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Gainesville Regional Utilities

Quarterly Financial Statements

3rd Quarter Ending June 30, 2005



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Management Overview and Analysis

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Overview

The City of Gainesville, Florida owns and operates a combined utility system doing business as Gainesville Regional Utilities (GRU) which provides five separate utility functions. The utility functions consist of an electric generation, transmission and distribution system (Electric System), water production and distribution system (Water System), wastewater collection and treatment systems (Wastewater System), natural gas distribution system (Gas System) and a telecommunication system (GRUcom). Each of these systems is accounted for internally as a separate enterprise fund but reported as a combined utility system for external financial reporting purposes.

We offer readers of this management discussion and analysis of the utility system's financial statements for the quarter ending June 30, 2005. It should be read in conjunction with the financial statements that follow this section.

Basis of Accounting

The financial statements are presented on the accrual basis of accounting, under Generally Accepted Accounting Principles (GAAP). Under this basis, revenues are recognized in the period earned and expenses are recognized in the period incurred. Additionally, separate financial statements are presented in accordance with the amended and restated Utilities System Revenue Bond Resolution (Bond Resolution). In the Bond Resolution statements, rates are designed to cover operating and maintenance expense, debt service and other uses, which exclude depreciation expense and other non-cash expense items.

The Bond Resolution financial statement method of reporting results in costs being included in the determination of rates in different periods than when these costs are recognized for GAAP financial statement purposes.

Gainesville Regional Utilities has adopted the uniform system of accounts prescribed by the Federal Energy Regulatory Commission (FERC) and the National Association of Regulatory Utility Commissioners (NARUC).

Current Year Performance-to-Date and Projected Results

Electric

Residential Sales revenues were approximately 3.9% below budget through the third quarter, and General Service Sales revenue were approximately 3.1% below budget through June. This is primarily due to milder than normal winter and spring weather conditions.

Fuel Adjustment revenue and Fuel expense are projected to be higher than budgeted by 5.3% and 4.4%, respectively. This is due primarily to higher than anticipated fuel costs and also one unplanned outage of DH2, necessitating the production of more power using natural gas and more than expected reliance on purchased power.

Interchange Sales and Interchange Fuel Expense are projected to be 49.7% and 47.8% lower than budgeted. With an aging fleet of smaller, less efficient gas units, we cannot be competitive with the excess capacity we have available, when others have larger, newer, and more efficient gas units that allow them to produce power at a lower cost. Even in off-peak nighttime hours when we have excess coal capacity, we are not as competitive when others have larger, newer, more efficient coal units.

Overall, projected interest income is less than budgeted due to a combination of higher fuel costs and hurricane recovery costs resulting in less working capital available for investment. Additionally, interest income between systems has been affected by a reallocation of construction funds.

The total Operation and Maintenance (O&M) expense projection, less fuel expense, is projected to be \$224K higher than budget. More specifically, the costs associated with the annual overhaul of Deerhaven were \$488K higher than anticipated. In addition, power production expenses for materials and supplies are anticipated to be up \$230K. These cost overruns are partially being offset by a projected reduction in costs associated with our part ownership in the Crystal River nuclear plant, as recently updated by Progress Energy. We also are seeing a reduction in transmission and distribution expenditures due to some operating efficiencies.

In the Administrative and General (A&G) total expenditures for combined systems are down 1%, though the allocation of expenditures between the different funds is different than budgeted. This is partly due to the re-allocation of "common plant" expenditures between the different systems and partly due to the normal process of re-allocating fringe benefit costs and the capitalization of costs.

Debt Service expenses are anticipated to come in below budget. The fixed rate financing anticipated for early summer was delayed pending revised capital numbers. In order to have sufficient funds for construction purposes, tax exempt commercial paper (TECP) was issued. The interest rate for TECP is currently lower than the interest rate for a fixed rate financing. A small portion of the savings related to this change is offset by higher than expected interest rates on our variable rate debt outstanding. Debt Service between systems was also impacted by a reallocation of construction funds and the related debt and interest payments.

Current Year Performance-to-Date and Projected Results (continued)

Gas

During the storms of September 2004, as many as one-third of gas bills were based on estimated meter readings. In many cases, estimated residential bills were based on higher than actual usage, and billing adjustments were made in October which led to October sales that were much lower than projected. Additionally, relatively warm weather in October and November contributed to lower than projected residential sales in November and December. The overall result is that residential sales revenues are 5.3% below budget through the third quarter. Commercial gas sales are less weather sensitive than residential sales, and vary less from month to month. Commercial firm sales are tracking 2.6% above budget, while combined Interruptible & Transportation sales are running about 1.9% ahead of budget.

The Purchased Gas Fuel Adjustment (PGA) revenue and Fuel expense – Purchased Gas projections are 13.7% and 13.0%, respectively, higher than budgeted due to higher gas prices than anticipated. Since fuel expenses are passed through to the customer, revenues are increased as fuel expenses increase. Even though the fuel expense is a pass through, there is a difference between PGA fuel revenue and fuel expense due to presenting the Cleanup Cost Recovery Factor separately and true-ups that affect the timing between reporting periods.

Overall, projected interest income is less than budgeted due to a combination of higher fuel costs and hurricane recovery costs resulting in less working capital available for investment. However, interest income between systems has been affected by a reallocation of construction funds.

O&M expenses, less fuel expense, are projected to be just slightly higher than budget for the year.

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Current Year Performance-to-Date and Projected Results (continued)

Water

Rainfall levels from September through May were 39% above normal, and rainfall during March, April and May (peak irrigation season) was 50% above normal, leading to water sales revenues that are tracking nearly 6% below budget.

Overall, projected interest income is less than budgeted due to a combination of higher fuel costs and hurricane recovery costs resulting in less working capital available for investment. However, interest income between systems has been affected by a reallocation of construction funds.

In the area of O&M, there have been substantial increases in softening agent prices amounting to \$180K greater than budget, increased electrical usage (\$45K), and increased maintenance of water distribution systems.

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Wastewater

Revenues from wastewater billings are projected to be 2.3% below budget, corresponding to lower than projected water sales.

Overall, projected interest income is less than budgeted due to a combination of higher fuel costs and hurricane recovery costs resulting in less working capital available for investment. However, interest income between systems has been affected by a reallocation of construction funds.

For O&M, electricity used in the treatment of wastewater, is projected to be higher than budget by \$300K and most of the remainder is related to increased costs for maintenance of lift stations.

Current Year Performance-to-Date and Projected Results (continued)

Wastewater, continued

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GRUCom

Through the second quarter of FY2005, combined GRUCom revenues are generally in line with the budget; however, Tower Lease Rental revenue is projected to be 5.4% higher than budget due to additional co-locators and Internet Access revenue is projected to be 12.8% lower than budget due to the lowering of internet rates to increase competitiveness in the industry.

In the O&M area, total projections for the year are \$619K less than budgeted due to potential costs savings for property taxes still being negotiated (\$300K), reduced O&M personal services costs as the result of more effort directed to capital projects (\$175K), and savings from signing a new backbone internet access agreement with Sprint (\$75K).

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Debt Service expenses are anticipated to be higher than budget. The interest rate on our variable rate debt is higher than expected due to the rising interest rate environment.

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