ALASKA AEROSPACE CORPORATION

Financial Statements

June 30, 2010

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ALASKA AEROSPACE CORPORATION

Table of Contents

	Page
Independent Auditor's Report	1-2
Management's Discussion and Analysis	4-7
Financial Statements	
Statement of Net Assets	9
Statement of Revenues, Expenses, and Changes in Net Assets	10
Statement of Cash Flows	11
Notes to Financial Statements	12-23

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Mikunda, Cottrell & Co., Inc.
Certified Public Accountants & Consultants

RSM McGladrey Network
An Independently Owned Member

Offices in Anchorage & Kenai

Independent Auditor's Report

Board of Directors
Alaska Aerospace Corporation
Anchorage, Alaska

We have audited the accompanying basic financial statements of Alaska Aerospace Corporation (AAC), a component unit of the State of Alaska, as of and for the year ended June 30, 2010. These financial statements are the responsibility of AAC's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes 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 the significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of AAC as of June 30, 2010, and the respective changes in the financial position and cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards,* we have also issued our report dated October 21, 2010 on our consideration of AAC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

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Board of Directors
Alaska Aerospace Corporation
Anchorage, Alaska

The Management's Discussion and Analysis on pages 4 through 7 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Mikunda, Cottrell & Co.

Anchorage, Alaska
October 21, 2010

MANAGEMENT'S DISCUSSION AND ANALYSIS

ALASKA AEROSPACE CORPORATION

Management's Discussion and Analysis

June 30, 2010

Our discussion and analysis of Alaska Aerospace Corporation's (AAC) financial performance provides an overview of AAC's financial activities for the fiscal year ended June 30, 2010. Please read it in conjunction with AAC's financial statements starting on page 7.

USING THIS FINANCIAL REPORT

This report consists of a series of financial statements. The Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets on pages 7 and 8, provide information about the activities of AAC and present an overview of AAC's finances. Total net assets increased from $91.5 million to $93.6 million. The analysis below focuses on the net assets of AAC's business-type activities.

Table 1
Statement of Net Assets

	Current Year	Prior Year	Change	Percent Change
Assets:				
Current assets	$ 13,350,812	19,558,480	(6,207,668)	(32%)
Capital assets, net	88,222,930	83,594,920	4,628,010	6%
Total assets	101,573,742	103,153,400	1,579,658	(2%)
Liabilities:				
Current liabilities	2,725,376	2,078,430	646,946	31%
Noncurrent liabilities	5,731,271	9,575,019	(3,843,748)	(40%)
Total liabilities	8,456,647	11,653,449	(3,196,802)	(27%)
Net assets:				
Invested in capital assets	88,222,930	83,594,920	4,628,010	6%
Unrestricted	4,894,165	7,905,031	(3,010,866)	(38%)
Total net assets	$ 93,117,095	91,499,951	1,677,144	2%

During FY2010, AAC received a $3.5 million capital appropriation for the construction of a rocket motor storage facility at Kodiak Launch Complex, to be completed in summer 2010, which was used, along with the prior year's appropriation of $3.5 million to fund this project which decreased the unrestricted portion of net assets. The increase in the invested in capital assets is a direct result of aforementioned construction project at Kodiak Launch Complex (KLC).

Business-type Activities
AAC's operating revenues are generated through launch support contracts with the Missile Defense Agency (MDA) and U.S. Air Force. In August of 2010, MDA opted to not exercise its sustainment option beyond the current contractual agreement (ending August 31, 2010).

Depreciation, amortization of the fiber optic IRU agreement, and repairs and maintenance of the launch complex continue to be a significant operating expense. Table 2 below focuses on the changes in net assets of AAC's business-type activities.

Table 2 - Changes in Net Assets

	Current Year	Prior Year	Change	Percent Change
Operating revenues	$ 11,336,598	18,620,231	(7,283,633)	(39%)
Operating expenses	17,320,663	23,587,123	(6,266,460)	(27%)
Net operating loss	(5,984,065)	(4,966,892)	(1,017,173)	20%
Non-operating revenues	149,601	1,054,865	(905,264)	(86%)
Loss before capital contributions	5,834,464	(3,912,027)	(1,922,437)	49%
State of Alaska capital appropriation	3,500,000	3,500,000	-	0%
Capital contributions	3,951,608	1,946,107	2,005,501	103%
Changes in net assets	1,617,144	1,534,080	83,064	5%
Net assets – beginning of the year	91,499,951	89,965,871	1,534,080	2%
Net assets – end of the year	$ 93,117,095	91,499,951	2,057,152	1%

- Decrease in operating activity resulted from two scheduled Air Force launches being rescheduled into FY2011. Management anticipates operating revenue for 2011 will be comparable to FY10 with the two Air Force launches moving into FY11. AAC is requesting sustainment funding through the State of Alaska.

- Operating expenses decreased in-line with operating revenues. It is anticipated expenses to support operating activity will increase in 2011, as the facility continues to mature and new assets come into service.

- Depreciation and amortization expense in fiscal year 2010 increased due to KLC capital project additions. Management expects the depreciation expense to increase in future years with the completion of current capital projects and as technology advances are updated and implemented.

- Personal service expenses remained comparable to FY2009. The Alaska Legislature provided funding relief to all PERS participating employers and agencies, off-setting the increased PERS employer costs. The PERS relief funding is reported as non-operating revenue for each year respectively.

- AAC has not received any general funds from the State of Alaska since 2002 with operations being funded through launch services contracts. During 2010, AAC received a capital contribution from the State of Alaska for construction of a rocket motor storage facility located at Kodiak Launch Complex which is anticipated to be completed during the summer of 2010. In view of MDA not exercising the sustainment option of its contract with AAC, AAC has requested sustainment funding through the State of Alaska.

AAC's Budgetary Highlights

The State of Alaska approves AAC's budget annually. Accordingly, neither the Board of Directors nor management has the authority to modify the budget. Historically, the budget includes provisions granting AAC "receive and expend authority" authorizing AAC to contemporaneously receive funding from launch customers and expend funds as necessary to provide support services.

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

At June 30, 2010, AAC had $88.2 million invested in various capital assets both in Kodiak and Anchorage that support its mission to foster the aerospace industry. This amount, net of accumulated depreciation/amortization, represents an increase in net capital asset value of $4.6 million, or 5.5%, from fiscal year 2009.

The overall change in capital assets includes net capital asset additions of $10.6 million and depreciation expense of just over $6.0 million. Construction in progress is related to design for a third launch pad, rocket motor storage facility design and other facility improvements.

Debt Administration

AAC has no long-term liabilities that require debt administration. AAC has the authority to issue bonds but has not issued any to date.

AAC participates in the State of Alaska Risk Management Pool, which costs considerably less than commercial insurance. Other obligations include accrued leave, compensated absences and personal leave. More detailed information about AAC's long-term liabilities is presented in the financial statement notes.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES

AAC's Board considered many factors when setting the fiscal year 2011 budget, such as construction projects, launch schedules, launch fees that will be charged for the business-type activities, and depreciation of the KLC facilities. Operating revenues are projected to be nearly $11 million. Management intends to utilize the National Guard Cooperative Agreement for further KLC infrastructure development.

AAC is commissioning an independent "2010 Economic Impact Study". The study is anticipated to be completed in the spring of 2011 and copies will be available on the Corporation's website at www.akaerospace.com.

CONTACTING AAC'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of AAC's finances and to show AAC's accountability for the money it receives. If you have questions about this report or need additional financial information, contact Alaska Aerospace Corporation at 4300 B Street, Suite 101, Anchorage, Alaska, (907) 561-3338.

FINANCIAL STATEMENTS

ALASKA AEROSPACE CORPORATION

Statement of Net Assets

June 30, 2010

(With Comparative Amounts for 2009)

Assets		2010	2009
Current assets:			
Cash and cash equivalents	$	9,779,420	15,343,436
Accounts receivable		1,861,639	1,940,969
Unbilled receivables		1,328,681	1,893,443
Inventory		381,072	380,632
Total current assets		13,350,812	19,558,480
Capital assets net of accumulated depreciation and amortization:			
Office furniture and equipment		483,092	112,460
Vehicles and other equipment		23,756,782	25,420,587
Buildings and structures		28,144,507	30,545,447
Infrastructure		4,688,064	5,055,571
Construction in progress		12,041,291	3,506,874
Intangible - Software		979,299	-
Intangible - Right of Use		18,129,895	18,953,981
Total capital assets, net		88,222,930	83,594,920
Total assets	$	101,573,742	103,153,400
Liabilities and Net Assets			
Liabilities:			
Current liabilities:			
Accounts payable		2,185,197	1,537,386
Accrued leave and compensation		540,179	541,044
Total current liabilities		2,725,376	2,078,430
Noncurrent liabilities - deferred revenue		5,731,271	9,575,019
Total liabilities		8,456,647	11,653,449
Net assets:			
Invested in capital assets		88,222,930	83,594,920
Unrestricted		4,894,165	7,905,031
Total net assets		93,117,095	91,499,951
Total liabilities and net assets	$	101,573,742	103,153,400

See accompanying notes to financial statements.

ALASKA AEROSPACE CORPORATION

Statement of Revenues, Expenses, and Changes in Net Assets

Year Ended June 30, 2010

(With Comparative Amounts for 2009)

		2010	2009
Operating revenues	$	11,336,598	18,620,231
Operating expenses:			
Personnel services		5,518,223	5,318,685
Travel		281,822	404,154
Contractual services		4,594,975	10,163,075
Supplies		723,056	1,728,930
Equipment		198,926	96,125
Depreciation and amortization		6,003,661	5,876,154
Total operating expenses		17,320,663	23,587,123
Net operating loss		(5,984,065)	(4,966,892)
Nonoperating revenues:			
Interest income unrestricted		8,349	44,114
Gain on disposal of capital assets		-	500
PERS relief from State of Alaska		138,140	355,300
Net pension obligation (NPO) write-off (special item)		-	582,579
Cooperative agreement		3,112	72,372
Total nonoperating revenues		149,601	1,054,865
Loss before capital contributions		(5,834,464)	(3,912,027)
State of Alaska capital appropriation		3,500,000	3,500,000
Capital contributions		3,951,608	1,946,107
Change in net assets		1,617,144	1,534,080
Net assets - beginning of the year		91,499,951	89,965,871
Net assets - end of the year	$	93,117,095	91,499,951

See accompanying notes to financial statements.

ALASKA AEROSPACE CORPORATION
Statement of Cash Flows
Year Ended June 30, 2010
(With Comparative Amounts for 2009)

	2010	2009
Cash flows from operating activities:		
Receipts from contracts	$ 11,980,690	17,283,160
Payments to suppliers	(5,151,408)	(11,801,997)
Payments to employees	(5,380,948)	(5,273,813)
Net cash provided by operating activities	1,448,334	207,350
Cash flows from noncapital financing activities - cooperative agreement received	3,112	72,372
Cash flows from capital and related financing activities:		
Capital appropriation received	3,951,608	1,946,107
Capital contribution from the State of Alaska	3,500,000	3,500,000
Proceeds from sale of fixed assets	-	500
Purchase of capital assets	(10,631,671)	(3,359,037)
Decrease in deferred revenue	(3,843,748)	(1,748,255)
Net cash provided (used) by capital and related financing activities	(7,023,811)	339,315
Cash flows from investing activities - interest received	8,349	44,114
Net increase (decrease) in cash and cash equivalents	(5,564,016)	663,151
Cash and cash equivalents at beginning of year	15,343,436	14,680,285
Cash and cash equivalents at end of year	$ 9,779,420	15,343,436
Reconciliation of operating loss to net cash provided (used) by operating activities:		
Operating loss	(5,984,065)	(4,966,892)
Adjustments to reconcile operating loss to net cash provided (used) by operating activities:		
Depreciation and amortization	6,003,661	5,876,154
Noncash expense - PERS relief	138,140	355,300
Noncash expense - NPO writeoff (special item)	-	582,579
Increase in accounts receivables	79,330	(247,637)
Increase in unbilled receivables	564,762	(1,089,434)
Decrease (increase) in inventory	(440)	14,126
Increase in accounts payable	647,811	576,161
Decrease in net pension obligation	-	(582,579)
Decrease in accrued expenses	(865)	(310,428)
Net cash provided by operating activities	$ 1,448,334	207,350

See accompanying notes to financial statements.

(1) **Organization**

The accompanying financial statements include all the activities of Alaska Aerospace Corporation (AAC or the Corporation). AAC was created in 1991 by an act of the State of Alaska Legislature (Legislature), Alaska Statute 14.40.821. AAC is a public corporation of the State established to promote the general welfare of the people in the state by encouraging long-term economic growth of the state by promoting, financing, developing and operating space launch and related facilities in Alaska.

On September 24, 2003, the Federal Aviation Administration issued a commercial space transportation license to operate a launch site at Kodiak Launch Complex (KLC) located on Kodiak Island, Alaska. The license term is five years from the effective date on the license. In September 2008, the Federal Aviation Administration renewed the license term for an additional five years. The Kodiak Launch Complex (KLC) has the capabilities for launching telecommunications, remote sensing and space science payloads of up to 8,000 pounds into low earth polar orbits. Construction on the KLC was completed in 2000. The launch complex is located on Narrow Cape, about 45 miles south of Kodiak on Kodiak Island, Alaska.

The financial activities of AAC are included in the State of Alaska's Comprehensive Annual Financial Report.

AAC is authorized to issue its own bonds and other obligations in such principal amounts as will be necessary to provide for sufficient funds for carrying out its purpose. Obligations issued are not deemed to constitute a debt of the State of Alaska. The issuance of bonds other than refunding bonds aggregating more than $1 million in a calendar year, or causing aggregate debt service in a calendar year on all proposed and outstanding bonds to exceed $1 million, require prior approval by the Legislature. No bonds have been issued to date.

(2) **Summary of Significant Accounting Policies**

Basis of Presentation

The accounts of AAC are organized as an enterprise fund. An enterprise fund is a proprietary type fund used to account for operations that are financed and operated in a manner similar to private business enterprises – where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges; or where the governing body has decided that periodic determination of revenues earned, expenses incurred, and/or net income is appropriate for capital maintenance, public policy, management control, accountability, or other purposes. Based upon the accounting and reporting standards set forth in Governmental Accounting Standards Board (GASB) Statement 20, the Corporation has opted to apply only those accounting and reporting pronouncements issued by the GASB subsequent to November 30, 1989.

Summary of Significant Accounting Policies, continued

Basis of Presentation, continued

In addition to the Enterprise Fund, Section 14.40.841 of the Alaska State Statutes established a revolving fund for AAC. The fund consists of appropriations made by the legislature, rents, fees or other money or assets transferred to the revolving fund by AAC. The amounts may be pledged to the payment of bonds of the Corporation or expended for the purposes of the Corporation as established by State Statute. This Section as amended states that the Corporation shall have custody of the fund and shall be responsible for its management and invest amounts in the fund in accordance with an investment policy adopted by the Corporation per AS 37.10.071. Disbursements may be made per AS 37.25.050 and reported annually in accordance with AS 14.40.866(b)(1).

During 2010, AAC expended monies from the fund for purposes of the Corporation. The Attorney General expressed an opinion dated March 15, 1995 that interest earned in a fund may be retained by AAC in that fund. The fund earned $30,207 of interest in fiscal year 2010. Of that amount, $21,858 is recorded in deferred revenue as it relates to interest on capital advances, and $8,349 is included in the current year activities.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The accompanying financial statements are reported using the "economic resources measurement focus," and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. AAC distinguishes *operating* revenues and expenses from *nonoperating* items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

Reserve Fund

Alaska Statute Sec. 14.40.951 created a reserve fund to account primarily for bond payments for principal and interest. The fund remained unfunded as of June 30, 2010.

State Appropriations

Appropriations may be made by the Legislature for AAC in the State revolving fund using monies from agency transfers and fees generated by AAC.

Other Accounting Basis

A proposed operating budget for the operations of the Corporation for the following fiscal year as well as a capital improvements budget for the next fiscal year are prepared annually in compliance with the Executive Budget Act (AS 37.07) and are subject to the State of Alaska's approval process. Appropriations for the operating budget lapse at the end of each fiscal year. Appropriations for capital projects, various grants and programs may carry over at year end. For the purpose of the statement of net assets, all highly liquid debt instruments with original maturities of three months or less are considered cash and cash equivalents.

Summary of Significant Accounting Policies, continued

Cash and Cash Equivalents

According to AAC's investment policy, funds in excess of current operating needs can be invested in quality securities to provide the maximum return on investment for an appropriate risk. These investments must have the ability to provide immediate liquid funds when needed. Quality securities include securities that are rated AAA or higher by Moody Corporation's rating and money market accounts consisting of securities eligible for direct purchases.

Revenue Recognition

Revenue from cost-type contracts is recognized on the basis of reimbursable costs incurred during the period plus fee earned. AAC provides currently for all known or anticipated losses on contracts. Variances between provisional rates and actual rates are accrued if the variance is unfavorable to AAC. If they are favorable to AAC, they are only accrued when AAC has the ability and intent to collect the variances. Revenue from fixed price contracts is recognized using the percentage-of-completion method, based primarily on contract costs incurred to date compared with total estimated costs. Revisions in cost and profit estimates are made during the course of work and are reflected when facts, which require revision become known. Provision for losses on uncompleted contracts is made in the period in which such losses are identified.

Receivables

AAC utilizes the allowance method of accounting to estimate losses due to uncollectible accounts. As of June 30, 2010, no allowance for doubtful accounts has been recorded due to AAC's past experience relative to collecting all receivables.

Unbilled Receivables

Unbilled amounts on cost-reimbursement contracts represent recoverable costs and accrued profits not yet billed. These amounts are billable upon receipt of contract funding, final settlement of incurred cost claim, or contract completion. As of June 30, 2010, no allowance for unrecoverable costs has been recorded due to AAC's past experience relative to collecting all receivables.

Inventories

Inventories consist of expendable supplies and critical spare parts for the Kodiak Launch Complex, and are carried at the lower of cost (first-in, first-out) or market (net realizable value). Inventory costs are reported as expenses in the period when inventory items are used, rather than in the period purchased.

Capital Assets

Capital assets purchased or acquired with an original cost of $5,000 or more are reported at fair market value as of the date received or placed in service. Additions, improvements and other capital outlays that significantly extend the useful life of an asset are capitalized. Other costs incurred for repairs and maintenance are expensed as incurred. Depreciation and amortization on all assets are provided on the straight-line basis over the following estimated useful lives:

ALASKA AEROSPACE CORPORATION

Notes to Financial Statements, continued

Summary of Significant Accounting Policies, continued

Capital Assets, continued

Computer Software and Related Equipment	3 years
Office Furniture and Related Equipment	5 years
Vehicles and Other Equipment	5 years
Heavy Equipment and Machinery	7-10 years
Kodiak Launch Complex Buildings/Structures	20 years
Kodiak Launch Complex Infrastructure	20 years
Intangible – Software	7 years
Intangible – Right of Use	20 years

Compensated Absences

Personal leave is accrued as follows: 2 days per month for employees with up to two years service; 2.25 days per month for employees with two to five years service; 2.5 days per month for employees with five to ten years service; and 3 days per month for employees with over ten years service. AAC's employees are compensated through the State of Alaska payroll system. AAC accrues unused leave at year end.

Investments

Alaska Statutes authorize AAC to establish trust funds for the investment and deposit of bond proceeds. No bonds have been issued to date.

Income Taxes

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

Deferred Revenue

Amounts received from the cooperative agreement restricted as to use and not yet expended, are shown as deferred revenue.

Operating and Non-Operating Revenue

Income related to professional services and operation of the Kodiak Launch Complex is considered operating revenue. All other income is considered nonoperating revenue.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

Summary of Significant Accounting Policies, continued

Subsequent Events

The Corporation has evaluated subsequent events through October 21, 2010, the date on which the financial statements were issued.

Recently Adopted Accounting Pronouncements

The Governmental Accounting Standards Board has passed several new accounting standards with upcoming implementation dates covering several topics as follows:

- GASB 57 – *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*
- GASB 58 – *Accounting and Financial Reporting for Chapter 9 Bankruptcies*
- GASB 59 – *Financial Instruments Omnibus*

In February 2009, the Governmental Accounting Standards Board issued Statement number 54 – *Fund Balance Reporting and Governmental Fund Type Definitions* (GASB 54). GASB 54 establishes a hierarchy of fund balance classifications based on the extent to which a government is bound to observe constraints imposed upon the use of the net assets held by the government. This statement is effective for fiscal years beginning after June 15, 2010 and must be applied retrospectively to all periods presented. AAC has elected to implement the provisions of GASB 54 in fiscal year 2010, one year early. AAC has retrospectively applied the provisions of this statement which did not have any effect on the presentation of the financial statements at June 30, 2009.

Prior Year Financial Information

The financial statements include certain prior-year comparative information in the Statement of Net Assets, Statement of Revenue, Expenses and Changes in Net Assets and Statement of Cash Flows. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the organization's financial statements for the year ended June 30, 2009, from which the prior year information was derived.

(3) **Cash and Cash Equivalents**

At June 30, 2010, AAC had the following investments:

Investment Type	
Cash and Money Market	$ 8,990,854
Preferred Securities	1,003,460
Net invested assets	9,994,314
Outstanding deposits and disbursements	(214,894)
Total cash and cash equivalents	$ 9,779,420

Cash and Cash Equivalents, continued

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. As a means of limiting its exposure to fair value losses arising from increasing interest rates, AAC's investment policy limits individual fixed rate securities to five years in maturity. The investments in the financial institutions at June 30, 2010 comprised of preferred securities, money market accounts and municipal coupons rated AAA or higher by the Moody's Corporation. The maturities of all the securities were 45 days or less.

Credit Risk

Credit risk is the risk that an issuer or other counter party to an investment will not fulfill its obligations. The investments in the other financial institutions at June 30, 2010 are comprised of preferred securities, money market accounts, and municipal coupons rated AAA or higher by the Moody's Corporation.

Custodial Credit Risk

Custodial credit risk is the risk that in the event of bank or broker failure, AAC's deposits and investments may not be returned. Of the $9,994,314 balance, $1,003,460 is collateralized with securities held by AAC, $8,740,854 is collateralized with securities held in the investment broker's name, and the rest is insured by the Federal Deposit Insurance Corporation.

(4) **Capital Assets**

The following is a summary of the changes in capital assets for the fiscal year ended June 30, 2010:

	Balance June 30, 2009	Increase	Decrease	Balance June 30, 2010
Capital assets not being depreciated - construction in progress	$ 3,506,874	10,202,514	1,668,097	12,041,291
Capital assets being depreciated:				
Office furniture and equipment	932,332	452,752	156,116	1,228,968
Vehicles and other equipment	34,269,507	606,763	94,635	34,781,635
Building and structures	45,897,051	19,440	78,160	45,838,331
Infrastructure	7,224,995	-	-	7,224,995
Intangible – Software	-	1,018,299	-	1,018,299
Intangible – Right of Use	20,602,153	-	-	20,602,153
Total capital assets being depreciated	$ 108,926,038	2,097,254	328,911	110,694,381

ALASKA AEROSPACE CORPORATION

Notes to Financial Statements, continued

Capital Assets , continued

	Balance June 30, 2009	Increase	Decrease	Balance June 30, 2010
Less accumulated depreciation and amortization for:				
Office furniture and equipment	$ 819,872	118,913	192,909	745,876
Vehicles and other equipment	8,848,920	2,235,920	59,987	11,024,853
Building and structures	15,351,604	2,418,235	76,015	17,693,824
Infrastructure	2,169,424	367,507	-	2,536,931
Intangible – Software	-	39,000	-	39,000
Intangible – Right of Use	1,648,172	824,086	-	2,472,258
Total accumulated depreciation	28,837,992	6,003,661	328,911	34,512,742
Capital assets being depreciated, net	80,088,046	(3,906,407)	-	76,181,639
Totals	$ 83,594,920	6,296,107	1,668,097	88,222,930

Construction in progress is related to design of a third launch pad, design and construction of a rocket motor storage facility, implementation of an enterprise resource planning system and facility improvements. Depreciation and amortization expense totaled $6,003,661 for the year ended June 30, 2010.

During 2007, AAC entered into an agreement with Kodiak Kenai Cable Company, LLC (KKCC) to provide fiber optic connectivity to KLC. AAC has obtained an Indefeasible Right of Use (IRU) purchase agreement for 25 years, which is included in Other Assets. The IRU Capacity will include one OC-12c unit of network capacity and one pair of dark fiber, terminating at the Points of Presence (POP) drop and insert points. In addition, the IRU Capacity shall include two DS-3's of capacity on the OC-12c IRU which shall be provided in a fully redundant, route diverse manner. If AAC does not light the pair of dark fiber within the first 12.5 years from the date of execution of this Agreement, the dark fiber IRU will revert back to KKCC.

The fiber optic connectivity to KLC was completed and placed in service on July 1, 2007 for a total cost of $20,602,153. AAC will amortize this cost over the life of the agreement. Amortization expense for the current period was $824,086.

Intangible software represents AAC's investment into a new Enterprise Resource Planning system to upgrade its information technology requirements. A $1,018,299 investment in software was implemented in April of 2010. This software is being amortized over 7 years.

(5) **Operating Leases**

AAC leases office space, property in Cordova, Alaska and equipment. Minimum future lease payments as of June 30, 2010, are as follows:

Year Ended June 30,	Office Lease	Land Lease	Equipment	Total
2010	$ 247,270	15,150	27,902	290,322
2011	-	15,150	6,975	22,125
2012	-	15,150	-	15,150
2013	-	15,150	-	15,150
2014	-	15,150	-	15,150
Thereafter	-	28,406	-	28,406
Total	$ 247,270	104,156	34,877	386,303

Rent expense for the fiscal year ended June 30, 2010 was $255,018.

(6) **Deferred Revenue**

AAC entered into a cooperative agreement with an initial award amount of $4,791,920 in fiscal year 1999 from the Army National Guard which has been subsequently increased to $87,639,383. The following schedule summarizes the activity related to these grants for the fiscal year ended June 30, 2010:

Deferred revenue at July 1, 2009	$ 9,575,019
Unrealized gains on advances	89,114
Interest earned on advances	21,858
	9,685,991
Expenditures made from grants	3,954,720
Deferred revenue at June 30, 2010	$ 5,731,271

(7) **Defined Benefit Pension Plan**

AAC participates in the Public Employees' Retirement System (PERS). PERS is a cost-sharing multiple employer plan which covers eligible State and local government employees, other than teachers. The plan was established and is administered by the State of Alaska Department of Administration to provide pension, postemployment healthcare, death, and disability benefits. Benefit and contribution provisions are established by State law and may be amended only by the State Legislature.

Defined Benefit Pension Plan, continued
The plan is included in a comprehensive annual financial report that includes financial statements and other required supplemental information. The report is available at the following address:

Department of Administration
Division of Retirement and Benefits
P.O. Box 110203
Juneau, Alaska 99811-0203

Conversion to Cost Sharing
In April 2008, the Alaska Legislature passed Senate Bill (SB) 125 which converted the existing Public Employees Retirement System (PERS) from an agent-multiple employer plan to a cost-sharing plan with an effective date of July 1, 2008. Under the cost-sharing arrangement, the State of Alaska Division of Retirement and Benefits no longer tracks individual employer assets and liabilities. Rather, all plan costs and past service liabilities are shared among all participating employers. The cost-sharing plan requires a uniform employer contribution rate of 22% of active member wages, subject to a wage floor. Legislation provides for State contributions in the event that the annually calculated and board adopted rate, which includes a provision to pay down the past-service liability, exceeds 22%. Any such additional contributions are recognized by AAC as an on-behalf payment.

In addition, in fiscal year 2008, the State of Alaska passed legislation (SB 123) which requires the employer contribution to be calculated on all PERS eligible wages, including wages attributable to the defined contribution pension plan described (Note 8).

Funding Policy
AAC employees are required to contribute 6.75% of their annual covered salary (2.50% for pension and 4.25% for healthcare). The funding policy provides for periodic employer contributions based on actuarially determined rates that, expressed as a percentage of annual covered payroll, are sufficient to accumulate sufficient assets to pay both pension and postemployment healthcare benefits when due.

Under current legislation, the employer contribution rate is statutorily capped at 22%, however, the State of Alaska contributes any amount over 22% such that the total contribution equals the Alaska Retirement Management Board adopted rate, generally consistent with the actuarially determined rate.

AAC's contribution rates for 2010 were determined as part of the June 30, 2007 actuarial valuation and are as follows:

Defined Benefit Pension Plan, continued

Funding Policy, continued

	ARM Board Contractual Rate	Adopted Rate	GASB 45* Rate
Pension	8.16%	10.25%	10.72%
Postemployment healthcare	13.84%	17.40%	53.96%
Total contribution rate	22.00%	27.65%	64.68%

*This rate uses a 4.5% OPEB discount rate and disregarding future Medicare Part D payments.

The projection of future benefits for an ongoing plan involves estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Projections of benefits are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits in force at the valuation date and the pattern of sharing benefit costs between AAC and the plan members at that point. Actuarial calculations reflect a long-term perspective and employ methods and assumptions that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial values of assets.

Projected benefits for financial reporting purposes do not incorporate any potential effects of legal or contractual funding limitations.

Annual Pension and Postemployment Healthcare Cost

AAC is required to contribute 22% of covered payroll, subject to a wage floor. In addition, the State of Alaska contributed approximately 13.22% of covered payroll to the Plan. In accordance with the provisions of GASB Statement Number 24, AAC has recorded the State on-behalf payment in the amount of $138,140 as revenue and expense in these financial statements. However, because AAC is not statutorily obligated for these payments, this amount is excluded from pension and OPEB cost as described here. Only two years of information are available at this time.

Defined Benefit Pension Plan, continued

Annual Pension and Postemployment Healthcare Cost, continued

Year Ended June 30	Annual Pension Cost	Annual OPEB Cost	Total Benefit Cost (TBC)	AAC Contri-butions	% of TBC Contributed
2010	$ 168,280	$ 285,416	$ 453,696	$ 453,696	100%
2009	$ 159,045	$ 353,594	$ 512,639	$ 513,639	100%

(8) **Defined Contribution Pension Plan**

The State of Alaska Legislature approved Senate Bill 141 to create the Public Employees' Retirement System (PERS) Tier IV for employees hired after July 1, 2006 or for employees converting from the PERS Tier I, II or III defined benefit plans. The plan is administered by the State of Alaska, Department of Administration, and benefit and contribution provisions are established by State law and may be amended only by the State Legislature. The Alaska Retirement Management Board may also amend contribution requirements. Included in the plan are individual pension accounts, retiree medical insurance plan and a separate Health Reimbursement Arrangement account that will help retired members pay medical premiums and other eligible medical expenses not covered by the medical plan. Employees are required to contribute 8.0% of their annual covered salary, and ACC is required to make the following contributions:

	Others Tier IV
Individual account	5.00%
Health reimbursement arrangement (HRA) *	3.00
Retiree medical plan	0.99
Occupational death and disability benefits	0.58
	9.57 %

*Health Reimbursement Arrangement – AS 39.30.370 requires that the employer contribute "an amount equal to three percent of the average employer's average annual employee compensation." For actual remittance, this amount is calculated as a flat rate for each full time or part-time employee per pay period.

Employees are immediately vested in their own contributions and vest 25% per year in employer contributions. AAC and employee contributions to PERS including the HRA contribution for the year ended June 30, 2010 were $110,619 and $176,990, respectively.

(9) **Risk Management**

With regards to workers' compensation insurance, AAC participates in the State of Alaska Risk Management Pool. The risks are transferred to the pool, and the premium is charged to AAC based on payroll expenditures. The State is an authorized self insurer under AS 23.30.090. Casualty and property insurance coverage is provided under endorsement to the State of Alaska Aviation and Airports program of insurance.

(10) **Land Assignment**

On 18 May 1994, the Alaska Department of Natural Resources and the Alaska Aerospace Corporation executed an Interagency Land Management Assignment (ILMA) for 3,077 acres of land situated at Narrow Cape, Kodiak Island, Alaska. The ILMA is identified in state records as ADL 226285. On 3 February 2003, ADL 226285 was amended to add 640 acres to the ILMA. ADL 226285 was amended a second time two years later, which added an additional 7,048 acres to the ILMA, by a record of decision dated 19 April 2005. Current lands assigned to AAC under ADL 226285 total in aggregate 10,765 acres. Stipulations to the ILMA require the lands be managed for multiple use and that access restrictions be limited to times when hazardous operations are underway.

(11) **Related Parties**

State of Alaska

In the normal course of business, AAC receives administrative, personnel, risk management, data processing, and other services from the State of Alaska.

(12) **Contingencies**

Expenses charged against amounts received or receivable from federal contracting agencies are subject to further audit and adjustment by the contracting agency. Any disallowed expenses would become a liability of AAC. Management does not believe there are any material items which may be disallowed.