ALASKA ENERGY AUTHORITY
(A Component Unit of the State of Alaska)

Basic Financial Statements and Schedules

June 30, 2012 and 2011

(With Independent Auditors' Report Thereon)

ALASKA ENERGY AUTHORITY
(A Component Unit of the State of Alaska)

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Overview of the Financial Statements

The Alaska Energy Authority's (AEA or Authority) is composed of the following programs – AEA owned hydroelectric and intertie projects, rural energy programs, and energy development programs. Further information on AEA's programs can be found in note 1 to the financial statements.

This financial report consists of three sections: management's discussion and analysis, basic financial statements, and supplementary schedules. AEA's operations are business type activities and are considered an enterprise fund. The Authority is a component unit of the State of Alaska (State) and is discretely presented in the State's financial statements. The Authority's basic financial statements are the Balance Sheets; the Statements of Revenues, Expenses, and Changes in Net Assets; the Statements of Cash Flows; and the Notes to Basic Financial Statements.

Basic Financial Statements

The *Balance Sheets* report the Authority's assets, liabilities, and resulting net assets. The net assets are reported as invested in capital assets less debt, restricted, and unrestricted. Restricted net assets are subject to external limits such as bond resolutions, legal agreements, or statutes.

The *Statements of Revenues, Expenses, and Changes in Net Assets* report the Authority's income, expenses, and resulting change in net assets during the periods reported.

Both statements report on the accrual basis of accounting and economic resources measurement focus.

The *Statements of Cash Flows* report the Authority's sources and uses of cash and change in cash balance resulting from the Authority's activities during the periods reported.

The *Notes to Basic Financial Statements* provide additional information required to fully understand the amounts reported in the basic financial statements.

Management's Discussion and Analysis

This section presents AEA management's analysis of the Authority's financial position and results of operations at and for the years ended June 30, 2012 and 2011. This information is presented to help the reader focus on significant financial issues and provide additional information regarding the activities of the Authority. This information should be read in conjunction with the Independent Auditors' Report, the audited financial statements and the accompanying notes.

Financial Highlights

AEA's assets exceeded its liabilities by $1.1 billion at both June 30, 2012 and 2011. Of the total net assets at June 30, 2012, $135 million was invested in capital assets net of related debt, $34 million was restricted and $902 million was unrestricted. Of the total net assets at June 30, 2011, $126 million was invested in capital assets net of related debt, $37 million was restricted and $913 million was unrestricted.

Financial Analysis

Financial Position

Total assets, total liabilities, and total net assets at June 30, 2012, 2011, and 2010 follows (stated in thousands):

		2012	2011	2010
Current assets	$	21,571	410,251	32,092
Capital assets, net		229,310	227,438	236,472
Other noncurrent and restricted assets		977,856	579,130	504,105
Total assets		1,228,737	1,216,819	772,669
Current liabilities		68,966	44,932	27,809
Noncurrent liabilities		89,143	95,978	101,812
Total liabilities		158,109	140,910	129,621
Total net assets		1,070,628	1,075,909	643,048
Total liabilities and net assets	$	1,228,737	1,216,819	772,669

Current assets were $388.7 million lower at June 30, 2012 compared to June 30, 2011 and $378.2 million higher at June 30, 2011 compared to June 30, 2010. The change was primarily caused by $400 million due from the State of Alaska at June 30, 2011 for the Power Cost Equalization (PCE) Endowment Fund; when received the amount became part of noncurrent restricted cash and investments.

Capital assets were $1.9 million higher at June 30, 2012 compared to June 30, 2011 substantially due to development of the Susitna-Watana Hydroelectric Project and other improvements, offset by depreciation of capital assets and the conveyance of the Napakiak Intertie Project to Napakiak Irecinraq Power Corporation. Capital assets were $9.0 million lower at June 30, 2011 compared to June 30, 2010 substantially due to depreciation of capital assets, offset by improvements and the transfer of the Larsen Bay Hydroelectric Project to the City of Larsen Bay. Improvements and transfers relating to the below projects (stated in millions) were:

		2012 vs. 2011	2011 vs. 2010
Bradley Lake Hydroelectric Project	$	3.0	1.0
Alaska Intertie Project		1.6	0.2
Susitna-Watana Hydroelectric Project		10.1	—
Larsen Bay Hydroelectric Project		—	(0.4)
Napakiak Intertie Project		(3.1)	—
	$	11.6	0.8

(Continued)

Other noncurrent and restricted assets were $398.7 million higher at June 30, 2012 compared to June 30, 2011 and $75.0 million higher at June 30, 2011 compared to June 30, 2010. The 2012 increase primarily related to the receipt of $400 million restricted to the PCE Endowment Fund, along with other restricted contributions offset by expenditures of restricted funds. The 2011 increase related to restricted contributions and investment income partially offset by expenditures of restricted funds.

Current liabilities were $24.0 million higher at June 30, 2012 compared to June 30, 2011 and $17.1 million higher at June 30, 2011 compared to June 30, 2010. The change related primarily to amounts due to the State of Alaska and accrued expenses.

The $6.8 million decrease in noncurrent liabilities between June 30, 2012 and 2011 was substantially caused by a decrease in the long-term portion of bonds payable, offset by an increase in the noncurrent portion of arbitrage interest payable and a decrease in other noncurrent liabilities. The $5.8 million decrease between June 30, 2011 and 2010 was substantially caused by a decrease in the long-term portion of bonds payable, offset by increases in the noncurrent portion of arbitrage interest payable and other noncurrent liabilities.

Net assets were $5.3 million lower at June 30, 2012 compared to June 30, 2011 and $432.9 million higher at June 30, 2011 compared to June 30, 2010. The net changes were substantially caused by (stated in millions):

		2012 vs. 2011	2011 vs. 2010
Operating loss	$	(61.9)	(71.4)
Contribution from State of Alaska to PCE Endowment Fund		—	400.0
Contributions from State of Alaska to other funds		29.0	37.2
Investment income		14.1	70.9
Loss on sale of Power Project Fund loans		—	(3.8)
State of Alaska capital grants		13.5	—
	$	(5.3)	432.9

(Continued)

Operations

Components of the Authority's operating revenues, operating expenses, nonoperating investment income and operating loss for the years ended June 30, follows (stated in thousands):

	2012	2011	2010
Operating revenues	$ 98,660	47,268	56,034
Operating expenses	160,576	118,676	107,656
Operating loss	(61,916)	(71,408)	(51,622)
Nonoperating:			
State of Alaska contributions, net	29,020	437,200	25,199
Loss on sale of Power Project Fund loans	—	(3,850)	—
Decrease in contingent liability from loan sale	84	22	—
Investment income, net	14,050	70,897	42,749
State of Alaska capital grants	13,481	—	—
(Decrease) increase in net assets	$ (5,281)	432,861	16,326

Operating revenues increased $51.3 million during the year ended June 30, 2012 compared to the prior year and decreased $8.7 million during the year ended June 30, 2011 compared to the prior year. Components of changes were (stated in millions):

	FY 2012-2011 Net change	FY 2011-2010 Net change
Increased (decreased) grant revenue from Denali Commission	$ 3.2	(1.2)
Decreased grant revenue from U.S. Department of Energy	(0.1)	(0.3)
Decreased revenue from other federal grantors	—	(0.9)
Fluctuations in revenue from operating plants	(1.3)	(1.1)
Increased (decreased) revenue from State for PCE grant program	8.0	(2.7)
Increased revenue from State for Railbelt energy projects to Alaska Railbelt utilities	22.4	—
Increased revenue from State for Eva Creek wind farm	10.0	—
Increased (decreased) revenue from other State general fund operating and capital appropriations	5.3	(3.9)
Increased revenue from other State agencies	3.8	2.1
Decreased revenue from loan interest and other miscellaneous revenues	—	(0.7)
	$ 51.3	(8.7)

Operating expenses increased $41.9 million during the year ended June 30, 2012 compared to the prior year and increased $11.0 million during the year ended June 30, 2011 compared to the prior year. Components of the changes were (stated in millions):

		FY 2012-2011 Net change	FY 2011-2010 Net change
Increased (decreased) federally funded grant and project expenses in active rural energy construction projects	$	3.1	(2.4)
Increased State funded grant and project expenses		24.9	9.6
Increased State agency and component unit funded expenses for interagency contracts		3.9	2.1
Increased PCE grant expenditures		7.7	—
Conveyance of intertie to local utility		3.1	—
Decreased bond interest expense		(0.5)	(0.9)
(Decreased) increased operating plants expense		(1.2)	0.5
Increased other expenses		0.9	2.1
	$	41.9	11.0

Nonperating State of Alaska contributions fluctuate from year to year depending on major initiatives of the state legislature. State of Alaska contributions in 2011 included $400 million for the PCE Endowment Fund and $10 million for the power project fund that did not occur in either 2010 or 2012.

Outlook

Annual operation of the owned hydroelectric and intertie projects are per annual budgets approved by the utilities that use the assets and pursuant to bond resolutions and other agreements. Susitna-Watana Hydroelectric project expenditures are per State capital appropriations and legislation. Annual operation of the rural energy programs and energy development programs and projects are per State legislation, annual appropriations and federal grant awards.

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Independent Auditors' Report

The Board of Directors
Alaska Energy Authority:

We have audited the accompanying balance sheets of the Alaska Energy Authority (a Component Unit of the State of Alaska) (Authority) as of June 30, 2012 and 2011, and the related statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these basic 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 financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing auditing procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Authority's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and the 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 the Authority as of June 30, 2012 and 2011, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 24, 2012, on our consideration of the Authority'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 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 1 - 5 be presented to supplement the basic financial statements. Such information although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Authority's basic financial statements. The supplementary information in schedules 1 through 3 is presented for purposes of additional analysis and is not a required part of the basic 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 basic financial statements. The supplementary information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated in all material respects in relation to the basic financial statements as a whole.

KPMG LLP

October 24, 2012

ALASKA ENERGY AUTHORITY
(A Component Unit of the State of Alaska)

Balance Sheets

June 30, 2012 and 2011

(Stated in thousands)

Assets		**2012**	**2011**
Current assets:			
Grants receivable	$	3,252	1,940
Loans receivable (note 6)		3,318	1,571
Operating revenue receivable		10,093	3,032
Due from State of Alaska		3,824	402,594
Accrued interest receivable		1,084	1,114
Total current assets		21,571	410,251
Noncurrent assets:			
Restricted cash and investments (note 3)		22,773	22,370
Cash and investments designated for specific purposes (note 3)		952,562	555,006
Loans receivable, net of allowance (note 6)		2,521	1,754
Capital assets (note 4)		461,426	449,812
Less accumulated depreciation		(232,116)	(222,374)
Capital assets, net		229,310	227,438
Total noncurrent assets		1,207,166	806,568
Total assets	$	1,228,737	1,216,819
Liabilities and Net Assets			
Current liabilities:			
Due to State of Alaska	$	22,235	7,232
Accounts payable		37,241	28,400
Bonds payable – current portion (note 5)		6,880	6,495
Accrued interest payable		2,610	2,805
Total current liabilities		68,966	44,932
Noncurrent liabilities:			
Bonds payable – noncurrent portion, net (note 5)		87,607	94,676
Arbitrage interest payable – noncurrent portion (note 5)		813	494
Other liabilities		723	808
Total noncurrent liabilities		89,143	95,978
Total liabilities		158,109	140,910
Net assets:			
Invested in capital assets, net of related debt		134,823	126,267
Restricted for debt service		20,163	19,565
Restricted by agreements with external parties		13,535	17,083
Unrestricted		902,107	912,994
Total net assets		1,070,628	1,075,909
Commitments and contingencies (notes 7 and 9)			
Total liabilities and net assets	$	1,228,737	1,216,819

See accompanying notes to basic financial statements.

ALASKA ENERGY AUTHORITY
(A Component Unit of the State of Alaska)

Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2012 and 2011

(Stated in thousands)

		2012	2011
Operating revenues:			
Federal grants	$	14,871	11,758
Revenue from operating plants		16,357	17,613
State of Alaska appropriations		60,283	14,645
Revenue from state agencies and component units		6,599	2,670
Interest on loans		302	484
Other revenue		248	98
Total operating revenues		98,660	47,268
Operating expenses:			
Grants and projects		97,047	62,072
Power cost equalization grants		38,899	31,180
Depreciation		9,742	10,291
Interest expense		5,032	5,540
Plant operating		4,501	5,674
General and administrative		5,267	3,933
Provision for loan loss (note 6)		88	(14)
Total operating expenses		160,576	118,676
Operating loss		(61,916)	(71,408)
Nonoperating:			
Loss on sale of Power Project Fund loans		—	(3,850)
Decrease in contingent liability on sold loans		84	22
State of Alaska contribution to the Emerging Energy Technology Fund		2,400	2,400
State of Alaska contribution to the Power Project Fund		—	10,000
State of Alaska contribution to the Power Cost Equalization Endowment Fund		—	400,000
State of Alaska returned contribution to the Power Cost Equalization and Rural Electric Capitalization Fund		—	(200)
State of Alaska contribution to the Renewable Energy Fund		26,620	25,000
Investment income, net		14,050	70,897
State of Alaska contributions for capital assets		13,481	—
Total nonoperating		56,635	504,269
(Decrease) increase in net assets		(5,281)	432,861
Net assets – beginning		1,075,909	643,048
Net assets – ending	$	1,070,628	1,075,909

See accompanying notes to basic financial statements.

ALASKA ENERGY AUTHORITY
(A Component Unit of the State of Alaska)

Statements of Cash Flows

Years ended June 30, 2012 and 2011

(Stated in thousands)

		2012	2011
Cash flows from operating activities:			
Receipts from federal grants	$	13,558	11,591
Receipts from customers and users		13,018	21,490
Receipts from State of Alaska appropriations		69,715	21,684
Receipts from state agencies and component units		6,449	1,717
Other operating receipts		250	129
Payments to suppliers		(25,836)	(11,842)
Payments to grantees		(112,890)	(85,262)
Net cash used for operating activities		(35,736)	(40,493)
Cash flows from noncapital and related financing activities:			
Net unremitted interest returned on State appropriation advances		2	(2)
PCE contribution from State appropriation		400,000	—
Emerging Energy Technology contribution from State appropriation		4,800	—
Renewable Energy Fund contribution from State appropriation		26,620	50,000
Power Project Fund contribution from State appropriation		—	10,000
Subrecipient grant advances		(8,114)	(278)
Net receipt related to operating loans from AIDEA		3,992	174
Net cash provided by noncapital and related financing activities		427,300	59,894
Cash flows from capital and related financing activities:			
Principal paid on bonds		(6,495)	(36,895)
Interest paid on bonds		(5,416)	(5,944)
Net proceeds from bond refunding		—	30,851
State of Alaska contribution for capital assets		14,655	—
Costs associated with bond refunding		—	(262)
Purchase of capital assets		(9,044)	(1,454)
Net cash used for capital and related financing activities		(6,300)	(13,704)
Cash flows from investing activities:			
Purchase of investments		(504,092)	(212,085)
Proceeds from sales and maturities of investments		140,467	204,526
Interest received from investments		17,288	12,064
Principal collected on loans		12,061	11,166
Proceeds from sale of Power Project Fund loans		—	20,631
Interest collected on loans		308	519
Loans originated		(14,661)	(11,028)
Net cash (used for) provided by investing activities		(348,629)	25,793
Net increase in cash and cash equivalents		36,635	31,490
Cash and cash equivalents at beginning of year		79,609	48,119
Cash and cash equivalents at end of year (note 3)	$	116,244	79,609
Reconciliation of operating loss to net cash used for operating activities:			
Operating loss	$	(61,916)	(71,408)
Adjustments to reconcile operating loss to net cash used for operating activities:			
Depreciation		9,742	10,291
Provision for loan loss and bad debt expense		88	(14)
Bond interest expense		5,032	5,540
Interest on loans		(302)	(484)
Conveyance of intertie to local utility included in grants and projects		3,131	—
Changes in assets and liabilities that provided (used) cash:			
Increase in due to State of Alaska		12,326	6,912
(Increase) decrease in due from the State of Alaska		(2,784)	21
(Increase) in grants receivable		(1,313)	(168)
Decrease (increase) in operating revenue receivable		1,053	(1,611)
(Decrease) increase in operating accounts payable		(793)	10,428
Net cash used for operating activities	$	(35,736)	(40,493)
Noncash capital and related financing and investing activities:			
Amount included in accounts payable for capital asset additions	$	6,582	285
Net (decrease) increase in fair value of investments		(20,536)	54,040
Conveyance of intertie project		(3,131)	—

See accompanying notes to basic financial statements.

(1) Organization and Operations

The Alaska Energy Authority (Authority or AEA) was created by the Alaska State Legislature in 1976. AEA is a public corporation and a component unit of the State of Alaska (State). AEA's mission is to reduce the cost of energy in Alaska.

Throughout the 1980's, AEA worked to develop the State's energy resources as a key element in diversifying Alaska's economy. A number of large–scale projects were constructed; four of those projects were sold in 2002 and one was transferred to the City of Larsen Bay in the fall of 2010. The Bradley Lake Hydroelectric project together with the Alaska Intertie's 170 miles of transmission line help provide Interior Alaska with the cheaper energy available in the Southcentral portion of the State.

Pursuant to statute, on August 12, 1993, the board of the Alaska Industrial Development and Export Authority (AIDEA), a public corporation and a political subdivision of the State, became the board of directors of AEA. AEA continues to exist as a separate legal entity. The corporate structure and operating assets of AEA were retained but the ability to have employees, and construct or acquire energy projects was eliminated. Among other things, AIDEA provides personnel services for AEA. The AEA executive director is an employee of AIDEA, but is separate and independent and is not subject to supervision by AIDEA's executive director. There is no commingling of funds, assets or liabilities between AIDEA and AEA and there is no responsibility of one for the debts or the obligations of the other. Consequently, the accounts of AIDEA are not included in the accompanying financial statements. The 1993 legislation required AEA, to the maximum extent feasible, to enter contracts with public utilities and other entities to carry out AEA duties respecting the ongoing operation and maintenance of the AEA owned operating assets; this has occurred with oversight responsibility retained by AEA.

Pursuant to legislation effective July 1, 1999, rural energy programs previously administered by the former Department of Community and Regional Affairs, Division of Energy, were transferred to AEA for administration, as part of a larger reorganization of state agencies. Five general energy programs comprising more than twenty smaller programs were moved to AEA. Rural energy programs were originally part of AEA prior to the reorganization that occurred in 1993. During fiscal year 2009, legislation added energy development programs to AEA.

Effective July 14, 2011, the legislature empowered AEA to acquire, construct, own and operate a hydroelectric project located on the Susitna River. Under this legislative authorization, AEA is working on planning, design and licensing of the Susitna-Watana Hydroelectric Project.

The following is a description of AEA's existing projects and programs:

(a) Bradley Lake Hydroelectric Project

The project has 120 megawatts of installed capacity and transmits its power to the State's main power grid via two parallel 20–mile transmission lines. The project, which cost in excess of $300 million, went into commercial operation in 1991. The project is now operated by Homer Electric Association under contract with AEA. Bradley Lake serves Alaska's Railbelt from the Kenai Peninsula to Fairbanks as well as the Delta Junction area.

(b) Alaska Intertie Project

The Alaska Intertie is a 170–mile transmission line, designed for 345 kilovolts and is operating at 138 kilovolts. It runs between Willow and Healy, and interconnects the power systems in the Anchorage and Fairbanks areas. The Intertie reduces the number of black/brownouts throughout the system by enabling power to move either north or south when major system disturbances occur. The Alaska Intertie allows Golden Valley Electric Association (GVEA) in Fairbanks to purchase lower cost electricity produced by Chugach Electric Association (CEA) and the Municipality of Anchorage, d/b/a Municipal Light and Power (ML&P). It also allows Southcentral Alaska utilities to purchase power from Fairbanks during power shortages. AEA contracts with the above Participating Utilities for operations and maintenance. These duties are overseen by the Intertie Management Committee (IMC) and AEA under the Alaska Intertie Agreement (Agreement).

Effective July 1, 2002, the State appropriated $20,300,000 to AEA to upgrade and extend a portion of the Alaska Intertie. In August 2007, AEA issued a contract to ML&P for $19,500,000 for the upgrade; the work began in September 2007.

Effective July 1, 2008, the State re-appropriated $10,000,000 of the original funds for certain specific capital repairs on the Intertie. As a result, AEA amended the existing contract with ML&P to reduce scope of work regarding extending a portion of the Intertie, and entered into a separate $10,000,000 contract on August 26, 2010 with ML&P to repair static VAR compensators (SVC) and a tower foundation.

Effective July 1, 2011, the State appropriated an additional $5,000,000 for substation upgrades and tower repairs related to the Alaska Intertie. Tower foundation repairs are now completed. A contract has been let to a contractor for design and construction of a new SVC. The estimated completion date of the SVC contract is December 31, 2013. AEA continues to work with the Railbelt Utilities on the logical extension destination of the Alaska Intertie.

AEA management and Participating Utilities identified defects in the Agreement that AEA management believed should be corrected. Attempts to cure the identified defects were unsuccessful because amending the Agreement required unanimous consent of each member of the Intertie Operating Committee (IOC), but at least one utility member objected to each proposed cure. AEA management, on October 16, 2006, issued contractually required notice that the Agreement would terminate in 48 months. This termination deadline was extended to November 2011, to enable AEA, the Participating Utilities, and the United States Army to complete negotiations on amendments to the Agreement.

An amended and restated Intertie Agreement was executed on November 18, 2011. The Agreement improves the reliability of the interconnected electrical systems, outlines how transfer of electrical capacity and energy among the participants will be done, and establishes the IMC. The IMC's primary responsibility is to provide governance, control, operation, maintenance, repair and improvement of the Intertie. The IMC is comprised of a representative from AEA and each of the Participating Utilities.

(c) Larsen Bay Hydroelectric Project

The 475–kilowatt project produces electricity and provides water for the City of Larsen Bay (City), an isolated Kodiak Island community. It went into commercial operation in 1991 and replaced the City's old water supply system and provided a better source of water with reduced maintenance and improved water quality. The Authority conveyed the project to the City in the fall of 2010.

(d) Susitna-Watana Hydroelectric Project

The Alaska Legislature appropriated $10 million in funding to AEA effective July 1, 2010 for the preliminary planning and conceptual design for a large hydroelectric project to be built in the Railbelt Region. A number of hydroelectric generation alternatives were studied and in November 2010, AEA issued a Preliminary Decision Document selecting what is now known as the Susitna-Watana Hydroelectric Project as the primary large hydroelectric project for the State to pursue.

The Alaska Legislature unanimously passed and the Governor signed Senate Bill 42 effective July 14, 2011, which authorized the Authority to acquire a Susitna River power project. Senate Bill 46 appropriated $65.7 million, effective July 1, 2011, to plan, design and obtain permitting of the project. On December 29, 2011, AEA filed Notice of Intent and Pre-Application Document with the Federal Energy Regulatory Commission (FERC) to begin the licensing process for the project. AEA is actively engaged in this FERC process.

The proposed Susitna-Watana Hydroelectric Project would be located approximately half-way between Anchorage and Fairbanks on the upper Susitna River. The Susitna-Watana dam would be located within a steep-sided valley of the Susitna River below Watana Creek at River Mile 184 above the mouth approximately 34 miles upstream of the Devil's Canyon rapids.

As currently envisioned, the project would include a single dam with a height providing nominal crest elevation at 2,025 feet mean sea level with a 20,000 acre, 41-mile long, 2-miles wide (at widest) reservoir. The type and final height of the dam constructions are still being evaluated as part of the engineering feasibility studies. Preliminary studies indicated the surface powerhouse should have an installed capacity of 600 Megawatts (MW). The powerhouse, dam and related facilities would be linked by transmission lines connecting the project to the Alaska Intertie. The project would produce nearly 50% of the Railbelt's electrical demand, or an annual average of 2,800,000 Megawatt Hours (Mwh).

(e) Rural Energy Programs

The rural energy programs include Bulk Fuel Storage Upgrades, Rural Power System Upgrades, Power Cost Equalization (PCE), Utility Training, and Technical Assistance, two active loan programs funded from the Bulk Fuel Revolving Loan Fund and the Power Project Fund, and one inactive loan program. The PCE Endowment fund provides the PCE program a long-term stable financing source in order to reduce electricity costs for residential and community facility customers in otherwise high-cost service areas. As discussed in note 10, the Bulk Fuel Loan program was transferred from AEA subsequent to year end.

(f) Energy Development Programs

The energy development programs include the Renewable Energy Grants and Recommendation Program, Alternative Energy and Energy Efficiency Programs, and the Emerging Energy Technology Fund Grant Program.

The purpose of the Renewable Energy Grants program is to finance renewable energy projects in Alaska. The purpose of the Emerging Energy Technology Fund is to promote and provide financial assistance to applicants to test, conserve, and improve emerging energy technologies.

(2) Summary of Significant Accounting Policies

(a) Basis of Accounting – Enterprise Fund Accounting

The accounts of the Authority are organized as an Enterprise Fund. Accordingly, the financial activities of the Authority are reported using the economic resources measurement focus and the accrual basis of accounting, whereby revenues are recorded when earned and expenses are recorded when goods or services are received or the related liability is incurred.

GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, provides two options for reporting proprietary fund activities (including component units using proprietary fund accounting). The Authority has elected to apply all applicable GASB pronouncements and all FASB Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins issued on or before November 30, 1989, unless they conflict with or contradict GASB pronouncements.

Operating Revenue and Expense

The Authority considers all its revenues and expenses, except investment income, the sale of program loans, fund transfers with the State and conveyance of capital assets, to be part of its principal ongoing operations and therefore classifies these revenues and expenses as operating in the statement of revenues, expenses, and changes in net assets.

(b) Capital Assets

Capital assets are stated at cost and depreciation is charged to operations by use of the straight–line method over their estimated useful lives. The estimated economic lives of the assets are as follows:

Utility plant	Life in years
Intangible	30 – 50
Production	30 – 50
Transmission	20 – 40
General	5 – 30

The Authority recognizes impairment losses for long–lived assets whenever there is a significant unexpected decline in service utility. AEA recognizes intangible assets per the guidance of GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*.

(c) Cash and Investments

All of AEA's cash and investments are restricted as to use. For the purposes of the statement of cash flows, cash and cash equivalents consist of cash, short term commercial paper and money market funds.

AEA's marketable securities are reported at fair value in the financial statements. Unrealized gains and losses are reported as components of the change in net assets. Fair values are obtained from independent sources.

(d) Loans and Related Interest Income

Loans are generally carried at amounts advanced less principal payments collected. Interest income is accrued as earned. Accrual of interest is discontinued whenever the payment of interest or principal is more than ninety days past due or when the loan terms are restructured. The Authority considers lending activities to be part of its principal operations and classifies it as operating in the statement of revenues, expenses, and changes in net assets. For purposes of the statement of cash flows, the loan program activities are treated as investing activities.

(e) Allowance for Loan Losses

The allowance for loan losses represents management's judgment as to the amount required to absorb probable losses in the loan portfolio. The factors used by management to determine the allowance required include historical loss experience, individual loan delinquencies, collateral values, economic conditions and other factors. Management's opinion is that the allowance is currently adequate to absorb known losses and inherent risks in the portfolio.

(f) Environmental Issues

The Authority's policy relating to environmental issues, including pollution and contamination remediation obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups, is to record a liability when the likelihood of Authority responsibility for clean–up is probable and the costs are reasonably estimable. At June 30, 2012, there were no outstanding environmental issues which met both of these criteria and, accordingly, no provision has been made in the accompanying financial statements for any potential liability which may result.

(g) Income Taxes

The Internal Revenue Code provides that gross income for tax purposes does not include income accruing to a state or territory or any political subdivision thereof which is derived from the exercise of any essential governmental function or from any public utility. AEA is a public corporation of the State performing an essential governmental function and is therefore exempt from State and Federal income taxes.

(Continued)

(h) Appropriations and Grants

The Authority recognizes grant revenue under the provisions of GASB Statement No. 33, *Accounting and Financial Reporting for Nonexchange Transactions*, whereby revenue is recognized when all applicable eligibility requirements, including time requirements, are met.

(i) Estimates

In preparing the financial statements, management of the Authority is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent assets and liabilities as of the date of the balance sheet. These estimates impact revenue and expenses for the period. Actual results could differ from those estimates.

(j) Reclassifications

A reclassification was made to the 2011 financial statements to change how the Authority disclosed cash flows relating to certain loans. The impact of the reclassification was to increase cash used for operating activities and increase cash provided by investing activities by $21,288,000.

(3) Cash and Investments

Pursuant to various agreements, appropriations and statutory requirements relating to its operations, AEA has established accounts for assets restricted to construction, operation, and financing activities (as used throughout this footnote, Fund means a separate account established by the State legislature and does not refer to a separate group of self-balancing accounts as contemplated by U.S. generally accepted accounting principles).

At June 30, 2012 and 2011, the Authority’s carrying amount of deposits (all of which were restricted or designated for specific purposes) was $116,244,000 and $79,609,000, respectively. The total of all bank balances on the same dates was $118,175,000 and $80,440,000, respectively.

(Continued)

The restricted and designated cash and investments were held in trust accounts for the following activities as of June 30, 2012 (stated in thousands):

		Cash and cash equivalents	Investments	Total
Power Cost Equalization Endowment Fund	$	6	751,775	751,781
Renewable Energy Grant Fund		—	44,588	44,588
Bradley Lake Hydroelectric Project		9,490	20,880	30,370
Rural Energy Loan Funds		16,264	37,048	53,312
Rural Energy and Energy Development Programs		9,692	—	9,692
Funds advanced from State and federal agencies		14	—	14
Renewable Energy Grant Program		46,316	—	46,316
Emerging Energy Technology Fund		—	4,800	4,800
Power Development Fund		34,063	—	34,063
Alaska Intertie Project		399	—	399
Total cash and investments	$	116,244	859,091	975,335

The restricted and designated cash and investments were held in trust accounts for the following activities as of June 30, 2011 (stated in thousands):

		Cash and cash equivalents	Investments	Total
Power Cost Equalization Endowment Fund	$	2,714	361,815	364,529
Renewable Energy Grant Fund		—	87,822	87,822
Bradley Lake Hydroelectric Project		9,300	21,014	30,314
Rural Energy Loan Funds		34,570	22,085	56,655
Rural Energy and Energy Development Programs		6,897	5,031	11,928
Funds advanced from State and federal agencies		16,722	—	16,722
Renewable Energy Grant Program		3,824	—	3,824
Power Development Fund		1,213	—	1,213
Alaska Intertie Project		4,369	—	4,369
Total cash and investments	$	79,609	497,767	577,376

At June 30, 2012 and 2011, amounts restricted for debt service totaled $22,773,000 and $22,370,000, respectively, for the Bradley Lake Hydroelectric Project.

Investment Holdings

Power Cost Equalization Endowment Fund, Renewable Energy Grant Fund and Emerging Energy Technology Fund – The Power Cost Equalization Endowment Fund (PCE Fund), created under Alaska Statute 42.45.070, the Renewable Energy Fund (RE Fund), created under Alaska Statute 42.45.045, and the Emerging Energy Technology Fund (EET Fund), created under AS 42.45.375, are under the fiduciary authority of the State Department of Revenue, Treasury Division (Treasury).

State investments, including those managed by Treasury for the Authority, are managed in pools. PCE Fund assets are held in the State's internally managed Short–term Fixed Income Pool and the Conservative Broad Market Pool (which consists solely of investments in the Broad Market and U.S. Treasury Fixed Income Pools), as well as the State's externally managed Domestic Equity account and International Equity Pool. RE and EET Fund assets are held in the State's internally managed General Fund and Other Non-Segregated Investments Pool (GeFONSI). The GeFONSI consists of investments in the State's internally managed Short-term and Intermediate-term Fixed Income Pools. The complete financial activity of the funds is shown in the Comprehensive Annual Financial Report available from the Division of Finance in the State Department of Administration.

Fixed income and international equity securities are valued each business day using prices obtained from a pricing service. The Domestic Equity account is valued each business day by the Trustee Committee in good faith and pursuant to procedures established by the Trustee. Securities expressed in terms of foreign currencies are translated into U.S. dollars at the prevailing exchange rates.

The accrual basis of accounting is used for investment income. Income in the other fixed income pools and the International Equity Pool is allocated to pool participants daily on a pro rata basis. Domestic equity income is distributed quarterly.

At June 30, 2012, AEA had the following cash and investments in the PCE, RE, and EET Funds (stated in thousands):

	Cash	Investments at fair value			
	PCE Fund	RE and EET Funds	PCE Fund		
Investment type	Short-term fixed income pool	Short and intermediate-terms fixed income pools	Broad market and U.S. Treasuries fixed income pools	Equity	Total
Commercial paper	$ 948	827	314	—	314
U.S. Treasury bonds	—	—	13,439	—	13,439
U.S. Treasury bills	14,715	17,742	2,764	—	2,764
U.S. Treasury notes	—	14,457	52,017	—	52,017
U.S. Treasury strip	—	13			
U.S. government agency	333	1,335	9,618	—	9,618
Mortgage-backed	236	1,005	84,149	—	84,149
Deposit	111	96	—	—	—
Other asset-backed	9,812	8,520	6,452	—	6,452
Corporate bonds	2,535	5,453	48,478	—	48,478
Yankee:					
Government	—	132	5,112	—	5,112
Corporate	583	501	11,411	—	11,411
Domestic equity	—	—	—	348,086	348,086
International equity	—	—	—	159,036	159,036
Total invested assets	29,273	50,081	233,754	507,122	740,876
Pool related net liabilities	(795)	(693)	(17,573)	—	(17,573)
Other pool ownership	(28,472)	—	28,472	—	28,472
Net invested assets	$ 6	49,388	244,653	507,122	751,775

At June 30, 2011, AEA had the following cash and investments in the PCE and RE Funds (stated in thousands):

	Cash	Investments at fair value			
	PCE Fund	RE Fund	PCE Fund		
Investment type	Short-term fixed income pool	Short and intermediate-term fixed income pools	Broad market and U.S. Treasuries fixed income pools	Equity	Total
Commercial paper	$ 1,383	3,799	—	—	—
U.S. Treasury bonds	—		2,454	—	2,454
U.S. Treasury bills	2,891	7,657	—	—	—
U.S. Treasury notes	—	27,159	40,590	—	40,590
U.S. Treasury strip	—	25	—		
U.S. government agency	341	2,719	3,927	—	3,927
U.S. government agency discount notes	506	1,339	971	—	971
Mortgage-backed	284	2,128	38,903	—	38,903
Other asset-backed	6,138	16,900	2,838	—	2,838
Overnight sweep account	165	437	—	—	—
Corporate bonds	6,117	23,154	21,864	—	21,864
Yankee:					
Government	—	308	1,067	—	1,067
Corporate	121	1,471	5,189	—	5,189
Domestic equity	—	—	—	177,311	177,311
International equity	—	—	—	51,411	51,411
Total invested assets	17,946	87,096	117,803	228,722	346,525
Pool related net assets (liabilities)	8	726	(15,540)	15,590	50
Other pool ownership	(15,240)	—	15,240	—	15,240
Net invested assets	$ 2,714	87,822	117,503	244,312	361,815

Other AEA Cash and Investments – Bradley Lake Hydroelectric Project investments are substantially invested pursuant to investment agreements with JP Morgan Chase Bank that guarantees annual interest earnings of 7.38% or 7.41% per annum that end the earlier of July 1, 2021 or the date of repayment of the Bradley Lake Power Revenue Bonds, First Series.

Under the Internal Revenue Code of 1986, as amended, certain earnings in excess of arbitrage yield on the Bradley Lake bonds must be rebated to the U.S. Treasury. The bulk of the Bradley Lake investments are subject to rebate computation.

All other AEA assets are managed by internal staff for liquidity and minimal risk. There is no AEA board approved investment policy, but staff follows AIDEA's board approved investment policy for internally managed investments. The AEA managed portfolio consists of the following eligible securities:

- Debt instruments issued or guaranteed by the U.S. government, its agencies and instrumentalities, and Government Sponsored Enterprises (GSEs); and
- Money market funds collateralized by U.S. Treasury and agency securities.

At June 30, 2012 and 2011, the fair values of AEA's cash and investments in its other funds (stated in thousands) were:

Investment type		2012	2011
Deposits	$	827	65
Money market funds		115,412	76,831
U.S. Treasury notes		37,047	27,115
Investment agreements		20,880	21,014
Total invested assets	$	174,166	125,025

Interest Rate Risk – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Duration is a measure of interest rate risk. It measures a security's sensitivity to a 100–basis point change in interest rates. Treasury uses industry–standard analytical software developed by The Yield Book Inc. to calculate effective duration. The software takes into account various possible future interest rates, historical and estimated prepayment rates, call options and other variable cash flows for purposes of the effective duration calculation. Duration for the AEA managed investments are as reported on Bloomberg.

Short–Term Fixed Income Pool – As a means of limiting its exposure to fair value losses arising from increasing interest rates, Treasury's investment policy limits individual fixed rate securities to fourteen months to maturity or fourteen months expected average life upon purchase. Floating rate securities are limited to three years to maturity or three years expected average life upon purchase. Treasury utilizes the actual maturity date for commercial paper and twelve-month prepay speeds for other securities. At both June 30, 2012 and 2011, the expected average life of individual fixed rate securities ranged from one day to one year and the expected average life of floating rate securities ranged from eight days to fourteen years.

Intermediate-Term Fixed Income Pool – Through its investment policy, Treasury manages its exposure to fair value losses arising from increasing interest rates by limiting effective duration of the Intermediate-term Fixed Income Pool to ± 20% of the Merrill Lynch 1-5 year Government Bond Index. The effective duration for the Merrill Lynch 1-5 year Government Bond Index was 2.66 years at June 30, 2012 and 2.54 years at June 30, 2011.

(Continued)

Broad Market and U.S. Treasury Fixed Income Pools – Through its investment policy, Treasury manages its exposure to fair value losses arising from increasing interest rates by limiting the effective duration of its other fixed income pool portfolios to the following:

> Broad Market Fixed Income Pool: ± 20% of the Barclay's Capital U.S. Aggregate Bond Index. The effective duration of the Index at June 30, 2012 was 5.07 years. The effective duration of the Index at June 30, 2011 was 5.19 years.

> U.S. Treasury Fixed Income Pool: ± 20% of the Barclay's Capital U.S. Aggregate Treasury Index. There were no investments in this pool at June 30, 2012. The effective duration of the Index at June 30, 2011 was 3.94 years.

AEA Internally Managed Investments – There is no written policy for interest rate risk for AEA's internally managed investments, but AIDEA's policy is followed. The duration for investments is 2 years or less. The maximum maturity of any issue is 3 years from the date of purchase.

Treasury has no policy with regard to interest rate risk for the money market balance held in the International Equity Pool.

At June 30, 2012 and 2011, the effective duration by investment type (not including the investment agreements) was as follows:

Managed by Treasury	Intermediate-term fixed income pool	Broad market fixed income pool	U.S. Treasury fixed income pool
		2012	
U.S. Treasury notes	2.78	5.23	—
U.S. Treasury strip	5.26	—	—
U.S. Treasury bills	0.30	0.43	—
U.S. Treasury bonds	—	15.53	—
U.S. government agency	1.24	5.40	—
Mortgage-backed	1.28	1.70	—
Other asset-backed	2.43	1.89	—
Corporate bonds	1.62	6.93	—
Yankees:			
Government	1.72	7.30	—
Corporate	2.63	4.20	—
Portfolio effective duration	2.23	4.28	—
		2011	
U.S. Treasury notes	3.09	4.74	3.89
U.S. Treasury strip	6.37	—	—
U.S. Treasury bonds	—	14.64	—
U.S. government agency	2.65	5.74	—
U.S. government agency discount notes	—	0.01	—
Mortgage-backed	1.52	3.25	—
Other asset-backed	1.08	0.97	—
Commercial Paper	0.05	—	—
Corporate bonds	2.01	5.93	—
Yankees:			
Government	1.92	6.38	—
Corporate	2.28	—	—
Portfolio effective duration	2.53	4.46	3.89

	Managed by AEA	
	2012	**2011**
Money market	0.11	0.07
U.S. Treasury notes	0.78	0.57
Portfolio effective duration	0.27	0.20

Credit Risk – Credit risk is the financial risk that an issuer or other counter party to an investment will not fulfill its obligations. Treasury's investment policy has the following limitations with regard to credit risk:

Short-Term Fixed Income Pool – Short-term Fixed Income Pool investments are limited to instruments with a long-term credit rating of at least A3 or equivalent and instruments with a short-term credit rating of at least P-1 or equivalent. Asset-backed and Nonagency mortgage securities must be rated A3 or equivalent. The A3 rating is defined as the median rating of the following three rating agencies: Standard & Poor's Corporation, Moody's and Fitch. Asset-backed and Nonagency mortgage securities may be purchased only if they are rated AAA.

Intermediate-Term Fixed Income Pool – Intermediate-term Fixed Income Pool investments are limited to securities with a long-term credit rating of at least Baa3 or equivalent and securities with a short-term credit rating of at least P-1 or equivalent. Asset-backed and Nonagency mortgage securities must be rated investment grade. The investment grade rating is defined as the median rating of the following three rating agencies: Standard & Poor's Corporation, Moody's and Fitch. Asset-backed and Nonagency mortgage securities may be purchased if only rated by one of these agencies if they are rated AAA.

Broad Market Fixed Income Pool – The Broad Market Fixed Income Pool investments are limited to securities with a long-term credit rating of at least Baa3 or equivalent and securities with a short-term credit rating of at least P-1 or equivalent. Asset-backed and Nonagency mortgage securities must be rated investment grade. The investment grade rating is defined as the median rating of the following three rating agencies: Standard & Poor's Corporation, Moody's and Fitch. Asset-backed and Nonagency mortgage securities may be purchased if only rated by one of these agencies if they are rated AAA.

U.S. Treasury Fixed Income Pool – In the U.S. Treasury Fixed Income Pool, commercial paper must be rated at least P-1 by Moody's and A-1 by Standard & Poor's Corporation. In addition, corporate, asset-backed and Nonagency mortgage securities must be rated investment grade. The investment grade rating is defined as the median rating of the following three rating agencies: Standard & Poor's Corporation, Moody's and Fitch. In addition, asset-backed and Nonagency mortgage securities may be purchased if only rated by one of these agencies if they are rated AAA. Corporate bonds may be purchased if rated by two of these agencies.

There is no written policy with regard to credit risk for investments managed by AEA. Since AEA only invests in highly rated money markets and U.S. government and agency securities and GSEs, credit risk is minimal.

The Bradley Lake Hydroelectric Project investments are substantially invested in guaranteed interest accounts collateralized by federal obligations, which minimize credit risk.

(Continued)

At June 30, 2012, the Pools managed by Treasury and the investments managed by AEA consisted of investments with credit quality ratings issued by nationally recognized statistical rating organizations as follows (using Standard & Poor's Corporation rating scale).

Investment type	Rating	Short-term fixed income pool	Intermediate-term fixed income pool	Broad market fixed income pool	AEA managed
Money market	AAA	—%	—%	—%	67%
Commercial paper	A-1	—	—	—	—
Commercial paper	Not Rated	3	—	—	—
U.S. Treasury notes	AA	—	65	20	21
U.S. Treasury bills	AA	52	8	1	—
U.S. Treasury bond	AA	—	—	5	—
U.S. government agency	AA	1	5	1	—
Mortgage-backed	AAA	—	2	3	—
Mortgage-backed	AA	—	1	27	—
Mortgage-backed	A	—	—	1	—
Mortgage-backed	Not Rated	—	1	3	—
Other asset-backed	AAA	26	—	2	—
Other asset-backed	AA	2	—	—	—
Other asset-backed	Not Rated	6	—	—	—
Other pool ownership	Not Rated	—	2	11	
Corporate bonds	AAA	—	1	1	—
Corporate bonds	AA	5	8	3	—
Corporate bonds	A	4	3	10	—
Corporate bonds	BBB	—	1	5	—
Corporate bonds	Not Rated	—	—	—	—
Yankees – government	AA	—	1	—	—
Yankees – government	Not Rated	—	—	3	—
Yankees – government	AAA	—	1	1	—
Yankees – corporate	AA	2	1	1	—
Yankees – corporate	A	1	—	1	—
Yankees – corporate	BBB	—	—	1	—
No credit exposure		(2)	—	—	—
Investment agreements	Not Rated	—	—	—	12
		100%	100%	100%	100%

At June 30, 2011, the Pools managed by Treasury and the investments managed by AEA consisted of investments with credit quality ratings issued by nationally recognized statistical rating organizations as follows (using Standard & Poor's Corporation rating scale).

Investment type	Rating	Short-term fixed income pool	Intermediate-term fixed income pool	Broad market fixed income pool	U.S. Treasury income pool	AEA managed
Money market	AAA	—%	—%	—%	—%	61%
Commercial paper	A-1	7	—	—	—	—
Commercial paper	Not Rated	1	—	—	—	—
U.S. Treasury notes	AAA	—	62	28	100	22
U.S. Treasury bills	AAA	16	—	2	—	—
U.S. government agency	AAA	2	4	4	—	—
U.S. government agency discount notes	Not Rated	3	1	1	—	—
Mortgage-backed	AAA	1	3	19	—	—
Mortgage-backed	AA	—	—	1	—	—
Mortgage-backed	A	—	—	1	—	—
Mortgage-backed	Not Rated	—	—	16	—	—
Other asset-backed	AAA	30	1	2	—	—
Other asset-backed	Not Rated	4	—	—	—	—
Corporate bonds	AAA	24	10	2	—	—
Corporate bonds	AA	1	1	3	—	—
Corporate bonds	A	3	3	9	—	—
Corporate bonds	BBB	—	1	6	—	—
Corporate bonds	Not Rated	6	—	—	—	—
Yankees – government	AA	—	1	1	—	—
Yankees – corporate	AAA	—	1	1	—	—
Yankees – corporate	AA	1	1	1	—	—
Yankees – corporate	A	—	1	2	—	—
Yankees – corporate	BBB	—	—	1	—	—
No credit exposure		1	10	—	—	—
Investment agreements	Not Rated	—	—	—	—	17
		100%	100%	100%	100%	100%

Custodial Credit Risk – Custodial credit risk is the risk that deposits may not be returned in the event of a bank failure. Treasury's policy with regard to custodial credit risk is to collateralize State deposits to the extent possible. At June 30, 2012, AEA's deposits managed by Treasury were uncollateralized and uninsured.

With respect to AEA managed investments, amounts totaling approximately $105,921,000 at June 30, 2012 and $67,531,000 at June 30, 2011, are held in money market funds not registered in AEA's name. The investment agreements are collateralized. All other investment securities are registered in AEA's name and are held by its custodian, the trust department of a commercial bank; therefore no custodial risk exists for these securities.

Foreign Currency Risk – The Commissioner of Revenue formally adopts asset allocation policies for AEA's PCE Fund at the beginning of each fiscal year which places policy limitations on the amount of international securities the PCE Fund is allowed to hold. The following policy was in place during fiscal years 2012 and 2011, and invested assets included the following holdings at June 30, 2012 and 2011, for the PCE Fund's investment in the International Equity Pool:

	Policy	Actual
FY12	23%+5%	21.15%
FY11	10%+5%	14.73

At June 30, 2012 and 2011, AEA's PCE Fund had exposure to foreign currency risk as follows (stated in thousands):

Currency		FY12 Fair value	FY11 Fair value
Deposits:			
Euro Currency	$	24	9
Japanese Yen		40	69
Danish Krone		—	2
		64	80
Investment – international equity:			
Australian Dollar		3,645	1,632
Canadian Dollar		1,334	821
Danish Krone		616	—
Euro Currency		16,872	11,894
Hong Kong Dollar		—	511
Japanese Yen		8,575	8,660
New Zealand Dollar		484	576
Norwegian Krone		—	355
Pound Sterling		14,562	12,224
Singapore Dollar		—	—
Swedish Krona		2,208	947
Swiss Franc		2,024	2,536
		50,320	40,156
Total	$	50,384	40,236

Concentration of Credit Risk – Treasury's policy with regard to concentration of credit risk is to prohibit the purchase of more than five percent of a pool's holdings in corporate bonds of any one company or affiliated group. However, such prohibition does not apply to securities backed by the full faith and credit of the U.S. government. Federal National Mortgage Association securities are not classified as corporate bonds. AEA has no written policy with respect to concentration of credit risk for its other investments.

At June 30, 2012, AEA did not have more than five percent of its investments in any one company or affiliated group.

At June 30, 2011, AEA's investments (excluding U.S. Treasury securities) included the following concentrations greater than 5% (dollar amounts stated in thousands):

Issuer	Amount	Percent
Federal National Mortgage Association	$ 28,777	5%

(4) Capital Assets

Capital asset activity for the years ended June 30, 2012 and 2011 was as follows (stated in thousands):

	Balance at July 1, 2011	Additions	Deletions	Balance at June 30, 2012
Capital assets:				
Intangible	$ 14	—	—	14
Production	254,011	13,029	—	267,040
Transmission	189,465	2,236	(3,131)	188,570
General	6,322	76	(596)	5,802
Total capital assets	449,812	15,341	(3,727)	461,426
Less accumulated depreciation for:				
Intangible	(4)	(1)	—	(5)
Production	(100,008)	(5,304)	—	(105,312)
Transmission	(117,206)	(4,350)	—	(121,556)
General	(5,156)	(87)	—	(5,243)
Total accumulated depreciation	(222,374)	(9,742)	—	(232,116)
Capital assets, net	$ 227,438	5,599	(3,727)	229,310

(Continued)

Assets not being depreciated included above are land and right of ways of $11,212,000 and construction in process of $13,681,000. Construction in process includes $11,532,000 of intangible assets.

	Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011
Capital assets:				
Intangible	$ 14	—	—	14
Production	253,296	953	(238)	254,011
Transmission	189,642	1	(178)	189,465
General	6,019	303	—	6,322
Total capital assets	448,971	1,257	(416)	449,812
Less accumulated depreciation for:				
Intangible	(4)	—	—	(4)
Production	(94,956)	(5,290)	238	(100,008)
Transmission	(112,424)	(4,960)	178	(117,206)
General	(5,115)	(41)	—	(5,156)
Total accumulated depreciation	(212,499)	(10,291)	416	(222,374)
Capital assets, net	$ 236,472	(9,034)	—	227,438

Assets not being depreciated included above are land and right of ways of $11,212,000 and construction in process of $4,443,000. Construction in process includes $880,000 of intangible assets.

In September 2010, AEA conveyed the fully depreciated Larsen Bay Hydroelectric Project to the City of Larsen Bay.

On August 19, 2011, AEA conveyed the Napakiak Intertie assets to the Napakiak Irecinraq Power Corporation pursuant to the federal grant agreement that provided funding for the project. The book value of the transferred assets was $3,131,000.

(5) Long–Term Debt

Long–term debt activity for the years ended June 30, 2012 and 2011 was as follows (stated in thousands):

		Balance at July 1, 2011	Additions	Deletions	Balance at June 30, 2012	Due within one year
Bradley Lake Power Revenue Bonds:						
` First Series (a)	$	100	—	—	100	—
Refunding, Third Series (a)		33,910	—	(4,040)	29,870	4,280
Refunding, Fourth Series (a)		36,755	—	(2,455)	34,300	2,600
Refunding, Sixth Series (a) (b)		28,800	—	—	28,800	—
Total bonds payable		99,565	—	(6,495)	93,070	6,880
Arbitrage interest payable (c)		494	319	—	813	—
Bond discount and deferred interest		1,606	—	(189)	1,417	—
	$	101,665	319	(6,684)	95,300	6,880

		Balance at July 1, 2010	Additions	Deletions	Balance at June 30, 2011	Due within one year
Bradley Lake Power Revenue Bonds:						
First Series (a)	$	100	—	—	100	—
Second Series (a)		2,305	—	(2,305)	—	—
Refunding, Third Series (a)		37,720	—	(3,810)	33,910	4,040
Refunding, Fourth Series (a)		36,895	—	(140)	36,755	2,455
Refunding, Fifth Series (a) (b)		30,640	—	(30,640)	—	—
Refunding, Sixth Series (a) (b)		—	28,800	—	28,800	—
Total bonds payable		107,660	28,800	(36,895)	99,565	6,495
Arbitrage interest payable (c)		407	211	(124)	494	—
Bond discount and deferred interest		18	2,299	(711)	1,606	—
	$	108,085	31,310	(37,730)	101,665	6,495

(a) AEA issued the Power Revenue Bonds, First and Second Series (Bradley Lake Bonds), in September 1989 and August 1990, respectively, for the long term financing of the construction costs of the Bradley Lake Hydroelectric Project and refunded AEA's Variable Rate Demand Bonds which were issued in November 1985 to provide interim financing of the project. AEA issued the Power Revenue Refunding Bonds, Third and Fifth Series in April 1999 to refund a portion of the First Series Bonds and to provide costs of issuance. AEA issued the Power Revenue Refunding Bonds, Fourth Series in April 2000 to refund a portion of the Second Series Bonds and to provide costs of issuance. All of the revenues derived by AEA from the operation of the project and all moneys, securities and funds (except the excess investment earnings fund), including a capital reserve fund, held or set aside are pledged and assigned to secure the payment of principal, redemption premium, if any, and interest on the bonds. No other revenues of AEA are pledged as security for the payment of the bonds. AEA has covenanted to notify the State Legislature of any failure to maintain the capital reserve fund at its required level. The bonds, except for the Sixth Series, are further secured by bond insurance. AEA collects from each power purchaser a percentage share of annual project costs. The outstanding Bradley Lake bonds mature annually each July 1 through the year 2021 with interest rates ranging from 2.5% to 6.25%.

(b) In July 2010 the Authority issued $28,800,000 of Power Revenue Refunding Bonds, Sixth Series, to refund and defease $30,640,000 aggregate outstanding principal amount of the Authority's Power Revenue Refunding Bonds, Fifth Series, and to pay costs of issuing the bonds. The refunding resulted in aggregate debt service payments over the next eleven years of approximately $3,316,000 less than the debt service payments which would have been due on the refunded bonds. There was an economic gain of approximately $2,350,000 which is calculated as the net difference between the present value of the old debt service requirements and the present value of the new debt service requirements, discounted at the effective interest rate and adjusted for additional cash paid. The refunded bonds were called on August 2, 2010.

(c) proceeds of each series of AEA's tax exempt Bradley Lake bonds over the related interest expense computed in accordance with Section 148 of the Internal Revenue Code of 1986, as amended. The accumulated arbitrage interest payable amount is computed each year, and the amount for each series is first due after the end of the fifth bond year and every five years thereafter. AEA maintains a separate account for each series with the trustee and each year sets aside a sufficient amount to satisfy the liability.

The minimum payments related to all bonds for the years subsequent to June 30, 2012 are as follows (stated in thousands):

	Principal	Interest	Total
Year ending June 30:			
2013	$ 6,880	5,014	11,894
2014	7,300	4,589	11,889
2015	7,735	4,138	11,873
2016	8,570	3,655	12,225
2017	9,090	3,138	12,228
2018 – 2022	53,495	7,285	60,780
	$ 93,070	27,819	120,889

In addition, the Authority has participated in the following debt agreements:

- *Other Debt* – In 1982, AEA assumed $44,859,000 of 5% mortgage notes payable which requires quarterly principal and interest payments to the Rural Utilities Service (RUS) in connection with the Solomon Gulch Hydroelectric Project. Concurrent with the assumption, AEA deposited with a trustee Treasury notes sufficient to satisfy and provide for timely repayment of all principal and interest due on the assumed RUS loans. Accordingly, the loans and related trust assets are not included in the financial statements of AEA. At June 30, 2012, the unpaid principal balance of the notes was $6,381,000 and the trust assets had a fair value of $6,928,000.
- *Conduit Financing – City and Borough of Sitka – Utility Revenue Refunding Bonds, Series 1997 and Utility Revenue Bonds, Series 1992* – In May 1992, AEA issued $56,890,000 of tax–exempt bonds that allowed the City and Borough of Sitka (Sitka) to refinance its 1979 municipal bonds, resulting in significant debt service savings to Sitka. In November 1997, AEA issued $22,080,000 of tax–exempt bonds to advance refund and defease $20,145,000 of the Series 1992 bonds (collectively with the Series 1992 bonds, the Sitka Bonds). The Sitka Bonds are not included in these financial statements.

  In December 2010, the Alaska Municipal Bond Bank issued bonds, the proceeds of which were used to refund and defease the Sitka Bonds. The Series 1992 bonds were defeased and $10,600,000 remain outstanding at June 30, 2012. The Series 1997 bonds were called and redeemed in January 2011.

(6) Loans

The Authority administers the Power Project Loan Program, the Rural Electrification Revolving Loan Program and the Bulk Fuel Revolving Loan Program. Loans outstanding at June 30, 2012 and 2011 are classified as follows (dollar amounts stated in thousands):

	2012		2011	
	No. of loans	**Amount**	**No. of loans**	**Amount**
Power Project Loan Program	5	$ 2,309	5	$ 1,329
Rural Electrification Revolving Loan Program	2	483	2	539
Bulk Fuel Revolving Loan Program	22	3,228	17	1,550
	29	6,020	24	3,418
Less allowance for loan losses		(181)		(93)
		$ 5,839		$ 3,325

Pursuant to legislation and an agreement, on September 30, 2010 AEA sold to AIDEA for $20,631,000, thirty-seven (37) Power Project Fund loans with a then outstanding balance of $24,254,000, plus accrued interest. Under the agreement, at AIDEA's request, AEA is required to repurchase any loan upon a payment default. As a result, AEA has recognized an estimated liability equal to AIDEA's allowance for loan losses attributable on the remaining outstanding principal balance of the sold loans. On June 30, 2012, the outstanding principal balance of the loans sold was $20,668,800, for which AEA has recognized an estimated liability of $620,000.

Pursuant to legislation, effective January 1, 2013, the Bulk Fuel program, all outstanding Bulk Fuel loans, and the Bulk Fuel Revolving Loan Fund that provides the program's funding will be transferred from AEA to the Department of Commerce, Community and Economic Development's Division of Community and Regional Affairs.

At June 30, 2012, there were no loan more than 90 days past due. At June 30, 2011, loans more than 90 days past due on which the accrual of interest has been discontinued amounted to $68,800.

An analysis of changes in the allowance for loan losses for the years ended June 30, 2012 and 2011 follows (stated in thousands):

		2012	2011
Balance at beginning of year	$	93	834
Loan sale		—	(727)
Provision for loan loss		88	(14)
Balance at end of year	$	181	93

(7) Risk Management

AEA is exposed to various risks of loss and obtains coverage for its risks through the purchase of commercial insurance and participation in the State Risk Management Pool.

(8) Related Parties

(a) Alaska Industrial Development and Export Authority

Pursuant to understandings and agreements between AIDEA and AEA, AIDEA provides administrative, treasury, personnel, data processing, communications, and other services to AEA. During 2012 and 2011, AEA expensed $6,298,000 and $5,678,000, respectively, for such services. During 2012 and 2011, AEA capitalized $657,000 and $14,000, respectively, for such services. AEA has a borrowing arrangement with AIDEA to provide working capital funds. At June 30, 2012 and 2011, AEA had $5,128,000 and $1,671,000, respectively, payable to AIDEA for services and borrowings.

As discussed in note 6, during 2011, AEA sold loans to AIDEA for $20,631,000.

(b) Alaska Intertie Management Committee

AEA is party to agreement with utilities using the Alaska Intertie for wheeling of electrical power. Pursuant to the Intertie Agreement, the Intertie Management Committee (IMC) was established to manage the system. The IMC is comprised of a representative from AEA and each of the utilities. AEA is reimbursed for operation and maintenance costs on a monthly basis with an annual settlement to adjust the payments to actual costs. AEA received $46,000 and $40,000 for fiscal year 2012 and 2011, respectively for administrative services.

(c) Bradley Lake Project Management Committee

Effective December 7, 1987, AEA entered into a power sales agreement with entities purchasing electric power produced by the Bradley Lake Hydroelectric Project. Pursuant to the agreement, a Project Management Committee (PMC) was formed. The PMC is comprised of a representative from AEA and each of the power purchasers. The participating power purchasers make monthly payments directly to the bond trustee based on their respective percentage share of the estimated annual project costs, including debt service and an annual administrative fee of $200,000 to AEA.

(9) Commitments and Contingencies

In the normal course of business, AEA also has various commitments, such as commitments for the extension of credit and award of grants. At June 30, 2012 and 2011, AEA had open loan commitments of $9,819,000 and $23,516,000, respectively. At June 30, 2012 and 2011, AEA had committed to grant awards to be funded by State appropriations and federal awards; the amounts committed were $101,786,000 and $87,729,000, respectively.

(10) Subsequent Event

Pursuant to legislation, effective January 1, 2013, the Bulk Fuel program, all outstanding Bulk Fuel loans, and the Bulk Fuel Revolving Loan Fund that provides the program’s funding will be transferred from AEA to the Department of Commerce, Community and Economic Development’s Division of Community and Regional Affairs.

Schedule 1

ALASKA ENERGY AUTHORITY
(A Component Unit of the State of Alaska)

Schedule of Bradley Lake Hydroelectric Project Trust Account Activities

Year ended June 30, 2012

(Stated in thousands)

		Debt service fund	Capital reserve fund	Renewal and contingency reserve fund	Excess investment earnings fund	Revenue fund	Operating fund	Operating reserve account	Total
Balance at July 1, 2011	$	9,300	12,779	3,872	291	2,225	944	903	30,314
Interest received		341	815	310	17	353	75	65	1,976
Bond principal paid		(6,495)	—	—	—	—	—	—	(6,495)
Bond interest paid		(5,416)	—	—	—	—	—	—	(5,416)
Operating budget surplus paid		—	—	—	—	(1,183)	—	—	(1,183)
Construction expenditures		—	—	(932)	—	(135)	—	—	(1,067)
Operating revenue received		—	—	—	—	16,205	—	—	16,205
Operating expenses paid		—	—	—	—	—	(3,963)	—	(3,963)
Transfers between funds		11,760	(815)	1,421	196	(16,554)	4,120	(128)	—
Balance at June 30, 2012	$	9,490	12,779	4,671	504	911	1,176	840	30,371

See accompanying independent auditors' report.

ALASKA ENERGY AUTHORITY
(A Component Unit of the State of Alaska)

Schedule of Projects and Programs– Balance Sheet

June 30, 2012

(Stated in thousands)

Assets	Bradley Lake Hydroelectric Project	Alaska Intertie Project	Susitna-Watana Hydroelectric Project	Rural Energy Projects	Administration and Power Development Fund	Rural Energy and Energy Development Programs	Combined balance
Current assets:							
Grants receivable	$ —	—	—	—	(479)	3,731	3,252
Loans receivable	—	—	—	—	—	3,318	3,318
Operating revenue receivable	—	118	—	—	—	9,975	10,093
Due (to) from State of Alaska	203	21	350	—	(1,554)	4,804	3,824
Accrued interest receivable	1,036	—	—	—	—	48	1,084
Total current assets	1,239	139	350	—	(2,033)	21,876	21,571
Noncurrent assets:							
Restricted cash and investments	22,773	—	—	—	—	—	22,773
Cash and investments designated for specific purposes	7,598	399	—	—	34,063	910,502	952,562
Loans receivable, net of allowance	—	—	—	—	—	2,521	2,521
Capital assets, net of accumulated depreciation	181,587	37,568	10,155	—	—	—	229,310
Total noncurrent assets	211,958	37,967	10,155	—	34,063	913,023	1,207,166
Total assets	$ 213,197	38,106	10,505	—	32,030	934,899	1,228,737
Liabilities and Net Assets							
Current liabilities:							
Due (from) to State of Alaska	$ —	—	(3,518)	—	29,671	(3,918)	22,235
Accounts payable	3,671	521	3,769	237	187	28,856	37,241
Bonds payable – current portion	6,880	—	—	—	—	—	6,880
Accrued interest payable	2,610	—	—	—	—	—	2,610
Total current liabilities	13,161	521	251	237	29,858	24,938	68,966
Noncurrent liabilities:							
Bonds payable – noncurrent portion, net	87,607	—	—	—	—	—	87,607
Arbitrage interest payable – noncurrent portion	813	—	—	—	—	—	813
Other liabilities	103		99	—	—	521	723
Total noncurrent liabilities	88,523	—	99	—	—	521	89,143
Total liabilities	101,684	521	350	237	29,858	25,459	158,109
Net assets:							
Invested in capital assets, net of related debt	87,099	37,568	10,155	—	—	—	134,822
Restricted for debt service	20,163	—	—	—	—	—	20,163
Restricted by agreements with external parties	4,251	17	—	—	—	9,267	13,535
Unrestricted	—	—	—	(237)	2,172	900,173	902,108
Total net assets	111,513	37,585	10,155	(237)	2,172	909,440	1,070,628
Total liabilities and net assets	$ 213,197	38,106	10,505	—	32,030	934,899	1,228,737

See accompanying independent auditors' report.

Schedule 3

ALASKA ENERGY AUTHORITY
(A Component Unit of the State of Alaska)

Schedule of Projects and Programs – Revenues, Expenses, and Changes in Net Assets

Year ended June 30, 2012

(Stated in thousands)

		Bradley Lake Hydroelectric Project	Alaska Intertie Project	Susitna-Watana Hydroelectric Project	Rural Energy Projects	Administration and Power Development Fund	Rural Energy and Energy Development Programs	Combined balance
Operating revenues:								
Federal grants	$	—	—	—	—	—	14,871	14,871
Revenue from operating plants		14,635	1,711	—	11	—	—	16,357
State of Alaska appropriations		—	—	—	—	—	60,283	60,283
Revenue from state agencies		—	—	—	—	—	6,599	6,599
Interest on loans		—	—	—	—	—	302	302
Other revenue		—	55	—	—	—	193	248
Total operating revenues		14,635	1,766	—	11	—	82,248	98,660
Operating expenses:								
Grants and projects		—	617	—	3,131	—	93,299	97,047
Power cost equalization grants		—	—	—	—	—	38,899	38,899
Depreciation		6,991	2,751	—	—	—	—	9,742
Interest expense		5,032	—	—	—	—	—	5,032
Plant operating		3,290	1,211	—	—	—	—	4,501
General and administrative		226	555	—	—	—	4,486	5,267
Provision for loan loss		—	—	—	—	—	88	88
Total operating expenses		15,539	5,134	—	3,131	—	136,772	160,576
Operating income (loss)		(904)	(3,368)	—	(3,120)	—	(54,524)	(61,916)
Nonoperating:								
Decrease in contingent liability on sold loans		—	—	—	—	—	84	84
State of Alaska contributions		1,070	2,256	10,155	—	—	29,020	42,501
Investment income, net		1,666	—	—	—	—	12,384	14,050
Increase (decrease) in net assets		1,832	(1,112)	10,155	(3,120)	—	(13,036)	(5,281)
Net assets – beginning		109,681	38,697	—	2,883	2,172	922,476	1,075,909
Net assets – ending	$	111,513	37,585	10,155	(237)	2,172	909,440	1,070,628

See accompanying independent auditors' report.