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Annual
Report

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Southcentral Power Project

Corporate Mission

Through superior service, safely provide reliable and competitively priced energy.

Corporate Vision

Powering Alaska's Future

Incorporation

Chugach Electric Association was incorporated in Alaska, March 1, 1948, with funding under the Rural Electrification Act of 1936, as amended. In 1991, Chugach refinanced and paid off its federal debt, leaving the REA program. Chugach remains a cooperative and ranks among the largest of the more than 900 electric cooperatives in the nation.

Equal Employment Opportunity

It is a policy of Chugach Electric Association, Inc., to recruit, hire, train, promote and compensate persons without regard to race, color, religion, national origin, sex, marital status, pregnancy, parenthood, physical or mental disability, veteran's status, age or any other classification protected by applicable federal, state or local law.



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On Jan. 11 Chugach completed a \$250 million bond financing, using the proceeds to pay down commercial paper and fund capital expansion – primarily its portion of the Southcentral Power Project. The bonds carry a weighted average interest rate of 4.36 percent, with the rate on individual tranches varying from 4.01 to 4.78 percent.

An unusual series of winter storms that began battering the Chugach system in December 2011 continued into January. The worst damage and outages were seen in the mountains of the northern Kenai Peninsula. A buildup of heavy snow and ice brought power lines to the ground across the area. After the state declined to declare a disaster, Chugach ratepayers were left with more than \$2 million in response and repair costs.

March saw continued progress on the effort by the Alaska Energy Authority to develop a necessary new Railbelt hydroelectric project. The Federal Energy Regulatory Commission held a series of scoping meetings across the region on AEA's proposed study plans.

The legislative session that ended in April produced good results for Chugach. The capital budget contained more than \$7.4 million in grants for several Chugach projects.

The annual meeting on May 17 drew

164 registered members. In the election, Sisi Cooper and Jim Nordlund were each elected to 3-year terms on the board of directors and four bylaw changes were approved. A total of 14.9 percent of the 66,824 members of record voted in the election, with 36.5 percent of the votes cast via the Internet.

Utilities gained natural gas storage capacity when a facility known as CINGSA (Cook Inlet Natural Gas Storage Alaska) became operational in the spring. The parent company of ENSTAR Natural Gas Company developed the project that provides tariffed service to utilities including Chugach. For Chugach, significant injections of gas into CINGSA began in May.

Chugach converted to a new customer information system in June, replacing one that had been in use for more than 20 years.

Summer saw the usual increase in construction activity. Work commenced in July in Girdwood on a group of nine different projects. Key among them were the construction of a second feeder and associated feeder tie.

September brought another round of powerful storms to Southcentral Alaska. Chugach and its customers suffered from the effects of three storms with winds in excess of 100 mph, a fourth

with 65 mph winds and flooding from sustained periods of heavy rain.

In October, the latest update of an ongoing study of the Cook Inlet natural gas supply and demand situation concluded that, while some new wells had been added in recent years, they were only about half of what was needed to stem the 16 percent annual production decline from existing wells with a gap predicted to develop in 2015 between supply and utility demand.

In November Chugach was able to resume economy energy sales to Golden Valley Electric Association in the Interior. Chugach successfully negotiated a contract with Hilcorp to support sales to GVEA over 24 months, commencing April 1, 2013. Chugach filed the contract with the RCA in October.

Construction of the Southcentral Power Project continued throughout the year. Each of the three gas turbine-generators in the plant was fired and tested in October. By years end, commissioning was well underway by contractor SNC Lavalin.

Left: In August Chugach began buying power from the 17.6-megawatt Fire Island wind project. Middle: Construction of the Southcentral Power Project continued throughout the year. Right: Trees falling into cleared easements caused most of the September storm outages.





Janet Reiser
Board Chair

It's comfortable to keep doing things as you always have. It's harder to take a critical look at your organization and business environment and ask yourself if change is in order. "Fortune favors the bold," noted Roman poet Virgil. "And the prepared," I'd add. To its credit, Chugach has not shied from the hard work of strategic thinking and strategic planning in recent years – demonstrating leadership in our Railbelt region.

Much is in flux for Chugach, with fuel supplies less secure, aging infrastructure in need of attention and changing relationships with other utilities. As a board, our challenge has been to navigate through these issues in a way that ensures Chugach members will continue to have reliable, economical power.

Over the past 50 years Southcentral Alaska has built an economy and infrastructure that depends upon the continued flow of reasonably priced natural gas for heat and electricity. With Cook Inlet fields aging, traditional producers leaving and new players entering the market, the energy foundation that has fueled the security and prosperity of our region is in transition. We will continue to keep a close eye on the Cook Inlet gas situation.

Generation diversification has long been an interest of the board. In an average

year about 90 percent of our kilowatt-hours have been generated by burning natural gas, with the other 10 percent coming from hydro power. We are overly dependent upon a single generation fuel and continue to look for alternative energy generation resources.

In 2012 we took a step in that direction. In August Chugach began purchasing energy from Fire Island Wind, LLC. The independent power producer (a subsidiary of Cook Inlet Region, Inc.) developed a 17.6-megawatt wind project on Fire Island, three miles offshore from Anchorage. We came to agreement on a project sized to Chugach's ability to regulate it. By year end, the project had produced 18,000 megawatts of energy.

Through our membership in our regional generation & transmission cooperative, Chugach continued to work with other utilities on Railbelt priorities and planning. When utilities came together in 2010 to create ARCTEC (the Alaska Railbelt Cooperative Transmission & Electric Company) it was with the idea that joint efforts could lead to savings in the most expensive areas of our businesses. Our message was heard in Juneau during the 2011 legislative session when ARCTEC was successful in securing \$36 million for regionally beneficial energy projects. That money was put to work in 2012.

As an organization representing Alaskans throughout the Railbelt, ARCTEC can be the catalyst for activity that benefits more than a single utility. For example, a very important project is the systematic rebuild of the transmission line between Anchorage and the Kenai Peninsula. This line, currently energized at 115-kilovolts, is the sole transmission link between those areas. It is also the line that moves power from the Bradley Lake Hydroelectric Project

to utilities north of the peninsula. In November 2012 Chugach began rebuilding a 15-mile segment of the line with a \$15 million state grant secured by ARCTEC. This project has tremendous regional value. It has been a successful team effort. ARCTEC gained state funding for the project, the grant flowed through the Alaska Energy Authority and Chugach managed the project. When completed, this segment of line will have been rebuilt to 230-kv standards and given decades of new life. Through ARCTEC, Chugach is also working to enable more renewable generation, expand production from the Bradley Lake Hydro Project, unconstrain the transmission system and diversify our generation mix.

As proud as I am of Chugach and its accomplishments, the truth is that some problems are too big for any single organization to solve. Chugach values working cooperatively with others for the common good and has led the way on key issues affecting our region. We're preparing for a future that will be different than our past – one that will require greater cooperation among utilities and the careful evaluation of a shifting range of options on how to make and move power economically, efficiently and reliably.

THE EXECUTIVE STAFF

Seated from left, Brad Evans, Chief Executive Officer; Lee Thibert, Sr. Vice President, Strategic Planning & Corporate Affairs. Standing from left are Paul Risse, Sr. Vice President, Power Supply; Ed Jenkin, Vice President, Power Delivery; Connie Owens, Executive Assistant; Mark Johnson, Corporate Counsel; Tyler Andrews, Vice President, Human Resources and Mike Cunningham, Sr. Vice President, Finance & Chief Financial Officer.

Concern about the continued flow of natural gas from wells in the Cook Inlet basin to utilities dominated much of our activity in 2012. The latest report from utility consultant Petrotechnical Resources Alaska concluded that, while some new wells have been added in recent years, they were insufficient to offset the decline from current wells. Chugach and the other utilities that have commissioned the ongoing studies sought to engage policymakers in discussions of how to address the predicted future gap between supply and utility demand. We also formed a working group to consider importing liquefied or compressed natural gas until local drilling or a pipeline from the North Slope can ensure we meet the demands of Alaskans for heat and power.

Chugach has taken a multi-faceted approach to the gas situation. We've supported drilling incentives, promoted consumer energy efficiency and conservation, contracted for wind power, joined in a utility gas storage project, constructed an efficient new power plant, backed more hydropower and joined other utilities and area governments in developing contingency plans. Those actions are all helping – but we also need continued production from the Cook Inlet basin. We appreciate the work the state has done to actively solicit companies to come to Alaska and drill for gas in Cook Inlet. We are hopeful those efforts will lead to increased production in the near future.

Utilities now have their own natural gas

storage capacity. ENSTAR Natural Gas Co.'s owner developed CINGSA (Cook Inlet Natural Gas Storage Alaska). The gas storage project is mutually beneficial, helping producers level production by providing a place for gas to flow in warm weather and giving utilities a peaking reserve on cold winter days. Chugach began major injections of gas into CINGSA in May.

A new significant hydro project for the Railbelt would help take pressure off the Southcentral natural gas system. In 2012 the Alaska Energy Authority continued studies and public process on the Susitna-Watana hydroelectric project. As a potential major customer, Chugach has supported actions by the legislature and governor to fund Watana and worked closely with AEA on the technical details. Estimates are that the proposed 600-megawatt project could provide up to 50 percent of the Railbelt's electric energy.

Chugach was able to again begin making economy energy sales to Golden Valley Electric Association late in the year. It was good news for customers of the Fairbanks-based utility. Purchasing gas-fired generation from Southcentral utilities like Chugach helps lower the cost of electric service for GVEA customers. Golden Valley has purchased power under the interruptible arrangement for decades, but sales depend upon Chugach having access to natural gas to support them. Chugach negotiated a contract with Hilcorp for natural gas to support 2 years worth of economy energy sales to GVEA starting April 1, 2013.

Work progressed on the Southcentral Power Project throughout 2012, with commissioning nearly completed at year's end. The efficient new, combined-cycle power plant is a joint project between Chugach (70 percent)



Bradley Evans
CEO

and Municipal Light & Power (30 percent). Chugach built SPP with ML&P to gain economies of scale and hold down costs for customers. Chugach assumed operational control of the plant on behalf of the utility owners late on Jan. 31, 2013. With a much-lower heat rate than the average of the other thermal units on the system, SPP will save customers of the two utilities millions of dollars annually in avoided fuel purchases.

Operationally, CINGSA and SPP were both very helpful during a mid-December cold spell. Chugach and ENSTAR each withdrew gas they had previously placed in CINGSA to meet peak demands. In addition, SPP's efficient new units were online in test mode much of the time – using less natural gas than other combustion turbine-generators on the system.

Weather dealt the Chugach system and customers some hard blows in 2012, with unusually severe and damaging storms in January and September. Through it all, Chugach employees and contractors, at times assisted by crews from other utilities, worked professionally and safely to handle customer calls and restore service. During and after the storms we analyzed our response and performance. Process improvements in these and other areas will continue in 2013.

Bradley Evans



Janet Reiser

Board Chair

Janet Reiser is the Director of Business and Resource Development for The Aleut Corporation. She was elected to the board in 2008, and re-elected in 2011. She is currently the Chair of the Board and serves on the Governance, Operations, Audit and Finance Committees. She is currently Chair of Alaska Railbelt Cooperative Transmission and Electric Company. Reiser is a National Rural Electric Cooperative Association Credentialed Cooperative Director and has earned her Board Leadership Certificate. She has a Bachelor of Science degree in Chemical Engineering.

Susan Reeves

Vice Chair

Susan Reeves is the managing member of Reeves Amodio LLC, where she practices law. She has been active on Alaska non-profit boards and commissions for many years. Reeves was elected to the board in 2010. She serves as the Vice Chair of the Board, Chair of the Governance Committee and is a member of the Audit and Finance Committee. She is also Chugach's APA Representative. She is a National Rural Electric Cooperative Association Credentialed Cooperative Director.

Jim Henderson

Secretary

Jim Henderson is a principal with New American Financial Group in the financial services industry. He specializes in asset-based finance products, reorganization, refinancing of distressed companies and assets, and accounting and disposition of capital assets. His primary emphasis is transportation, industrial machinery and aviation operations, assets and industry development.

He has over 30 years of experience in consulting and analysis and finance of capital assets. Henderson has served on various committees for Chugach in the past. He was elected to the board in 2011. He serves on the Operations and Finance Committee and is a National Rural Electric Cooperative Association Credentialed Cooperative Director.

P.J. Hill

Treasurer

P.J. Hill is a retired economics professor from the School of Business and Public Policy at the University of Alaska Anchorage. He is an economic consultant and a commercial fisherman. He was elected to the board in 2007 and re-elected in 2010. Hill is the Board Treasurer, Chairs the Finance and Audit Committee and is a member of the Governance Committee. He is a National Rural Electric Cooperative Association Credentialed Cooperative Director and has completed the Board Leadership Program

Sisi Cooper

Director

Sisi Cooper is a project engineer with Doyon Emerald, LLC. She specializes in process safety and risk management, energy-sector project management, and process/facility engineering and design. Cooper is a former small business owner of North Ridge Home Inspections, LLC where she was the principal inspector. She was elected to the board in 2012. She serves on the Operations, Audit and Governance



Seated from left: Jim Henderson, Janet Reiser, and P. J. Hill. Standing from left: Susan Reeves, Sisi Cooper, Harry Crawford, and Jim Nordlund.

Committee. She has a Bachelor of Science degree in industrial engineering.

Harry T. Crawford, Jr.

Director

Harry Crawford is a former Alaska state legislator, retired iron worker and a small-real estate developer. He was elected to the board in 2011. He currently serves on the Operations, Audit, and Finance Committee and is the board liaison to the Elections Committee. He is a National Rural Electric Cooperative Association Credentialed Cooperative Director.

Jim Nordlund

Director

Jim Nordlund is Alaska State Director of USDA-Rural Development, as well as the owner of Nordlund Carpentry, LLC. He was elected to the board in 2006 and re-elected in 2009 and 2012. Nordlund is a former legislator and State Director of Public Assistance. He has served as Chairman of the Board and currently serves as Chair of the Operations Committee and is a member of the Finance Committee. He is a National Rural Electric Cooperative Association Credentialed Cooperative Director.

Chugach's successful financial and regulatory efforts continued in 2012. The long-term financing for the Southcentral Power Project (SPP) was finalized in January, securing debt at a blended average interest rate of 4.36 percent. The last of Chugach's bullet debt was repaid in February, with proceeds from our 2011 refinancing efforts, marking the final step in Chugach's transition from the public to private debt market.

During 2012 we continued to recognize the benefit of low interest rates provided by our Commercial Paper Program which ranged between 0.22 and 0.38 percent. We successfully extended the credit agreement used to backstop our commercial paper to 2016 and right sized the capacity to meet future needs which further reduced costs. Chugach also successfully renewed our \$50 million line of credit, which will provide additional liquidity until 2017.

In September, Chugach invested funds it received from last year's sale of the Bernice Lake Power Plant in marketable securities or short-term bond funds. The overall investment return on marketable securities has substantially out performed a prior money market investment strategy.

Chugach's efforts to lobby for grants culminated in over \$55 million of grant funding available during the year. This effort will save our members by reducing borrowing costs and depreciation expense over time.

Chugach filed two Simplified Rate Filing (SRF) adjustments in 2012, which resulted in a net decrease, as members continued to see the impact of Chugach's successful refinancing efforts.

In late December, the 2012 General Rate Case was also filed with the RCA to coincide with SPP's commercial operation date. In addition to recovering SPP costs, the filing included a decrease to the fuel rate based on the

expected efficiency of SPP. The filing also requested approval to update and expand our operating tariff to accommodate transmission wheeling services in anticipation of the expiration of the wholesale power sales agreements with HEA and MEA.

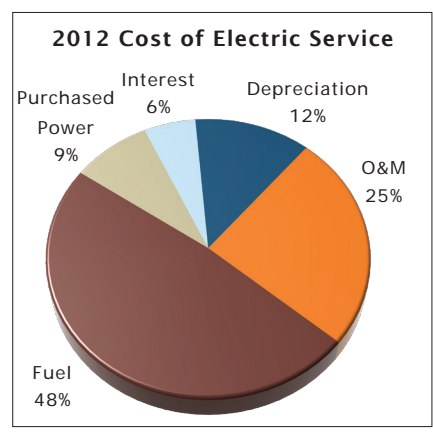
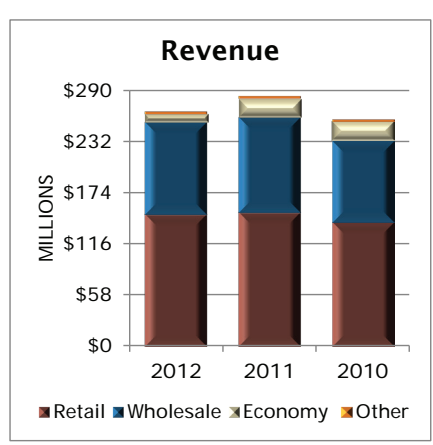
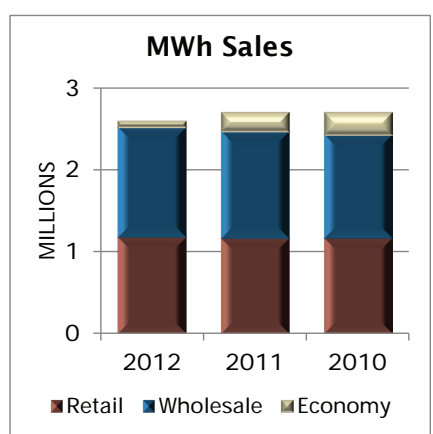
Chugach's 2012 margins (a cooperative's bottom line or revenues in excess of current costs) totaled \$5.5 million. Our Margins-for-Interest-to-Interest ratio was 1.23, well above our indenture metric of 1.10. Our Equity-to-Total-Capitalization ratio, required to be kept at or above 22 percent, was 24.2 percent.

Total energy sales to retail, wholesale and economy customers were 2,606,723 megawatt-hours compared to 2,704,412 in 2011. Even though sales were slightly down from last year, retail and wholesale sales were above the 2012 budget. Total revenue was \$267.0 million, down from \$283.6 million in 2011 and from the 2012 budget of \$284.5 million. Variances in revenue from 2011 and from the 2012 budget were largely driven by lower economy energy sales and a decrease in fuel recovered in revenue through the fuel and purchased power adjustment process.

Chugach's sound, financial performance, improved capital structure, strong regulatory support and new, more efficient generation caused a national rating agency to reaffirm our bond rating and outlook as "A-/positive". Another national rating agency also reaffirmed our bond rating and outlook as "A-/stable".

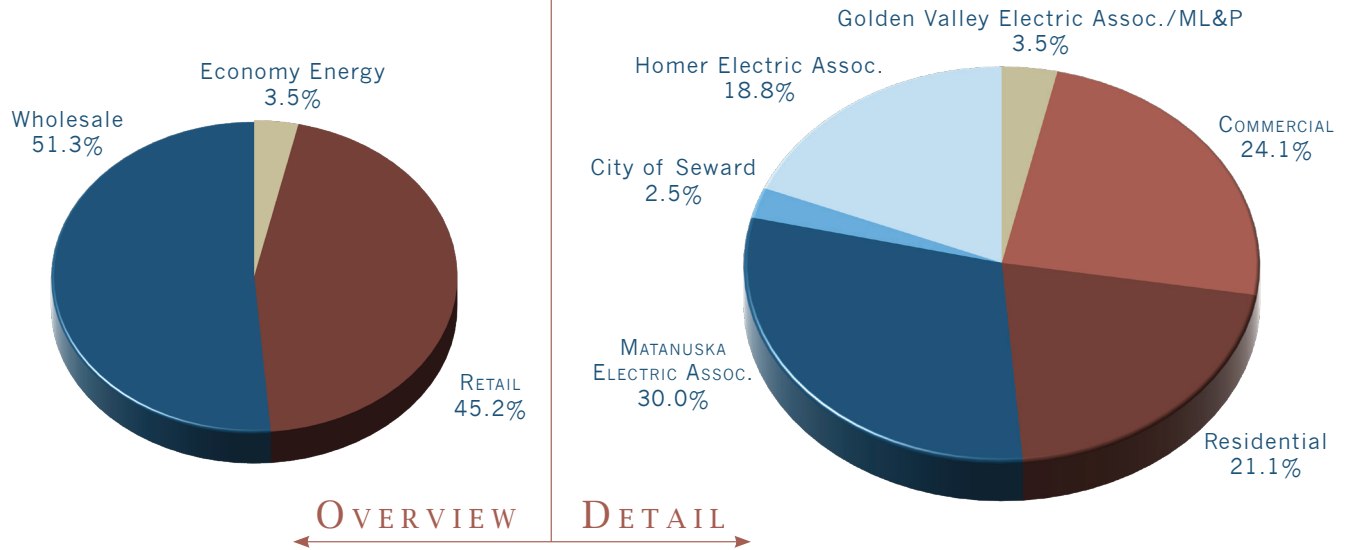



P.J. Hill
Treasurer



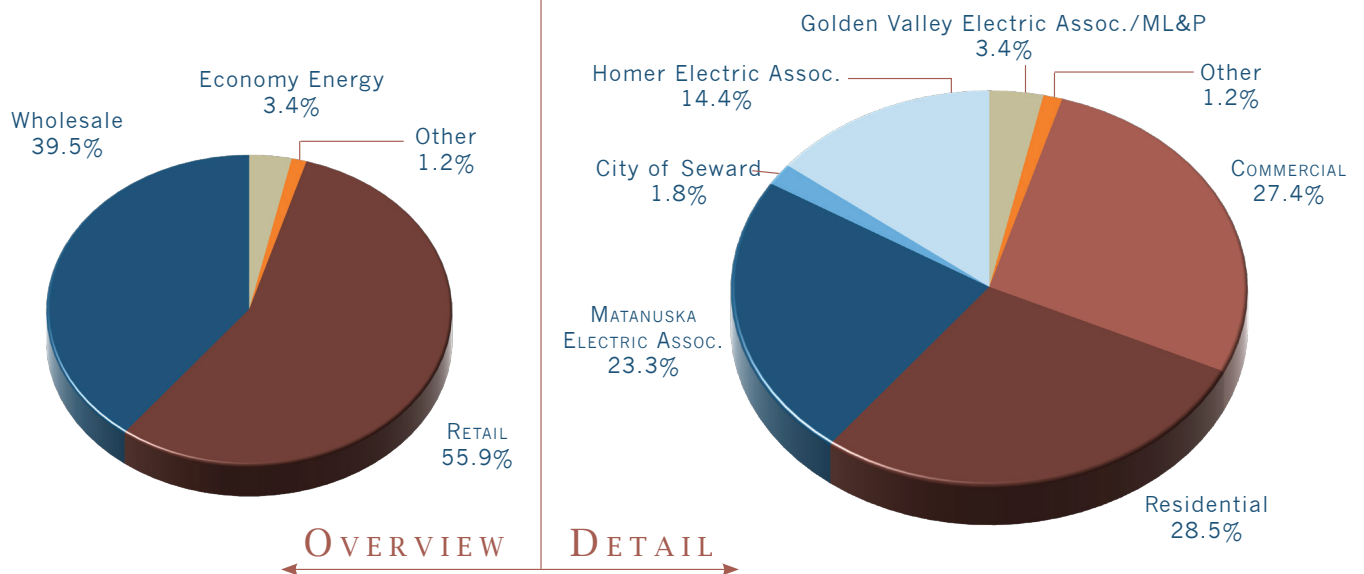
BY KILOWATT-HOURS

TOTAL: 2,606,722,849

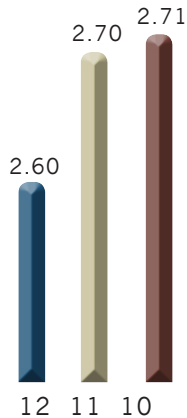


BY OPERATING REVENUES

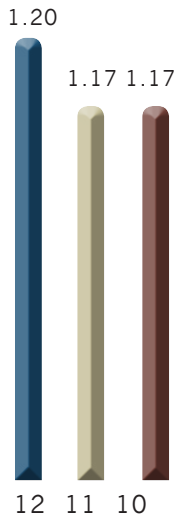
TOTAL: \$266,971,468



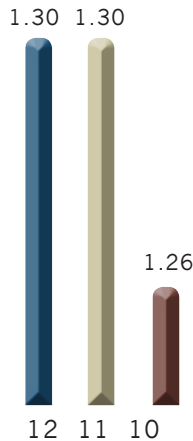
KILOWATT-HOURS SOLD (IN BILLIONS)



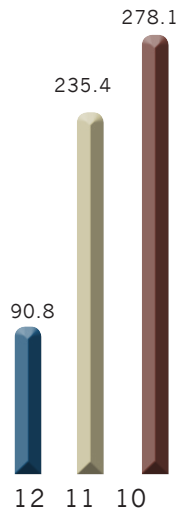
RETAIL KWH (IN BILLIONS)



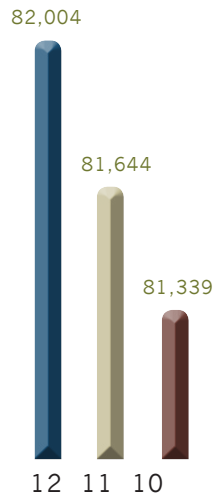
WHOLESALE KWH (IN BILLIONS)



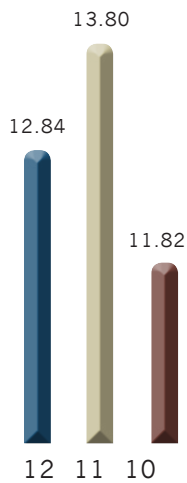
ECONOMY ENERGY KWH (IN MILLIONS)



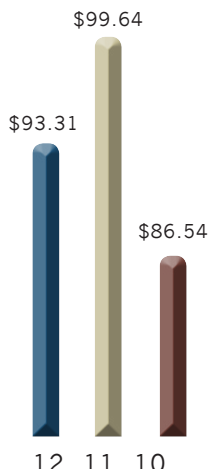
SERVICE LOCATIONS AT YEAR-END



COST PER RESIDENTIAL KWH IN DECEMBER* (CENTS/KWH)

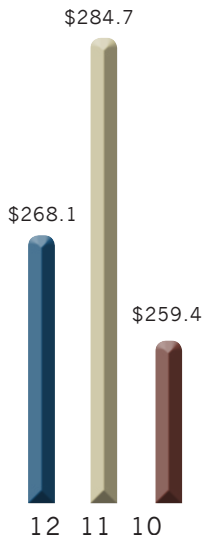


COST OF 650 KWH RESIDENTIAL SERVICE IN DECEMBER*

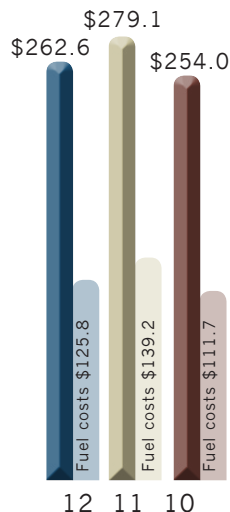


*INCLUDES CUSTOMER AND ENERGY CHARGES, FUEL AND PURCHASE POWER CHARGE AND REGULATORY COST CHARGE. DOES NOT INCLUDE 2 PERCENT MOA UNDERGROUNDING CHARGE

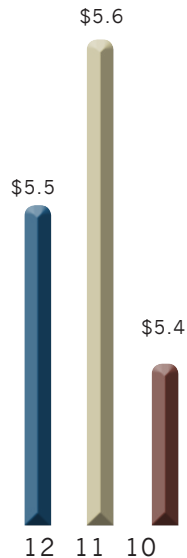
TOTAL REVENUE INCLUDING NON-OPERATING MARGINS (IN MILLIONS)



EXPENSES (IN MILLIONS)



MARGINS (IN MILLIONS)



*NOT INCLUDING THE CUSTOMER CHARGE AND THE 2 PERCENT MOA UNDERGROUNDING CHARGE

GENERATION SOURCE BY KWH

2012	89% Natural Gas	10% Hydro	1% Wind
2011	92% Natural Gas	8% Hydro	
2010	89% Natural Gas	11% Hydro	

OUTAGE STATISTICS

Chugach averaged 8.92 outage hours per customer in 2012, up considerably from the 2.03 hours in 2011 due to unusually severe storms. The 5-year average for customer outage hours increased to 3.52 hours in 2012, up from 2.13 hours in 2011.

Report of Independent Registered Public Accounting Firm

The Board of Directors
Chugach Electric Association, Inc.

We have audited the accompanying balance sheets of Chugach Electric Association, Inc. as of December 31, 2012 and 2011, and the related statements of operations, changes in equities and margins, and cash flows for each of the years in the three-year period ended December 31, 2012. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (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 examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and 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 Chugach Electric Association, Inc. as of December 31, 2012 and 2011, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2012, in conformity with U.S. generally accepted accounting principles.

KPMG LLP

March 22, 2013
Anchorage, Alaska

Balance Sheets
December 31, 2012 and 2011

<u>Assets</u>	<u>2012</u>	<u>2011</u>
Utility plant:		
Electric plant in service	\$891,781,509	\$862,362,243
Construction work in progress	263,459,794	206,005,783
Total utility plant	1,155,241,303	1,068,368,026
Less accumulated depreciation	(493,894,390)	(470,282,210)
Net utility plant	661,346,913	598,085,816
Other property and investments, at cost:		
Nonutility property	84,735	84,735
Investments in associated organizations	10,552,683	11,134,496
Special funds	570,027	420,783
Total other property and investments	11,207,445	11,640,014
Current assets:		
Cash and cash equivalents, including repurchase agreements of \$100 in 2012 and \$100 in 2011	14,047,469	17,118,118
Special deposits	153,233	149,701
Restricted cash equivalents	1,953,085	122,006,738
Marketable securities	10,158,016	0
Fuel cost under-recovery	0	1,213,484
Accounts receivable, less provision for doubtful accounts of \$490,413 in 2012 and \$408,429 in 2011	46,650,901	42,373,995
Materials and supplies	32,867,971	32,994,454
Fuel stock	9,466,767	0
Prepayments	2,156,862	1,911,789
Other current assets	252,146	229,858
Total current assets	117,706,450	217,998,137
Deferred charges, net	27,712,243	25,205,690
Total assets	\$817,973,051	\$852,929,657
	<u>2012</u>	<u>2011</u>
<u>Liabilities, Equities and Margins</u>		
Equities and margins:		
Memberships	\$1,559,344	\$1,517,488
Patronage capital	153,832,674	148,355,246
Other	11,372,355	11,358,692
Total equities and margins	166,764,373	161,231,426
Long-term obligations, excluding current installments:		
Bonds payable	491,916,666	264,333,333
National Bank for Cooperatives note payable	29,680,420	31,756,775
Total long-term obligations	521,597,086	296,090,108
Current liabilities:		
Current installments of long-term obligations	24,493,022	133,360,210
Commercial paper	11,500,000	175,000,000
Accounts payable	16,488,323	22,800,190
Consumer deposits	4,279,901	3,949,052
Fuel cost over-recovery	13,710,049	0
Accrued interest	6,807,207	6,843,473
Salaries, wages and benefits	8,369,203	7,597,691
Fuel	20,868,078	24,399,157
Other current liabilities	4,559,981	3,350,692
Total current liabilities	111,075,764	377,300,465
Deferred compensation	570,027	420,783
Deferred liabilities	1,769,172	1,703,277
Patronage capital payable	6,858,367	6,646,068
Deferred proceeds on sale of asset	9,338,262	9,537,530
Total liabilities, equities and margins	\$817,973,051	\$852,929,657

See accompanying notes to financial statements.

Statements of Operations
Years ended December 31, 2012, 2011 and 2010

	<u>2012</u>	<u>2011</u>	<u>2010</u>
Operating revenues	\$266,971,468	\$283,618,369	\$258,325,345
Operating expenses:			
Fuel	125,836,659	139,179,413	111,718,947
Production	16,739,931	16,853,232	18,248,656
Purchased power	22,104,687	25,861,814	26,691,968
Transmission	5,802,009	6,809,401	5,697,446
Distribution	15,822,104	13,387,477	12,216,252
Consumer accounts	6,013,419	5,465,315	5,323,551
Administrative, general and other	23,519,246	22,169,039	21,434,273
Depreciation and amortization	32,356,900	32,616,175	32,636,108
Total operating expenses	248,194,955	262,341,866	233,967,201
Interest expense:			
Long-term debt and other	24,085,371	18,681,680	21,014,387
Charged to construction	(9,682,440)	(1,934,703)	(1,008,689)
Interest expense, net	14,402,931	16,746,977	20,005,698
Net operating margins	4,373,582	4,529,526	4,352,446
Nonoperating margins:			
Interest income	447,434	297,983	310,964
Allowance for funds used during construction	258,301	159,916	83,966
Capital credits, patronage dividends and other	446,190	585,837	662,633
Total nonoperating margins	1,151,925	1,043,736	1,057,563
Assignable margins	\$5,525,507	\$5,573,262	\$5,410,009

See accompanying notes to financial statements.

Statements of Changes in Equities and Margins
Years ended December 31, 2012, 2011 and 2010

	<u>Memberships</u>	<u>Other Equities and Margins</u>	<u>Patronage Capital</u>	<u>Total</u>
Balance, January 1, 2010	\$1,432,054	\$10,660,322	\$144,228,221	\$156,320,597
Assignable margins	0	0	5,410,009	5,410,009
Retirement of capital credits	0	0	(94,278)	(94,278)
Unclaimed capital credit retirements	0	90,320	0	90,320
Memberships and donations received	42,815	72,821	0	115,636
Balance, December 31, 2010	1,474,869	10,823,463	149,543,952	161,842,284
Assignable margins	0	0	5,573,262	5,573,262
Retirement of capital credits	0	0	(6,761,968)	(6,761,968)
Unclaimed capital credit retirements	0	367,277	0	367,277
Memberships and donations received	42,619	167,952	0	210,571
Balance, December 31, 2011	1,517,488	11,358,692	148,355,246	161,231,426
Assignable margins	0	0	5,525,507	5,525,507
Retirement of capital credits	0	0	(48,079)	(48,079)
Unclaimed capital credit retirements	0	(12,949)	0	(12,949)
Memberships and donations received	41,856	26,612	0	68,468
Balance, December 31, 2012	\$1,559,344	\$11,372,355	\$153,832,674	\$166,764,373

See accompanying notes to financial statements.

Statements of Cash Flows
Years ended December 31, 2012, 2011 and 2010

<u>Cash flows from operating activities:</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Assignable margins	\$5,525,507	\$5,573,262	\$5,410,009
Adjustments to reconcile assignable margins to net cash provided by operating activities:			
Depreciation	32,356,900	32,616,175	32,636,108
Amortization and depreciation cleared to operating expenses	5,882,580	5,472,557	5,457,480
Allowance for funds used during construction	(258,301)	(159,916)	(83,966)
Loss on disposal of assets	991,871	851,756	210,596
Other	(135,739)	(93,834)	74,726
(Increase) decrease in assets:			
Accounts receivable, net	(4,276,906)	(7,128,876)	670,424
Fuel cost under-recovery	1,213,484	1,158,147	(2,093,467)
Materials and supplies	(189,092)	2,563,223	(6,061,005)
Fuel stock	(9,466,767)	0	0
Prepayments	(245,073)	13,635	(663,527)
Other assets	27,937	(2,049,082)	(96,522)
Deferred charges	(4,335,252)	(6,358,154)	(1,511,639)
Increase (decrease) in liabilities:			
Accounts payable	1,454,677	1,891,089	(1,321,046)
Consumer deposits	330,849	(1,276,677)	(267,221)
Fuel cost over-recovery	13,710,049	0	(3,511,422)
Accrued interest	(36,266)	793,942	(18,099)
Salaries, wages and benefits	771,512	863,849	777,522
Fuel	(3,531,079)	2,829,619	6,911,480
Other current liabilities	3,094,139	3,011,319	2,701,345
Deferred liabilities	120,204	239,761	(70,335)
Net cash provided by operating activities	43,005,234	40,811,795	39,151,441
<u>Cash flows from investing activities:</u>			
Proceeds on sale of Bernice Lake Power Plant	0	9,537,530	0
Investment in associated organizations	663,697	1,153,470	311,593
Investment in restricted cash equivalents	0	(270,000,000)	0
Investment in marketable securities	(10,096,304)	0	0
Proceeds from restricted cash equivalents	120,000,000	150,000,000	0
Extension and replacement of plant	(109,180,413)	(123,679,854)	(73,214,825)
Net cash provided by (used in) investing activities	1,386,980	(232,988,854)	(72,903,232)
<u>Cash flows from financing activities:</u>			
Payments for debt issue costs	(1,850,199)	(1,949,027)	(1,493,572)
Proceeds from short-term obligations	24,500,000	76,500,000	47,000,000
Proceeds from long-term obligations	250,000,000	275,000,000	0
Repayments of short-term obligations	(188,000,000)	0	0
Repayments of long-term obligations	(133,360,210)	(152,851,500)	(4,118,029)
Memberships and donations received	55,519	189,385	205,956
Retirement of patronage capital and estate payments	(48,079)	(309,188)	(146,596)
Net receipts of consumer advances for construction	1,240,106	644,794	870,980
Net cash provided by (used in) financing activities	(47,462,863)	197,224,464	42,318,739
Net changes in cash and cash equivalents	(3,070,649)	5,047,405	8,566,948
<u>Cash and cash equivalents at beginning of period</u>	<u>\$17,118,118</u>	<u>\$12,070,713</u>	<u>\$3,503,765</u>
<u>Cash and cash equivalents at end of period</u>	<u>\$14,047,469</u>	<u>\$17,118,118</u>	<u>\$12,070,713</u>
Supplemental disclosure of non-cash investing and financing activities:			
Retirement of plant	\$10,405,777	\$11,317,319	\$6,666,875
Extension and replacement of plant included in accounts payable	\$10,620,219	\$15,561,199	\$15,919,688
Supplemental disclosure of cash flow information – interest expense paid, net of amounts capitalized	\$13,092,576	\$12,590,296	\$18,057,000

See accompanying notes to financial statements.

(1) Description of Business

Chugach Electric Association, Inc. (Chugach) is the largest electric utility in Alaska. Chugach is engaged in the generation, transmission and distribution of electricity to directly serve retail customers in the Anchorage and upper Kenai Peninsula areas. Through an interconnected regional electrical system, Chugach's power flows throughout Alaska's Railbelt, a 400-mile-long area stretching from the coastline of the southern Kenai Peninsula to the interior of the state, including Alaska's largest cities, Anchorage and Fairbanks.

Chugach also supplies much of the power requirements of three wholesale customers, Matanuska Electric Association, Inc. (MEA), Homer Electric Association, Inc. (HEA) and the City of Seward (Seward). We sell available generation in excess of our own needs to produce electric energy for sale to Golden Valley Electric Association, Inc. (GVEA). In addition, on a periodic basis, we provide electricity to Anchorage Municipal Light & Power (ML&P). Chugach's retail and wholesale members are the consumers of the electricity sold.

Chugach was organized as an Alaska electric cooperative in 1948 and operates on a not-for-profit basis and, accordingly, seeks only to generate revenues sufficient to pay operating and maintenance costs, the cost of purchased power, capital expenditures, depreciation, and principal and interest on all indebtedness and to provide for reserves. Chugach is subject to the regulatory authority of the Regulatory Commission of Alaska (RCA).

(2) Significant Accounting Policies

a. Management Estimates

In preparing the financial statements in conformity with generally accepted accounting principles, the management of Chugach is required to make estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the balance sheet and revenues and expenses for the reporting period. Estimates include allowance for doubtful accounts, workers compensation, deferred charges and credits, unbilled revenue and the estimated useful life of utility plant. Actual results could differ from those estimates.

b. Regulation

The accounting records of Chugach conform to the Uniform System of Accounts as prescribed by the Federal Energy Regulatory Commission (FERC). Chugach meets the criteria, and accordingly, follows the accounting and reporting requirements of Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 980, "Topic 980 - Regulated Operations." FASB ASC 980 provides for the recognition of regulatory assets and liabilities as allowed by regulators for costs or credits that are reflected in current rates or are considered probable of being included in future rates. Our regulated rates are established to recover all of our specific costs of providing electric service. In each rate filing, rates are set at levels to recover all of our specific allowable costs and those rates are then collected from our retail and wholesale customers. The regulatory assets or liabilities are then reduced as the cost or credit is reflected in earnings and our rates, see Note (2j) - "Deferred Charges and Credits."

c. Utility Plant and Depreciation

Additions to electric plant in service are recorded at original cost of contracted services, direct labor and materials, indirect overhead charges and capitalized interest. For property replaced or retired, the book value of the property, plus removal cost, less salvage, is charged to accumulated depreciation. Renewals and betterments are capitalized, while maintenance and repairs are normally charged to expense as incurred.

In accordance with FASB ASC 360, "Topic 360 - Property, Plant, and Equipment," certain utility plant is reviewed for impairment whenever events or changes in circumstances indicate the carrying amount of an asset may not be recoverable in rates. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset.

Depreciation and amortization rates have been applied on a straight-line basis and at December 31 are as follows:

	Annual Depreciation Rate Ranges			
	06/01/08	10/31/10	11/01/10	12/31/12
Steam production plant	4.45%	5.85%	4.81%	7.04%
Hydraulic production plant	1.22%	3.00%	1.06%	3.00%
Other production plant	3.77%	10.56%	3.98%	10.15%
Transmission plant	1.61%	6.67%	1.58%	7.86%
Distribution plant	1.95%	9.77%	2.17%	9.63%
General plant	1.25%	26.11%	1.57%	20.00%
Other	2.75%	2.75%	2.75%	2.75%

On November 1, 2010, the RCA approved revised depreciation rates effective November 1, 2010 in Docket U-09-097. Chugach's depreciation rates include a provision for cost of removal. Given that the estimated timing and amount cannot be reasonably estimated, Chugach does not record a separate liability for its obligation associated with the retirement of plant.

d. Capitalized Interest

Allowance for funds used during construction (AFUDC) and interest charged to construction - credit (IDC) are the estimated costs of the funds used during the period of construction from both equity and borrowed funds. AFUDC and IDC are applied to specific projects during construction. AFUDC and IDC calculations use the net cost of borrowed funds when used and is recovered through RCA approved rates as utility plant is depreciated. Chugach capitalized such funds at the weighted average rate (adjusted monthly) of 4.0 percent during 2012, 4.1 percent during 2011 and 4.8 percent during 2010. Chugach capitalized actual interest expense and related fees associated with the construction of Southcentral Power Plant (SPP).

e. Investments in Associated Organizations

The loan agreements with CoBank, ACB (CoBank) and National Rural Utilities Cooperative Finance Corporation (NRUCFC) requires as a condition of the extension of credit, that an equity ownership position be established by all borrowers. Chugach's equity ownership in these organizations is less than 1 percent. These investments are non-marketable and accounted for at cost. Management evaluates these investments annually for impairment. No impairment was recorded during 2012, 2011 and 2010.

f. Fair Value of Financial Instruments

FASB ASC 825, "Topic 825 - Financial Instruments," requires disclosure of the fair value of certain on and off balance sheet financial instruments for which it is practicable to estimate that value. The following methods are used to estimate the fair value of financial instruments:

- Cash and cash equivalents - the carrying amount approximates fair value because of the short maturity of those instruments.
- Consumer deposits - the carrying amount approximates fair value because of the short refunding term.
- Long-term obligations - the fair value is estimated based on the quoted market price for same or similar issues (see note 11).
- Restricted cash - the carrying amount approximates fair value because of the short maturity of those instruments.
- Repurchase agreement - the carrying amount approximates fair value because of the short maturity of those instruments.

g. Cash and Cash Equivalents / Restricted Cash Equivalents

For purposes of the statement of cash flows, Chugach considers all highly liquid instruments with a maturity of three months or less upon acquisition by Chugach to be cash equivalents. In November of 2011, Chugach opened a concentration account with First National Bank Alaska (FNBA). There is no rate of return or fees on this account. On December 30, 2011, Chugach opened a money market account with UBS Financial Services, Inc. (UBS) with an initial deposit of \$10.0 million, which was subsequently invested in marketable securities in September of 2012. Chugach also maintains an Overnight Repurchase Agreement with FNBA, however, in November of 2011 this account was placed into an inactive status. Prior to November of 2011 the daily balance was invested by FNBA and Chugach received varying interest rates for our investment pursuant to our Overnight Purchase Agreement. The concentration account had an average balance of \$8,942,631 and \$6,481,639 for the years ended December 31, 2012 and 2011, respectively. The Overnight Repurchase Agreement account had an average balance in 2012 and 2011 of \$100 and \$5,210,009, at an average interest rate of 0.00 percent and 0.06 percent, respectively.

On January 12, 2012, Chugach opened a money market account with KeyBank with the balance of proceeds from the 2012 Series A bond purchase, after repaying the outstanding balance of commercial paper. Chugach's initial deposit was \$69.0 million. Chugach used the proceeds primarily to fund capital expenditures associated with SPP and closed the account in February of 2013.

Restricted cash equivalents include State of Alaska construction bonds and funds on deposit for future workers compensation claims. In 2011, restricted cash equivalents included \$120.0 million of proceeds from the issuance of the 2011 Series A Bonds, which was used to retire the 2002 Series A Bonds on February 1, 2012.

h. Accounts Receivable

Trade accounts receivable are recorded at the invoiced amount. The allowance for doubtful accounts is management's best estimate of the amount of probable credit losses in existing accounts receivable. Chugach determines the allowance based on its historical write-off experience and current economic conditions. Chugach reviews its allowance for doubtful accounts monthly. Past due balances over 90 days in a specified amount are reviewed individually for collectability. All other balances are reviewed in aggregate. Account balances are charged off against the allowance after all means of collection have been exhausted and the potential for recovery is considered remote. Chugach does not have any off-balance-sheet credit exposure related to its customers. Included in accounts receivable are invoiced amounts to ML&P for fuel and their proportionate share of current SPP costs, which amounted to \$3.0 and \$4.8 million in 2012 and 2011, respectively. In addition, accounts receivable includes an invoiced amount to the Alaska Energy Authority (AEA) for reimbursable expenditures related to a grant for the Cook Inlet Gas Gathering System (CIGGS) project, which amounted to \$4.0 million in 2012.

i. Materials and Supplies

Materials and supplies are stated at average cost.

j. Deferred Charges and Credits

In accordance with FASB ASC 980, Chugach's financial statements reflect regulatory assets and liabilities. Continued accounting under FASB ASC 980, requires that certain criteria be met. We capitalize all or part of costs that would otherwise be charged to expense if it is probable that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for ratemaking purposes and future revenue will be provided to permit recovery of the previously incurred cost. Management believes Chugach's operations currently satisfy these criteria.

Chugach regulatory asset recoveries are embedded in base rates approved by the RCA. Specific costs incurred and recorded as Regulatory Assets, including the amortization period for recovery, are approved by the RCA either in standard SRFs, general rate case filings or specified independent requests. The rates approved related to the regulatory assets are matched to the amortization of actual expenditures recognized on the books. The regulatory assets are amortized and collected through rates over differing periods depending upon the period of benefit as established by the RCA. Deferred credits, primarily representing regulatory liabilities, are amortized to operating expense over the period required for ratemaking purposes. It also includes refundable contributions in aid of construction, which are credited to the associated cost of construction of property units. Refundable contributions in aid of construction are held in deferred credits pending their return or other disposition. If events or circumstances should change so the criteria are not met, the write off of regulatory assets and liabilities could have a material effect on Chugach's financial position or results of operations.

k. Patronage Capital

Revenues in excess of current period costs (net operating margins and nonoperating margins) in any year are designated on Chugach's statement of revenues and expenses as assignable margins. These excess amounts (i.e. assignable margins) are considered capital furnished by the members, and are credited to their accounts and held by Chugach until such future time as they are retired and returned without interest at the discretion of the Board of Directors (Board). Retained assignable margins are designated on Chugach's balance sheet as patronage capital. This patronage capital constitutes the principal equity of Chugach. The Board may also approve the return of capital to former members and estates who request early retirements at discounted rates under a discounted capital credits retirement plan authorized by the Board in September 2002.

In 2007, Chugach entered into an agreement with HEA to return all of its patronage capital within five years after expiration of its power sales agreement, which is January 1, 2014. This patronage capital retirement was related to a settlement agreement associated with the 2005 Test Year General Rate Case (Docket U-06-134). The RCA accepted the parties' settlement agreement on August 9, 2007. HEA's patronage capital is classified as patronage capital payable and was \$6.9 million at December 31, 2012.

l. Operating Revenues

Revenues are recognized upon delivery of electricity. Operating revenues are based on billing rates authorized by the RCA, which are applied to customers' usage of electricity. Chugach's rates are established, in part, on test period sales levels that reflect actual operating results. Chugach calculates unbilled revenue at the end of each month to ensure the recognition of a calendar year's revenue. Chugach accrued \$8,548,660 and \$8,977,409 of unbilled retail revenue at December 31, 2012 and 2011, respectively. Wholesale revenue is recorded from metered locations on a calendar month basis, so no estimation is required. Chugach's tariffs include provisions for the recovery of gas costs according to gas supply contracts, as well as purchased power costs.

m. Fuel and Purchased Power Costs Recovery

Expenses associated with electric services include fuel used to generate electricity and power purchased from others. Chugach is authorized by the RCA to recover fuel and purchased power costs through the fuel and purchased power adjustment process, which is adjusted quarterly to reflect increases and decreases of such costs. We recognize differences between projected recoverable fuel costs and amounts actually recovered through rates. The fuel cost under/over recovery on our Balance Sheet represents the net accumulation of any under or over collection of fuel and purchase power costs. Fuel cost under-recovery will appear as an asset on our Balance Sheet and will be collected from our members in subsequent periods. Conversely, fuel cost over-recovery will appear as a liability on our Balance Sheet and will be refunded to our members in subsequent periods. Fuel costs were over-recovered by \$13,710,049 in 2012 and under-recovered by \$1,213,484 in 2011. Total fuel and purchased power costs in 2012, 2011, and 2010 were \$147,941,346, \$165,041,227, and \$138,410,915, respectively.

n. Environmental Remediation Costs

Chugach accrues for losses and establishes a liability associated with environmental remediation obligations when such losses are probable and can be reasonably estimated. Such accruals are adjusted as further information develops or circumstances change. Estimates of future costs for environmental remediation obligations are not discounted to their present value. However, various remediation costs may be recoverable through rates and accounted for as a regulatory asset.

o. Income Taxes

Chugach is exempt from federal income taxes under the provisions of Section 501(c)(12) of the Internal Revenue Code and for the years ended December 31, 2012, 2011 and 2010 was in compliance with that provision. In addition, as described in "Note (15) - Commitments and Contingencies," Chugach collects sales tax and is assessed gross receipts and excise taxes which are presented on a net basis in accordance with FASB ASC 605-45-50, "Topic 605 - Revenue Recognition - Subtopic 45 - Principal Agent Considerations - Section 50 - Disclosure."

Chugach applies a more-likely-than-not recognition threshold for all tax uncertainties. FASB ASC 740, "Topic 740 - Income Taxes," only allows the recognition of those tax benefits that have a greater than fifty percent likelihood of being sustained upon examination by the taxing authorities. Chugach's management reviewed Chugach's tax positions and determined there were no outstanding, or retroactive tax positions, that were not highly certain of being sustained upon examination by the taxing authorities.

Management has concluded that there are no significant uncertain tax positions requiring recognition in its financial statements for all periods presented. Chugach's evaluation was performed for the tax periods ended December 31, 2009 through December 31, 2012 for U.S. Federal Income Tax, the tax years which remain subject to examination by major tax jurisdictions as of December 31, 2012.

p. Consumer deposits

Consumer deposits are the amounts certain customers are required to deposit to receive electric service. Consumer deposits for the years ended December 31, 2012 and 2011, totaled \$2.4 million and \$2.2 million, respectively. Consumer deposits also represent customer credit balances as a result of prepaid accounts. Credit balances for the years ended December 31, 2012 and 2011 totaled \$1.9 million and \$1.7 million, respectively.

q. Grants

Chugach has received federal and state grants to offset storm related expenditures and to support the construction of facilities to transport fuel, divert water and transmit electricity to its consumers. Grant proceeds used to construct or acquire equipment are offset against the carrying amount of the related assets while grant proceeds for storm related expenditures are offset against the actual expense incurred, which totaled \$30.5 million and \$4.3 million in 2012 and 2011, respectively. The assets constructed from grant awards may not be sold, or used as collateral for any reason.

r. Fuel Stock

Fuel Stock is the weighted average cost of fuel injected into the Cook Inlet Natural Gas Storage Alaska (CINGSA), which began service in the second quarter of 2012. Limited withdrawals of gas began in the third quarter of 2012. Chugach's fuel balance in storage amounted to \$9.5 million for the year ended December 31, 2012.

s. Marketable Securities

In September of 2012, Chugach implemented a bond and equity investment portfolio. Chugach's initial investment was \$10.0 million. The investments are classified as marketable securities, reported at fair value with gains and losses included in earnings. At December 31, 2012, the carrying amount and fair value was \$10.1 million.

(3) Recent Accounting Pronouncements

ASC Update 2013-02 "Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income"

In January 2013, the FASB issued ASC Update 2013-02, "Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income." ASC Update 2013-02 expands the disclosure requirements for amounts reclassified out of accumulated other comprehensive income. This update is effective for reporting periods beginning after December 15, 2012. Chugach began application of ASC 2013-02 on January 1, 2013. Chugach does not have any items included in other comprehensive income. Therefore, assign margins and comprehensive income are the same amount and the adoption did not have any effect on results of operations, financial position, and cash flows.

ASC Update 2013-01 "Balance Sheet (Topic 210): Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities"

In January 2013, the FASB issued ASC Update 2013-01, "Balance Sheet (Topic 210): Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities." ASC Update 2013-01 clarifies the scope of Update 2011-11 to apply to derivatives accounted for in accordance with Topic 815, Derivatives and Hedging, including bifurcated embedded derivatives, repurchase agreements and reverse repurchase agreements, and securities borrowing and securities lending transactions that are either offset in accordance with Section 210-20-45 or Section 815-10-45 or subject to an enforceable master netting arrangement or similar agreement. This update is effective for fiscal years beginning on or after January 1, 2013 and interim periods within those annual periods. Chugach began application of ASC 2013-01 on January 1, 2013. Adoption did not have any incremental effect on results of operations, financial position, and cash flows.

ASC Update 2012-04 "Technical Amendments and Improvements"

In October 2012, the FASB issued ASC Update 2012-04, "Technical Amendments and Improvements." ASC Update 2012-04 amends a wide range of Topics in the FASB Codification, however the main provisions were to correct source literature guidance, provide clarity by updating and correcting wording and references, relocating guidance to a more appropriate location within the Codification, and conform terminology and clarify guidance to fully reflect the fair value measurement and disclosure requirements of Topic 820. This update is effective for the first interim or annual reporting period beginning after December 15, 2012. Chugach began application of ASC 2012-04 on January 1, 2013. Adoption did not have any incremental effect on results of operations, financial position, and cash flows.

ASC Update 2012-03 "Technical Amendments and Corrections to SEC Sections: Amendments to SEC Paragraphs to SEC Staff Accounting Bulletin No. 114, Technical Amendments Pursuant to SEC Release No. 33-9250, and Corrections Related to FASB Accounting Standards Update 2010-22 (SEC Update)"

In August 2012, the FASB issued ASC Update 2012-03, "Technical Amendments and Corrections to SEC Sections: Amendments to SEC Paragraphs to SEC Staff Accounting Bulletin No. 114, Technical Amendments Pursuant to SEC Release No. 33-9250, and Corrections Related to FASB Accounting Standards Update 2010-22 (SEC Update)." ASC Update 2012-03 amends various SEC paragraphs pursuant to the issuance of Staff Accounting Bulletin (SAB) No. 114, which revised or removed portions of the interpretive guidance included in the FASB Codification of the SAB Series to ensure consistency of referencing throughout the SAB Series. This update is effective upon issuance. Chugach began application of ASC 2012-03 on its issuance date of August 27, 2012. Adoption did not have any incremental effect on results of operations, financial position, and cash flows.

ASC Update 2011-04 "Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS"

In May 2011, the FASB issued ASC Update 2011-04, "Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS." ASC Update 2011-04 amends current U.S. GAAP to create more commonality with IFRS by changing some of the wording used to describe requirements for measuring fair value and for disclosing information about fair value measurements. This update is effective for the first interim or annual reporting period beginning after December 15, 2011. Chugach began application of ASC 2011-04 on January 1, 2012. Adoption did not have any incremental effect on results of operations, financial position, and cash flows.

ASC Update 2011-12 "Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05"

In December 2011, the FASB issued ASC Update 2011-12, "Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05." ASC Update 2011-12 defers the effective date of the requirements to present separate line items on the income statement for reclassification adjustments of items out of accumulated other comprehensive income into net income for all periods presented. This update does not change the other requirements of ASC Update 2011-05. This update is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Chugach began application of ASC 2011-12 in the period ended March 31, 2012. Chugach does not have any items included in other comprehensive income. Therefore, assignable margins and comprehensive income are the same amount and the adoption did not have any effect on results of operations, financial position, and cash flows.

(4) Fair Value of Assets and Liabilities

Fair Value Hierarchy

In accordance with FASB ASC 820, Chugach groups its financial assets and liabilities measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value. These levels are:

Level 1 – Valuation is based upon quoted prices for identical instruments traded in active exchange markets, such as the New York Stock Exchange. Level 1 also includes U.S. Treasury and federal agency securities, which are traded by dealers or brokers in active markets. Valuations are obtained from readily available pricing sources for market transactions involving identical assets or liabilities.

Level 2 – Valuation is based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant assumptions are observable in the market.

Level 3 – Valuation is generated from model-based techniques that use significant assumptions not observable in the market. These unobservable assumptions reflect Chugach's estimates of assumptions that market participants would use in pricing the asset or liability. Valuation techniques include use of option pricing models, discounted cash flow models and similar techniques.

The table below presents the balance of Chugach's Overnight Repurchase Agreement, marketable securities, money market and restricted cash equivalents assets measured at fair value on a recurring basis at December 31, 2012, and December 31, 2011.

	Total	Level 1	Level 2	Level 3
<u>December 31, 2012</u>				
Repurchase agreement	\$100	\$0	\$100	\$0
Money market	\$2,829,397	\$2,829,397	\$0	\$0
Marketable securities	\$10,158,016	\$10,158,016	\$0	\$0
<u>December 31, 2011</u>				
Repurchase agreement	\$100	\$0	\$100	\$0
Money market	\$10,000,000	\$10,000,000	\$0	\$0
Restricted cash equivalents	\$122,006,738	\$122,006,738	\$0	\$0

Chugach had no Level 3 assets or liabilities measured at fair value on a recurring basis. Fair value estimates are dependent upon subjective assumptions and involve significant uncertainties resulting in variability in estimates with changes in assumptions. The fair value of long-term debt has been determined using discounted future cash flows at borrowing rates currently available to Chugach. The fair value of cash and cash equivalents, accounts receivable and payable, and other short-term monetary assets and liabilities approximate carrying value due to their short-term nature.

(5) Regulatory Matters

Modification to Certificate of Public Convenience and Necessity

On May 29, 2012, Chugach submitted a request to amend its service area contained within its certificate of public convenience and necessity to include Fire Island and the City of Whittier, and to adjust the service area boundary between Chugach and the City of Seward, d/b/a Seward Electric System in the Moose Pass area where both utilities are currently authorized to provide electric service. Chugach also requested that its service area be modified to include the areas of expansion in which electric service is currently being provided but are not described in Chugach's certificate, and to include other service areas where potential future customer requests for electric service can be reasonably expected. Chugach also proposed that several sections of its certificate be removed as these areas are well outside of any reasonable likelihood of service requests. On July 9, 2012, the City of Seward submitted comments in support of resolving the boundary area overlap between Chugach and Seward. Seward did not oppose the service area changes proposed by Chugach. A hearing was held on September 4, 2012, in which Chugach made a presentation on the proposed modifications to its service territory and responded to questions from the RCA. On January 25, 2013, the RCA approved Chugach's request.

Petition to Establish Depreciation Rates for SPP

Chugach submitted proposed depreciation rates for SPP on February 22, 2012, with a recommended 35 year life for the project. The filing also included depreciation rates for transmission plant specific to the project with a recommended life consistent with the depreciation rates of Chugach's existing transmission assets. The RCA opened Docket U-12-009 on March 2, 2012, to adjudicate the case. Petitions to intervene were received from the Attorney General (AG), HEA and MEA. No responsive testimony was received from any of the parties. A hearing was held on July 2, 2012. On August 31, 2012, the RCA issued an order in the case, approving depreciation rates for SPP with an effective date equal to its in-service date, requested filing requirements and closed the docket.

Seward Power Sales Agreement

Effective March 1, 2012, the RCA approved Amendment No. 2 to the 2006 Agreement for the Sale and Purchase of Electric Power and Energy between Chugach and the City of Seward (2006 Agreement). Amendment No. 2 allows Seward to accept power from Small Power Projects on terms that are financially neutral to both Chugach and Seward for wholesale power service provided to Seward, without changing Seward's status under the 2006 Agreement as a partially interruptible requirements customer of Chugach. In addition, Amendment No. 2 facilitates Seward offering net metering service from eligible on-site generation sources to its retail customers without attendant compensation to Chugach. Chugach and Seward have structured the net metering conditions to be consistent with the net metering regulations adopted by the RCA.

Fire Island Wind Project

On October 10, 2011, the RCA issued an order approving Chugach's request for assurance of cost recovery associated with a new power purchase agreement (PPA) between Chugach and Fire Island Wind, LLC (FIW), a special purpose entity wholly-owned by Cook Inlet Region, Inc. The PPA is a 25-year agreement whereby Chugach purchases the output of the facility commencing January 1, 2013. The Fire Island Wind project is comprised of eleven 1.6- megawatt wind turbine generators with a total nameplate capacity of 17.6 megawatts which are expected to generate approximately 50,000 megawatt hours (MWh) per year. The generators are located on the southern part of Fire Island, three miles west of Anchorage, Alaska. Chugach began receiving power from the project on August 17, 2012. An affiliate of FIW is responsible for the construction of the interconnection between the project and Chugach's transmission system. Chugach is the recipient of a grant in the amount of approximately \$25.0 million appropriated from the State of Alaska. The grant was used to offset construction of the transmission line. Construction expenditures applied against the grant were \$20.3 million in 2012 and \$3.2 million in 2011. Chugach is not expected to incur any unreimbursed capital costs associated with this line and will acquire the line once construction is successfully completed.

Chugach submitted a specific rate recovery plan in compliance with U-11-100(5) on April 2, 2012, and project status reports on June 30, 2012 and October 31, 2012. The rate recovery plan addressed customer intergenerational impacts resulting from purchases made under the PPA's fixed pricing structure. The RCA held a hearing on June 5, 2012, for Chugach to supplement its filing with an oral presentation explaining the rate impacts and equities to ratepayers. As a result of the hearing, Chugach submitted an updated rate recovery proposal on July 31, 2012, requesting that purchases made under the PPA be recovered on a direct cost basis for recovery through the fuel and purchased power surcharge process. Chugach withdrew its April 2, 2012, compliance filing.

On September 28, 2012, the RCA opened Docket U-12-134 and issued an order granting Chugach interim approval of its cost disclosure and rate recovery proposals relating to the Fire Island wind project and invited participation from the Attorney General (AG). Chugach and the AG stipulated on key matters of the filing and requested RCA approval in a stipulation submitted to the RCA on November 15, 2012. The RCA held a hearing on January 17, 2013, to review the stipulation, with participation from both Chugach and the AG. On February 12, 2013, the RCA issued Order No. 3 of Docket U-12-134 accepting the stipulation.

Regulatory Assets

Storm Expenditures

On November 8, 2012, Chugach submitted a petition to the RCA requesting authorization to create a regulatory asset for deferred recovery of expenditures associated with extensive storm damage that occurred in September of 2012. Repeated windstorms were followed by considerable amounts of rain, resulting in outages and flooding, primarily caused by falling and uprooted trees. Chugach requested approval to recover in future electric rates over a twelve month period approximately \$1.8 million of costs. On November 19, 2012, the RCA opened Docket U-12-144, designated a commission panel and appointed an administrative law judge. The AG submitted comments on December 14, 2012, opposing Chugach's request. The RCA held a hearing on January 14, 2013. On January 30, 2013, the RCA issued Order No. 3 of Docket U-12-144 and did not accept Chugach's request, however, the RCA provided Chugach the opportunity to augment the record and re-submit its petition at a later time. Chugach is evaluating the option of supplementing the record and re-submitting its request.

Interest and Financing Costs

On January 11, 2012, Chugach issued \$75.0 million of First Mortgage Bonds (2012 Series A, Tranche A) at an interest rate of 4.01 percent, \$125.0 million of First Mortgage Bonds (2012 Series A, Tranche B) at an interest rate of 4.41 percent and \$50.0 million of First Mortgage Bonds (2012 Series A, Tranche C) at an interest rate of 4.78 percent. The proceeds of the 2012 Series A Bonds were used to repay outstanding commercial paper and to finance SPP construction.

On March 12, 2012, Chugach submitted a petition to the RCA requesting authorization to create a regulatory asset for deferred recovery of interim interest expense associated with SPP financing and also requested approval to recover the financing transaction costs in future electric rates over the life of the 2012 Series A Bonds. Chugach's request included the approval to defer the interest expense on the portion of the proceeds not immediately expended on SPP and recover it in future electric rates over the life of the bonds, or between 20 and 30 years. The deferral of interest for the portion of the 2012 bonds not immediately expended totaled approximately \$1.1 million. The RCA opened Docket U-12-015 on March 21, 2012. On May 22, 2012, Chugach and the AG of the State of Alaska submitted a stipulation whereby the AG did not oppose the regulatory and accounting treatment requested by Chugach. On June 19, 2012, the RCA issued Order No. 2 accepting the stipulation and closing the docket.

2012 General Rate Case

In anticipation of commercial operation of SPP, on December 21, 2012, Chugach submitted a general rate case with the RCA to increase system base rate revenues by \$30.0 million, or approximately 26 percent on total base rate revenues of \$115.0 million. Chugach requested that the proposed rates become effective on an interim and refundable basis beginning in February of 2013. In addition to the base rate increases, the filing requests approval to update and expand Chugach's operating tariff to include both firm and non-firm transmission wheeling service and attendant ancillary services in support of third-party transactions on the Chugach system. The expansion of the tariff was made, in part, to accommodate wheeling services in anticipation of the expiration of the HEA and MEA wholesale customer contracts in 2014. Because of efficiency improvements associated with the commercial operation of SPP, Chugach also submitted a request in a separate filing to the RCA to adjust its fuel rates effective at the same time as the requested base rate increases contained in the general rate case filing. This allows the interim base rate increases to be synchronized with expected reductions in fuel costs reflected in Chugach's fuel rates.

On February 1, 2013, Chugach submitted a supplemental filing to the RCA removing the impacts associated with a one-year amortization of distribution storm-related costs (see discussion on Storm Expenditures above) from its retail revenue requirement. On February 6, 2013, the Commission opened Docket U-13-007 and issued Order No. 1 approving Chugach's supplemental filing for rates effective February 6, 2013 on an interim and refundable basis. In addition, the Commission also approved Chugach's request to assess transmission wheeling charges on economy energy transactions that originate from the Chugach system.

In total, when factoring both base rate increases and reductions in fuel costs, the net increase to Chugach retail end-users is approximately 6 percent, while the net increase to retail end-users of Chugach's wholesale customers is approximately 4 percent to 7 percent.

Removal of Margin Cap on Economy Energy Sales

On October 31, 2012, Chugach submitted a request to the RCA for approval to remove the current eight mill margin cap on economy energy transactions but retain the requirement that such transactions must fall between Chugach's incremental and the purchasing utility's decremental cost of generation. The RCA approved the filing on January 24, 2013. The expected impact of the approval, in combination with the Chugach-GVEA sales arrangement, is additional system margin contributions in excess of \$2 million over the upcoming year.

Recovery of Qualified Facility Purchases and the Establishment of a Balancing Account

On October 31, 2012, Chugach submitted a filing to the RCA requesting approval to include a new cost element in Chugach's purchased power cost recovery process to recover non-firm energy purchases from Qualified Facilities, and to create a balancing account for use in the development of quarterly buyback rates associated with purchases from Qualified Facilities. On January 30, 2013, the RCA issued a letter order approving the filing.

Recovery of Natural Gas Compression Costs

Chugach submitted a filing to the RCA on October 31, 2012, requesting approval to add a new cost element in Chugach's fuel adjustment mechanism to recover charges associated with natural gas compression on the Kenai Nikiski Pipeline needed to allow bidirectional flows on the Cook Inlet Gas Gathering System. The new cost element includes operations and maintenance charges, facility rental charges, fuel and control service charges.

On December 7, 2012, the Regulatory Affairs and Public Advocacy Section of the Office of the Attorney General submitted comments opposing Chugach's request to recover compression costs through the fuel rate adjustment process. Chugach submitted a response on December 13, 2012. The RCA issued a letter order on January 14, 2013, approving Chugach's request for purchases through July 31, 2013. After July 31, 2013, a separate tariffed rate is expected to be developed by Hilcorp.

June 30, 2012 Test Year Simplified Rate Filing

On September 28, 2012, Chugach submitted a SRF to the RCA and requested a system demand and energy rate decrease of 1.7 percent, or approximately \$1.9 million on an annual basis. The filing was based on the June 30, 2012 test year for proposed rate adjustments effective in November 2012. On a customer class basis, Chugach requested demand and energy rate decreases of 1.7 percent to Chugach retail customers and decreases of 2.1 percent and 1.9 percent to its wholesale customers HEA and MEA, respectively, and a 1.6 percent increase to Seward. The RCA issued a letter order on November 6, 2012, approving the filing. The updated rates were effective on and after November 12, 2012.

December 31, 2011 Test Year Simplified Rate Filing

On March 30, 2012, Chugach submitted a SRF to the RCA and requested a system demand and energy rate decrease of 0.1 percent, or approximately \$0.8 million on an annual basis. The filing was based on the December 31, 2011 test year for proposed rate adjustments effective in May 2012. On a customer class basis, Chugach requested demand and energy rate increases of 1.3 percent to Chugach retail customers and decreases of 2.9 percent to its wholesale classes. The RCA issued a letter order on May 10, 2012, approving the filing. The updated rates were effective on and after May 14, 2012.

Economy Energy Sales and Transmission Wheeling Service

On April 23, 2012, Chugach submitted a filing to the RCA requesting approval to update its economy energy and transmission wheeling services tariffs to reflect current costs and operating conditions associated with transactions at the bulk power supply level. After public comments and meetings Chugach withdrew the filing and will file updated rates for transmission and related ancillary services in conjunction with its 2012 general rate case.

(6) Utility Plant

Major classes of utility plant as of December 31 are as follows:

	<u>2012</u>	<u>2011</u>
Electric plant in service:		
Steam production plant	\$60,462,671	\$60,462,671
Hydraulic production plant	20,513,746	20,456,395
Other production plant	127,980,607	134,434,574
Transmission plant	252,910,740	252,561,598
Distribution plant	257,587,220	257,341,532
General plant	51,901,426	45,144,425
Unclassified electric plant in service ¹	109,023,464	80,559,413
Intangible plant ¹	4,710,912	4,710,912
Other ¹	6,690,723	6,690,723
Total electric plant in service	<u>891,781,509</u>	<u>862,362,243</u>
Construction work in progress ²	263,459,794	206,005,783
Total electric plant in service and construction work in progress	<u>\$1,155,241,303</u>	<u>\$1,068,368,026</u>

¹Unclassified electric plant in service consists of complete unclassified general plant, generation plant, transmission plant and distribution plant. Depreciation of unclassified electric plant in service has been included in functional plant depreciation accounts in accordance with the anticipated eventual classification of the plant investment. Intangible plant represents Chugach's share of a Bradley Lake transmission line financed internally. Other represents Electric Plant Held for Future Use.

²The amount associated with the construction of SPP included in construction work in progress was \$245.5 million and \$177.4 million at December 31, 2012 and 2011, respectively.

(7) Investments in Associated Organizations

Investments in associated organizations include the following at December 31:

	<u>2012</u>	<u>2011</u>
National Rural Utilities Cooperative Finance Corporation	\$6,095,980	\$6,095,980
CoBank, ACB	4,392,948	4,974,755
NRUCFC capital term certificates / Other	63,755	63,761
Total Investments in Associated Organizations	<u>\$10,552,683</u>	<u>\$11,134,496</u>

The Farm Credit Administration, CoBank's federal regulators, requires minimum capital adequacy standards for all Farm Credit System institutions. Loan agreements and financing arrangements with CoBank and NRUCFC require, as a condition of the extension of credit, that an equity ownership position be established by all borrowers.

(8) Deferred Charges and Credits

Deferred Charges

Deferred charges, or regulatory assets, net of amortization, consisted of the following at December 31:

	<u>2012</u>	<u>2011</u>
Debt issuance and reacquisition costs	\$4,126,529	\$3,432,665
Refurbishment of transmission equipment	141,976	151,235
Feasibility Studies	76,390	351,727
Beluga Gas Compression	2,035,466	2,544,332
Cooper Lake Relicensing / projects	5,800,417	5,930,520
Fuel supply negotiations	815,451	1,118,439
Major overhaul of steam generating unit	1,510,046	2,265,069
Other regulatory deferred charges	4,473,037	2,126,335
Bond interest – market risk management	7,527,357	6,034,443
Environmental matters and other	1,205,574	1,250,925
Total deferred charges	<u>\$27,712,243</u>	<u>\$25,205,690</u>

Deferred charges, or regulatory assets, not currently being recovered in rates charged to consumers, consisted of the following at December 31:

	<u>2012</u>	<u>2011</u>
Fuel supply (negotiations/studies/compression)	\$1,072,002	\$0
Studies/Other	236,401	578,327
Wind project	391,285	144,866
Financing related costs	1,757,624	51,129
Beluga Unit 8 inspection	1,061,838	0
Total deferred charges	<u>\$4,519,150</u>	<u>\$774,322</u>

We believe all regulatory assets not currently being recovered in rates charged to consumers are probable of recovery in the future based upon prior recovery of similar costs allowed by our regulator. The recovery of regulatory assets is requested in SRF or general rate case rate adjustments filed with the RCA. In most cases, deferred charges are recovered over the life of the underlying asset.

Deferred Credits

Deferred credits, or regulatory liabilities, at December 31 consisted of the following:

	<u>2012</u>	<u>2011</u>
Refundable consumer advances for construction	\$777,323	\$727,917
Estimated initial installation costs for meters	92,149	75,660
Post retirement benefit obligation	<u>899,700</u>	<u>899,700</u>
Total deferred credits	<u>\$1,769,172</u>	<u>\$1,703,277</u>

(9) Patronage Capital

Chugach has a Board approved capital credit retirement policy, which is contained in Chugach's Financial Forecast. This establishes, in general, a plan to return the capital credits of wholesale and retail customers based on the members' proportionate contribution to Chugach's assignable margins. At December 31, 2012, Chugach had \$153,832,674 of patronage capital (net of capital credits retired in 2012), which included \$148,307,167 of patronage capital that had been assigned and \$5,525,507 of patronage capital to be assigned to its members. Approval of actual capital credit retirements is at the discretion of Chugach's Board. Chugach records a liability when the retirements are approved by the Board. During 2008, the Board approved the deferral of capital credit retirements after 2009, excluding discounted capital credits, due to the construction of new generation and the anticipated loss of wholesale load in 2014. The Second Amended and Restated Indenture of Trust and the CoBank Amended and Restated Master Loan Agreement prohibit Chugach from making any distribution of patronage capital to Chugach's customers if an event of default under the Second Amended and Restated Indenture of Trust or CoBank Amended and Restated Master Loan Agreement exists. Otherwise, Chugach may make distributions to Chugach's members in each year equal to the lesser of 5 percent of Chugach's patronage capital or 50 percent of assignable margins for the prior fiscal year. This restriction does not apply if, after the distribution, Chugach's aggregate equities and margins as of the end of the immediately preceding fiscal quarter are equal to at least 30 percent of Chugach's total liabilities and equities and margins.

Chugach entered into an agreement with HEA to return all of its patronage capital within five years after expiration of its power sales agreement, which is January 1, 2014. This patronage capital retirement was related to a settlement agreement associated with the 2005 Test Year General Rate Case (Docket U-06-134). The RCA accepted the parties' settlement agreement on August 9, 2007. HEA's patronage capital payable was \$6.9 million and \$6.6 million at December 31, 2012 and 2011, respectively.

Capital credits retired were \$48,079, \$309,188, and \$94,278 for the years ended December 31, 2012, 2011, and 2010, respectively. There was no outstanding liability for capital credits authorized but not paid at December 31, 2012 and 2011, respectively.

(10) Other Equities

A summary of other equities at December 31 follows:

	<u>2012</u>	<u>2011</u>
Nonoperating margins, prior to 1967	\$23,625	\$23,625
Donated capital	1,647,869	1,621,257
Unclaimed capital credit retirement ¹	<u>9,700,861</u>	<u>9,713,810</u>
Total other equities	<u>\$11,372,355</u>	<u>\$11,358,692</u>

¹Represents unclaimed capital credits that have met all requirements of section 34.45.200 of Alaska's unclaimed property law and has therefore reverted to Chugach.

(11) Debt

Long-term obligations at December 31 are as follows:

	<u>2012</u>	<u>2011</u>
CoBank 3 and 4, 2.55% variable rate notes maturing in 2022, with interest payable monthly and principal due annually beginning in 2003	\$31,756,775	\$33,659,141
CoBank 5, 2.55% variable rate note maturing in 2012, with interest and principal payable monthly	0	791,177
2002 Series A Bond of 6.20%, maturing in 2012, with interest payable semi-annually February 1 and August 1	0	120,000,000
2011 Series A Bond of 4.20%, maturing in 2031, with interest payable semi-annually March 15 and September 15 and principal due annually beginning in 2012	85,500,000	90,000,000
2011 Series A Bond of 4.75%, maturing in 2041, with interest payable semi-annually March 15 and September 15 and principal due annually beginning in 2012	178,833,333	185,000,000
2012 Series A Bond of 4.01%, maturing in 2032, with interest payable semi-annually March 15 and September 15 and principal due annually beginning in 2013	75,000,000	0
2012 Series A Bond of 4.41%, maturing in 2042, with interest payable semi-annually March 15 and September 15 and principal due annually between 2013 and 2020 and between 2032 and 2042	125,000,000	0
2012 Series A Bond of 4.78%, maturing in 2042, with interest payable semi-annually March 15 and September 15 and principal due annually beginning in 2023	<u>50,000,000</u>	<u>0</u>
Total long-term obligations	\$546,090,108	\$429,450,318
Less current installments	<u>24,493,022</u>	<u>133,360,210</u>
Long-term obligations, excluding current installments	<u>\$521,597,086</u>	<u>\$296,090,108</u>

Covenants

Effective January 20, 2011, Chugach is required to comply with all covenants set forth in the Second Amended and Restated Indenture of Trust that secured the 2002 Series A Bonds through February 1, 2012, and now secures the 2011 Series A Bonds, the 2012 Series A Bonds and the 2011 promissory note to CoBank, which has replaced the outstanding CoBank 3, 4 and 5 promissory notes.

On January 19, 2011, CoBank and Chugach replaced the CoBank 3, 4 and 5 promissory notes with a promissory note that is governed by the Amended and Restated Master Loan Agreement, which is now secured by the Second Amended and Restated Indenture of Trust dated January 20, 2011.

Chugach is also required to comply with the 2010 Credit Agreement, between Chugach and NRUCFC, KeyBank National Association, Bank of America, N.A., Bank of Montreal, CoBank, ACB and Chang Hwa Commercial Bank, Ltd., Los Angeles Branch dated November 17, 2010, and updated June 29, 2012, governing loans and extensions of credit associated with Chugach's commercial paper program, in an aggregate principal amount not exceeding \$100.0 million at any one time outstanding.

Chugach is also required to comply with other covenants set forth in the Revolving Line of Credit Agreement with NRUCFC.

Security

The Second Amended and Restated Indenture of Trust (the Indenture), which became effective on January 20, 2011, imposes a lien on substantially all of Chugach's assets to secure Chugach's long-term debt obligations. Assets that are generally not subject to the lien of the Indenture include cash (other than cash deposited with the indenture trustee); instruments and securities; patents, trademarks, licenses and other intellectual property; vehicles and other movable equipment; inventory and consumable materials and supplies; office furniture, equipment and supplies; computer equipment and software; office leases; other leasehold interests for an original term of less than five years; contracts (other than power sales agreements with members having an original term exceeding three years, certain contracts specifically identified in the indenture, and other contracts relating to the ownership, operation or maintenance of generation, transmission or distribution facilities); non-assignable permits, licenses and other contract rights; timber and minerals separated from land; electricity, gas, steam, water and other products generated, produced or purchased; other property in which a security interest cannot legally be perfected by the filing of a Uniform Commercial Code financing statement, and certain parcels of real property specifically excepted from the lien of the Indenture. The lien of the Indenture may be subject to various permitted encumbrances that include matters existing on the date of the Indenture or the date on which property is later acquired; reservations in U.S. patents; non-delinquent or contested taxes, assessments and contractors' liens; and various leases, rights-of-way, easements, covenants, conditions, restrictions, reservations, licenses and permits that do not materially impair Chugach's use of the mortgaged property in the conduct of Chugach's business.

Rates

The Second Amended and Restated Indenture of Trust also requires Chugach, subject to any necessary regulatory approval, to establish and collect rates reasonably expected to yield margins for interest equal to at least 1.10 times total interest expense. If there occurs any material change in the circumstances contemplated at the time rates were most recently reviewed, the Second Amended and Restated Indenture of Trust requires Chugach to seek appropriate adjustment to those rates so that they would generate revenues reasonably expected to yield margins for interest equal to at least 1.10 times interest charges, provided, however, upon review of rates based on a material change in circumstances, rates are required to be revised in order to comply and there are less than six calendar months remaining in the current fiscal year, Chugach can revise its rates so as to reasonably expect to meet the covenant for the next succeeding twelve-month period after the date of any such revision.

The CoBank Master Loan Agreement also required Chugach to establish and collect rates reasonably expected to yield margins for interest equal to at least 1.10 times interest expense. The Amended and Restated Master Loan Agreement with CoBank, which became effective on January 19, 2011, did not change this requirement.

The 2010 Credit Agreement governing the unsecured facility providing liquidity for Chugach's Commercial paper program requires Chugach to maintain a minimum margins for interest of at least 1.10 times interest charges for each fiscal year. Margins for interest generally consist of Chugach's assignable margins plus total interest expense.

Distributions to Members

The Second Amended and Restated Indenture of Trust and the CoBank Amended and Restated Master Loan Agreement prohibits Chugach from making any distribution of patronage capital to Chugach's customers if an event of default under the Second Amended and Restated Indenture of Trust or CoBank Amended and Restated Master Loan Agreement exists. Otherwise, Chugach may make distributions to Chugach's members in each year equal to the lesser of 5 percent of Chugach's patronage capital or 50 percent of assignable margins for the prior fiscal year. This restriction does not apply if, after the distribution, Chugach's aggregate equities and margins as of the end of the immediately preceding fiscal quarter are equal to at least 30 percent of Chugach's total liabilities and equities and margins.

Maturities of Long-term Obligations

Long-term obligations at December 31, 2012, mature as follows:

Year ending December 31	2011 Series A Bonds	CoBank Note	2012 Series A Bonds	Total
2013	10,666,667	2,076,355	11,750,000	24,493,022
2014	10,666,667	2,266,145	11,750,000	24,682,812
2015	10,666,667	2,473,110	10,750,000	23,889,777
2016	10,666,667	2,699,313	10,750,000	24,115,980
2017	10,666,667	2,945,954	10,750,000	24,362,621
Thereafter	210,999,998	19,295,898	194,250,000	424,545,896
	<u>\$264,333,333</u>	<u>\$31,756,775</u>	<u>\$250,000,000</u>	<u>\$546,090,108</u>

Lines of credit

Chugach maintains a \$50.0 million line of credit with National Rural Utilities Cooperative Finance Corporation (NRUCFC). Chugach did not utilize this line of credit in 2012, and therefore had no outstanding balance at December 31, 2012. In addition, Chugach did not utilize this line of credit during 2011 and had no outstanding balance at December 31, 2011. The borrowing rate is calculated using the total rate per annum and may be fixed by NRUCFC. At December 31, 2012, and December 31, 2011, the borrowing rate was 2.90 percent and 3.20 percent, respectively.

The NRUCFC Revolving Line Of Credit Agreement requires that Chugach, for each 12-month period, for a period of at least five consecutive days, pay down the entire outstanding principal balance.

On September 26, 2012, the Board approved a resolution to renew this line of credit under substantially the same terms as the previous agreement. The NRUCFC line of credit now expires October 12, 2017.

This line of credit is immediately available for unconditional borrowing.

Commercial Paper

On November 17, 2010, Chugach entered into a \$300.0 million Unsecured Credit Agreement, which is used to back Chugach's Commercial Paper program. The participating banks were NRUCFC, Bank of America, N.A., KeyBank National Association, JPMorgan Chase Bank, N.A., Bank of Montreal, CoBank, ACB, Goldman Sachs Bank USA, Bank of Taiwan, Los Angeles Branch and Chang Hwa Commercial Bank, Ltd., Los Angeles Branch. Effective May 4, 2012, Chugach reduced the commitment amount to \$100.0 million and on June 29, 2012, amended and extended the Credit Agreement to update the pricing and extend the term. The new pricing includes an all-in drawn spread of one month London Interbank Offered Rate (LIBOR) plus 107.5 basis points, along with a 17.5 basis points facility fee (based on an A-/A3 unsecured debt rating). The Amended Unsecured Credit Agreement now expires on November 17, 2016. The participating banks include NRUCFC, KeyBank National Association, Bank of America, N.A., Bank of Montreal, CoBank, ACB and Chang Hwa Commercial Bank, Ltd., Los Angeles Branch. Our commercial paper can be repriced between one day and two hundred seventy days. Chugach is expected to continue to issue commercial paper in 2013, as needed, however, the requirement for short-term borrowing has decreased.

Chugach had \$11.5 million and \$175.0 million of commercial paper outstanding at December 31, 2012 and 2011, respectively.

The following table provides information regarding 2012 monthly average commercial paper balances outstanding (dollars in millions), as well as corresponding weighted average interest rates:

Month	Average Balance	Weighted Average Interest Rate	Month	Average Balance	Weighted Average Interest Rate
January	\$62.7	0.27	July	\$0	0.00
February	\$0	0.00	August	\$0	0.00
March	\$8.0	0.38	September	\$4.2	0.34
April	\$6.3	0.36	October	\$9.3	0.29
May	\$0.8	0.35	November	\$14.5	0.28
June	\$0	0.00	December	\$11.9	0.29

Financing

On January 11, 2012, Chugach issued \$75.0 million of First Mortgage Bonds, 2012 Series A, due March 15, 2032 (Tranche A), \$125.0 million of First Mortgage Bonds, 2012 Series A, due March 15, 2042 (Tranche B) and \$50.0 million of First Mortgage Bonds, 2012 Series A, due March 15, 2042 (Tranche C), for the purpose of repaying outstanding commercial paper used to finance SPP construction and for general corporate purposes. The 2012 Series A Bonds (Tranche A) will mature on March 15, 2032, and will bear interest at 4.01 percent per annum. The 2012 Series A Bonds (Tranche B) will mature on March 15, 2042, and will bear interest at 4.41 percent per annum. The 2012 Series A Bonds (Tranche C) will mature on March 15, 2042, and will bear interest at 4.78 percent per annum. Interest will be paid each March 15 and September 15, commencing on September 15, 2012. The 2012 Series A Bonds (Tranche A) will pay principal in equal installments on an annual basis beginning March 15, 2013, resulting in an average life of approximately 10.7 years. The 2012 Series A Bonds (Tranche B) will pay principal between March 15, 2013 and March 15, 2020 and between March 15, 2032 and March 15, 2042, resulting in an average life of approximately 15.7 years. The 2012 Series A Bonds (Tranche C) will pay principal in equal installments on an annual basis beginning March 15, 2023, resulting in an average life of approximately 20.7 years. The bonds and all other long-term debt obligations are secured by a lien on substantially all of Chugach's assets, pursuant to the Second Amended and Restated Indenture of Trust, which became effective on January 20, 2011.

On January 21, 2011, Chugach issued \$90.0 million of First Mortgage Bonds, 2011 Series A, due March 15, 2031 and \$185.0 million of First Mortgage Bonds, 2011 Series A, due March 15, 2041 for the purpose of refinancing the 2001 and 2002 Series A Bonds due March 15, 2011, and February 1, 2012, respectively, and for general corporate purposes. As anticipated, on February 1, 2012, Chugach retired its 2002 Series A Bonds with proceeds from the 2011 Series A bond issuance. The 2011 Series A Bonds due March 15, 2031, will bear interest at 4.20 percent per annum, payable semi-annually on March 15 and September 15 of each year commencing on September 15, 2011. Principal on the 2011 Series A Bonds due March 15, 2031 will be paid in equal annual installments beginning March 15, 2012, resulting in an average life of approximately 10 years. The 2011 Series A Bonds due March 15, 2041, will bear interest at 4.75 percent per annum, payable semi-annually on March 15 and September 15 of each year commencing on September 15, 2011. Principal on the 2011 Series A Bonds due March 15, 2041 will be paid in equal annual installments beginning March 15, 2012, resulting in an average life of approximately 15.5 years.

Chugach has a term loan facility with CoBank. Loans made under this facility are evidenced by the 2011 CoBank Note, which is governed by the Amended and Restated Master Loan Agreement dated January 19, 2011 and secured by the Second Amended and Restated Indenture.

Fair Value of Debt Instruments

The estimated fair values (in thousands) of the long-term obligations included in the financial statements at December 31 are as follows:

	2012		2011	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Long-term obligations (including current installments)	\$546,090	\$573,912	\$429,450	\$442,711

(12) Employee Benefit Plans

Pension Plans

Pension benefits for substantially all union employees are provided through the Alaska Electrical Pension Trust Fund and the UNITE HERE National Retirement Fund, multi-employer plans. Chugach pays an hourly amount per eligible union employee pursuant to the collective bargaining unit agreements. In these master, multi-employer plans, the accumulated benefits and plan assets are not determined or allocated separately to the individual employer.

Pension benefits for non-union employees are provided by the National Rural Electric Cooperative Association (NRECA) Retirement and Security Plan (RS Plan). The RS Plan is a defined benefit pension plan qualified under Section 401 and tax-exempt under Section 501(a) of the Internal Revenue Code. Under ASC 960, "Topic 960 – Plan Accounting – Defined Benefit Pension Plans," the plan is a multi-employer plan, in which the accumulated benefits and plan assets are not determined or allocated separately to individual employers. Chugach makes annual contributions to the pension plan equal to the amounts accrued for pension expense. Chugach made contributions to all significant pension plans for the years ended December 31, 2012, 2011 and 2010 of \$6.6 million, \$6.0 million and \$6.0 million, respectively. The rate and number of employees in all significant pension plans did not materially change for the years ended December 31, 2012, 2011 and 2010. The following table provides information regarding pension plans which Chugach considers individually significant:

	Alaska Electrical Pension Plan ³			NRECA Retirement Security Plan ³		
	2012	2011	2010	2012	2011	2010
Employer Identification Number		92-6005171			53-0116145	
Plan Number		001			333	
Year-end Date		December 31			December 31	
Expiration Date of CBA's		June 30, 2013			N/A ²	
Subject to Funding Improvement Plan		No			No ⁴	
Surcharge Paid		N/A			N/A ⁴	
Zone Status	Green	Green	Green	N/A ¹	N/A ¹	N/A ¹
Required minimum contributions	None	None	None	N/A	N/A	N/A
Contributions (in millions)	\$3.6	\$3.0	\$2.9	\$3.0	\$3.0	\$3.1
Contributions > 5% of total plan contributions	Yes	Yes	Yes	No	No	No

¹A "zone status" determination is not required, and therefore not determined under the Pension Protection Act (PPA) of 2006. In total, the NRECA RS Plan was between 65 percent and 80 percent funded at January 1, 2012 and 2011, respectively, based on the PPA funding target and PPA actuarial value of assets on those dates.

²The CEO is the only non-union employee subject to an employment agreement, which is effective through July 1, 2013.

³The Alaska Electrical Pension Plan is publically available. The NRECA RS Plan is available on Chugach's website at www.chugachelectric.com.

⁴The provisions of the PPA do not apply to the RS Plan, therefore, funding improvement plans and surcharges are not applicable. Future contribution requirements are determined each year as part of the actuarial valuation of the plan and may change as a result of plan experience.

Health and Welfare Plans

Health and welfare benefits for union employees are provided through the Alaska Electrical Health and Welfare Trust and the Alaska Hotel, Restaurant and Camp Employees Health and Welfare and Pension Trust Fund. Chugach participates in multi-employer plans that provide substantially all union workers with health care and other welfare benefits during their employment with Chugach. Chugach pays a defined amount per union employee pursuant to collective bargaining unit agreements. Amounts charged to benefit costs and contributed to the health and welfare plans for these benefits for the years ending December 31, 2012, 2011, and 2010 were \$4.3 million, \$3.7 million, and \$3.7 million, respectively.

Chugach participates in a multi-employer plan through the Group Benefits Program of NRECA for non-union employees. Amounts charged to benefit cost and contributed to this Plan for those benefits for the years ended December 31, 2012, 2011, and 2010 totaled \$2.5 million, \$2.4 million, and \$2.2 million respectively.

Money Purchase Pension Plan

Chugach participates in a multi-employer defined contribution money purchase pension plan covering some employees who are covered by a collective bargaining agreement. Contributions to the Plan are made based on a percentage of each employee's compensation. Contributions to the money purchase pension plan for the years ending December 31, 2012, 2011, and 2010 were \$141.0 thousand, \$128.7 thousand, and \$124.1 thousand, respectively.

401(k) Plan

Chugach has a defined contribution 401(k) retirement plan which covers substantially all employees who, effective January 1, 2008, can participate immediately. Employees who elect to participate may contribute up to the Internal Revenue Service's maximum of \$17,000, \$16,500, and \$16,500 in 2012, 2011, and 2010 respectively, and allowed catch-up contributions for those over 50 years of age of \$5,500, \$5,500, and \$5,500 in 2012, 2011, and 2010, respectively. Chugach does not make contributions to the plan.

Deferred Compensation

Chugach adopted NRECA's unfunded Deferred Compensation Program (the Program) to allow highly compensated employees who elect to participate in the Program to defer a portion of their current compensation and avoid paying tax on the deferrals until received. The program is a non-qualified plan under Internal Revenue Code 457(b).

Deferred compensation accounts are established for the individual employees, however, they are considered to be owned by Chugach until a distribution is made. The amounts credited to the deferred compensation account, including gains or losses, are retained by Chugach until the entire amount credited to the account has been distributed to the participant or to the participant's beneficiary. The balance of the Program for the years ending December 31, 2012, 2011 and 2010 was \$570,027, \$420,783 and \$395,833, respectively.

Potential Termination Payments

Pursuant to a Chugach Operating Policy, non-represented employees, including the executive officers except the Chief Executive Officer, who are terminated by Chugach for reasons unrelated to employee performance are entitled to severance pay for each year or partial year of service as follows: two weeks for each year of service to a maximum of twenty-six (26) weeks for thirteen (13) years or more of service.

(13) Bradley Lake Hydroelectric Project

Chugach is a participant in the Bradley Lake Hydroelectric Project (Bradley Lake). Bradley Lake was built and financed by the Alaska Energy Authority (AEA) through State of Alaska grants and \$166.0 million of revenue bonds. Chugach and other participating utilities have entered into take-or-pay power sales agreements under which shares of the project capacity have been purchased and the participants have agreed to pay a like percentage of annual costs of the project (including ownership, operation and maintenance costs, debt service costs and amounts required to maintain established reserves). Under these take-or-pay power sales agreements, the participants have agreed to pay all project costs from the date of commercial operation even if no energy is produced. Chugach has a 30.4 percent share, or 27.4 megawatts as currently operated, of the project's capacity. The share of Bradley Lake indebtedness for which we are responsible is approximately \$28.7 million. Upon the default of a Bradley Lake participant, and subject to certain other conditions, AEA is entitled to increase each participant's share of costs pro rata, to the extent necessary to compensate for the failure of another participant to pay its share, provided that no participant's percentage share is increased by more than 25 percent. Upon default, Chugach could be faced with annual expenditures of approximately \$5.1 million as a result of Chugach's Bradley Lake take-or-pay obligations. Management believes that such expenditures, if any, would be recoverable through the fuel recovery process.

On July 1, 2010, AEA issued \$28.8 million of Power Revenue Refunding Bonds, Sixth Series, for purposes of refunding \$30.6 million of the Fifth Series Bonds. The refunded Fifth Series Bonds were called on August 2, 2010. The refunding resulted in aggregate debt service payments over the next eleven years in a total amount approximately \$3.3 million less than the debt service payments which would have been due on the refunded bonds. Refunding the Fifth Series Bonds resulted in an economic gain of approximately \$2.4 million. Chugach's share of these savings will be approximately \$0.7 million, which represents the reduction in debt-service costs recorded as purchased power expense.

The State of Alaska has provided an initial grant for work on a project to divert water from Battle Creek into Bradley Lake. The project is being managed by the Alaska Energy Authority and pending financing, could be completed in 2014. Based on stream flow measurements from 1991 through 1993, diverting a portion of Battle Creek into Bradley Lake has the potential to increase annual energy output up to 40,000 MWh. Chugach would be entitled to 30.4 percent of the additional energy produced.

The following represents information with respect to Bradley Lake at June 30, 2012 (the most recent date for which information is available). Chugach's share of expenses was \$4,223,784 in 2012, \$4,643,641 in 2011, and \$5,120,958 in 2010 and is included in purchased power in the accompanying financial statements.

<u>(In thousands)</u>	<u>Total</u>	<u>Proportionate Share</u>
Plant in service	\$ 181,587	\$ 55,202
Long-term debt	87,607	26,633
Interest expense	5,032	1,530

Chugach's share of a Bradley Lake transmission line financed internally is included in Other Electric Plant.

(14) Eklutna Hydroelectric Project

During October 1997, the ownership of the Eklutna Hydroelectric Project formally transferred from the Alaska Power Administration to the participating utilities. This group, including their corresponding interest in the project, consists of Chugach (30 percent), MEA (16.7 percent) and Anchorage Municipal Light & Power (ML&P) (53.3 percent).

Plant in service in 2012 includes \$4,725,470, net of accumulated depreciation of \$1,671,335, which represents Chugach's share of the Eklutna Hydroelectric Project. In 2011 plant in service included \$4,880,583, net of accumulated depreciation of \$1,491,704. Chugach and ML&P jointly operate the facility. Each participant contributes their proportionate share for operation, maintenance and capital improvement costs to the plant, as well as to the transmission line between Anchorage and the plant. Under net billing arrangements, Chugach then reimburses MEA for their share of the costs. Chugach's share of expenses was \$682,757, \$662,035, and \$664,747 in 2012, 2011, and 2010, respectively and is included in power production and depreciation expense in the accompanying financial statements. ML&P performs major maintenance at the plant. Chugach provides personnel for the daily operation and maintenance of the power plant, who perform daily plant inspections, meter reading, monthly report preparation, and other activities as required.

(15) Commitments and Contingencies

Contingencies

Chugach is a participant in various legal actions, rate disputes, personnel matters and claims both for and against Chugach's interests. Management believes the outcome of any such matters will not materially impact Chugach's financial condition, results of operations or liquidity.

Concentrations

Approximately 70 percent of our employees are members of the International Brotherhood of Electrical Workers (IBEW). Chugach has three Collective Bargaining Unit Agreements (CBA) with the IBEW. We also have an agreement with the Hotel Employees and Restaurant Employees (HERE). All three IBEW CBA's were extended by the Board on February 24, 2010. The contract extensions expire on June 30, 2013. On April 28, 2010, the Board approved a three year extension of the HERE agreement. The contract extension also expires on June 30, 2013. Two of the bargaining units have ratified tentative agreements extending their labor agreements through June 30, 2017. Chugach is currently negotiating with the final IBEW bargaining unit.

Chugach is the principal supplier of power under long-term wholesale power contracts with MEA and HEA. These contracts represented \$100.6 million or 39 percent of sales revenue in 2012, \$104.0 million or 37 percent in 2011, and \$89.1 million or 35 percent in 2010. The HEA contract expires January 1, 2014, and the MEA contract expires December 31, 2014. Non-renewal of these contracts could have a negative impact on the rates charged to other Chugach customers. Notification was made by MEA and HEA that neither organization intends to renew these contracts. MEA advised Chugach that it desired to open discussions regarding power sales possibilities beyond 2014. Chugach proposed a power supply offer to MEA on January 11, 2011, and again on January 31, 2012. Chugach received a response on February 29, 2012, indicating that MEA was following the path its membership most favored and is moving forward with plans to build its own generation plant. All rates are established by the RCA.

Fuel Supply Contracts

Chugach has fuel supply contracts from various producers at market terms. Previous contracts expired at the end of the currently committed volumes in 2010 and 2011. A gas supply contract between Chugach and ConocoPhillips Alaska, Inc. and ConocoPhillips, Inc. (collectively "COP"), was approved by the RCA effective August 21, 2009. The new contract provided gas beginning in 2010 and will terminate December 31, 2016. The total amount of gas under the contract is now estimated to be 60 BCF. The RCA approved a new natural gas supply contract with Marathon Alaska Production, LLC (MAP) effective May 17, 2010. The new MAP contract provided gas beginning April 1, 2011 and will terminate December 31, 2014, which includes two contract extensions that were exercised in 2011. The total amount of gas under contract is now estimated up to 40 billion cubic feet (BCF). These contracts fill 100 percent of Chugach's needs through December 2014, approximately 70 percent of Chugach's needs through December 2015 and approximately 40 percent in 2016. All of the production is expected to come from Cook Inlet, Alaska. In 2012, 89 percent of our power was generated from gas, compared to 92 percent and 89 percent in 2011 and 2010 respectively. Of that gas-fired power, 83 percent was generated at Chugach's Beluga Power Plant in 2012 compared with 79 percent in 2011 and 78 percent in 2010.

The terms of the COP and MAP agreements require Chugach to handle the natural gas transportation over the connecting pipeline systems. Effective October 1, 2012, Chugach and Hilcorp Alaska, LLC (Hilcorp) entered into a gas exchange agreement to exchange gas between the east and west side of Cook Inlet. This agreement terminates on September 30, 2013. We have gas transportation agreements with ENSTAR Natural Gas Company (ENSTAR) and Marathon Oil Company. The following represents the cost of fuel purchased and or transported from these vendors as a percentage of total fuel costs for the years ended December 31:

	2012	2011	2010
Marathon Oil Company	72.0%	44.9%	24.1%
Chevron/UNOCAL/Hilcorp	1.3%	16.1%	26.4%
ML&P	0.0%	3.6%	14.2%
ConocoPhillips (COP)	24.2%	31.9%	35.1%
ENSTAR	2.2%	1.3%	0.2%
Miscellaneous	0.3%	2.2%	0.0%

Patronage Capital Payable

In 2007, Chugach entered into an agreement with HEA to return all of its patronage capital within five years after expiration of its power sales agreement, which was related to a settlement agreement associated with the 2005 Test Year General Rate Case (Docket U-06-134). The agreement was contingent on the RCA accepting the parties' settlement agreement in Docket U-06-134, which occurred on August 9, 2007. HEA's patronage capital should have been classified as a liability at that time. HEA's patronage capital was \$6.5 million at December 31, 2010. As the amount of the patronage capital was not material for any period, Chugach recorded an adjustment in the first quarter of 2011 to reclassify the amount of \$6.5 million from patronage capital to patronage capital payable and is included in the retirement of capital credits on our Statements of Changes in Equities and Margins. HEA's patronage capital was \$6.9 million at December 31, 2012 and \$6.6 million at December 31, 2011, and is classified as patronage capital payable on our Balance Sheet.

Regulatory Cost Charge

In 1992, the State of Alaska Legislature passed legislation authorizing the Department of Revenue to collect a Regulatory Cost Charge from utilities to fund the governing regulatory commission, which is currently the RCA. The tax is assessed on all retail consumers and is based on kilowatt-hour (kWh) consumption. The tax is collected monthly and remitted to the State of Alaska quarterly. The Regulatory Cost Charge has changed since its inception (November 1992) from an initial rate of \$0.000626 per kWh to the current rate of \$0.000568, effective July 1, 2012. The tax is reported on a net basis and the tax is not included in revenue or expense.

Sales Tax

Chugach collects sales tax on retail electricity sold to Kenai and Whittier consumers. The tax is collected monthly and remitted to the Kenai Peninsula Borough quarterly. Sales tax is reported on a net basis and the tax is not included in revenue or expense.

Gross Receipts Tax

Chugach pays to the State of Alaska a gross receipts tax in lieu of state and local ad valorem, income and excise taxes on electricity sold in the retail market. The tax is accrued monthly and remitted annually. The tax is reported on a net basis and the tax is not included in revenue.

Production taxes

Production taxes on Chugach fuel purchases are paid directly to our gas producers and are recorded under "Fuel" in Chugach's financial statements.

Underground Compliance Charge

In 2005 the Anchorage Municipal Assembly adopted an ordinance to require utilities to convert overhead distribution lines to underground. To comply with the ordinance, Chugach must invest 2 percent of gross retail revenue in the Municipality of Anchorage annually in moving existing distribution overhead lines underground. Consistent with State of Alaska undergrounding requirement, Chugach is permitted to amend its rates by adding a 2 percent charge to its retail members' bills to recover the actual costs of the program. The rate amendments are not subject to RCA review or approval. Chugach's liability was \$3,786,031 and \$2,611,110 for this charge at December 31, 2012 and 2011, respectively and will use the funds to offset the costs of the projects.

Environmental Matters

The Clean Air Act and Environmental Protection Agency (EPA) regulations under the Clean Air Act establish ambient air quality standards and limit the emission of many air pollutants.

New Clean Air Act regulations impacting electric utilities may result from future events or new regulatory programs. On October 30, 2009, the EPA published new federal regulations requiring the mandatory reporting of greenhouse gases from all sectors of the economy. Chugach is subject to this new regulation, which is not expected to have a material effect on our results of operations, financial position, and cash flows. While we cannot predict whether any additional new regulation would occur or its limitation, it is possible that new laws or regulations could increase our capital and operating costs. We have obtained or applied for all Clean Air Act permits currently required for the operation of our generating facilities.

SPP was required by its Air Quality Permit to collect ambient air background data. Data collection began on September 1, 2011 and continued through August 31, 2012. On December 19, 2012, the Alaska Department of Environmental Conservation (ADEC) determined that the ambient pollutant data at SPP meets the requirements of the Prevention of Significant Deterioration (PSD) program set forth by the EPA. This action completed the data collection requirement.

Chugach is subject to numerous other environmental statutes including the Clean Water Act, the Resource Conservation and Recovery Act, the Toxic Substances Control Act, the Endangered Species Act, and the Comprehensive Environmental Response, Compensation and Liability Act and to the regulations implementing these statutes. We do not believe that compliance with these statutes and regulations to date has had a material impact on our financial condition or results of operation. However, new laws or regulations, implementation of final regulations or changes in or new interpretations of these laws or regulations could result in significant additional capital or operating expenses.

Generation Commitments

Chugach is in the process of developing a natural gas-fired generation plant on land owned by Chugach near its Anchorage headquarters. SPP was developed and owned by Chugach and ML&P as tenants in common. Chugach will own and take approximately 70 percent of the new plant's output and ML&P will own and take the remaining output. Chugach will proportionately account for its ownership in SPP. Chugach executed a gas turbine purchase agreement for the purchase of three gas turbines and a spare engine for maintenance purposes with GE Packaged Power, Inc. (GEPP). Chugach has also executed an owner's engineer services contract, a steam turbine generator (STG) purchase agreement, an engineering, procurement, and construction (EPC) contract, a once through steam generator (OTSG) equipment and transportation contracts for transportation of all purchased equipment. All equipment, including the spare engine, has been received. Chugach received an air quality permit from the Alaska Department of Environmental Conservation in 2010, allowing the project to begin construction in the spring of 2011 as planned. On March 15, 2011, the initial building permit was received from the Municipality of Anchorage. Chugach made payments of \$85.7 million in 2012 and \$130.5 million in 2011 pursuant to its contracts associated with SPP. Additional payments of \$13.0 million have been paid or are expected to be paid in 2013. Commercialization of the project occurred on February 1, 2013.

Economy Energy Sales

On October 5, 2012, Chugach and GVEA finalized arrangements for Chugach to provide economy energy to GVEA until March of 2015. Sales will be made under the terms and conditions of Chugach's economy energy sales tariff. The price to GVEA will include the cost of fuel, variable operations and maintenance expense and a margin. Chugach has also entered into gas supply arrangements for GVEA economy energy sales.

Cooper Lake Hydroelectric Project

The Cooper Lake Hydroelectric Project received a 50-year license from FERC in August of 2007. A condition of that license is a requirement to construct a Stetson Creek diversion structure, a pipeline to Cooper Lake, and a bypass structure to release warmer water from Cooper Lake into Cooper Creek. If the project is not feasible or if the cost estimate materially exceeds the terms of the license, Chugach has the option to request a license amendment. At the time the project was being relicensed the estimated cost to complete the project was \$12.0 million. The current estimate to complete the project is now \$21.9 million. As an alternative to requesting a license amendment from FERC, Chugach requested grants from the State of Alaska. Funding for this project includes \$0.6 million in grants received, \$5.8 million in grants authorized and \$3.5 million in grants requested. The Chugach Board authorized expenditures for the project November 15, 2012. The diversion project will be constructed in 2013 and 2014, and will operate through the duration of the license.

(16) Quarterly Results of Operations (unaudited)

	<u>2012 Quarter Ended</u>			
	<u>Dec. 31</u>	<u>Sept. 30</u>	<u>June 30</u>	<u>March 31</u>
Operating Revenue	\$74,483,455	\$62,675,511	\$58,631,729	\$71,180,773
Operating Expense	68,250,215	60,200,529	55,725,151	64,019,060
Net Interest	<u>3,492,044</u>	<u>3,495,865</u>	<u>3,542,676</u>	<u>3,872,346</u>
Net Operating Margins	2,741,196	(1,020,883)	(636,098)	3,289,367
Nonoperating Margins	<u>632,775</u>	<u>261,487</u>	<u>123,962</u>	<u>133,701</u>
Assignable Margins	<u>\$3,373,971</u>	<u>\$ (759,396)</u>	<u>\$(512,136)</u>	<u>\$3,423,068</u>
	<u>2011 Quarter Ended</u>			
	<u>Dec. 31</u>	<u>Sept. 30</u>	<u>June 30</u>	<u>March 31</u>
Operating Revenue	\$76,828,268	\$68,778,352	\$68,517,526	\$69,494,223
Operating Expense	70,143,069	65,509,750	65,592,311	61,096,736
Net Interest	<u>4,102,750</u>	<u>3,544,204</u>	<u>4,209,482</u>	<u>4,890,541</u>
Net Operating Margins	2,582,449	(275,602)	(1,284,267)	3,506,946
Nonoperating Margins	<u>628,697</u>	<u>161,595</u>	<u>120,363</u>	<u>133,081</u>
Assignable Margins	<u>\$ 3,211,146</u>	<u>\$ (114,007)</u>	<u>\$(1,163,904)</u>	<u>\$3,640,027</u>

Power Supply is responsible for operating and maintaining Chugach's power plants, its power control center, environmental compliance, Supervisory Control and Data Acquisition (SCADA) system and communications infrastructure.

Construction continued on the Southcentral Power Project throughout 2012. SPP is a joint project between Chugach (70 percent) and Municipal Light & Power (30 percent). Chugach managed the project on behalf of the utility owners, with contractor SNC Lavalin Constructors hired to build the facility. In 2012 the plant's three gas turbines, steam turbine, three boilers and four generators were all delivered, installed and tested. Commissioning and air emissions testing took place in the latter half of the year. As with all large projects, numerous activities took place to keep the project on schedule. Key permits were secured. The air emissions permit required the collection of 12 months of ambient air data, which was completed. Health, safety and environmental procedures were created. Connections were made for water, sewer, natural gas, telecommunications and electric services. The staff that operates and maintains the plant was assembled and trained. On behalf of the utility owners, Chugach assumed control of SPP at 11:59 p.m. on Jan. 31, 2013.

At the Beluga Power Plant, (long the mainstay of Chugach's generation portfolio) after 84,000 fired-hours the burners of Unit 6 were replaced for the first time since an upgrade in 2000. A major overhaul was completed on Unit 7, which resulted in the replacement of a number of parts. Unit 8 underwent a 25,000-hour inspection and rotor maintenance.

Other work was underway at Chugach's

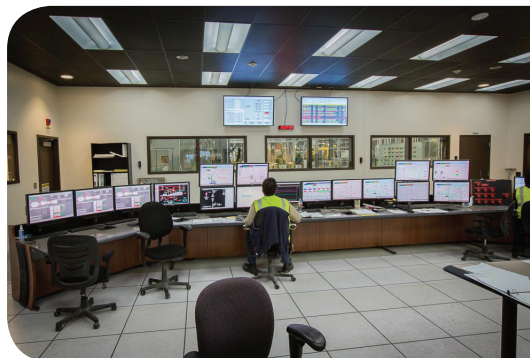
Cooper Lake Hydroelectric Project. Planning continued for the diversion of cold water from Stetson Creek into the Cooper reservoir, with the subsequent release of warmer lake water into the Cooper Creek drainage, potentially enhancing fish habitat. The construction of facilities for the diversion and release were agreed to in the process of securing a new 50-year operating license for the project from the Federal Energy Regulatory Commission in 2007. In 2012 key permits were approved, 100 percent of engineering design was completed, confirmation that no significant dam safety issues associated with the project was verified by FERC and a construction contract was awarded. Construction of the diversion and release structures will take place in 2013 and 2014.

Chugach is part-owner and the operator of the Eklutna Hydroelectric Project on behalf of joint owners ML&P and Matanuska Electric Association. During 2012 the project met its compliance requirements for a continued certificate of operations from the Alaska Department of Natural Resources.

The Bernice Lake Power Plant was sold by Chugach to Homer Electric Association in late 2011. Closeout

items related to the sale were completed in early 2012.

The Power Control Center dealt with major snow and ice storms early in the year, and severe windstorms in September. It also successfully integrated the Southcentral Power Project into the generation mix during testing and commissioning in the latter part of the year. Power Control also met the requirement to integrate a new variable resource after Chugach began buying power from the Fire Island wind project in August. Power Control played a role in the changing relationship with long-time wholesale customer Homer Electric Association by providing integration support to HEA controls upgrades at the Bernice Lake, Nikiski and Bradley Lake generation projects.



Top: Microwave communications were installed at the Southcentral Power Project in 2012.

Middle: SPP's many controls and systems were tested during the plant's commissioning.

Bottom right: The rotor was inspected as part of a major overhaul of Beluga Unit No. 7.

Bottom left: Operators in the SPP control room can monitor systems throughout the new power plant.



Top: The International Transmission Substation ties the new Southcentral Power Project to the grid.

Bottom left: New underground feeders at the DeBarr Substation were installed as one of Chugach's overhead-to-underground conversion projects in 2012.

Middle: During winter storms early in the year, heavy ice formed on transmission and distribution lines in the mountains of the northern Kenai Peninsula.

Bottom right: As part of a project to add a second feeder to serve Girdwood customers, Chugach used a state grant to install an underground feeder tie along Arlberg Road.



Power Delivery is responsible for delivering safe and reliable power from the generators to Chugach's members through its Engineering, Substation & Line Operations functions.

Winter storms in the mountains of the northern Kenai Peninsula caused a buildup of heavy ice and snow that brought down both transmission and distribution lines. Customers in Hope and Sunrise were out of power for extended periods due to outages on the 17-mile radial distribution line that serves them. Multiple spans of the 115-kilovolt transmission sagged to the ground due to a foot or more of icing. The weight of ice brought down a 3,000-foot stretch of conductor at the crossing of Canyon Creek. Until repaired, utilities north of the Kenai Peninsula were unable to get their Bradley Lake hydropower.

Underground cable projects continued to be a priority during 2012. In the course of the year, Chugach did all or part of three overhead-to-underground conversion projects, nine cable-replacement projects and nineteen cable-injection projects. Approximately 46 percent of the 1,688 miles of distribution line on Chugach's system is underground. Underground cable maintenance is an increasingly costly function for Chugach.

Chugach maintained an active vegetation management program in 2012, re-clearing 32.4 miles of transmission and 171 miles of distribution lines. The cooperative uses a 8-year clearing cycle for transmission and 3-year cycle for distribution easements and rights of way. Chugach also cut 7,641 danger trees in 2012. Chugach strives to clear rather than trim its permitted areas.

Throughout September repeated storms battered the Chugach system and neighboring utilities with 100-mph winds and periods of sustained heavy rain. A windstorm that hit the evening of Sept. 4 caused the most widespread damage and prolonged outages. Thousands of trees fell into power lines across the Chugach service area. Most of the problems were caused by heavy, large cottonwood trees caught in full leaf

with their roots in soil softened by summer rains. About 32,000 Chugach customers lost power at the height of the storm. While most were back on the next day, it took up to 5 days to restore service to all customers. Even though two other storms that followed in September also packed winds over 100 mph, they didn't cause as many outages, in

part because the first storm felled and stripped the leaves from so many vulnerable trees.

Power Delivery managed a number of significant construction activities in 2012. The largest was the construction of the new International Transmission Substation adjacent to the Southcentral Power Project. The \$20 million project (Chugach's share was \$15 million) to connect the new power plant to the grid was completed in the summer, ahead of schedule and under budget. In the latter half of the year Chugach completed a package of projects in Girdwood, including a second feeder and feeder tie that will make power more reliable for members in that community.

The Finance division is responsible for Chugach's Accounting, Finance, Regulatory Affairs and Pricing departments and risk management functions.

In 2012 Chugach used its commercial paper program to provide short-term financing for construction of the Southcentral Power Project (SPP) and for general corporate purposes. With the completion of SPP, short-term borrowing needs were greatly reduced. Thus, Chugach reduced the commitment amount to \$100 million from \$300 million and amended the Credit Agreement to improve the pricing and extend the term to Nov. 17, 2016.

Completion of SPP also allowed for the short-term financing to construct the project to be converted to long-term debt. This occurred in late 2012 with the closing of a \$250 million privately placed bond issue. The bonds carry a weighted average interest rate of 4.36 percent and will be amortized over the expected life of SPP.

Completion of SPP required rate adjustments to recover its costs equitably over the expected life of the plant. Thus, Chugach proposed and received RCA approval for depreciation rates for SPP and new transmission plant specific to the project. Chugach continued the cost recovery process for SPP by submitting a general rate case based on a June 2012 test year. The RCA approved interim rates effective with the commercial operation of SPP.

In addition to base rate adjustments for SPP, the filing included extensive tariff modifications in support of rates, rules and conditions of service for transmission wheeling and related ancillary services in preparation for the expira-



Top left: In addition to filing to amend its retail service territory to include Fire Island, Chugach also received recognition for renewable credits for energy provided by the island's wind farm.

Bottom left: A tariff proposal filed with the Regulatory Commission of Alaska proposed rates and rules for transmission wheeling.

Right: Chugach used \$250M in new financing to finance most of its share of the Southcentral Power Project.

tion of the wholesale power contracts with Matanuska Electric Association and Homer Electric Association. The filing also included the assessment of wheeling charges on economy energy sales that originate from the Chugach system.

Other significant regulatory events in 2012 included approval by the RCA for Chugach to:

- Amend its Certificate of Public Convenience and Necessity to include Fire Island, the City of Whittier and areas in and around the Shotgun Cove area of Prince William Sound, and to adjust the service area boundary between Chugach and the City of Seward (doing business as Seward Electric System) in the Moose Pass area where both utilities are currently authorized to provide electric service.
- Recover through rates costs for energy purchases from the Fire

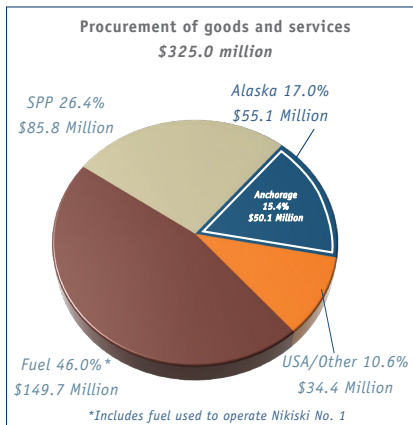
Island wind project and costs incurred at Cook Inlet Natural Gas Storage Alaska, a gas storage facility that went into service in 2012.

- Amend its tariff to allow Interactive Voice Response technology for customer notification of a pending electric service disconnection of a delinquent account. An automated phone contact is much less expensive and more efficient than the previously required in-person contact by phone or on-site visit to a customer's premise.

Finally, Chugach secured North American Renewables Registry approval of the Fire Island wind generators as a renewable energy generation resource. This allows for the creation, tracking and sale of renewable energy certificates.

Administration is responsible for Chugach's Administrative Services (procurement, facilities and security), Information Services, Member Services and energy efficiency and conservation departments and functions.

Administrative Services procurement of goods and services for 2012 totaled \$325 million. Of that, \$149.7 million or 46 percent of the total expenditure was for fuel to produce power and \$85.8 million or 26 percent was for SPP construction. Of the remaining \$89.6 million, Chugach spent \$55.1 million in Alaska, with \$50.1 million of that being spent within the local Anchorage economy. Goods and services included materials and supplies for routine and major operations and maintenance, capital projects, utilities and professional services.



Administrative Services also completed a variety of facilities projects which included roof replacements, heating, ventilating and air conditioning (HVAC) boiler replacements with high-efficiency (98 percent) boilers, remodels of 25-year-old common areas, an overhaul of the main HVAC intake fan and the beginning of a 3-year painting project for the headquarters building.

Member Services, Information Services and Finance implemented a new customer information system, CIS Infinity, replacing one that was installed in 1995. The new system is much more flexible and will provide a more efficient and productive information system for its users. It uses a common enterprise database (Oracle) that has been integrated with Chugach's Operation Work Management, Geographic Information System and on-line outage reporting.

Member Services continued its outreach program with energy efficiency presentations in Anchorage schools, publications, and participation in events such as the "Sustainable Spenard" Farmer's

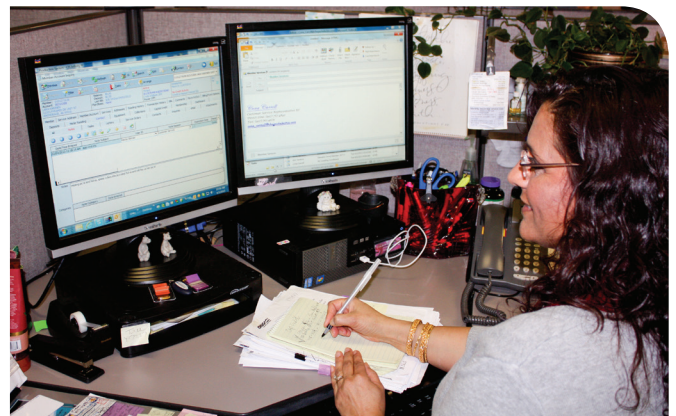
Market and the Renewable Energy Alaska Project's renewable energy fair. Outreach will be enhanced further with a \$142,600 grant secured from the Alaska Energy Authority for a web-based social media energy efficiency tool to provide Chugach members more information on usage and opportunities for saving energy.

Information Services continued to support the technical needs of a wide variety of systems and applications that enable efficient performance of Chugach's business processes. Major accomplishments during 2012 included upgrading the HR/Payroll system, implementation of a new asset management system, upgrading desktops company-wide to Office 2010 and the Window 7 operating system, replacement of the unbilled revenue model, company-wide training on the Microsoft Office software suite, and deployment of enterprise wide reporting software.

Left: Chugach provided information on LED lighting technology, products and savings at venues like the Spenard Farmers Market.

Middle: Chugach's Information Services department is responsible for the installation and maintenance of software and data systems across the company.

Right: In June, Member Services went live with a new customer information system that provides service representatives more information and enhanced reporting capabilities.

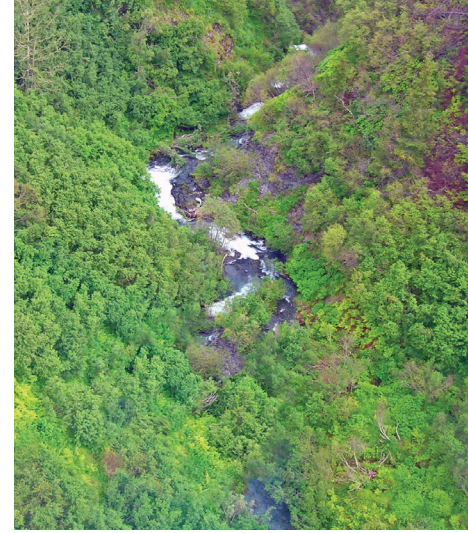
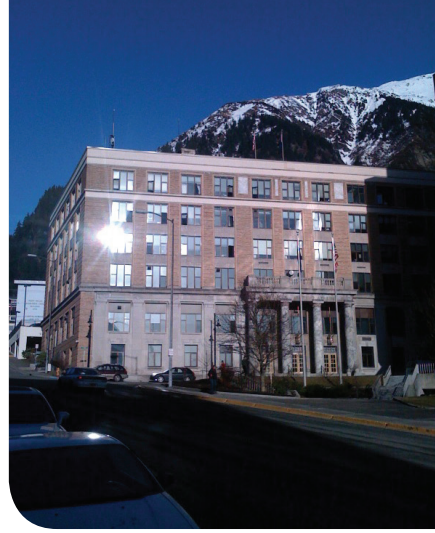


Strategic Planning & Corporate Affairs is responsible for long-term planning, fuel supply, new business development, corporate business analysis and Government Relations & Corporate Communications.

The supply and deliverability of natural gas to fuel Chugach's power plants is a critical issue due to the rapidly diminishing production of gas from the Cook Inlet. To enhance its fuel supply security, Chugach contracted for additional gas, reserved capacity in the gas storage facility developed by Cook Inlet Natural Gas Storage Alaska and took the lead in securing \$4 million of State grant funding to help pay for a gas infrastructure project that enables the delivery of gas to the west-side of Cook Inlet where Chugach's Beluga Power plant is located. Chugach has partnered with other South-central Alaska utilities to investigate options to import liquefied natural gas or compressed natural gas to remedy the expected gas supply shortfalls.

The addition of new renewable energy to the Chugach system continues to be a priority, and became a reality, with the first deliveries of wind energy from the Fire Island wind project in 2012. Chugach spent considerable effort to develop solutions to integrate and regulate this intermittent energy resource.

Chugach also continued to advance the development of other renewable energy projects including the Susitna-Watana Hydroelectric Project, a diversion of Battle Creek to put more water into Bradley Lake to increase hydroelectric production, and a project to divert Stetson Creek to increase the energy produced by Chugach's Cooper



Lake Hydroelectric Project.

Chugach has been very successful in acquiring funding to support renewable energy projects. Chugach used a \$576,080 state grant to help fund the design and permitting of Stetson Creek and secured a \$5,825,000 grant in 2012 to apply toward construction. Prospective grant applications, which have been recommended for funding in the 2014 state capital budget by the Alaska Energy Authority, included \$3.4 million for Stetson Creek construction and \$40,000 for a fuel characterization study, a first step towards a feasibility study of a waste-to-energy project.

Wholesale power sales contracts with Homer Electric Association and Matanuska Electric Association end on Jan. 1, 2014 and Dec. 31, 2014, respectively. Chugach will continue to work with these and other Railbelt electric utilities to meet their needs for generation and transmission services. Along these lines, Chugach executed a power sales agreement to sell economy energy to Golden Valley Electric Association for a two-year period beginning April 1, 2013.

The legislative session that ended in April 2012 produced good results for Chugach and electric customers across the state. The capital budget contained more than \$7.4 million in grants for several Chugach projects. The legisla-



Top left: Chugach and other utilities closely followed events in the state Capitol where legislators and the governor addressed a variety of energy issues during the 2012 session. Top Right: As a condition of its new 50-year license for the Cooper Lake Hydroelectric Project, Chugach will build the structures necessary to divert the cold waters of Stetson Creek into the reservoir and release warmer lake water into the Cooper Creek drainage to enhance salmon habitat.

Bottom: During a cold snap in December, Chugach drew on its reserves at the Cook Inlet Gas Storage Alaska to meet its daily requirements for natural gas.

ture extended the Renewable Energy Grant Fund for another 10 years, expressing legislative intent that it be funded at \$50 million a year. Legislators also approved creation of a new loan fund for energy projects and appropriated funds to continue popular home energy rebate and weatherization programs run by the Alaska Housing Finance Corporation.

Chugach uses various generation resources to ensure reliable, affordable power. At the end of December 2012, Chugach had 462.6 megawatts of installed capacity at Chugach-owned facilities (not counting SPP). The unit ratings shown are taken at 30 degrees Fahrenheit. Chugach also takes power from the state-owned Bradley Lake Hydroelectric Project near Homer, from Homer Electric Association's gas-fired units at Nikiski and Bernice Lake and from the Fire Island wind project. In 2012, 89 percent of the kilowatt-hours Chugach sold came from natural gas units, 10 percent from hydroelectric resources and 1 percent from wind.



Beluga

Located on the west side of Cook Inlet near Tyonek; Unit Nos. 1-3 and 5-7 are fueled by natural gas; Unit 8 is a steam turbine.

Units	Commissioned	Power Rating (megawatts)
No. 1	1968	19.6
No. 2	1968	19.6
No. 3	1973	64.8
No. 5	1975	68.7
No. 6	1976	79.2
No. 7	1978	80.1
No. 8	1981	53.0
TOTAL		385.0



Cooper Lake

Located near Cooper Landing on the Kenai Peninsula; units are hydro turbines.

Units	Commissioned	Power Rating (megawatts)
No. 1	1960	9.6
No. 2	1960	9.6
TOTAL		19.2



Eklutna

Located along the Knik River and jointly owned with Municipal Light & Power and Matanuska Electric Association. Chugach's share is 30 percent, up to an 11.7-megawatt maximum. Units are hydro turbines.

Units	Commissioned	Power Rating (megawatts)
No. 1	1955	23.5
No. 2	1955	23.5
TOTAL		47.0



International

Located off International Airport Road in Anchorage; units are natural gas combustion turbines.

Units	Commissioned	Power Rating (megawatts)
No. 1	1964	14.1
No. 2	1965	14.1
No. 3	1969	18.5
TOTAL		46.7



SPP

Located off International Airport Road in Anchorage; Units 11-13 are natural gas combustion turbines and Unit 10 is a steam turbine.

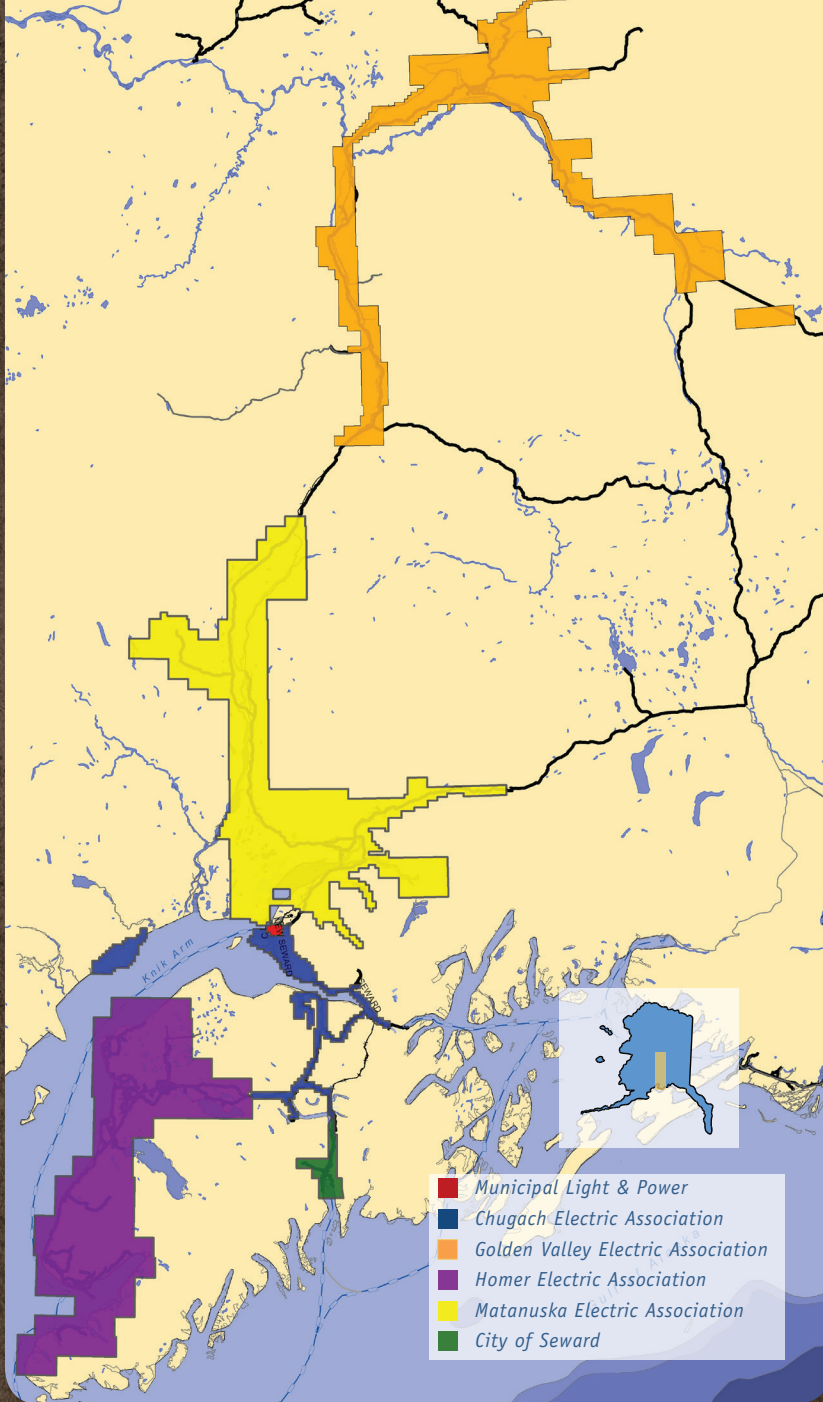
Units	Commissioned	Power Rating (megawatts)
No. 10	2013	57.4
No. 11	2013	47.6
No. 12	2013	47.6
No. 13	2013	47.6
TOTAL		200.2

The Railbelt

Chugach power flows to nearly three-fourths of Alaska's population. Chugach serves 82,004 retail service locations in an area extending from Anchorage to the northern Kenai Peninsula, and from Whittier on Prince William Sound to Tyonek on the west side of Cook Inlet including Fire Island. Chugach provides power for Alaskans from Homer to Fairbanks through wholesale and economy energy sales to Homer Electric Association, the City of Seward, Matanuska Electric Association and Golden Valley Electric Association. On occasion, Chugach sells to, or buys energy from, Municipal Light & Power.

In 2012, Chugach had 462.6 megawatts of installed generation capacity at four power plants. Chugach operates 2,227 miles of energized line. Chugach has 539 miles of transmission line, including 128 miles of leased transmission lines and Chugach's share of the jointly-owned Eklutna transmission line. Chugach has 912 miles of overhead distribution line and 776 miles of underground distribution line.

Chugach set its 2012 system peak load on Dec. 17, when demand hit 475 megawatts in the hour ending at 7 p.m. The temperature at the time at Chugach headquarters was minus 1 degree Fahrenheit. Power sales for the year totaled 2.6 billion kilowatt-hours.



CHUGACH
POWERING ALASKA'S FUTURE

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