One of HEA Board of Directors’ biggest surprises of late, our members’ vote in late 2016 to reject independence from the Regulatory Commission of Alaska (RCA). In other words, “Local Control.” Among other things on the Board, we have learned to, “always remember to test our assumptions.” Before engaging in the Local Control vote, we had not stopped around our thoughts to share our considerations and get feedback. Your Board continues to learn and you will see the value of learning, embodied in each of three long-term initiatives identified at a valuable strategic planning session in October 2017.

The electric utility industry around the world, in the U.S., and in Alaska faces a myriad of social and technological drivers for change that have potential to upend our economic environment at intervals of three to 15 years. For example, in 2010 the RCA decided to decouple the price of Cook Inlet natural gas from lower-48 Henry Hub indexed prices. Over the next five years, the new rate design predictably led to higher costs for natural gas, roughly doubling what we paid in previous years and the ability for utilities to secure financially attractive long-term supply contracts diminished greatly. With the days of securing multiple decades-long natural gas contracts (with commensurate price stability and predictability) behind us, short-term natural gas contracts have added uncertainty and risk in our efforts to deliver members reliable electricity at stable prices. As a result of the increased risk, HEA’s efforts moving forward and reflected in our previously mentioned strategic plan include continuing the efforts to increase the efficiency of existing assets and secure additional resources to generate electricity that are not dependent on fossil fuel.

Turning to the future, your Board sees several short-term and long-term strategic initiatives. Our first strategic initiative is to reduce our dependence on natural gas and diversify our primary energy source portfolio. This means increasing efficiency measures and adopting renewables when and to the extent we can do so, wisely.

The second strategic initiative is to engage effectively in on-going conversations about re-structuring management of Alaska’s inter-connected Railbelt electrical grid. This has involved a large-scale collaborative effort among the utilities to analyze potential benefits that might accrue by re-organizing the methods we use to deliver wholesale power on the Railbelt. Raiebait, Raiebait, co-op conversations about re-organization are both arcane and complex — and not entirely without political aspects. In addition, most Railbelt-level engagements occur in Anchorage, this already involves increased travel costs for management, staff, and your Board.

The third strategic initiative we identified pertains to your Board’s desire to improve communications with you, our members. Better yet, improve on a two-way communication so that we can provide better service and make better decisions. We would like to share information that you might find helpful and engages you, to help us in an informed way in our decision-making challenges. When the HEA staff and Board can work with you effectively, we can be MORE POWERFUL TOGETHER.

In closing, we would like to acknowledge HEA’s hardworking staff and Board for an outstanding year as we have accomplished another successful year and we look forward to numerous opportunities in the future.

Dan Chay, HEA Board President
Brad Janorschke, General Manager

Mission To safely provide reliable electricity to our members and our community through superior customer service and innovative energy solutions at fair and reasonable prices.

Vision For our members and community to benefit from reliable electricity and superior customer service through Homer Electric’s leadership in the application of innovative energy solutions at fair and reasonable prices.

MORE POWERFUL TOGETHER

Dan Chay
HEA Board President

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MORE POWERFUL TOGETHER

2018–2020 STRATEGIC PLAN INITIATIVES

The following strategic initiatives were developed by the Homer Electric Association, Inc. (HEA) board and management team and were based on an in-depth review of internal capabilities and external business drivers. These three initiatives represent the key areas of focus for our team, for the next three years.

1. Reduce HEA’s overall dependence on natural gas through:
   a) Adoption of increased efficiency measures;
   b) Use of alternative energy sources, including specifically renewables; and
   c) Adoption of strategies to control HEA’s future price exposure.

2. Engage with the other Railbelt utilities, regulators and other key third parties to best position HEA in the evolution of Railbelt operations. HEA Board of Directors will identify and develop a plan to engage in peer-to-peer events to further discussion and cooperation in Railbelt development.

3. Develop and implement a plan to increase engagement with HEA members, of all ages through education, learning, and communication about cooperative operations, strategic initiatives, and the energy industry, utilizing innovative technology platforms.

Homer Electric Association, Inc. (HEA) is more than just a utility provider. Homer Electric employees are committed to building even stronger connections with our members and the communities we serve. We are a lifestyle. We are cooperative. We are more powerful together.

Innovative Homer Electric is more than an energy company. We offer solutions and find alternatives. Your cooperative listens to our members’ ideas and goals. Homer Electric is more than power poles and wires. We are building a launch pad for future economic growth. We are each part of the local lifeline to support and strengthen our communities. We are cooperative power. We are more powerful together.

Expert Your electric cooperative is your resource for power, information on the energy industry and creates learning opportunities for our members of all ages throughout the year. We are cooperative power. We are more powerful together.

Local Homer Electric members are more than just customers. We are local. We are neighbors, businesses, schools, organizations — we are partners with one another. We offer community outreach programs and support local non-profits. Homer Electric is the Kenai Peninsula’s advocate within Railbelt utility issues. We are cooperative power. We are more powerful together.
2017 YEAR IN REVIEW

One of Homer Electric’s strategic goals is to reduce our overall dependence on natural gas and continually make improvements to maximize efficient use of our existing infrastructure. Here are some highlights from our 2017 projects toward that goal.

Battle Creek Project
In an effort to increase the annual output of the state-owned Bradley Lake Hydroelectric Plant, the upcoming Battle Creek Project will divert runoff from the Battle Creek Glacier into Bradley Lake. The project will enable the facility, which currently produces the lowest cost power between Homer and Fairbanks, to increase its annual output by about 10% (enough to serve almost 5,500 homes) for the next 80 years. The roughly $48 million project would include a new 2.9 mile (enough to serve almost 5,500 homes) for the next 80 years.

Grant Lake Hydroelectric Project Update
The Federal Energy Regulatory Commission (FERC) continued its assessment of the Grant Lake Hydroelectric License Application. FERC issued two sets of Additional Information Requests (AIRs) and requested a field study to assess visual impacts to a section of the commemorative Iditarod National Historic Trail (INHT) near the proposed project. Homer Electric filed responses to the AIRs in April and September of 2017. After completing the required fieldwork and renderings, Homer Electric submitted the Final Study Report on the INHT Visual Resources Evaluation and expects a licensing decision from FERC in late 2018 or early 2019. Additionally, Homer Electric continued collaboration and consultation efforts with interested stakeholders, working with National Marine Fisheries Service and the U.S. Fish & Wildlife Service to develop and file a technical memo outlining the details of the Tailrace fish exclusion barrier.

Seldovia Plant Repower Project
The Seldovia Plant Repower Project was completed in 2017 to improve the backup plant reliability and resolve a number of operational and maintenance issues. The plant was redesigned to replace one of the existing generation units and replace the very old switchgear building. The facility provides back up power to Seldovia, Port Graham, and Nanwalek when power is lost from the Homer Electric system.

Advocating For Our Members: Big Year at the RCA for Gas Pipeline Tariffs
Representing and protecting Homer Electric’s interest at the Regulatory Commission of Alaska (RCA) is important to controlling the fuel component costs of a member’s power bill. Homer Electric intervened in the Kenai Beluga Pipeline (KBPL) rate case filed by Hilcorp at the RCA in 2016 and settled in early 2017. The settled rate to transport gas on this pipeline is estimated to save HEA over $1 million per year over the rate proposed in the filing. With the annual cost of fuel and fuel transportation costing our members about $33 million, the settlement reflects a three percent savings on the Cost of Power Adjustment (CPA) portion of members’ bills.

Also, as part of the negotiated settlement, HEA received a refund of $537,657 in over collected 2016 interim rates and interest.

HEA also participated in the ENSTAR rate case that culminated in a three-week hearing before the Commission in June of 2017. The settled rate case resulted in HEA ratepayers paying $60,000 less per year than what they were currently paying and over $75,000 per year less than ENSTAR’s proposed rates.

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**Treasurer’s 2017 Annual Report**

Organized as a rural electric cooperative, Homer Electric Association Inc. operates as a not-for-profit entity under section 501(c)(2) of the Internal Revenue Code. Established by the members to provide service at the lowest possible cost, any excess revenue (or margin) is used to improve service before it is eventually returned to members in the form of capital credit retirements. In April 2017, approximately 10,000 current and former members received $1.5 million in capital credit money. In 2017, Homer Electric’s financial position remained strong as we continued to work towards our mission of providing safe, reliable electricity at fair and reasonable prices to you, our members. Through diligent monitoring and testing, we continue to meet our financial goals with positive margins and favorable key ratios.

Homer Electric concluded the year 2017 with total consolidated assets of $472 million, total liabilities of $384 million, and a capital credit balance of $358 million. Despite a decrease of $36 million in the year, rate changes were stable and revenues held steady, which allowed for capital credits to be returned to members.

### Expenses

In 2017, total expenses were $462 million, an increase of almost $4 million or about four percent compared to 2016. Fuel and purchased power costs increased by $1 million and comprised 37 percent of total expenses. Operating costs increased almost five percent from 2016.

### Capital Credits

Capital credits represent Homer Electric members’ share of equity in the Cooperative 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, Homer Electric allocates margins to its members in proportion to the amount they paid for electric service during the year.

Annually, the Board of Directors considers the general retirement of capital credits. Healthy equity levels continue to allow HEA to retire capital credits. In 2017, the Board of Directors approved a $261,000 for the retirement of capital credits to estates of deceased members.

### Financial Goals

In conclusion, Homer Electric met its financial goals with positive margins and met required loan agreement ratios in 2017. Homer Electric’s financial management and resulting financial performance allow the Cooperative to continue to meet the energy needs of our members through innovative energy solutions, while ensuring fair and reasonable rates.

---

**Energy Sales**

<table>
<thead>
<tr>
<th>Fuel &amp; Purchased Power</th>
<th>Production</th>
<th>Distribution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industrial</td>
<td>479 kW</td>
<td>472 kW</td>
</tr>
<tr>
<td>Large General Service</td>
<td>477 kW</td>
<td>477 kW</td>
</tr>
<tr>
<td>General Service</td>
<td>476 kW</td>
<td>477 kW</td>
</tr>
<tr>
<td>Residential</td>
<td>477 kW</td>
<td>477 kW</td>
</tr>
</tbody>
</table>

---

**Where Your Dollar Went**

- **Electricity:** 70 percent
- **Fuel & Purchased Power:** 28 percent
- **Distribution:** 2 percent

---

**Homer Electric**

Homer Electric is committed to providing safe, reliable electricity at fair and reasonable rates to our members. Through diligent monitoring and testing, we continue to meet our financial goals with positive margins and favorable key ratios.

---

**Homer Electric**

Homer Electric is committed to helping build even stronger connections with our members and our local communities. One of the ways we are delivering this goal is by providing you with information, resources and services that are as reliable and useful as the electricity we supply. Homer Electric is your trusted information, resources and services that are as reliable and confident in the way we are delivering this goal is by providing you with connections with our members and our local communities. One of the ways we have connected with members and shared information on your cooperative, electrical safety, energy efficiency and new technologies:

- Community meetings in Soldotna, Port Graham, Ninilchik, Kaslof, Funny River, Sterling, and Nikiski.
- New Technology Workshops – Homer Electric hosted its first New Technology Workshop in November at the Kenai Peninsula College in Soldotna. The well-attended workshop provided an opportunity for members to learn more about solar energy, home energy efficiencies, heat pumps and electric vehicles.

---

**Local Cooperative Spirit**

Homer Electric is committed to providing several community outreach programs to promote higher education through our scholarships; cooperative principles through our Youth Rally; energy efficiency through our Power Pledge Program; safety through our Electric City school and fair demonstrations; and emerging technologies through our New Technology Workshops.

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

**Retirements:**

- Harvey Ambrose 8 years
- Gregory Fast 4 years
- Darlene Jonas 39½ years
- Marti McKeeny 16 years
- Roxanne Northcutt 10 years
- Maynard Smith 14 years
- Cindy Frazier 20 years
- Julia Climer 10 years
- Jesse Cress 10 years
- Kathy Heindl 10 years
- Barry Jackman 10 years
- Travis Kincad 10 years
- Sarah Lamb 10 years
- Diane Massengill 10 years
- Rosanne Northcutt 10 years
- Ed Pontious 10 years
- Nikki Rich 10 years
- Glenn (Sandy) West 10 years

**Anniversaries:**

- Glenn (Sandy) West
- Jim Seeley 26 years
- Ed Oberts 10 years
- Harvey Ambrose 8 years
- Harvey Ambrose 8 years
- Diane Massengill 10 years
- Travis Kincad 10 years
- Barry Jackman 10 years
- Sarah Lamb 10 years
- Kathy Heindl 10 years
- Cindy Frazier 20 years
- Julia Climer 10 years
- Jesse Cress 10 years
- Kathy Heindl 10 years
- Barry Jackman 10 years
- Travis Kincad 10 years
- Sarah Lamb 10 years
- Diane Massengill 10 years
- Rosanne Northcutt 10 years
- Ed Pontious 10 years
- Nikki Rich 10 years
- Glenn (Sandy) West 10 years
## Consolidated Balance Sheets

<table>
<thead>
<tr>
<th>December 31,</th>
<th>2017</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assets</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Utility Plant at Cost</td>
<td>$590,535,539</td>
<td>$579,216,752</td>
</tr>
<tr>
<td>Electric plant in service</td>
<td>1,166,067</td>
<td>1,166,067</td>
</tr>
<tr>
<td>Construction work in progress</td>
<td>7,866,936</td>
<td>10,943,553</td>
</tr>
<tr>
<td>Less accumulated depreciation and amortization</td>
<td>(196,451,530)</td>
<td>(184,967,399)</td>
</tr>
<tr>
<td>Total utility plant at cost</td>
<td>403,117,012</td>
<td>406,358,973</td>
</tr>
<tr>
<td>Construction work in progress</td>
<td>7,866,936</td>
<td>10,943,553</td>
</tr>
<tr>
<td>Electric plant held for future use</td>
<td>1,166,067</td>
<td>1,166,067</td>
</tr>
<tr>
<td>Electric plant in service</td>
<td>590,535,539</td>
<td>579,216,752</td>
</tr>
<tr>
<td>Investments in associated organizations</td>
<td>22,187,694</td>
<td>24,082,128</td>
</tr>
<tr>
<td>Other Assets and Investments</td>
<td>403,117,012</td>
<td>406,358,973</td>
</tr>
<tr>
<td>Total Current Assets</td>
<td>27,764,175</td>
<td>25,108,397</td>
</tr>
<tr>
<td><strong>Deferred Charges</strong></td>
<td>3,743,407</td>
<td>5,402,853</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td>$457,329,973</td>
<td>$461,802,977</td>
</tr>
</tbody>
</table>

## Consolidated Statements of Operations and Patronage Capital

<table>
<thead>
<tr>
<th>Year Ended December 31,</th>
<th>2017</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Operating Revenues</strong></td>
<td>$99,650,323</td>
<td>$96,784,876</td>
</tr>
<tr>
<td><strong>Operating Expenses</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Fuel costs</td>
<td>31,698,007</td>
<td>30,514,757</td>
</tr>
<tr>
<td>Production operations and maintenance</td>
<td>6,930,276</td>
<td>6,820,313</td>
</tr>
<tr>
<td>Purchased power costs</td>
<td>3,022,687</td>
<td>3,219,705</td>
</tr>
<tr>
<td>Transmission operations and maintenance</td>
<td>7,221,640</td>
<td>6,022,279</td>
</tr>
<tr>
<td>Distribution operations and maintenance</td>
<td>3,022,687</td>
<td>3,219,705</td>
</tr>
<tr>
<td>Consumer accounts, service and sales</td>
<td>3,022,687</td>
<td>3,219,705</td>
</tr>
<tr>
<td>Administrative, general and other</td>
<td>17,771,472</td>
<td>17,274,406</td>
</tr>
<tr>
<td>Depreciation and amortization</td>
<td>17,771,472</td>
<td>17,274,406</td>
</tr>
<tr>
<td><strong>Total Operating Expenses</strong></td>
<td>81,378,707</td>
<td>77,214,613</td>
</tr>
<tr>
<td><strong>Interest Expense</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Long-term debt and other</td>
<td>13,520,569</td>
<td>13,936,297</td>
</tr>
<tr>
<td>Allowance for funds used during construction</td>
<td>(232,339)</td>
<td>(153,627)</td>
</tr>
<tr>
<td><strong>Net Interest Expense</strong></td>
<td>13,288,230</td>
<td>13,782,670</td>
</tr>
<tr>
<td><strong>Nonoperating Margins</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest income</td>
<td>183,623</td>
<td>155,838</td>
</tr>
<tr>
<td>Gain (loss) on sale of assets</td>
<td>(33,583)</td>
<td>-</td>
</tr>
<tr>
<td>Other income (expense)</td>
<td>(970)</td>
<td>(8,278)</td>
</tr>
<tr>
<td>Capital credits, patronage dividends and other</td>
<td>693,407</td>
<td>849,695</td>
</tr>
<tr>
<td><strong>Total Nonoperating Margins</strong></td>
<td>842,477</td>
<td>997,255</td>
</tr>
<tr>
<td><strong>Net Margins</strong></td>
<td>5,825,863</td>
<td>6,784,848</td>
</tr>
<tr>
<td><strong>Patronage Capital, beginning of year</strong></td>
<td>91,592,274</td>
<td>85,100,128</td>
</tr>
<tr>
<td><strong>Less retirement of patronage capital credits</strong></td>
<td>(1,754,057)</td>
<td>(292,702)</td>
</tr>
<tr>
<td><strong>Patronage Capital, end of year</strong></td>
<td>$95,664,080</td>
<td>$91,592,274</td>
</tr>
</tbody>
</table>