougan Award for best overall communication effort of the year



COOPERATIVE SPIRIT STARTS WITH EMPLOYEES

Over the years, Homer Electric employees strive to make a difference inside and outside the office, whether it's through volunteering, recycling, or supporting community civic programs. The following are just a few examples of how Homer Electric Association and its employees promoted the cooperative spirit in our communities in 2014:

- Homer Electric employees voluntarily contributed a record breaking \$12,000 to the Kenai Peninsula United Way fundraiser
- The Cooperative recycled 803.5 pounds of dated electronics in the 9th annual Homer Electronics Recycle Event
- Many employees participated in the Relay for Life in Soldotna and in Homer

Homer Electric employees are huge assets to the Cooperative and a vital part of our community – in your church, as your child's coach, performing in our theaters, as your hockey teammate, on service boards, volunteering in schools, and contributing in various community civic groups. Homer Electric is grateful for its team of professional and compassionate employees. Thank you for making a difference.

Employment Anniversaries in 2014

Congratulations to the following employees who have served our membership over many years in the office, in the field, and behind the scenes!

Jeanette Dick	20 years	Heather Smith	10 years
Anne Huhndorf	10 years	Nathan Smith	10 years
Brad Janorschke	10 years	Robert Tachick	10 years
Jeff Leete	10 years	Bobby Taylor	10 years
John McCullough	10 years		



2014 TREASURER'S REPORT



David B. Thomas
Treasurer

Homer Electric Association is committed to establishing electric rates that allow us to provide reliable electricity at fair and reasonable prices to our members.

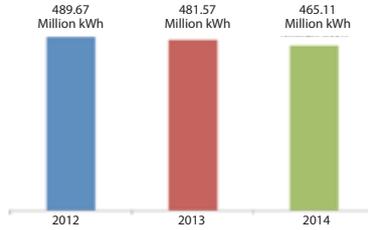
Homer Electric concluded the year 2014 with total consolidated revenues and non-operating income of \$95 million. That, combined with total consolidated costs of electric service of \$92 million, resulted in a positive margin of \$3 million. The following is a financial summary for the year.

System

There were 33,392 services in place at year end. The net increase of 310 services in 2014 was a 1% increase over 2013 services.

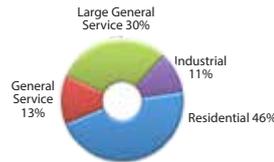
Energy Sales

Homer Electric sold 465 million kilowatt-hours of electricity in 2014, a decrease of 3% from 2013. The decrease in sales was primarily due to a 5% decrease in the residential sales class and a 3% decrease in the small commercial class.



Revenues

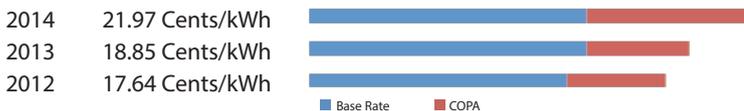
Revenue generated from energy sales totaled \$91 million, an increase of 13% from the previous year.



Cost of Power Adjustment (COPA)

This is the blended rate component that reflects changes in the cost of purchased power due primarily to the fluctuating cost of fuel. The cost of power adjustment increased from 7.139 cents per kWh on January 1, 2014 to 8.194 cents per kWh on December 31, 2014.

Blended Rate per Residential kWh (as of December 31)



Expenses

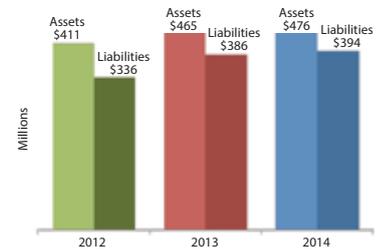
In 2014, total expenses were \$92 million up \$2 million or 3% from 2013. Purchased power costs decreased \$8 million and comprised 41% of the total costs. Operating costs, depreciation expense, and interest expense increased \$10 million or 22% from 2013 expenses. The shift in costs from purchased power to operating costs, depreciation expense, and interest expense is due to the wholesale power contract with Chugach Electric Association expiring December 31, 2013 and Homer Electric generating and supplying its own power January 1, 2014.

Key Ratios

The equity-to-total-assets ratio measures the percentage of total assets owned by the members and is used as an indicator of financial health. HEA's ratio was 36% at year end. This ratio at the end of 2013 was 35%. The same ratio for Alaska Electric & Energy Cooperative (AEEC), HEA's subsidiary which owns our generation and transmission assets, was 10%, the same as the prior year. Both ratios are in compliance with our lender's debt covenant requirements.

Total Assets and Total Liabilities

Total assets were \$476 million in 2014. This is a 2% increase over \$465 million in 2013. Over a two-year period, total assets have increased 16%. Total liabilities were \$394 million in 2014. This is a 2% increase over \$386 million in 2013. Both asset and liability increases are primarily due to completing the financing of New Generation asset additions.



Capital Credits

Capital credits represent Homer Electric members' share of equity in the utility and are one of the benefits of being a member of an electric cooperative. Capital credits are based on margins, which are the difference between total expenses and total revenues of the cooperative. Each year, HEA allocates margins to its members in proportion to the amount they paid for electric service.

Annually, the Board of Directors considers separately the general retirement of capital credits. There were no general retirements in 2014, as we were investing in the construction of our new generation assets. This is similar to saving for a down payment on a home or choosing to take fewer vacations to pay for college costs out of pocket.

However, in 2014, the Board of Directors approved the retirement of \$133,370 in Capital Credits paid to Estates.

Financial Goals

In conclusion, Homer Electric met its financial goals of a positive margin and a stable equity-to-assets ratio in 2014. HEA's careful financial management and resulting strong financial performance allows HEA to continue to meet the energy needs of our members through innovative energy solutions, while ensuring as fair and reasonable rates as possible.

WHERE YOUR DOLLAR WENT

Purchased Power	41¢
Depreciation & Amortization	17¢
Interest & Taxes	15¢
Maintenance & Operation of Lines and Production	12¢
Administrative & General	10¢
Consumer Accounts Expense	5¢



Homer Electric Association, Inc. and Subsidiary

Consolidated Balance Sheets

December 31,	2014	2013
Assets		
Utility plant, at cost:		
Electric plant in service	\$ 566,514,237	\$ 471,015,472
Electric plant held for future use	1,162,802	3,447,637
Construction work in progress	11,333,638	93,276,084
Total utility plant, at cost	579,010,677	567,739,193
Less accumulated depreciation and amortization	(161,903,809)	(158,256,729)
Net utility plant	417,106,868	409,482,464
Other assets and investments:		
Investments in associated organizations	22,660,049	20,740,154
Notes receivable, net of current portion	400,019	567,262
Non-utility property, net of accumulated depreciation of \$442,243 (\$406,547 in 2013)	302,869	338,565
Total other assets and investments	23,362,937	21,645,981
Current Assets		
Cash and cash equivalents	10,791,429	6,748,714
Accounts receivable, less allowance for doubtful accounts of \$94,691 (\$112,660 in 2013)	7,636,287	9,400,153
Unbilled revenue	5,776,145	4,823,966
Materials, fuel and supplies inventory	5,894,047	6,629,038
Notes receivable, current portion	524,751	524,592
Other current and accrued assets	448,617	371,871
Total Current Assets	31,071,276	28,498,334
Deferred charges	4,939,409	5,794,608
Total Assets	\$ 476,480,490	\$ 465,421,387

Homer Electric Association, Inc. and Subsidiary

Consolidated Balance Sheets, continued

December 31,	2014	2013
Equities and Liabilities		
Equities		
Memberships	\$ 55,835	\$ 58,630
Patronage capital	79,518,903	76,712,436
Other equities - donated capital	2,733,058	2,665,429
Total Equities	82,307,796	79,436,495
Long-term debt - mortgage notes payable	363,353,654	362,357,918
Current Liabilities		
Current portion of long-term debt	17,257,018	8,683,749
Accounts payable	7,804,078	9,524,543
Consumer deposits	1,193,441	1,125,062
Accrued payroll and benefits	2,687,007	2,630,792
Accrued taxes and other current liabilities	1,332,645	1,123,217
Total Current Liabilities	30,274,189	23,087,363
Deferred credits	544,851	539,611
Total Equities and Liabilities	\$ 476,480,490	\$ 465,421,387

Homer Electric Association, Inc. and Subsidiary

Consolidated Statements of Operations and Patronage Capital

Years Ended December 31,	2014	2013
Operating Revenues	\$ 91,893,737	\$ 91,940,785
Operating Expenses		
Purchased power costs	37,949,847	45,465,861
Transmission expense	1,085,668	967,979
Distribution operations	2,091,840	2,290,067
Distribution maintenance	4,492,616	5,643,658
Production maintenance	3,470,109	2,243,190
Consumer accounts	3,552,880	3,664,410
Customer service and information	574,307	540,338
Sales expense	118,098	111,389
Administrative and general	8,526,867	8,482,243
Depreciation and amortization	15,175,690	10,688,475
Taxes	231,230	238,595
Miscellaneous	429,351	171,722
Total Operating Expenses	77,698,703	80,507,927
Operating margins before fixed charges	14,195,034	11,432,858
Fixed Charges		
Interest on debt, net of capitalized interest	13,987,768	8,930,363
Allowance for funds used during construction	(153,443)	(671,472)
Net Fixed Charges	13,834,325	8,258,891
Operating margins after fixed charges	360,709	3,173,967
Patronage Capital Allocation	2,421,045	1,695,468
Net operating margins	2,781,754	4,869,435
Nonoperating Margins		
Interest income	182,663	204,649
Other income (expense)	(24,580)	(35,106)
Total Nonoperating Margins	158,083	169,543
Net margins	2,939,837	5,038,978
Patronage capital, beginning of year	76,712,436	71,785,269
Less retirement of patronage capital credits	(133,370)	(111,811)
Patronage Capital, end of year	\$ 79,518,903	\$ 76,712,436