Homer Electric Association, Inc. and Subsidiary
(Alaska 5 and Alaska 33 Kenai)

Consolidated Financial Statements and Supplementary Information
Years Ended December 31, 2018 and 2017

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Contents

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Independent Auditor's Report

Board of Directors
Homer Electric Association, Inc. and Subsidiary
Homer, Alaska

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Homer Electric Association, Inc. and Subsidiary (the "Association"), which comprise the consolidated balance sheets as of December 31, 2018 and 2017, and the related consolidated statements of operations and patronage capital, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Homer Electric Association, Inc. and Subsidiary as of December 31, 2018 and 2017, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Supplementary Information
Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating balance sheets and consolidating statements of operations and patronage capital are presented for purposes of additional analysis and are not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated, in all material respects, in relation to the consolidated financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 26, 2019 on our consideration of Homer Electric Association, Inc. and Subsidiary's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of Homer Electric Association Inc. and Subsidiary's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Homer Electric Association, Inc. and Subsidiary's internal control over financial reporting and compliance.

BDO USA, LLP

Anchorage, Alaska
March 26, 2019

Consolidated Financial Statements

Homer Electric Association, Inc. and Subsidiary

Consolidated Balance Sheets

December 31,	2018	2017
Assets		
Utility Plant at Cost		
Electric plant in service	$ 597,669,211	$ 590,535,539
Electric plant held for future use	1,166,067	1,166,067
Construction work in progress	6,808,924	7,866,936
Total utility plant at cost	605,644,202	599,568,542
Less accumulated depreciation and amortization	(206,406,131)	(196,451,530)
Net Utility Plant	399,238,071	403,117,012
Other Assets and Investments		
Investments in associated organizations	20,344,937	22,187,694
Notes receivable, net of current portion	256,015	321,904
Non-utility property, net of accumulated depreciation of $585,027 ($549,331 in 2017)	160,085	195,781
Total Other Assets and Investments	20,761,037	22,705,379
Current Assets		
Cash and cash equivalents	3,898,971	4,063,658
Accounts receivable, less allowance for doubtful accounts of $171,436 ($107,295 in 2017)	7,997,128	7,752,458
Unbilled revenue	6,375,977	6,112,933
Materials, fuel and supplies inventory	7,617,357	6,548,092
Notes receivable, current portion	181,246	267,138
Other current and accrued assets	1,482,130	3,019,896
Total Current Assets	27,552,809	27,764,175
Deferred Charges	4,006,639	3,743,407
Total Assets	$ 451,558,556	$ 457,329,973

See accompanying notes to consolidated financial statements.

Homer Electric Association, Inc. and Subsidiary

Consolidated Balance Sheets, continued

December 31,	2018	2017
Equities and Liabilities		
Equities		
Memberships	$ 47,025	$ 48,820
Patronage capital	97,086,108	95,664,080
Other equities - donated capital	3,747,606	3,251,715
Total Equities	100,880,739	98,964,615
Liabilities		
Long-term Debt - mortgage notes payable	319,960,828	331,568,039
Current Liabilities		
Current portion of long-term debt	17,493,495	16,118,989
Line of credit	1,000,000	-
Accounts payable	6,158,919	4,915,072
Consumer deposits	1,308,359	1,223,154
Accrued payroll and benefits	2,543,198	2,483,930
Accrued taxes and other current liabilities	1,337,686	1,348,181
Total Current Liabilities	29,841,657	26,089,326
Deferred Credits	875,332	707,993
Total Equities and Liabilities	$ 451,558,556	$ 457,329,973

See accompanying notes to consolidated financial statements.

Homer Electric Association, Inc. and Subsidiary

Consolidated Statements of Operations and Patronage Capital

Years Ended December 31,	2018	2017
Operating Revenues	$ 97,876,247	$ 99,650,323
Operating Expenses		
Fuel costs	30,752,954	31,698,007
Production operations and maintenance	7,049,833	6,930,276
Purchased power costs	4,060,682	3,022,687
Transmission operations and maintenance	1,491,910	1,236,977
Distribution operations and maintenance	8,244,752	7,221,640
Consumer accounts, service and sales	3,852,265	3,688,744
Administrative, general and other	9,071,818	9,808,904
Depreciation and amortization	17,655,194	17,771,472
Total Operating Expenses	82,179,408	81,378,707
Interest Expense		
Long-term debt and other	13,428,560	13,520,569
Allowance for funds used during construction	(153,176)	(232,339)
Net Interest Expense	13,275,384	13,288,230
Net operating margins	2,421,455	4,983,386
Nonoperating Margins		
Interest income	365,219	183,623
Loss on sale of assets	(2,613)	(33,583)
Other income (expense)	134,998	(970)
Capital credits, patronage dividends and other	731,373	693,407
Total Nonoperating Margins	1,228,977	842,477
Net margins	3,650,432	5,825,863
Patronage capital, beginning of year	95,664,080	91,592,274
Less retirement of patronage capital credits	(2,228,404)	(1,754,057)
Patronage Capital, end of year	$ 97,086,108	$ 95,664,080

See accompanying notes to consolidated financial statements.

Homer Electric Association, Inc. and Subsidiary

Consolidated Statements of Cash Flows

Years Ended December 31,	2018	2017
Cash Flows from Operating Activities		
Cash received from customers	$ 96,974,502	$ 100,169,694
Cash paid to suppliers and employees	(61,523,327)	(64,912,650)
Interest and dividends received	365,219	183,623
Interest paid	(13,060,915)	(13,520,569)
Taxes paid	(236,085)	(220,201)
Other	132,385	(34,553)
Net cash from operating activities	22,651,779	21,665,344
Cash Flows for Investing Activities		
Plant additions	(16,024,023)	(15,517,016)
Contributions in aid of construction, including grant reimbursements	2,715,108	2,035,798
Salvage on plant retirements	107,081	125,825
Cost of removal	(473,639)	(773,096)
Patronage refunds from associated organizations	2,683,307	2,823,379
Investments in associated organizations	(108,677)	(235,538)
Changes in assets and liabilities that provided (used) cash:		
Materials, fuel and supplies inventories	(1,069,265)	(76,032)
Deferred charges	282,580	1,348,551
Deferred credits	167,339	(169,007)
Net cash for investing activities	(11,720,189)	(10,437,136)
Cash Flows for Financing Activities		
Proceeds from long-term debt	12,400,000	7,000,000
Line of credit advances (payments), net	1,000,000	-
Principal payments on long-term debt	(15,998,891)	(16,490,975)
Increase in advance payments unapplied	(6,848,283)	(430,852)
Retirement of capital credits	(1,732,513)	(1,293,907)
Changes in assets and liabilities that provided (used) cash:		
Consumer deposits	85,205	7,701
Memberships	(1,795)	(1,985)
Net cash for financing activities	(11,096,277)	(11,210,018)
Net increase (decrease) in cash and cash equivalents	(164,687)	18,190
Cash and Cash Equivalents, beginning of year	4,063,658	4,045,468
Cash and Cash Equivalents, end of year	$ 3,898,971	$ 4,063,658
Supplemental Disclosure of Non-cash Information - Refinance of long-term debt:		
Prepayment fees and retirement of existing debt with refinance note	$ 4,796,784	$ -

See accompanying notes to consolidated financial statements.

Homer Electric Association, Inc. and Subsidiary

Consolidated Statements of Cash Flows, continued

Years Ended December 31,	2018	2017
Reconciliation of Net Margins to Net Cash From Operating Activities		
Net margins	$ 3,650,432	$ 5,825,863
Adjustments to reconcile net margins to net cash from operating activities:		
Depreciation and amortization	17,743,286	17,854,699
Allowance for funds used during construction	(153,176)	(232,339)
Refinancing fees and interest (non-cash)	214,469	-
Patronage capital from associated organizations (non-cash)	(731,873)	(693,407)
(Increase) decrease in assets:		
Accounts receivable, net	(244,670)	(64,093)
Notes receivable	151,781	110,000
Unbilled revenue	(263,044)	162,569
Cost of power adjustment (COPA)	(545,812)	310,895
Other current and accrued assets	1,537,766	(2,689,001)
Increase (decrease) in liabilities:		
Accounts payable	1,243,847	1,181,125
Accrued payroll and benefits	59,268	(119,256)
Accrued taxes and other current liabilities	(10,495)	18,289
Total adjustments	19,001,347	15,839,481
Net Cash From Operating Activities	$ 22,651,779	$ 21,665,344

See accompanying notes to consolidated financial statements.

1. Business Organization

Homer Electric Association, Inc. (HEA) is an electric utility engaged in the generation, transmission and distribution of electricity for its members. HEA was formed in 1945 as Alaska's fifth rural electric cooperative. Today it serves over 24,000 members across the 3,166 square-mile service territory on the southern Kenai Peninsula, including several remote communities across Kachemak Bay. Generation facilities consist of an 80-megawatt combined cycle facility in Nikiski, a 48-megawatt aero derivative simple cycle unit at Soldotna and three gas turbines at Bernice Lake facility capable of 80 megawatts.

HEA operates on a not-for-profit basis and is recognized by the IRS as a 501(c)(12) organization. Accordingly, it seeks only to generate revenues sufficient to pay operating and maintenance costs, the cost of purchased power, capital expenditures, depreciation, debt service, and to provide for reserves.

2. Summary of Significant Accounting Policies

The accounting records of Homer Electric Association, Inc. conform to the Uniform System of Accounts prescribed by the Federal Energy Regulatory Commission as modified for electric borrowers of the Rural Utilities Service (RUS). HEA's accounting policies conform to generally accepted accounting principles as applied to the Financial Accounting Standards Board's (FASB) Accounting Standards Codification (ASC) 980 relating to accounting for regulated entities.

Principles of Consolidation

The consolidated financial statements include a 100% owned subsidiary, Alaska Electric and Energy Cooperative, Inc. (AEEC). AEEC is a single-member cooperative with sales exclusively to HEA and provides all power requirements to HEA. All significant inter-company balances and transactions have been eliminated in consolidation.

Plant Additions, Replacements and Retirements

Additions and replacements of electric plant in service are at original cost of contracted services, direct labor and materials, and indirect overhead charges. Except for certain specifically identifiable units of equipment, replacements and retirements of plant are charged to the accumulated provision for depreciation at the average unit cost of the property unit plus removal cost less salvage. The cost of replacement is added to electric plant.

Amortization

Deferred charges are amortized on a straight-line basis over periods ranging from 12 months to 180 months.

Contributions in Aid of Construction

Contributions in aid of construction are credited to the associated cost of the property unit constructed.

Allowance for Funds Used During Construction

HEA capitalizes, as an additional cost of property, an allowance for funds used during construction that represents the allowed cost of borrowings and equity used to finance a portion of construction work in progress. The allowance for funds used during construction is recorded as revenue and allocated to special projects over $10,000.

Income Taxes

HEA and AEEC are exempt from federal income taxes under provisions of Section 501(c)(12) of the Internal Revenue Code.

HEA applies the provisions of Topic 740 of the Financial Accounting Standards Board (FASB) Accounting Standards Codification relating to accounting for uncertainty in income taxes. HEA annually reviews its tax positions taken in accordance with the recognition standards. It is HEA management's opinion that it has no uncertain tax positions which would require disclosure or adjustment in these financial statements.

Cost of Power Adjustment

HEA, with regulatory approval, recovers fuel and purchased power costs through a Cost of Power Adjustment (COPA), which is updated quarterly. The accumulated amount over or under collected from members at any point in time is classified as a debit or credit on the balance sheet.

Accounting Estimates

The presentation of the consolidated financial statements in conformity with generally accepted accounting principles 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.

Fair Value of Financial Instruments

HEA measures certain items in these financial statements at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, that is, other than in a forced liquidation or distress sale.

HEA's financial assets and liabilities carried at fair value have been classified based on a hierarchy as defined in generally accepted accounting principles and are generally measured using the market approach or the income approach.

Reclassification

Certain prior year amounts included in the comparative financial statements have been reclassified to achieve comparability with current year presentation.

3. Utility Plant and Depreciation Rates and Procedures

Major classes of HEA's utility plant at December 31, 2018 and 2017 are as follows:

	2018	2017
Production plant	$ 244,407,194	$ 245,859,512
Distribution plant	241,472,876	231,798,175
Transmission plant	70,336,563	68,346,650
General plant	33,047,916	32,063,554
Plant in service, unclassified	6,644,235	10,707,221
Plant leased to others	1,760,427	1,760,427
Total electric plant in service	597,669,211	590,535,539
Electric plant held for future use	1,166,067	1,166,067
Construction work in progress	6,808,924	7,866,936
Total Utility Plant, at Cost	$ 605,644,202	$ 599,568,542

Current leased plant consists of fiber optic lines. Depreciation of plant leased to others is reflected as a reduction of operating revenues in the consolidated statements of operations and patronage capital.

The Bernice Lake Power Plant purchased from Chugach Electric Association on December 31, 2012, included an acquisition adjustment of approximately $7.4 million. HEA received regulatory approval to recover the amortization of the acquisition adjustment through rates over a period of 15 years. The asset is recorded as part of production plant.

Electric plant held for future use reflects vacant land owned by HEA.

Construction work in progress at December 31, 2018 includes approximately $4.5 million for distribution construction projects and $2.3 million in generation and transmission projects. Construction work in progress at December 31, 2017 includes approximately $7.4 million for distribution construction projects and $0.5 million in generation and transmission projects.

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Depreciation

HEA completed a Depreciation Study of utility plant approved by the Regulatory Commission of Alaska (RCA) with an effective date of January 1, 2016. The annual depreciation accrual rates were developed using the straight line method, vintage group procedure and remaining life technique. Depreciation accrual rates used in 2017 and 2018 vary by specific asset type according to these ranges:

	Range		
Production plant	1.00%	to	8.95%
Distribution plant	1.69%	to	6.51%
Transmission plant	0.71%	to	5.31%
General plant:			
Fiber equipment			0.18%
Vehicles and equipment	15.00%	to	19.36%
Other general plant	1.00%	to	15.23%
Plant leased to others			5.00%

Major overhauls and hot gas path inspections on generation plant are capitalized and depreciated over the projected life of the repairs. Depreciation on vehicles and equipment is charged to transportation clearing accounts.

Total depreciation and amortization for the years ended December 31, 2018 and 2017 is summarized below:

	2018	2017
Depreciation and amortization expense	$ 17,655,194	$ 17,771,472
Depreciation on leased plant	88,092	88,092
Total Depreciation and Amortization	$ 17,743,286	$ 17,859,564
Depreciation Charged to Clearing Accounts	$ 469,606	$ 505,568

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4. Investments in Associated Organizations

Investments in associated organizations at December 31, 2018 and 2017 consisted of the following:

	2018	2017
National Rural Utilities Cooperative Finance Corporation:		
Patronage capital credits	$ 5,678,102	$ 5,356,791
Capital term certificates, non-interest bearing, maturing in years 2019 through 2040	2,242,675	2,331,192
Capital term certificates, earning up to 5% interest, maturing in years 2020 through 2080	1,753,308	2,003,308
Membership	2,000	2,000
Chugach Electric Association – Patronage capital credits	3,931,295	5,931,295
Investment in Kenai Hydro LLC	3,750,912	3,642,235
Alaska Rural Electric Cooperative Association (ARECA) Insurance Exchange:		
Subscriber savings account	2,095,385	2,034,816
Capital reserve account	40,362	40,362
National Rural Telecommunications Cooperative (NRTC) - Patronage capital credits	562,069	562,069
Other capital credits and memberships	288,829	283,626
Total Investments in Associated Organizations	$ 20,344,937	$ 22,187,694

5. Current Assets

Cash and Cash Equivalents

HEA maintains its cash with First National Bank Alaska. Cash deposits in checking accounts held by the bank are insured up to the $250,000 Federal Deposit Insurance Corporation (FDIC) limit. At December 31, 2018 and 2017, the uninsured cash balances were zero and $2,194,993, respectively. In 2018, HEA opened two repurchase agreements with the bank that are not insured under the FDIC program, but are collateralized by government securities. The consolidated balance in the repurchase accounts at December 31, 2018 was $4,100,207.

Other financial instruments, which potentially subject HEA to concentrations of credit risk, include temporary cash investments made with National Rural Utilities Cooperative Finance Corporation (NRUCFC) throughout the year. At December 31, 2018 and 2017, there were zero and $121,322 short-term cash investments, respectively.

For purposes of the statements of cash flows, HEA considers all cash and short-term investments that are readily convertible to known amounts of cash and that present an insignificant risk of change in value due to changes in interest rates or other factors to be cash equivalents.

Accounts Receivable

Major classes of accounts receivable at December 31, 2018 and 2017 consisted of the following:

		2018		2017
Consumer accounts (energy bills)	$	7,254,018	$	7,111,367
Contract services		726,451		369,510
Grants receivable		28,809		88,033
Other		159,286		290,843
Total accounts receivable		8,168,564		7,859,753
Less accumulated provision for uncollectible accounts		(171,436)		(107,295)
Total Accounts Receivable, net	$	7,997,128	$	7,752,458

Concentrations of credit risk with respect to trade receivables are limited to HEA's large number of customers. For 2018 and 2017, the top three commercial members, based on total patronage, represent 15.8% and 16.0% of total operating revenues, respectively.

Unbilled Revenue

Revenues are recognized based on cycle billings rendered to customers monthly and adjusted by estimated amount for services rendered but not billed.

Materials, Fuel and Supplies

Materials and supplies primarily held for HEA's use in construction and maintenance projects are stated at a moving weighted-average cost. Spare parts and supplies for generation plant maintenance are stated at cost. Fuel inventory is the weighted average cost of fuel injected into Cook Inlet Natural Gas Storage Alaska (CINGSA). AEEC's fuel balance in storage for the years ended December 31, 2018 and 2017 amounted to $0.9 million and $0.5 million, respectively.

Other Current and Accrued Assets

Other current and accrued assets at December 31, 2018 and 2017 consisted of the following:

		2018		2017
Deposits	$	3,380	$	3,380
Short-term prepayments		151,948		1,372,189
Other receivables		203,218		201,041
Payments to the Battle Creek capital reserve account		1,123,584		1,443,286
Total Other Current and Accrued Assets	$	1,482,130	$	3,019,896

Short-term prepayments included accelerated payments to Alaska Energy Authority for Bradley Lake operating costs of zero and $1,189,164 for 2018 and 2017, respectively.

6. Deferred Charges

Deferred charges, net of accumulated amortization at December 31, 2018 and 2017 consisted of the following:

	2018	2017
Unused steam rights, to be amortized over 15 years	$ 2,426,656	$ 2,773,324
HEA rate case	637,040	849,387
Other regulatory assets	260,552	379,868
Facilities and projects in progress	3,137	6,805
Deferred credits on cost of power adjustment	(19,667)	(565,479)
Preliminary engineering	309,026	143,139
Costs of pending contract, tariff and rate cases	389,895	156,363
Total Deferred Charges	$ 4,006,639	$ 3,743,407

7. Equities

Equities at December 31, 2018 and 2017 consisted of the following:

	2018	2017
Memberships	$ 47,025	$ 48,820
Patronage capital:		
Assignable	3,650,432	5,825,863
Assigned	95,664,080	91,592,274
Total patronage capital	99,314,512	97,418,137
Less capital credits retired:		
General retirement	(1,718,259)	(1,493,309)
Estates of deceased	(307,364)	(136,169)
Discounted portion	(202,781)	(124,643)
Applied to customer accounts	-	64
Total capital credits retired	(2,228,404)	(1,754,057)
Net patronage capital	97,086,108	95,664,080
Other equities – donated capital at beginning of year	3,251,715	2,791,565
Net transfers from patronage capital discounted and other adjustments	495,891	460,150
Other equities – donated capital at end of year	3,747,606	3,251,715
Total Equities	$ 100,880,739	$ 98,964,615

Patronage capital credits are paid to the estates of deceased members and applied to customer accounts in accordance with the by-law requirements. In March 2018, the Board of Directors approved the general retirement of $1.72 million in patronage capital credits for distribution in April 2018. In the prior year, $1.5 million in patronage capital credits was retired in April 2017.

Provisions in the long-term debt agreements with NRUCFC allow return of patrons' capital if after the distribution, equity of HEA will be at least twenty percent (20%) of its total assets. If, after giving effect to the distribution, total equity of HEA will be less than twenty percent (20%) of its total assets, then HEA may nevertheless make distributions up to thirty percent (30%) of its patronage capital or operating margins for the preceding calendar year.

8. Long-term Debt and Lines of Credit

Long-term debt consists of notes payable to National Rural Utilities Cooperative Finance Corporation (NRUCFC), National Cooperative Services Corporation (NCSC), Farmer Mac (FMAC) and Rural Utilities Service Guaranteed Federal Financing Bank (RUS FFB). The interest rates may be fixed or variable under conversion options provided in the loan agreements. The loans are collateralized by all of HEA's and AEEC's assets except for vehicles. The loans require HEA to maintain an average modified debt service coverage ratio of not less than 1.35. AEEC's loans require an average modified debt service coverage ratio of not less than 1.05, a minimum equity ratio of 12% through 2017, and 15% minimum ratio from 2018 through maturity. The RUS loan requires a 1.05 minimum TIER. HEA and AEEC were in compliance with these debt covenants. Interest and principal payments are made quarterly to NRUCFC, NCSC and RUS FFB and made semi-annually to FMAC. The notes mature at various times from 2019 to 2048.

Mortgage notes payable at December 31, 2018 and 2017 were as follows:

	2018	2017
HEA:		
NRUCFC – variable rate notes	$ 542,385	$ -
NRUCFC – fixed rate notes ranging from 3.20 to 5.80%	111,605,232	105,163,508
FMAC – variable rate notes	4,637,424	2,991,998
FMAC – fixed rate notes ranging from 3.97 to 4.96%	20,560,795	23,218,363
AEEC:		
NRUCFC – fixed rate notes ranging from 4.25 to 6.15%	43,338,036	49,121,380
NRUCFC – variable rate notes	4,416,527	910,059
NCSC – fixed rate notes ranging from 3.50% to 4.70%	35,373,186	36,792,321
RUS FFB – fixed rate notes ranging from 2.79 to 3.06%	124,528,302	130,188,679
RUS Cushion of Credit – advanced payments unapplied	(7,547,564)	(699,280)
Total long-term debt	337,454,323	347,687,028
Less current portion	(17,493,495)	(16,118,989)
Net Long-term Debt	$ 319,960,828	$ 331,568,039

Receipt of NRUCFC loans requires commitments to purchase non-interest bearing capital term certificates. Balances of these NRUCFC certificates were $2,242,675 and $2,331,192 for 2018 and 2017, respectively (See Note 4).

The annual requirements for reduction of long-term debt outstanding as of December 31, 2018, are estimated to be as follows:

Year Ending December 31,	
2019	$ 17,493,495
2020	16,903,909
2021	15,041,502
2022	15,161,851
2023	14,156,945
Thereafter	258,696,621
	$ 337,454,323

In August 2018, HEA executed a new $60 million power vision loan facility with NRUCFC to replace one that termed out. In January 2018, AEEC completed a non-cash refinancing transaction with NRUCFC for $4.8 million to cover fees and prepay $4.6 million of long-term debt. At December 31, 2018, HEA and AEEC had long-term unadvanced loan facilities available from NRUCFC of $56,000,000 and $18,203,216, respectively. At December 31, 2017, HEA and AEEC had long-term unadvanced loan facilities available from NRUCFC of $12,000,000 and $23,000,000, respectively.

In 2015, AEEC established an account in the RUS Cushion of Credit program. The advance payments unapplied amount represents the balance in the program. The program allows RUS borrowers to make unscheduled advance payments on their RUS FFB notes. The advance payments earn interest at five percent per annum and the advance payments plus accrued interest cannot be withdrawn and may only be used to pay principal and interest on RUS FFB notes. The 2018 Farm Bill eliminated the option of new deposits and will reduce the interest rates beginning in fiscal year 2020.

HEA and AEEC each established a revolving line of credit loan with NRUCFC in amounts not to exceed $5,000,000 and $10,000,000, respectively. Advances are subject to CFC approval and variable rate interest payments are due quarterly. The line of credit for HEA is perpetual and the maturity date for AEEC is May 2019. There were $1,000,000 and zero outstanding balances on the lines of credit at December 31, 2018 and 2017, respectively. Subsequently, HEA paid off the remaining balance on the line of credit in January 2019.

9. Deferred Credits

Deferred credits at December 31, 2018 and 2017 consisted of the following:

	2018	2017
Consumer prepayments	$ 4,233	$ 9,457
Standard labor on transformers and meters	871,099	698,536
Total Deferred Credits	$ 875,332	$ 707,993

10. Employee Benefits

Defined Benefit Pension Plans

Pension benefits for substantially all employees are provided through participation in the National Rural Electric Cooperative Association (NRECA) and Alaska Electrical Trust Fund retirement programs. Both plans are master multi-employer defined benefit plans qualified under Section 401 and tax-exempt under Section 501(a) of the Internal Revenue Code. A unique characteristic of a multi-employer plan compared to a single employer plan is that all plan assets are available to pay benefits of any plan participant. Separate asset accounts are not maintained for participating employers. This means that assets contributed by one employer may be used to provide benefits to employees of other participating employers.

NRECA Retirement Security Plan Information

The National Rural Electric Cooperative Association (NRECA) Retirement Security Plan (RS Plan) is considered a multi-employer plan under the accounting standards. The plan sponsor's employer identification number is 53-0116145 and the Plan Number is 333. HEA contributions to the RS Plan in 2018 and 2017 represented less than 5% of the total contributions made to the RS Plan by all participating employers. HEA contributed to the RS Plan $2,709,822 in 2018 and $2,575,080 in 2017. There have been no significant changes that affect the comparability of 2018 and 2017 contributions.

For the RS Plan, a "zone status" determination is not required, and therefore not determined, under the Pension Protection Act (PPA) of 2006. In addition, the accumulated benefit obligations and plan assets are not determined or allocated separately by individual employer. In total, the RS Plan was over 80% funded on January 1, 2018 and 2017 based on the PPA funding target and PPA actuarial value of assets on those dates.

Because the provisions of the PPA do not apply to the RS Plan, funding improvement plans and surcharges are not applicable. Future contribution requirements are determined each year as part of the actuarial valuation of the RS Plan and may change as a result of plan experience.

Alaska Electrical Pension Plan Information

The Alaska Electrical Pension Plan sponsor's Employer Identification Number is 92-6005171 and the Plan Number is 001. HEA contributions to the Plan in 2018 and 2017 represented less than 5% of the total contributions made to the Plan by all participating employers. HEA contributed to the Plan $1,595,566 in 2018 and $1,504,376 in 2017. There have been no significant changes that affect the comparability of 2018 and 2017 contributions. In total, the Alaska Electrical Pension Plan was certified by the Plan actuary with a green zone status at December 31, 2018 and 2017. The Plan is not subject to funding improvement plans or rehabilitation plans and as a result, HEA is not subject to contribution surcharges. There are no minimum funding commitments as negotiated contributions currently satisfy HEA's commitment towards meeting the annual minimum funding requirement for the Alaska Electrical Pension Plan.

Collective Bargaining Agreements

Approximately 57% of HEA employees are covered by collective bargaining agreements with the International Brotherhood of Electrical Workers (IBEW). The current agreements expire as follows: the Generation agreement expires April 30, 2023, the Outside agreement expires April 30, 2020, and the Inside agreement expires April 30, 2021.

401(k) Plan

Effective January 1, 1988, HEA adopted a 401(k) plan covering substantially all employees who elect to participate. Employees are allowed to contribute up to the maximum dollar amounts permitted by the IRS each year. HEA contributes 1% of the straight time compensation for nonunion employees and an additional 2% on a matching basis. HEA contributes 6% of the straight time compensation on inside union employees. HEA contributes 5.5% of the straight time compensation of generation union employees. Beginning January 1, 2017, HEA stopped contributions to the NRECA 401(k) Plan for employees covered by the outside bargaining agreement. The total contributions to the Plan for the years ended December 31, 2018 and 2017 were $414,274 and $388,632, respectively.

Alaska Electrical Trust Fund Money Purchase Plan

Beginning January 1, 2017, HEA contributed $1.75 per hour to the Alaska Electrical Trust Fund Money Purchase Plan for employees covered by the outside bargaining agreement. On May 1, 2017, the employer contribution became $2.72 per compensable hour. The total contributions to the Plan for the years ended December 31, 2018 and 2017 were $222,325 and $204,089, respectively.

Deferred Compensation Plan

HEA participates in the deferred compensation plan offered to similar cooperatives by NRECA. This program provides a deferral of current earnings by select or qualifying employees to a future period and is entirely funded by the employee.

11. Bradley Lake Hydroelectric Project

The Bradley Lake Hydroelectric Project Power Sales Agreement between the owner, the Alaska Energy Authority, and the utility participants was approved by RUS on June 29, 1989. In exchange for HEA's payment of its proportionate share of the debt service on the project bonds and actual operation and maintenance costs, HEA is entitled to a 12% share or between 10.8 and 13.8 megawatts (MW) and 12% of the plant's energy production, of which HEA's share currently averages 53,067 megawatt hours annually. As of 2014, HEA schedules its own Bradley Lake Power through the project dispatcher, Chugach Electric Association.

The Alaska Energy Authority is managing a project to divert water from Battle Creek into Bradley Lake, increasing the potential energy output of the Bradley Lake Plant. HEA will be entitled to a share of the additional energy produced. Financing for this effort is provided by a combination of bonds and cash calls from the participating utilities. In 2018, HEA expensed $998,576 for Battle Creek operating costs and has a capital reserve balance of $1,123,584 (see Note 5 Other Current and Accrued Assets). In 2017, HEA paid $83,920 toward construction costs and $1,443,286 toward the capital reserve. Subsequent to December 31, 2017, a portion of the capital reserve payment was redirected to FY18 Battle Creek operating costs.

12. Regulatory Matters

HEA was granted approval by the Regulatory Commission of Alaska (RCA) to use the Simplified Rate Filing Procedures (SRF) for Electric Cooperatives on June 10, 1991. HEA filed for a 5.0% rate increase on an across the board basis under the SRF on February 13, 2019, for demand and energy rates effective April 1, 2019.

On November 14, 2013, HEA filed a request with the RCA for approval of transmission and related ancillary service tariffs. As of December 31, 2018, this case is still pending final approval from the RCA; hence no associated revenues are recorded in 2018 or 2017. This issue also had pending litigation at the State Supreme Court. On February 22, 2019, the State Supreme Court resolved the issues around transmission and related ancillary service tariffs, ruling that the RCA does not have authority to approve the rates applying to transmission of Bradley Lake energy.

13. Affiliated Organizations

Kenai Hydro, a limited liability company, was formed in 2008 for the purpose of evaluating, investigating and planning low impact hydroelectric facilities on the Kenai Peninsula. Grants from the State of Alaska awarded to Kenai Hydro LLC have been used to pursue a FERC license for hydroelectric facilities. HEA transferred its membership in Kenai Hydro to AEEC in 2015. As a single-member LLC, Kenai Hydro is considered by the IRS as a disregarded entity for tax purposes.

14. Grant Revenues

HEA and AEEC receive grant funding from various state agencies to assist with the costs of different projects, including repair and construction of transmission lines and structures, re-clearing activities, and replacement of facilities damaged by wildfires. In accordance with industry standards, HEA has chosen to account for grant revenues either as a reduction of expenses or as a reduction in the costs of capital improvements. Total grant reimbursable expenses incurred were $157,208 and $273,943 in 2018 and 2017, respectively.

15. Contingencies and Commitments

HEA is subject to extensive federal, state and local environmental laws and regulations. These laws and regulations, which are constantly changing, regulate the discharge of materials into the environment and may require HEA to remove or mitigate the environmental effects of the disposals or release of substances at various sites. Environmental expenditures are expensed or capitalized depending on their future economic benefit. Expenditures that relate to an existing condition caused by past operations and that have no economic benefits are either expensed in the current period or amortized over an approved period of time. Liabilities for expenditures of a noncapital nature are recorded when environmental assessments and/or remediation is probable, and the costs can be reasonably estimated.

Although the level of future expenditures for environmental matters is impossible to determine, it is management's opinion that such costs when finally determined will not have a material effect on the financial position of HEA.

In the normal course of business, HEA is involved in various claims and litigation. In the opinion of management and HEA's legal counsel, the disposition of these matters is not expected to have a material adverse effect on HEA's financial statements.

16. Subsequent Events

HEA has evaluated subsequent events and transactions for potential recognition or disclosure through March 26, 2019, the date on which the financial statements were available to be issued.

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Supplementary Information

Homer Electric Association, Inc. and Subsidiary

Consolidating Balance Sheet

December 31, 2018	Homer Electric Association	Alaska Electric and Energy Cooperative	Eliminations	Consolidated Totals
Assets				
Utility Plant at Cost				
Electric plant in service	$ 282,506,029	$ 315,163,182	$ -	$ 597,669,211
Electric plant held for future use	1,166,067	-	-	1,166,067
Construction work in progress	4,518,852	2,290,072	-	6,808,924
Total utility plant at cost	288,190,948	317,453,254	-	605,644,202
Less accumulated depreciation and amortization	(112,194,692)	(94,211,439)	-	(206,406,131)
Net Utility Plant	175,996,256	223,241,815	-	399,238,071
Other Assets and Investments				
Investments in associated organizations	50,742,464	10,380,547	(40,778,074)	20,344,937
Notes receivable, net of current portion	256,015	-	-	256,015
Non-utility property, net of accumulated depreciation of $585,027	160,085	-	-	160,085
Total Other Assets and Investments	51,158,564	10,380,547	(40,778,074)	20,761,037
Current Assets				
Cash and cash equivalents	2,452,507	1,446,464	-	3,898,971
Accounts receivable, less allowance for doubtful accounts of $171,436	9,124,697	4,329,032	(5,456,601)	7,997,128
Unbilled revenue	6,375,977	-	-	6,375,977
Materials, fuel and supplies inventory	3,982,671	3,634,686	-	7,617,357
Notes receivable, current portion	181,246	-	-	181,246
Other current and accrued assets	355,416	1,126,714	-	1,482,130
Total Current Assets	22,472,514	10,536,896	(5,456,601)	27,552,809
Deferred Charges	1,309,822	2,696,817	-	4,006,639
Total Assets	$ 250,937,156	$ 246,856,075	$ (46,234,675)	$ 451,558,556

Homer Electric Association, Inc. and Subsidiary

Consolidating Balance Sheet, continued

December 31, 2018	Homer Electric Association	Alaska Electric and Energy Cooperative	Eliminations	Consolidated Totals
Equities and Liabilities				
Equities				
Memberships	$ 47,025	$ -	$ -	$ 47,025
Patronage capital	97,086,108	31,578,033	(31,578,033)	97,086,108
Other equities - donated capital	3,747,606	9,200,041	(9,200,041)	3,747,606
Total Equities	100,880,739	40,778,074	(40,778,074)	100,880,739
Liabilities				
Long-term Debt - mortgage notes payable	129,990,278	189,970,550	-	319,960,828
Current Liabilities				
Current portion of long-term debt	7,355,558	10,137,937	-	17,493,495
Line of credit	1,000,000	-	-	1,000,000
Accounts payable	5,646,006	5,969,514	(5,456,601)	6,158,919
Consumer deposits	1,308,359	-	-	1,308,359
Accrued payroll and benefits	2,543,198	-	-	2,543,198
Accrued taxes and other current liabilities	1,337,686	-	-	1,337,686
Total Current Liabilities	19,190,807	16,107,451	(5,456,601)	29,841,657
Deferred Credits	875,332	-	-	875,332
Total Equities and Liabilities	$ 250,937,156	$ 246,856,075	$ (46,234,675)	$ 451,558,556

Homer Electric Association, Inc. and Subsidiary

Consolidating Statement of Operations and Patronage Capital

Year Ended December 31, 2018	Homer Electric Association	Alaska Electric and Energy Cooperative	Eliminations	Consolidated Totals
Operating Revenues	$ 97,743,688	$ 61,581,118	$ (61,448,559)	$ 97,876,247
Operating Expenses				
Fuel costs	44,227	30,708,727	-	30,752,954
Production operations and maintenance	227,884	6,821,949	-	7,049,833
Purchased power costs	61,451,319	4,057,922	(61,448,559)	4,060,682
Transmission operations and maintenance	-	1,491,910	-	1,491,910
Distribution operations and maintenance	8,244,752	-	-	8,244,752
Consumer accounts, service and sales	3,852,265	-	-	3,852,265
Administrative, general and other	8,307,500	764,318	-	9,071,818
Depreciation and amortization	7,854,128	9,801,066	-	17,655,194
Total Operating Expenses	89,982,075	53,645,892	(61,448,559)	82,179,408
Interest Expense				
Long-term debt and other	5,479,628	7,948,932	-	13,428,560
Allowance for funds used during construction	(153,176)	-	-	(153,176)
Net Interest Expense	5,326,452	7,948,932	-	13,275,384
Net operating margins	2,435,161	(13,706)	-	2,421,455
Nonoperating Margins				
Interest income	143,370	221,849	-	365,219
Loss on sale of assets	(2,613)	-	-	(2,613)
Other income	14,998	120,000	-	134,998
Capital credits, patronage dividends and other	1,059,516	238,479	(566,622)	731,373
Total Nonoperating Margins	1,215,271	580,328	(566,622)	1,228,977
Net margins	3,650,432	566,622	(566,622)	3,650,432
Patronage capital, beginning of year	95,664,080	31,011,411	(31,011,411)	95,664,080
Less retirement of patronage capital credits	(2,228,404)	-	-	(2,228,404)
Patronage Capital, end of year	$ 97,086,108	$ 31,578,033	$ (31,578,033)	$ 97,086,108