



ALASKA ENERGY AUTHORITY
(A Component Unit of the State of Alaska)
Basic Financial Statements and Schedules
June 30, 2009 and 2008
(With Independent Auditors' Report Thereon)

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

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ALASKA ENERGY AUTHORITY
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Management's Discussion and Analysis

June 30, 2009 and 2008

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, 2009 and 2008. 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 \$627 million at June 30, 2009 and by \$597 million at June 30, 2008. Of the total net assets at June 30, 2009, \$132 million was invested in capital assets net of related debt, \$42 million was restricted and \$453 million was unrestricted. Of the total net assets at June 30, 2008, \$134 million was invested in capital assets net of related debt, \$43 million was restricted and \$420 million was unrestricted.

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Management's Discussion and Analysis

June 30, 2009 and 2008

Financial Analysis

Financial Position

Total assets, total liabilities, and total net assets at June 30, 2009, 2008, and 2007 follows (stated in thousands):

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Current assets	\$ 12,133	16,825	7,386
Capital assets	245,054	251,834	259,816
Other noncurrent and restricted assets	515,785	478,603	524,425
Total assets	<u>772,972</u>	<u>747,262</u>	<u>791,627</u>
Current liabilities	38,672	37,757	44,137
Noncurrent liabilities	107,578	112,838	118,234
Total liabilities	<u>146,250</u>	<u>150,595</u>	<u>162,371</u>
Total net assets	<u>626,722</u>	<u>596,667</u>	<u>629,256</u>
Total liabilities and net assets	<u>\$ 772,972</u>	<u>747,262</u>	<u>791,627</u>

Current assets were \$4.7 million lower at June 30, 2009 compared to June 30, 2008 and \$9.4 million higher at June 30, 2008 compared to June 30, 2007. Components of the changes were (stated in millions):

	<u>2009 vs.</u> <u>2008</u>	<u>2008 vs.</u> <u>2007</u>
Decrease in investment interest receivable	\$ (0.1)	(0.1)
(Decrease) increase in receivable from Department of Energy	(0.5)	0.4
(Decrease) increase in operating receivable from operating plants	(0.2)	0.1
Increase (decrease) in receivable from Denali Commission	1.3	(0.7)
(Decrease) increase in receivable for advanced grant funds to grantee	(4.3)	9.3
Net (decrease) increase in short-term loans originated, net of loan collections	(0.9)	0.4
	<u>\$ (4.7)</u>	<u>9.4</u>

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Capital assets were \$6.8 million lower at June 30, 2009 compared to June 30, 2008 and \$7.9 million lower at June 30, 2008 compared to June 30, 2007 substantially due to depreciation of capital assets, offset by improvements. Improvements to the below projects (stated in millions) were:

	2009 vs. 2008	2008 vs. 2007
Bradley Lake Hydroelectric Project	\$ 0.5	1.4
Alaska Intertie Project	0.2	0.5
Napakiak Intertie Project	2.7	0.3
	\$ 3.4	2.2

Other noncurrent and restricted assets were \$37.2 million higher at June 30, 2009 compared to June 30, 2008 and \$45.8 million lower at June 30, 2008 compared to June 30, 2007. Components of the changes were (stated in millions):

	2009 vs. 2008	2008 vs. 2007
Decrease in PCE Endowment Fund securities lending	\$ —	(15.7)
(Decrease) increase in PCE Endowment Fund realized investment income	(7.0)	3.9
Decrease in PCE Endowment Fund fair value	(42.1)	(31.6)
Contribution to Renewable Energy Fund	100.0	—
Contribution to Bulk Fuel Revolving Loan Fund	5.5	—
Net increase in other funds from investment income and fair value	4.3	—
Decrease due to increased grant expenditures	(30.0)	(1.5)
Decrease due to increased capital expenditures	(1.2)	—
Increase in long-term loan fundings	1.4	0.6
Net increase (decrease) in State advances on appropriations	6.3	(1.5)
	\$ 37.2	(45.8)

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June 30, 2009 and 2008

Current liabilities were \$0.9 million higher at June 30, 2009 compared to June 30, 2008 and \$6.4 million lower at June 30, 2008 compared to June 30, 2007. Components of the changes were (stated in millions):

	2009 vs. 2008	2008 vs. 2007
Increase in PCE Endowment Fund securities lending	\$ —	(15.7)
Net (decrease) increase in State advances on appropriations	(12.2)	6.0
Increase (decrease) in short-term borrowings	0.2	(0.4)
(Decrease) increase in current portion of arbitrage interest payable	(0.7)	1.0
Increased budgeted revenues in excess of actual expenses on hydroelectric and intertie projects	0.1	3.0
Increase (decrease) in other accrued expenditures	13.5	(0.3)
	\$ 0.9	(6.4)

The decreases in noncurrent liabilities between June 30, 2009 and 2008 and between June 30, 2008 and 2007 were caused by the decrease in the long-term portion of bonds payable at each year end and the decrease in the noncurrent portion of arbitrage interest payable. There were no new borrowings.

The increase in net assets from June 30, 2008 to June 30, 2009 resulted primarily from the \$100 million Renewable Energy contribution from the State of Alaska offset by the investment losses in the PCE Endowment Fund. The decrease in net assets from June 30, 2007 to June 30, 2008 resulted primarily from the \$39.9 million unrealized loss in the PCE Endowment Fund offset by increased realized investment gains.

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Management's Discussion and Analysis

June 30, 2009 and 2008

Operations

Components of the Authority's operating revenues, operating expenses, nonoperating investment income and operating loss for the years ended June 30, 2009 through 2007 follows (stated in thousands):

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Operating revenues:			
Federal grants	\$ 20,545	19,817	21,881
Revenue from operating plants	17,890	17,185	16,962
State appropriations	61,394	22,612	14,539
Other	1,763	2,312	1,718
Total operating revenues	<u>101,592</u>	<u>61,926</u>	<u>55,100</u>
Operating expenses:			
Grants and projects	72,010	27,594	24,239
PCE grants	37,074	28,235	25,145
Depreciation	10,233	10,160	10,034
Interest expense	7,116	7,577	7,938
Plant operating	5,077	4,489	4,242
General and administrative	1,940	1,894	1,673
Provision for loan loss and bad debt expense	(40)	(106)	(349)
Total operating expenses	<u>133,410</u>	<u>79,843</u>	<u>72,922</u>
Operating loss	(31,818)	(17,917)	(17,822)
Nonoperating:			
State of Alaska Bulk Fuel Revolving Loan Fund contribution	5,500	—	182,700
State of Alaska Renewable Energy Fund contribution	100,001	—	—
Investment (loss) income, net	(43,628)	(14,672)	49,235
Increase (decrease) in net assets	<u>\$ 30,055</u>	<u>(32,589)</u>	<u>214,113</u>

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Management's Discussion and Analysis

June 30, 2009 and 2008

Operating revenues increased \$39.6 million during the year ended June 30, 2009 compared to the prior year and increased \$6.8 million during the year ended June 30, 2008 compared to the same period in 2007. Components of the changes were (stated in millions):

	<u>FY 2009-2008</u> <u>Net change</u>	<u>FY 2008-2007</u> <u>Net change</u>
Decreased grant revenue from Denali Commission	\$ (1.8)	(1.9)
(Decreased) increased grant revenue from Department of Energy	(0.7)	0.2
Increased revenue from other grantors	3.2	—
Fluctuations in Bradley Lake approved budget expenditures	0.7	—
(Decreased) increased revenue from other State agencies	(0.6)	0.5
Increased revenue from State for PCE grants	2.8	2.5
Increased revenue from State general fund operating and capital appropriations	<u>36.0</u>	<u>5.5</u>
	<u>\$ 39.6</u>	<u>6.8</u>

Operating expenses increased \$53.6 million during the year ended June 30, 2009 compared to the prior year and were \$6.9 million higher during the year ended June 30, 2008 compared to the same period in 2007. Components of the changes were (stated in millions):

	<u>FY 2009-2008</u> <u>Net change</u>	<u>FY 2008-2007</u> <u>Net change</u>
Increased (decreased) federal funded grant and project expenses in active rural energy construction projects	\$ 0.7	(2.0)
Increased State funded grant and project expenses	44.4	5.0
Decreased (increased) State agency funded expenses for interagency contracts	(0.6)	0.6
Increased PCE grant expenditures	8.8	3.1
Decreased bond interest expense	(0.4)	(0.4)
Increased operating plants expense	0.6	0.2
Increased administrative costs due to increased state funding	—	0.3
Increased other expenses	<u>0.1</u>	<u>0.1</u>
	<u>\$ 53.6</u>	<u>6.9</u>

During the year ended June 30, 2009, the PCE Endowment had unrealized losses of \$42 million and realized losses of \$13.4 million that offset \$6.2 million in net interest income and realized gains from other funds.

During the year ended June 30, 2008, the PCE Endowment had unrealized losses of \$39.6 million that offset \$24.7 million in net interest income and realized gains from other funds.

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June 30, 2009 and 2008

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. Annual operation of the rural energy programs and energy development programs 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, 2009 and 2008, 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 opinions.

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, 2009 and 2008, 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 23, 2009, 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.

The Management's Discussion and Analysis on pages 1 through 7 is not a required part of the basic financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.



Our audits were made for the purpose of forming an opinion on the financial statements taken as a whole. The supplementary information included in schedules 1 to 3 is presented for the purpose of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

KPMG LLP

October 23, 2009

ALASKA ENERGY AUTHORITY
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Balance Sheets

June 30, 2009 and 2008

(Stated in thousands)

Assets	2009	2008
Current assets:		
Grants receivable	\$ 3,566	2,810
Loans receivable (note 7)	1,970	2,857
Operating revenue receivable	5,355	9,843
Accrued interest receivable	1,242	1,315
Total current assets	12,133	16,825
Noncurrent assets:		
Restricted cash and investments (note 3)	23,015	22,863
Cash and investments designated for specific purposes (note 3)	467,464	431,876
Loans receivable, net of allowance (note 7)	25,306	23,864
Capital assets (note 5)	447,276	443,823
Less accumulated depreciation	(202,222)	(191,989)
Capital assets, net	245,054	251,834
Total noncurrent assets	760,839	730,437
Total assets	\$ 772,972	747,262
Liabilities and Net Assets		
Current liabilities:		
Due to State of Alaska	\$ 2,143	14,081
Accounts payable	27,022	13,624
Bonds payable – current portion (note 6)	6,030	5,820
Arbitrage interest payable – current portion (note 6)	357	1,007
Accrued interest	3,120	3,225
Total current liabilities	38,672	37,757
Noncurrent liabilities:		
Bonds payable – noncurrent portion, net (note 6)	107,301	112,454
Arbitrage interest payable noncurrent portion (note 6)	174	281
Other liabilities	103	103
Total noncurrent liabilities	107,578	112,838
Total liabilities	146,250	150,595
Net assets:		
Invested in capital assets, net of related debt	131,723	133,560
Restricted for debt service	19,896	19,638
Restricted by agreements with external parties	21,883	23,088
Unrestricted net assets	453,220	420,381
Total net assets	626,722	596,667
Commitments and contingencies (notes 8 and 10)		
Total liabilities and net assets	\$ 772,972	747,262

See accompanying notes to basic financial statements.

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Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2009 and 2008

(Stated in thousands)

	2009	2008
Operating revenues:		
Federal grants	\$ 20,545	19,817
Revenue from operating plants	17,890	17,185
State of Alaska appropriations	61,394	22,612
Revenue from state agencies	551	1,221
Interest on loans	1,099	1,020
Other revenue	113	71
	101,592	61,926
Total operating revenues		
Operating expenses:		
Grants and projects	72,010	27,594
Power cost equalization grants	37,074	28,235
Depreciation	10,233	10,160
Interest expense	7,116	7,577
Plant operating	5,077	4,489
General and administrative	1,940	1,894
Provision for loan loss and bad debt expense (note 7)	(40)	(106)
	133,410	79,843
Total operating expenses		
Operating loss	(31,818)	(17,917)
Nonoperating:		
State of Alaska Bulk Fuel Revolving Loan Fund contribution	5,500	—
State of Alaska Renewable Energy Fund contribution	100,001	—
Investment loss, net	(43,628)	(14,672)
	61,873	(14,672)
Total nonoperating		
Increase (decrease) in net assets	30,055	(32,589)
Net assets – beginning	596,667	629,256
Net assets – ending	\$ 626,722	596,667

See accompanying notes to basic financial statements.

ALASKA ENERGY AUTHORITY
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Statements of Cash Flows

Years ended June 30, 2009 and 2008

(Stated in thousands)

	2009	2008
Cash flows from operating activities:		
Receipts from federal grants	\$ 19,789	20,080
Receipts from customers and users	17,473	17,388
Receipts from State of Alaska appropriations	49,190	28,660
Principal collected on loans	11,716	9,431
Receipts from state agencies	787	1,051
Interest collected on loans	1,101	1,029
Other operating receipts	62	71
Loans originated	(12,232)	(10,125)
Payments to suppliers	(13,073)	(13,733)
Payments to grantees	(84,240)	(54,432)
Net cash used by operating activities	(9,427)	(580)
Cash flows from noncapital and related financing activities:		
Net unremitted interest returned on State appropriation advances	(21)	(88)
Renewable Energy Fund contribution from State appropriation	100,001	—
Bulk Fuel Revolving Loan Fund contribution from State appropriations	5,500	—
Decrease in State appropriation advance held in trust for others	(432)	(567)
Net receipt from operating loans from AIDEA	27	174
Net cash provided (used) by noncapital and related financing activities	105,075	(481)
Cash flows from capital and related financing activities:		
Principal paid on bonds	(5,820)	(5,810)
Interest paid on bonds	(6,344)	(6,457)
Purchase of capital assets	(3,421)	(2,961)
Net cash used by capital and related financing activities	(15,585)	(15,228)
Cash flows from investing activities:		
Purchase of investments	(354,684)	(113,845)
Proceeds from sales and maturities of investments	289,767	110,661
Interest received from investments	11,353	17,049
Net cash (used) provided by investing activities	(53,564)	13,865
Net increase (decrease) in cash and cash equivalents	26,499	(2,424)
Cash and cash equivalents at beginning of year	30,741	33,165
Cash and cash equivalents at end of year (note 3)	\$ 57,240	30,741
Reconciliation of operating loss to net cash used by operating activities:		
Operating loss	\$ (31,818)	(17,917)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Depreciation	10,233	10,160
Provision for loan loss and bad debt expense	(40)	(106)
Bond interest expense	7,116	7,577
Changes in assets and liabilities:		
(Decrease) increase in due to State of Alaska	(11,917)	5,882
(Increase) decrease in grants receivable	(756)	263
Increase in loans receivable	(516)	(694)
Increase in interest receivable	1	9
Decrease (increase) in operating revenue receivable	4,488	(9,434)
Decrease in operating accounts payable	13,782	3,680
Net cash used by operating activities	\$ (9,427)	(580)
Noncash capital activities:		
Amount included in accounts payable for fixed asset additions	\$ 248	216
Net decrease in fair value of investments	(42,092)	(39,367)

See accompanying notes to basic financial statements.

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Notes to Basic Financial Statements

June 30, 2009 and 2008

(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. Today, AEA's two hydroelectric projects have an installed capacity in excess of 90 megawatts, and the Alaska Intertie's 170 miles of transmission line link Interior Alaska with the cheaper energy available in the Southcentral portion of the State.

Pursuant to statute, on August 12, 1993, the board of directors 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 board appointed, on April 10, 2008, a separate AEA executive director who is an employee of AIDEA. Previously, the AEA and AIDEA executive directors were the same. 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 2008, legislation added energy development programs to AEA.

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

(a) *Bradley Lake Hydroelectric Project*

The project has installed capability, under optimal conditions, of 126 megawatts 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 Homer to Fairbanks as well as the Delta Junction area.

(b) *Alaska Intertie Project*

The 170-mile, 345-kilovolt transmission line runs between Willow and Healy, and interconnects the power distribution systems of Anchorage and Fairbanks. The Alaska Intertie allows Golden Valley

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Electric Association in Fairbanks to purchase electricity produced with lower cost energy, such as natural gas and hydroelectric, from the Anchorage and Kenai Peninsula utilities and allows utilities from the Mat-Su Valley, Anchorage and the Kenai Peninsula to purchase power from Fairbanks during power shortages. The Alaska Intertie reduces the number of black/brownouts throughout the system. Operations and maintenance duties are overseen by the Intertie Operating Committee 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. Through June 30, 2008, AEA incurred \$489,000 in costs for preliminary design work. In August 2007, AEA issued a contract to the Municipality of Anchorage dba Municipal Light and Power (ML&P) for \$19,500,000 for the upgrade and the work began in September 2007. Effective July 1, 2008, the State re-appropriated up to \$10,000,000 of the original funds for certain specific capital repairs on the Intertie. As a result, AEA is renegotiating the existing contract with ML&P to reduce scope of work to upgrade and extend a portion of the Intertie, and is negotiating with ML&P to repair static VAR compensators and a tower foundation. Due to reduction of funds in original project and related scope change, the major upgrades and repairs funded by the appropriations are estimated to be completed by late 2014. However this estimate of date is dependent on the final scope of work and availability of funds.

AEA management and participating utilities identified defects in the Agreement that AEA management believes should be corrected. Attempts to cure the identified defects were unsuccessful because amending the Agreement requires unanimous consent of each member of the Intertie Operating Committee, and at least one utility member objected to each proposed cure. AEA management, on October 16, 2006, issued contractually required notice that the Agreement will terminate in 48 months, on October 17, 2010. AEA management anticipates that the necessary amendments to the Agreement can be implemented on or before the effective date of the termination of the existing Agreement.

(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 City operates the project.

The Authority and the City have agreed that the Authority will convey the project to the City and the City will accept all responsibility for it when the Authority completes repair work currently being performed under a project management agreement with the City.

(d) ***Rural Energy Programs***

The rural energy programs include Bulk Fuel Storage Upgrades, Rural Power System Upgrades, Power Cost Equalization (PCE), Alternative Energy, 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.

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Notes to Basic Financial Statements

June 30, 2009 and 2008

(e) ***Energy Development Programs***

The energy development programs include the energy sustainability plan and renewable energy grants program pursuant to legislation passed in 2008.

(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 and fund transfers with the State, 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:

<u>Utility plant</u>	<u>Life in years</u>
Intangible	30 – 50
Production	30 – 50
Transmission	20 – 40
General	5 – 30

The Authority recognizes impairment losses for long-lived assets whenever events or changes in circumstances result in the carrying amount of the assets exceeding the sum of the expected future cash flows associated with such assets.

(c) ***Cash and Investments***

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

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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, loans are treated as program loans.

(e) *Allowance for Loan Losses*

The allowance for loan losses represents management's judgment as to the amount required to absorb potential 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 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, 2009 and 2008, there were no 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 political subdivision of the State performing an essential governmental function and is therefore exempt from State and federal income taxes.

(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) *Segment Information*

The financial statements disclose all financial information required by the Authority's Bradley Lake bond indenture.

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(j) *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.

(k) *Recent Accounting Pronouncement*

In November 2006, GASB issued Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, which is effective for periods beginning after December 15, 2007. This statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. No liability existed under this standard at June 30, 2009.

(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 herein, 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 accounting principles generally accepted in the United States of America).

At June 30, 2009 and 2008 the Authority's carrying amount of deposits (all of which were restricted) was \$57,240,000 and \$30,741,000, respectively. The total of all bank balances was \$58,536,000 and \$31,507,000, respectively.

The restricted and designated cash and investments were held in trust accounts for the following activities as of June 30, 2009 (stated in thousands):

	Cash and cash equivalents	Investments	Total
Power Cost Equalization Endowment Fund	\$ 13	303,341	303,354
Renewable Energy Grant Fund	—	87,143	87,143
Bradley Lake Hydroelectric Project	9,149	18,626	27,775
Rural Energy Loan Funds	17,405	8,587	25,992
Rural Energy and Energy Development Programs	3,067	15,542	18,609
Funds advanced from State and federal agencies	13,879	—	13,879
Renewable Energy Grant Program	11,021	—	11,021
Power Development Fund	1,867	—	1,867
Alaska Intertie Project	839	—	839
Total cash and investments	<u>\$ 57,240</u>	<u>433,239</u>	<u>490,479</u>

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The restricted and designated cash and investments were held in trust accounts for the following activities as of June 30, 2008 (stated in thousands):

	Cash and cash equivalents	Investments	Total
Power Cost Equalization Endowment Fund	\$ 2	368,704	368,706
Bradley Lake Hydroelectric Project	9,045	17,933	26,978
Rural Energy Loan Funds	9,180	11,539	20,719
Rural Energy and Energy Development Programs	1,387	18,831	20,218
Funds advanced from State and federal agencies	7,925	—	7,925
Power Development Fund	1,940	—	1,940
Power Cost Equalization and Rural Electric Capitalization Fund	746	6,991	7,737
Alaska Intertie Project	516	—	516
Total cash and investments	<u>\$ 30,741</u>	<u>423,998</u>	<u>454,739</u>

At June 30, 2009 and 2008, amounts restricted for debt service totaled \$23,015,000 and \$22,863,000, respectively, for the Bradley Lake Hydroelectric Project.

Investment Holdings

Power Cost Equalization Endowment Fund and Renewable Energy Grant Fund – The Power Cost Equalization Endowment Fund (PCE Fund), created under Alaska Statute 42.45.070, and the Renewable Energy Grant Fund (RE Fund), created under Alaska Statute 42.45.045, are under the fiduciary authority of the State Department of Revenue, Treasury Division (Treasury). The purpose of the PCE fund is to provide for a long-term stable financing source for power cost equalization in order to provide affordable levels of electric utility costs in otherwise high-cost service areas in the state. The purpose of the RE Fund is to finance renewable energy projects in Alaska.

State investments 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 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 Short-term and Intermediate-term Fixed Income Pools. A complete description of the investment policy for each pool is included in the Department of Revenue, Treasury Division, Policies and Procedures.

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.

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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, 2009, AEA had the following cash and investments in the PCE and RE Funds (stated in thousands):

Investment type	Cash		Investments at fair value		
	PCE Fund	RE Fund	PCE FUND		Total
	Short-term fixed income pool	Short and intermediate-terms fixed income pool	Broad market and U.S. Treasuries fixed income pools	Equity	
Deposit	\$ 19	105	—	—	—
Short-term Investment Fund	—	—	—	1,069	1,069
Commercial paper	382	2,111	—	—	—
U.S. Treasury bonds	—	—	3,146	—	3,146
U.S. Treasury bills	2,156	11,907	—	—	—
U.S. Treasury notes	—	23,650	24,215	—	24,215
U.S. government agency	167	16,335	4,260	—	4,260
Mortgage-backed	241	6,213	48,802	—	48,802
Other asset-backed	761	4,526	1,220	—	1,220
Corporate bonds	2,059	17,057	20,420	—	20,420
Yankee:					
Government	—	406	273	—	273
Corporate	442	4,688	3,936	—	3,936
Domestic equity	—	—	—	141,032	141,032
International equity	—	—	—	50,286	50,286
Total invested assets	6,227	86,998	106,272	192,387	298,659
Pool related net liabilities	(14)	145	(1,744)	226	(1,518)
Other pool ownership	(6,200)	—	6,200	—	6,200
Net invested assets	\$ 13	87,143	110,728	192,613	303,341

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At June 30, 2008, AEA had the following cash and investments in the PCE Fund (stated in thousands):

<u>Investment type</u>	<u>Cash</u>	<u>Investments at fair value</u>		
	<u>Short-term fixed income pool</u>	<u>Broad market fixed income pool</u>	<u>Equity</u>	<u>Total investments</u>
Overnight sweep account	\$ 27	—	—	—
Commercial paper	877	—	—	—
Municipal bonds	—	18	—	18
U.S. Treasury notes	—	12,170	—	12,170
U.S. Treasury bonds	—	4,929	—	4,929
U.S. government agency	5,854	2,541	—	2,541
Mortgage-backed	470	90,741	—	90,741
Other asset-backed	2,727	8,265	—	8,265
Corporate bonds	2,581	34,438	—	34,438
Yankee:				
Government	—	382	—	382
Corporate	774	4,264	—	4,264
Domestic equity	—	—	137,785	137,785
International equity	—	—	69,192	69,192
Total invested assets	13,310	157,748	206,977	364,725
Pool related net liabilities	(7)	(10,225)	903	(9,322)
Other pool ownership	(13,301)	13,301	—	13,301
Net invested assets	\$ 2	160,824	207,880	368,704

Other AEA Cash and Investments – Bradley Lake Hydroelectric Project investments are substantially invested pursuant to investment agreements with JP Morgan Chase Bank that end the earlier of July 1, 2021 or the date of repayment of the Bradley Lake Power Revenue Bonds, First and Second Series. 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. 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 and repurchase agreements collateralized by U.S. Treasury and agency securities.

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At June 30, 2009 and 2008, AEA had the following cash and investments in its other funds (stated in thousands):

Investment type	2009 Fair value short-term fixed income	2008 Fair value short-term fixed income
Deposits	\$ 29	17
Money market	57,198	30,721
GSE-Mortgage-backed	5,031	25,897
U.S. Treasury notes	19,098	11,464
Investment agreements	18,626	17,934
Total invested assets	<u>\$ 99,982</u>	<u>86,033</u>

Interest Rate Risk – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment.

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 in maturity or fourteen months expected average life. Floating rate securities are limited to three years in maturity or three years expected average life. Treasury utilizes the actual maturity date for commercial paper and twelve month prepay speeds for other securities. At June 30, 2009, the expected average life of individual fixed rate securities ranged from one day to six and one-half years and the expected average life of floating rate securities ranged from one day to eight years. At June 30, 2008 the expected average life of fixed rate securities ranged from eight days to less than three months.

Intermediate-Term Fixed Income Pool – 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 \pm 20% of the Merrill Lynch 1-5 year Government Bond Index. The effective duration for this index at June 30, 2009 was 2.54 years. AEA held no investments in this pool in 2008.

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 pools to the following:

For 2009, Treasury limited Broad Market Fixed Income Pool to \pm 20% of the Barclay’s Capital U.S. Aggregate Bond Index. The effective duration of the Index at June 30, 2009 was 4.3 years. For 2008, Treasury limited the pool to \pm 20% of the Lehman Brothers Aggregate Bond Index. The effective duration for the Lehman Brothers Aggregate Bond Index at June 30, 2008, was 4.7 years.

For 2009, Treasury limited U.S. Treasury Fixed Income Pool to \pm 20% of the Barclay’s Capital U.S. Aggregate Treasury Index. The effective duration of the Index at June 30, 2009 was 5.13 years. AEA held no investments in this pool in 2008.

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Investment Agreements – Bradley Lake Hydroelectric Project investments are invested pursuant to agreements with JP Morgan Chase Bank that guarantees annual interest earnings of 7.38% or 7.41% per annum until the earlier of July 1, 2021 or the date of repayment of the Bradley Lake Power Revenue Bonds, First and Second Series. The investment contracts are collateralized.

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.

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 the investments is 2 years or less. The maximum maturity of any issue is 3 years from the date of purchase.

Duration – Duration is a measure of interest rate risk. It measures a security’s sensitivity to a 100–basis point change in interest rates. Duration is a weighted average term–to–maturity of an investment’s cash flows.

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.

Treasury has no policy with regard to interest rate risk for the money market balance held in the International Equity Pool. Additionally, the Conservative Broad Market Fixed Income pool does not have its own investment policy because it invests only in existing pools, which do have established policies.

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At June 30, 2009 and 2008, the effective duration by investment type (not including the investment agreements) was as follows:

<u>Managed by Treasury</u>	<u>Intermediate- term fixed income pool</u>	<u>Broad market fixed income pool</u>	<u>U.S. Treasury fixed income pool</u>
		2009	
U.S. Treasury notes	—	6.01	4.70
U.S. Treasury bonds	3.07	12.81	9.58
U.S. government agency	2.02	6.92	8.95
Mortgage-backed	2.42	—	—
Other asset-backed	0.71	—	—
Corporate bonds	2.10	—	2.57
Yankees:			
Government	2.73	11.37	—
Corporate	2.81	4.80	—
Portfolio effective duration	2.52	4.19	5.12
		2008	
U.S. Treasury notes	—	7.24	—
U.S. Treasury bonds	—	13.48	—
U.S. government agency	—	4.85	—
Municipal bonds	—	10.96	—
Mortgage-backed	—	4.37	—
Other asset-backed	—	2.58	—
Corporate bonds	—	4.91	—
Yankees:			
Government	—	11.93	—
Corporate	—	5.48	—
Portfolio effective duration	—	4.57	—
		Managed by AEA	
		2009	2008
Money market		0.16	0.18
U.S. Treasury notes		0.33	0.95
U.S. government agency and GSE discount notes		0.03	0.25
Portfolio effective duration		0.37	0.34

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Credit Risk – Credit risk is the financial risk that an issuer or other counterparty to an investment will not fulfill its obligations and a loss will result. 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 if only rated by one of these agencies if they are rated AAA.

Intermediate-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 – Commercial paper in the U.S. Treasury Fixed Income Pool must be rated at least P-1 by Moody’s and A-1 by Standard and 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.

Treasury has no policy with regard to credit risk for the money market balance held in the International Equity Pool. The Conservative Broad Market Fixed Income pool does not have its own investment policy because it invests only in existing pools, which have established policies.

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 collateralized investment agreements, which minimizes credit risk.

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At June 30, 2009, 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).

<u>Investment type</u>	<u>Rating¹</u>	<u>Short-term fixed income pool</u>	<u>Intermediate- term fixed income pool</u>	<u>Broad market fixed income pool</u>	<u>U.S. Treasury income pool</u>	<u>AEA managed</u>
Money market	AAA	—%	—%	—%	—%	57%
Commercial paper	A-1	1	—	—	—	—
Commercial paper	Not Rated	5	—	—	—	—
U.S. Treasury notes	AAA	—	—	16	69	19
U.S. Treasury bills	AAA	35	44	—	—	—
U.S. Treasury bonds	AAA	—	—	2	11	—
U.S. government agency and GSE discount notes	AAA	3	28	2	—	5
U.S. government agency and GSE	Not Rated	—	1	1	6	—
Mortgage-backed	AAA	3	7	46	—	—
Mortgage-backed	Not Rated	—	2	4	—	—
Other asset-backed	AAA	11	—	1	—	—
Other asset-backed	AA	1	—	—	—	—
Corporate bonds	AAA	19	5	2	8	—
Corporate bonds	AA	6	1	3	—	—
Corporate bonds	A	8	3	9	—	—
Corporate bonds	BBB	—	2	6	—	—
Yankees – government	AA	—	1	—	—	—
Yankees – corporate	AAA	2	3	1	—	—
Yankees – corporate	AA	4	1	—	—	—
Yankees – corporate	A	—	—	2	—	—
Yankees – corporate	BBB	2	—	1	—	—
No credit exposure		—	2	4	6	—
Investment agreements	Not Rated	—	—	—	—	19
		<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

¹Rating modifiers are not disclosed.

The International Equity Pool was 100% no credit exposure.

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At June 30, 2008, 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):

<u>Investment type</u>	<u>Rating¹</u>	<u>Short-term fixed income pool</u>	<u>Broad market fixed income pool</u>	<u>International equity pool</u>	<u>AEA managed</u>
Money market	AAA	—%	—%	—%	36%
Commercial paper	Not Rated	7	—	—	—
U.S. Treasury notes	AAA	—	8	—	13
U.S. Treasury bonds	AAA	—	3	—	—
U.S. government agency and GSE discount notes	AAA	44	1	—	20
U.S. government agency and GSE	AAA	—	—	—	10
Mortgage-backed	AAA	3	46	—	—
Mortgage-backed (agency)	Not Rated	—	11	—	—
Other asset-backed	AAA	16	3	—	—
Other asset-backed	AA	1	—	—	—
Other asset-backed	A	3	1	—	—
Other asset-backed	BB	1	—	—	—
Corporate bonds	AAA	2	2	—	—
Corporate bonds	AA	12	5	—	—
Corporate bonds	A	4	9	—	—
Corporate bonds	BBB	—	5	—	—
Corporate bonds	Not Rated	1	1	—	—
Yankees – corporate	AA	4	1	—	—
Yankees – corporate	A	1	1	—	—
Yankees – corporate	BBB	—	1	—	—
Yankees – corporate	Not Rated	1	—	—	—
No credit exposure		—	2	100	—
Investment agreements	Not Rated	—	—	—	21
		<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

¹Rating modifiers are not disclosed.

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, 2009, AEA's deposits managed by Treasury were uncollateralized and uninsured.

With respect to AEA managed investments, amounts totaling approximately \$48,048,000 at June 30, 2009 and \$21,676,000 at June 30, 2008, are held in money market funds not registered in AEA's name. The investment contracts 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.

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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 2009 and 2008, and invested assets included the following holdings at June 30, 2009 and 2008, for the PCE Fund’s investment in the International Equity Pool:

	Policy	Actual
FY09	18%+5%	17.00%
FY08	17%+5%	19.01%

At June 30, 2009 and 2008, AEA’s PCE Fund had exposure to foreign currency risk as follows (stated in thousands):

Currency	FY09 Fair value	FY08 Fair value
Deposits:		
Euro Currency	\$ —	28
Japanese Yen	7	—
Pound Sterling	(7)	72
	—	100
Investment – international equity:		
Canadian Dollar	565	1,295
Danish Krone	421	—
Euro Currency	14,396	19,167
Hong Kong Dollar	345	—
Japanese Yen	7,347	8,304
Norwegian Krone	—	560
Pound Sterling	9,578	12,373
Singapore Dollar	843	1,703
Swedish Krona	531	488
Swiss Franc	4,109	6,978
	38,135	50,868
Total	\$ 38,135	50,968

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. Federal National Mortgage Association and Federal Home Loan Mortgage Corporation securities are not classified as corporate bonds. AEA has no written policy with respect to concentration of credit risk for its other investments.

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At June 30, 2009, AEA's investments (excluding U.S. Treasury securities) included the following concentrations greater than 5% (dollar amounts stated in thousands):

<u>Issuer</u>	<u>Amount</u>	<u>Percent</u>
Federal National Mortgage Association	\$ 57,375	12%

At June 30, 2008, AEA's investments included the following concentrations greater than 5% (dollar amounts stated in thousands):

<u>Issuer</u>	<u>Amount</u>	<u>Percent</u>
Federal National Mortgage Association	\$ 61,664	14%
Federal Home Loan Bank	22,793	5

(4) Securities Lending

Prior to 2008, a portion of the funds managed by Treasury were in the State Department of Revenue's securities lending program. Alaska Statute 37.10.071 authorizes the Commissioner of Revenue to lend assets, under an agreement and for a fee, against deposited collateral of equivalent fair value. During 2008, the Commissioner suspended the securities lending agreement with State Street Corporation (the Bank), which lent equity and domestic fixed income securities. Prior to suspension, the Bank, acting as the Commissioner's agent under the agreement, transferred securities to broker agents or other entities for collateral in the form of cash or securities and simultaneously agreed to return the collateral for the same securities in the future. At June 30, 2009 and 2008 there were no securities on loan.

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(5) Capital Assets

Capital asset activity for the years ended June 30, 2009 and 2008 was as follows (stated in thousands):

	<u>Balance at June 30, 2008</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance at June 30, 2009</u>
Capital assets:				
Intangible	\$ 14	—	—	14
Production	252,199	342	—	252,541
Transmission	186,459	2,267	—	188,726
General	5,151	844	—	5,995
Total capital assets	<u>443,823</u>	<u>3,453</u>	<u>—</u>	<u>447,276</u>
Less accumulated depreciation for:				
Intangible	(4)	—	—	(4)
Production	(84,411)	(5,267)	—	(89,678)
Transmission	(102,531)	(4,934)	—	(107,465)
General	(5,043)	(32)	—	(5,075)
Total accumulated depreciation	<u>(191,989)</u>	<u>(10,233)</u>	<u>—</u>	<u>(202,222)</u>
Capital assets, net	<u>\$ 251,834</u>	<u>(6,780)</u>	<u>—</u>	<u>245,054</u>

	<u>Balance at June 30, 2007</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance at June 30, 2008</u>
Capital assets:				
Intangible	\$ 14	—	—	14
Production	250,937	1,262	—	252,199
Transmission	185,660	799	—	186,459
General	5,034	117	—	5,151
Total capital assets	<u>441,645</u>	<u>2,178</u>	<u>—</u>	<u>443,823</u>
Less accumulated depreciation for:				
Intangible	(4)	—	—	(4)
Production	(79,198)	(5,213)	—	(84,411)
Transmission	(97,597)	(4,934)	—	(102,531)
General	(5,030)	(13)	—	(5,043)
Total accumulated depreciation	<u>(181,829)</u>	<u>(10,160)</u>	<u>—</u>	<u>(191,989)</u>
Capital assets, net	<u>\$ 259,816</u>	<u>(7,982)</u>	<u>—</u>	<u>251,834</u>

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(6) Long-Term Debt

Long-term debt activity for the years ended June 30, 2009 and 2008 was as follows (stated in thousands):

	Balance at June 30, 2008	Additions	Deletions	Balance at June 30, 2009	Due within one year
Bradley Lake Power					
Revenue Bonds:					
First Series (a)	\$ 100			100	—
Second Series (a)	6,910		(2,305)	4,605	2,300
Refunding, Third Series (a)	44,705		(3,390)	41,315	3,595
Refunding, Fourth Series (a)	37,155		(125)	37,030	135
Refunding, Fifth Series (a)	30,640			30,640	—
Total bonds payable	119,510	—	(5,820)	113,690	6,030
Arbitrage interest payable (b)	1,288	250	(1,007)	531	357
Less bond discount and deferred interest	(1,236)		877	(359)	—
	<u>\$ 119,562</u>	<u>250</u>	<u>(5,950)</u>	<u>113,862</u>	<u>6,387</u>
	Balance at June 30, 2007	Additions	Deletions	Balance at June 30, 2008	Due within one year
Bradley Lake Power					
Revenue Bonds:					
First Series (a)	\$ 3,370	—	(3,270)	100	—
Second Series (a)	9,215	—	(2,305)	6,910	2,305
Refunding, Third Series (a)	44,820	—	(115)	44,705	3,390
Refunding, Fourth Series (a)	37,275	—	(120)	37,155	125
Refunding, Fifth Series (a)	30,640	—	—	30,640	—
Total bonds payable	125,320	—	(5,810)	119,510	5,820
Arbitrage interest payable (b)	984	304	—	1,288	1,007
Less bond discount and deferred interest	(2,363)	—	1,127	(1,236)	—
	<u>\$ 123,941</u>	<u>304</u>	<u>(4,683)</u>	<u>119,562</u>	<u>6,827</u>

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June 30, 2009 and 2008

The minimum payments related to all bonds for the years subsequent to June 30, 2009 are as follows (stated in thousands):

Year ending June 30:	Principal	Interest	Total
2010	\$ 6,030	6,127	12,157
2011	6,255	5,897	12,152
2012	6,495	5,583	12,078
2013	6,880	5,182	12,062
2014	7,300	4,757	12,057
2015 – 2019	46,020	16,248	62,268
2020 – 2022	34,710	2,857	37,567
	<u>\$ 113,690</u>	<u>46,651</u>	<u>160,341</u>

- (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 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 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 5% to 6.25%.
- (b) The arbitrage interest payable is due to the United States Treasury for the excess of investment income on the 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. 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.

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

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June 30, 2009 and 2008

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, 2009, the unpaid principal balance of the notes was \$13,396,000 and the trust assets had a fair value of \$14,627,000.

- *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. As of June 30, 2009, the outstanding balance was \$37,455,000.

The Sitka Bonds are special obligations of AEA secured under a trust indenture by and between AEA and U.S. Bank National Association, as trustee. The Sitka Bonds are payable solely from the sources provided under the trust indenture. They are equally and ratably secured by a pledge and assignment of the municipal revenue bonds of Sitka held by AEA under the trust indenture, the obligation of Sitka to make payments under its loan agreement with AEA and the money and securities held under the trust indenture, including a capital reserve fund. AEA has covenanted to notify the State Legislature of any failure to maintain the capital reserve fund at its required level. The bonds are further secured by bond insurance.

The Sitka Bonds do not constitute an indebtedness or other liability of the State, including AEA, and do not directly, indirectly or contingently obligate the State, including AEA, or any political subdivision thereof to levy any form of taxation for the payment of the bonds. Neither the full faith and credit nor the taxing power of the State, including AEA, or Sitka is pledged for the payment of the Sitka Bonds.

(7) 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, 2009 and 2008 are classified as follows (dollar amounts stated in thousands):

	2009		2008	
	<u>No. of loans</u>	<u>Amount</u>	<u>No. of loans</u>	<u>Amount</u>
Power Project Loan Program	47	\$ 26,330	42	\$ 24,944
Rural Electrification Revolving Loan Program	2	646	2	698
Bulk Fuel Revolving Loan Program	23	1,352	25	2,171
	<u>72</u>	<u>28,328</u>	<u>69</u>	<u>27,813</u>
Less allowance for loan losses		(1,052)		(1,092)
		<u>\$ 27,276</u>		<u>\$ 26,721</u>

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June 30, 2009 and 2008

Loans that are more than 90 days past due on which the accrual of interest has been discontinued amounted to \$368,520 and \$266,000 at June 30, 2009 and 2008, respectively.

An analysis of changes in the allowance for loan losses for the years ended June 30, 2009 and 2008 follows (stated in thousands):

	2009	2008
Balance at beginning of year	\$ 1,092	1,177
Recoveries	—	21
Write-offs	—	—
Provision for loan loss	(40)	(106)
Balance at end of year	\$ 1,052	1,092

(8) 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.

(9) 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 2009 and 2008, AEA expensed \$4,344,000 and \$3,430,000, respectively, for such services. During 2009 and 2008, AEA capitalized \$31,000 and \$64,000, respectively, for such services. AEA has a borrowing arrangement with AIDEA to provide working capital funds. At June 30, 2009 and 2008, AEA had \$1,852,000 and \$1,440,000, respectively, payable to AIDEA for services and borrowings.

(b) Alaska Intertie Operating Committee

Effective May 1, 1986, AEA entered into an agreement with utilities using the Alaska Intertie for wheeling of electrical power. Pursuant to the agreement, the Intertie Operating Committee (IOC) was established to manage the system. The IOC 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 management on October 16, 2006, issued contractually required notice that the agreement will terminate in 48 months as a mechanism to implement cures to identified defects in the agreement (note 1(b)).

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June 30, 2009 and 2008

(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 annual administrative fee to AEA.

(10) Commitments and Contingencies

AEA, in the normal course of business, is involved in various claims and pending litigation. The State Department of Law manages all pending litigation of AEA, and any liability arising from the settlement of pending claims is a liability for which the Department of Law or AEA requests an appropriation from the Legislature to satisfy judgment in the event that the judgment exceeds available funds or the proceeds from applicable insurance policies. In the opinion of management, the disposition of current claims and pending litigation is not presently expected to have a material adverse effect on AEA's financial position.

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, 2009 and 2008, AEA had open loan commitments of \$12,253,000 and \$4,596,000, respectively. At June 30, 2009 and 2008, AEA had committed to grant awards to be funded by State appropriations and federal awards; the amounts committed were \$146,201,000 and \$60,770,000, respectively.

At June 30, 2009 and 2008, AEA held approximately \$5,795,000 and \$5,750,000 at fair value, respectively, of investments in escrow under an agreement.

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Schedule of Bradley Lake Hydroelectric Project Trust Account Activities

Year ended June 30, 2009

(Stated in thousands)

	<u>Debt service account</u>	<u>Capital reserve account</u>	<u>Renewal and contingency account</u>	<u>Excess earnings account</u>	<u>Revenue account</u>	<u>Operating account</u>	<u>Operating reserve account</u>	<u>Total</u>
Balance at June 30, 2008	\$ 9,045	12,834	1,082	984	1,852	446	735	26,978
Interest received	318	809	124	(979)	352	43	49	716
Bond principal paid	(5,820)	—	—	—	—	—	—	(5,820)
Bond interest paid	(6,344)	—	—	—	—	—	—	(6,344)
Construction expenditures	—	—	(197)	—	—	—	—	(197)
Operating revenue received	—	—	—	—	16,142	—	—	16,142
Operating expenses paid	—	—	—	—	—	(3,700)	—	(3,700)
Transfers between funds	11,951	(809)	1,322	304	(16,380)	3,656	(44)	—
Balance at June 30, 2009	<u>\$ 9,150</u>	<u>12,834</u>	<u>2,331</u>	<u>309</u>	<u>1,966</u>	<u>445</u>	<u>740</u>	<u>27,775</u>

See accompanying independent auditors' report.

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Schedule of Projects – Balance Sheet

June 30, 2009

(Stated in thousands)

Assets	Bradley Lake Hydroelectric Project	Alaska Intertie Project	Rural Energy Projects	Administration and Power Development Fund	Rural Energy and Energy Development Programs	Combined balance
Current assets:						
Grants receivable	\$ —	—	106	(284)	3,744	3,566
Loans receivable	—	—	—	—	1,970	1,970
Operating revenue receivable	68	216	—	—	5,071	5,355
Accrued interest receivable	924	—	—	—	318	1,242
Total current assets	<u>992</u>	<u>216</u>	<u>106</u>	<u>(284)</u>	<u>11,103</u>	<u>12,133</u>
Noncurrent assets:						
Restricted cash and investments	23,015	—	—	—	—	23,015
Designated for specific purposes	4,760	839	—	15,746	446,119	467,464
Loans receivable, net of allowance	—	—	—	—	25,306	25,306
Capital assets net of accumulated depreciation	196,824	45,129	3,101	—	—	245,054
Total noncurrent assets	<u>224,599</u>	<u>45,968</u>	<u>3,101</u>	<u>15,746</u>	<u>471,425</u>	<u>760,839</u>
Total assets	<u>\$ 225,591</u>	<u>46,184</u>	<u>3,207</u>	<u>15,462</u>	<u>482,528</u>	<u>772,972</u>
Liabilities and Net Assets						
Current liabilities:						
Due to State of Alaska	\$ —	(64)	—	22,890	(20,683)	2,143
Accounts payable	1,225	1,102	341	(9,600)	33,954	27,022
Bonds payable – current portion	6,030	—	—	—	—	6,030
Accrued interest	3,120	—	—	—	—	3,120
Arbitrage interest payable – current portion	357	—	—	—	—	357
Total current liabilities	<u>10,732</u>	<u>1,038</u>	<u>341</u>	<u>13,290</u>	<u>13,271</u>	<u>38,672</u>
Noncurrent liabilities:						
Bonds payable – noncurrent portion, net	107,301	—	—	—	—	107,301
Arbitrage interest payable – noncurrent portion	174	—	—	—	—	174
Other liabilities	103	—	6	—	(6)	103
Total noncurrent liabilities	<u>107,578</u>	<u>—</u>	<u>6</u>	<u>—</u>	<u>(6)</u>	<u>107,578</u>
Total liabilities	<u>118,310</u>	<u>1,038</u>	<u>347</u>	<u>13,290</u>	<u>13,265</u>	<u>146,250</u>
Net assets:						
Investment in capital assets net of related debt	83,493	45,129	3,102	—	—	131,724
Restricted for debt service	19,896	—	—	—	—	19,896
Restricted by agreements with external parties	3,892	17	—	—	17,974	21,883
Unrestricted net assets	—	—	(242)	2,172	451,289	453,219
Total net assets	<u>107,281</u>	<u>45,146</u>	<u>2,860</u>	<u>2,172</u>	<u>469,263</u>	<u>626,722</u>
Commitments and contingencies						
Total liabilities and net assets	<u>\$ 225,591</u>	<u>46,184</u>	<u>3,207</u>	<u>15,462</u>	<u>482,528</u>	<u>772,972</u>

See accompanying independent auditors' report.

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

Year ended June 30, 2009

(Stated in thousands)

	Bradley Lake Hydroelectric Project	Alaska Intertie Project	Rural Energy Projects	Administration and Power Development Fund	Rural Energy and Energy Development Programs	Combined balance
Operating revenues:						
Federal grants	\$ —	—	2,722	—	17,823	20,545
Revenue from operating plants	16,597	1,281	12	—	—	17,890
State of Alaska appropriations	—	291	8	—	61,095	61,394
Revenue from state agencies	—	—	—	—	551	551
Interest on loans	—	—	—	—	1,099	1,099
Other revenue	1	—	—	—	112	113
	<u>16,598</u>	<u>1,572</u>	<u>2,742</u>	<u>—</u>	<u>80,680</u>	<u>101,592</u>
Total operating revenues						
Operating expenses:						
Grants and projects	—	40	—	—	71,970	72,010
Power cost equalization grants	—	—	—	—	37,074	37,074
Depreciation	6,874	3,360	—	—	—	10,234
Interest expense	7,116	—	—	—	—	7,116
Plant operating	3,796	1,256	24	—	—	5,076
General and administrative	261	29	1	—	1,649	1,940
Provision for loan loss and bad debt expense	—	—	—	—	(40)	(40)
	<u>18,047</u>	<u>4,685</u>	<u>25</u>	<u>—</u>	<u>110,653</u>	<u>133,410</u>
Total operating expenses						
Operating income (loss)	(1,449)	(3,113)	2,717	—	(29,973)	(31,818)
Nonoperating:						
State of Alaska fund transfers	—	—	—	—	105,501	105,501
Investment income, net	1,490	4	—	—	(45,122)	(43,628)
	<u>41</u>	<u>(3,109)</u>	<u>2,717</u>	<u>—</u>	<u>30,406</u>	<u>30,055</u>
Increase (decrease) in net assets						
Net assets – beginning	107,240	48,255	143	2,172	438,857	596,667
Net assets – ending	<u>\$ 107,281</u>	<u>45,146</u>	<u>2,860</u>	<u>2,172</u>	<u>469,263</u>	<u>626,722</u>

See accompanying independent auditors' report.