

FINANCIAL STATEMENTS

Gainesville Regional Utilities
Years Ended September 30, 2008 and 2007
With Report of Independent Certified Public Accountants

Gainesville Regional Utilities

Financial Statements

Years Ended September 30, 2008 and 2007

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Management's Discussion and Analysis

The City of Gainesville, Florida owns and operates a combined utility system (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), a wastewater collection and treatment system (Wastewater System), a 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 GRU's financial statements this management discussion and analysis of GRU's financial statements for the fiscal years ended September 30, 2008 and 2007. It should be read in conjunction with the financial statements that follow this section.

Required Financial Statements

Balance Sheet. This statement includes all of GRU's assets and liabilities and provides information about the nature and amounts of investments in resources (assets) and the obligations to GRU's creditors (liabilities). It also provides the basis for computing rate of return, evaluating the capital structure of the System and assessing the liquidity and financial flexibility of GRU.

Statement of Revenues, Expenses and Changes in Net Assets. All of the current year's revenues and expenses are accounted for in this statement. This statement measures the success of the combined utility system's operations over the past year.

Statement of Cash Flows. The primary purpose of this statement is to provide information about the combined utility system's cash receipts and cash payments during the reporting period. This statement reports cash receipts, cash payments, and net changes in cash resulting from operating, investing and financing activities.

Notes to Financial Statements. The notes provide additional information that is essential to fully understanding the data provided in the financial statements. The notes to the financial statements can be found on pages 18 - 46 of this report.

Management's Discussion and Analysis

Financial Analysis of the Combined Utility System

The Combined Utility System net assets increased by \$18.3 million from 2007 to 2008, and increased by \$19.1 million from 2006 to 2007. Table 1 below focuses on the net assets.

Table 1
Combined Utility System Net Assets

	2008	September 30 2007	2006
	<i>(In Thousands)</i>		
Current and other assets	\$ 486,458	\$ 395,996	\$ 470,462
Capital assets, net	954,762	839,422	761,539
Total assets	1,441,220	1,235,418	1,232,001
Long-term debt outstanding	748,603	574,164	592,315
Current and other liabilities	308,308	295,290	292,808
Total liabilities	1,056,911	869,454	885,123
Net assets:			
Invested in capital assets, net of related debt	322,254	319,757	299,811
Restricted	46,859	37,862	41,400
Unrestricted	15,195	8,345	5,666
Total net assets	\$ 384,308	\$ 365,964	\$ 346,877

Changes in net assets can be further explained using the following condensed statements of revenues, expenses, and changes in net assets.

Management's Discussion and Analysis

Table 2
Combined Utility System Changes in Net Assets

	2008	September 30 2007	2006
	<i>(In Thousands)</i>		
Operating revenues	\$ 349,970	\$ 294,840	\$ 290,039
Interest income	9,272	11,317	10,025
Gain on sale of investments	97	—	—
Total revenues	359,339	306,157	300,064
Operating expenses	285,831	243,869	253,698
Interest expense, net	28,195	26,943	26,920
Total expenses	314,026	270,812	280,618
Income before contributions and transfers	45,313	35,345	19,446
Capital contributions, net	4,483	14,139	4,707
Operating transfer to City of Gainesville	(31,452)	(30,397)	(29,431)
Change in net assets	18,344	19,087	(5,278)
Net assets, beginning of year	365,964	346,877	352,155
Net assets, end of year	\$ 384,308	\$ 365,964	\$ 346,877

Capital Asset and Debt Administration

Capital Assets. GRU's investment in capital assets as of September 30, 2008, amounts to \$954.8 million (net of accumulated depreciation). This investment in capital assets includes land, generation, transmission and distribution systems, buildings and fixed equipment, and furniture, fixtures and equipment. The net increase in the investment in capital assets (net of accumulated depreciation) for the current fiscal year was 13.7%. In fiscal 2007 it increased 10.2%.

Management's Discussion and Analysis

The following table summarizes the System's capital assets, net of accumulated depreciation and changes for the years ended September 30, 2008, 2007 and 2006.

Combined Utility System Capital Assets (Net of accumulated depreciation)

	September 30		
	2008	2007	2006
	<i>(In Thousands)</i>		
Generation	\$ 150,474	\$ 162,613	\$ 164,413
Transmission, distribution and collection	392,026	368,347	364,403
Treatment	62,172	62,842	64,924
General plant	42,164	44,825	28,460
Plant held for future use	6,054	6,054	6,054
Plant unclassified	776	8,959	8,704
Construction work in progress	301,095	185,782	124,581
Total net utility plant	\$ 954,761	\$ 839,422	\$ 761,539

Major capital asset events included the following:

- Following the successful implementation of its new Customer Information System in 2007, GRU is continuing its SAP software utilization with the implementation of a Financial Management Information System, which is planned to go live in Spring 2009. \$1.9 million was incurred in 2008 of the project's total \$9.0 estimated cost.
- Electric transmission and distribution expansion was \$13.8 million in 2008 and \$7.4 million in 2007. For 2008, \$5.6 million was pertaining to underground system improvements.
- GRU is in the second year of construction of its South Energy Center. The South Energy Center is a combined heat and power facility built to provide the Shands Medical campus with steam, chilled water and backup power in case of a disaster, and is planned to be operational in 2009. In 2008, GRU incurred \$30 million of the total estimated \$45 million project cost.
- GRU began work on its Air Quality Control project at Deerhaven 2 in 2007. The project incurred \$62.6 million in 2008, for a total of \$89.5 spent to date. GRU expects the Air Quality Control project to be completed by summer 2009, at a total cost of \$141 million.

Management's Discussion and Analysis

- Water Plant system expansion is highlighted by the filter system upgrade at the Murphree Plant. In 2008, \$3.4 million was incurred versus \$0.5 million in 2007. The final phase of this upgrade is planned to occur in 2010, bringing the estimated total cost of this project to \$8.5 million.
- Telecommunication fiber cable expansion was \$1.7 million in 2008 and \$0.9 million in 2007.
- Gas distribution plant was expanded \$1.0 million in 2008 compared to \$0.9 million in 2007.

The Utility's 2009 capital budget is \$181.6 million and was \$189.3 million in 2008. These projects will be funded from a combination of internal equity and debt.

Additional information on capital assets may be found in Note 3 on page 24 of this report.

Long-Term Debt. At September 30, 2008 and September 30, 2007, GRU had total long-term debt outstanding of \$792 million and \$616 million, respectively, comprised of revenue bonds and other long-term debt.

Outstanding Debt at September 30

	2008	2007	2006
	<i>(In Thousands)</i>		
Senior Lien revenue bonds	\$ 730,495	\$ 550,750	\$ 551,665
Subordinated revenue bonds	–	65,300	68,500
Tax-exempt Commercial Paper	62,000	–	–
Total	\$ 792,495	\$ 616,050	\$ 620,165

On April 28, 2008, the City issued Utilities System Commercial Paper Notes, Series C in the amount of \$62,000,000 to refund the 2002 Series A Bonds and the 2002 Series B Bonds.

On February 13, 2008, the City issued Utilities System Revenue Bonds, Series 2008A in the amount of \$105,000,000 and Utilities System Revenue Bonds, Series 2008B in the amount of \$90,000,000. The 2008A Bonds mature on various dates from October 1, 2009 to October 1, 2020. The 2008B Bonds mature on various dates from October 1, 2022 to October 1, 2038. The 2008A Bonds and the 2008B Bonds were issued to pay costs of acquisition and construction of the City's utilities systems.

On March 1, 2007, the City issued Utilities System Revenue Bonds, Series 2007A in the amount of \$139,505,000. The 2007A Bonds were issued to advance-refund a portion of the City's outstanding Utilities System Revenue Bonds, 2005 Series A and a portion of the City's outstanding Utilities System Revenue Bonds, 2003 Series A.

Management's Discussion and Analysis

On July 6, 2006, the City issued Utilities System Revenue Bonds, Series 2006A in the amount of \$53,305,000. The 2006A Bonds mature on various dates from October 1, 2010 to October 1, 2026. The 2006A Bonds were issued to refund a portion of the City's outstanding Utilities System Revenue Bonds, 1996 Series A and to pay costs of acquisition and construction of the City's utility systems.

The System maintains ratings of Aa2 and AA with Moody's Investors Services and Standard & Poor's (S&P), respectively for its revenue bonds. The System has ratings of A-1 and P-1 for its commercial paper.

Additional information on long-term debt can be found in Note 4 on pages 25 - 35 of this report.

Financial Highlights. The most significant changes in GRU's financial condition are summarized below:

- Operating sales revenue increased \$41.7 million or approximately 14.3% and \$6.3 million or approximately 2.2%, in fiscal 2008 and 2007, respectively. Included in this amount is an increase in revenue of approximately \$23.9 million related to higher fuel costs in fiscal 2008, and approximately \$10.4 million associated with lower fuel costs incurred in fiscal 2007, as compared to 2006. Fuel costs are passed directly through to our customers as part of a fuel adjustment charge, which is recorded as revenue. The remaining increase in sales revenue is a result of rate increases implemented in October 2007.
- Net capital contributions from developers decreased in fiscal 2008 over fiscal 2007 by \$9.7 million and increased in fiscal 2007 over fiscal 2006 by \$9.4 million. This decrease is primarily due to a large number of developments being completed during fiscal 2007. Contributions are recorded when the project is placed in service.
- Fiscal 2008 year end fuels payable increased \$1.8 million, or approximately 24.8%, compared to fiscal 2007 year end. The primary reason for this increase is an increase in coal prices. During fiscal year 2008, several short-term coal contracts expired, causing GRU to purchase coal on the spot market at higher prices.
- Gross utility plant in service increased \$43.0 million, or 3.8%, and net capital assets increased \$115.3 million, or 13.7% in fiscal 2008. In fiscal 2007, gross utility plant in service increased \$45.5 million, or 4.2%, and net capital assets increased \$77.9 million, or 10.2%. This is summarized under "Capital Assets," on page 25.
- Long-term debt increased \$174.4 million, or 30.4%, in fiscal 2008, because of the issuance of Revenue bonds totaling \$195 million and Commercial Paper totaling \$62 million, offset by refunding of other debt and the scheduled paydown of principal. Long-term debt decreased \$18.1 million, or 3.1%, in fiscal 2007, due to the scheduled paydown of principal. See "Long-Term Debt" on page 5, and the detail, on pages 26 - 34.

Management's Discussion and Analysis

- The number of customers for electric, water, wastewater and gas services increased 3.3%, 3.0%, 2.2%, and 2.0%, respectively in fiscal 2008, and 1.4%, 1.9%, 1.7%, and 1.9% respectively, in fiscal 2007.
- GRU is in the process of remediation efforts at a former manufactured gas plant site. The costs incurred to date total \$4.3 million and GRU estimates that remaining costs of the project will be approximately \$13.3 million. However, to date GRU has recovered \$3.3 million from insurance. After recognizing collection fees paid, a net recovery of \$2.2 million has been realized which will directly reduce the amount to be recovered through customer billings. GRU has accrued a regulatory asset and liability to account for the cost and cost recovery of the expense, which is being amortized as costs are incurred and customer revenues are received. Further explanation of this activity is presented in Note 13, page 41 of this report.
- GRU's service territory incurred approximately \$1.1 million of damage to its facilities as a result of Tropical Storm Fay in September 2008. The \$1.1 million in storm-related expenses were accrued as fiscal 2008 activity and reported in current liabilities. Requests for Federal Emergency Management Agency (FEMA) funding are being submitted. GRU expects to receive a recovery of 75% from federal and 12.5% from state emergency funds as a result of this request. A receivable of \$965,000, or 87.5%, of expenses has been recorded in fiscal 2008.

Currently Known Facts or Conditions that May Have a Significant Effect on GRU's Financial Condition or Results of Operations

The primary factors affecting the utility industry include environmental regulations, restructuring of the wholesale energy market, the formation of independent bulk power transmission systems and the increasing strategic and price differences among various types of fuels.

Utilities, and particularly electric utilities, are subject to increasing federal, state and local statutory and regulatory requirements with respect to the siting and licensing of facilities, safety and security, air and water quality, land use and other environmental factors.

Reinstatement of the Clean Air Interstate Rule (CAIR) and Clean Air Mercury Rule (CAMR), or the promulgation of other rules to the same end, create uncertainty as to the capital, operating and maintenance expenditures which will be required by the Deerhaven and JR Kelly generating stations in 2009 and 2010, which may be significant.

Restructuring of wholesale markets and the formation of independent transmission systems has slowed considerably. No state legislation is pending or proposed at this time for retail competition in Florida. Any such restructuring of the Florida retail electric utility industry would be expected to affect the System. Currently, there is no initiative concerning retail electric deregulation in Florida or nationwide.

Management's Discussion and Analysis

Currently Known Facts or Conditions that May Have a Significant Effect on GRU's Financial Condition or Results of Operations (continued)

On October 1, 2008, GRU implemented a 7% revenue requirement increase in the electric system to be recovered across all classes. The customer charge for all classes and all service was increased to the cost of service. GRU also increased the revenue requirement for the water system by 9%, for the wastewater system by 10% and for the gas system by 19%. This represents an overall monthly increase of \$13.06 for a typical residential customer with all four services.

To meet increased costs of service, GRU increased water and wastewater connection fees 3.2%.

The base rate increases noted above may affect the financial condition and results of operations.

The emerging role of municipalities as telecommunications providers has resulted in a number of state-level legislative initiatives across the nation to curtail this activity. In Florida, this has culminated in the passage of SB1322. Although the system has special status as a grandfathered entity under this legislation, there are some implications should GRU seek to expand into additional areas of service.

GRU's long term energy supply strategy is to aggressively pursue the maximum cost effective energy conservation and renewable energy. Based on the most recent forecasts, which include the effects of aggressive conservation programs, GRU has adequate reserves of generating capacity to meet forecasted loads plus a 15% reserve margins through 2022. This forecast differs from previous years due to additional generation capacity, new population forecasts, and changed economic circumstances. Additional capacity includes 7 megawatts of distributed generation (4 combined heat and power and 3 renewable), and 2.5 megawatts of additional nuclear capacity due to Progress Energy Florida's planned upgrade of the Crystal River 3 nuclear unit (of which GRU owns a small share). Management bases its forecast of future energy needs upon the population forecast for Gainesville produced annually by the Bureau of Economic and Business Research at the University of Florida. GRU management has also been authorized by the City Commission to negotiate a long term contract to secure the output from a 100 megawatt biomass fueled power plant. The proposed facility will be located on a portion of land leased from GRU's Deerhaven power plant site, but owned and operated by a third party. The project is expected to provide a long term hedge against volatile fossil fuel costs and potential federal and state renewable energy requirements and/or carbon regulations.

On December 10, 1998, the City entered into a lease/leaseback transaction for all of the Deerhaven Unit 1 and a substantial portion of the Deerhaven Unit 2 generating facilities. Under the terms of the transaction, the City entered into a 38-year lease and simultaneously a 20-year leaseback. At the end of the leaseback period term, the City has an option to buy out the remainder of the lease for a fixed purchase option amount.

Management's Discussion and Analysis

Currently Known Facts or Conditions that May Have a Significant Effect on GRU's Financial Condition or Results of Operations (continued)

Under the terms of the transaction, the City continues to own, operate, maintain, and staff the facilities.

The proceeds received by the City from this transaction were approximately \$249 million. From these proceeds, GRU deposited \$142 million as a payment undertaking agreement and a second deposit of \$72 million in the form of a collateralized Guaranteed Investment Contract (GIC), both with Ambac Assurance Corporation (Ambac), a financial guaranty insurance company that also provided credit enhancement for the transaction. The deposit instruments will mature in amounts sufficient to meet the annual payment obligations under the leaseback including the end of term fixed purchase option if elected by GRU.

The net benefit of this transaction, after payment of transaction expenses, was approximately \$35 million and resulted in a deferred gain, which is being amortized as income on a straight-line basis over the leaseback period of 20 years.

On May 17, 2006, President Bush signed into law an act entitled the "Tax Increase Prevention and Reconciliation Act of 2005" (the Act). Among other provisions, the Act imposes an excise tax on certain types of leasing transactions entered into by tax-exempt entities, including states and their political subdivisions (including the City). Based on regulations released by the Internal Revenue Service in 2007, GRU currently anticipates that it will owe little, if any, excise tax under the Act, but this result is not certain given the interpretive questions that still remain with respect to the excise tax.

In November, 2008, Moody's Investors Service and Standard & Poor's downgraded their respective credit ratings of Ambac. Under the terms of the lease/leaseback transaction documents, the City is required to provide substitute credit enhancement within 30 days of the occurrence of Ambac's ratings downgrades. GRU currently is working with its financial advisor and legal counsel to evaluate its options. Based on that evaluation, GRU has determined that the termination of the LILO transaction is the most appropriate action. GRU staff has negotiated the termination price with BNY and has worked with Ambac to value the GIC. The difference between the two amounts is approximately \$13.2 million, and is an obligation of the City. This difference will be paid by GRU upon the closing of the LILO termination scheduled in late February.

GRU currently carries a reserve balance of \$2.25 million, primarily for possible liability related to the oil contamination at the Kelly Generating Station. In July of 2006, GRU was notified by the Florida Department of Environmental Protection (FDEP) that provisions of Chapter 62-780, F.A.C. must be complied with on this site. This Rule is currently being utilized to establish a process and time schedule for assessment and remediation of the site. GRU's liability utilizing

Management's Discussion and Analysis

this Rule is unknown and cannot be reasonably estimated at this time. Therefore, GRU will make no changes to the reserve balance until further information is received and a reasonable estimate can be established.

Requests for Information

This financial report is designed to provide a general overview of the Combined Utility System's finances for all those with an interest in the Combined Utility System's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Chief Financial Officer, City of Gainesville Regional Utilities, P.O. Box 147117, Station A-105, Gainesville, Florida 32614-7117.

Report of Independent Certified Public Accountants

The Honorable Mayor and Members of the City Commission
City of Gainesville, Florida

We have audited the accompanying balance sheets of Gainesville Regional Utilities (a department of the City of Gainesville, Florida) as of September 30, 2008 and 2007, and the related statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These financial statements are the responsibility of Gainesville Regional Utilities' management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States 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. We were not engaged to perform an audit of Gainesville Regional Utilities' internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Gainesville Regional Utilities' internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only Gainesville Regional Utilities (the Combined Utility Fund of the City of Gainesville, Florida) and are not intended to present fairly the financial position of the City of Gainesville, Florida, or the changes in its financial position and cash flows of its proprietary fund types in conformity with accounting principles generally accepted in the United States.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Gainesville Regional Utilities as of September 30, 2008 and 2007, and the changes in financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 10, 2009 on our consideration of Gainesville Regional Utilities' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, 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.

Management's Discussion and Analysis, as listed in the table of contents, is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

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

Ernst + Young LLP

February 10, 2009

Gainesville Regional Utilities

Balance Sheets

	September 30	
	2008	2007
Assets		
Current assets:		
Cash and cash equivalents	\$ 4,568,881	\$ 497,495
Accounts receivable, net of allowance for uncollectible accounts of \$757,161 in 2008 and \$711,287 in 2007	51,428,892	48,982,445
Prepaid rent – lease/leaseback	10,686,909	10,686,909
Fuels contracts	1,167,586	2,753,935
Deferred charges	8,670,229	10,698,039
Inventories:		
Fuel	5,961,105	10,346,461
Materials and supplies	9,935,476	9,047,385
Total current assets	92,419,078	93,012,669
Restricted assets:		
Utility deposits – cash and investments	5,821,407	4,900,401
Debt service – cash and investments	37,683,248	29,560,285
Rate stabilization – cash and investments	63,886,197	52,828,569
Construction Fund – cash and investments	131,330,393	66,740,573
Utility plant improvement fund – cash and investments	24,495,171	16,071,384
Investment in The Energy Authority	2,447,440	2,513,497
Decommissioning reserve – cash and investments	8,529,188	7,594,434
Total restricted assets	274,193,044	180,209,143
Prepaid rent – lease/leaseback	97,963,332	108,650,241
Other noncurrent assets	21,882,979	14,124,276
Capital assets:		
Utility plant in service	1,172,650,704	1,129,689,362
Plant unclassified	1,294,690	9,636,128
Less: accumulated depreciation and amortization	526,333,349	491,739,199
	647,612,045	647,586,291
Plant held for future use	6,053,926	6,053,926
Construction in progress	301,094,810	185,781,802
Net capital assets	954,760,781	839,422,019
Total assets	\$ 1,441,219,214	\$ 1,235,418,348

	September 30	
	2008	2007
Liabilities and net assets		
Current liabilities:		
Fuel payable	\$ 9,297,148	\$ 7,449,745
Accounts payable and accrued liabilities	17,005,247	11,587,288
Operating lease – lease/leaseback	12,461,916	12,461,916
Deferred credits	6,452,527	21,022,919
Due to other funds	3,658,313	3,216,566
Total current liabilities	<u>48,875,151</u>	<u>55,738,434</u>
Payable from restricted assets:		
Utility deposits	5,821,408	4,900,401
Rate stabilization deferred credit	63,886,197	52,828,569
Construction fund:		
Accounts payable and accrued liabilities	10,386,482	6,824,337
Debt payable – current portion	21,984,991	18,555,000
Accrued interest payable	15,907,528	11,053,714
Total payable from restricted assets	<u>117,986,606</u>	<u>94,162,021</u>
Long-term debt:		
Utilities system revenue bonds	708,510,009	535,495,000
Subordinated utilities system revenue bonds	–	62,000,000
Commercial paper notes	62,000,000	–
Unamortized loss on refinancing	(28,600,928)	(31,167,400)
Unamortized bond premium discount	6,693,973	7,836,301
Total long-term debt	<u>748,603,054</u>	<u>574,163,901</u>
Operating lease – lease/leaseback	114,225,173	126,686,285
Other noncurrent liabilities	27,221,470	18,703,314
Total liabilities	<u>1,056,911,454</u>	<u>869,453,955</u>
Net assets:		
Invested in capital assets, net of related debt	322,253,279	319,757,469
Restricted	46,861,035	37,861,548
Unrestricted	15,193,446	8,345,376
Total net assets	<u>384,307,760</u>	<u>365,964,393</u>
Total liabilities and net assets	<u>\$ 1,441,219,214</u>	<u>\$ 1,235,418,348</u>

See accompanying notes.

Gainesville Regional Utilities

Statements of Revenues, Expenses and Changes in Net Assets

	Year Ended September 30	
	2008	2007
Operating revenue:		
Sales and service charges	\$ 333,371,432	\$ 291,686,112
Transfers from (to) rate stabilization	5,088,582	(6,759,131)
Other operating revenue	11,509,582	9,912,886
Total operating revenue	<u>349,969,596</u>	<u>294,839,867</u>
Operating expenses:		
Operation and maintenance	202,704,048	172,451,692
Administrative and general	38,402,370	31,220,383
Depreciation and amortization	44,724,361	40,197,132
Total operating expenses	<u>285,830,779</u>	<u>243,869,207</u>
Operating income	<u>64,138,817</u>	50,970,660
Non-operating income (expense):		
Interest income	9,272,250	11,317,499
Interest expense, net of AFUDC	(28,194,844)	(26,942,796)
Gain on sale of investments	97,050	-
Total non-operating expense	<u>(18,825,544)</u>	<u>(15,625,297)</u>
Income before contributions and transfers	<u>45,313,273</u>	35,345,363
Capital contributions:		
Contributions from developers	4,805,277	14,310,635
Reduction of plant costs recovered through contributions	(323,300)	(171,349)
Net capital contributions	<u>4,481,977</u>	14,139,286
Operating transfer to City of Gainesville General Fund	<u>(31,451,885)</u>	<u>(30,397,527)</u>
Change in net assets	<u>18,343,365</u>	19,087,122
Net assets – beginning of year	<u>365,964,393</u>	346,877,271
Net assets – end of year	<u>\$ 384,307,758</u>	<u>\$ 365,964,393</u>

See accompanying notes.

Gainesville Regional Utilities

Statements of Cash Flows

	Year Ended September 30	
	2008	2007
Operating activities		
Cash received from customers	\$ 331,845,993	\$ 284,077,990
Cash payments to suppliers for goods and services	(168,718,291)	(147,890,172)
Cash payments to employees for services	(52,805,765)	(48,477,008)
Cash payments for operating transactions with other funds	(8,676,985)	(7,968,835)
Other operating receipts	14,823,961	1,379,552
Net cash provided by operating activities	116,468,913	81,121,527
Noncapital financing activities		
Transfers to other funds	(31,451,885)	(30,397,527)
Net cash used in noncapital financing activities	(31,451,885)	(30,397,527)
Capital and related financing activities		
Principal repayments on long-term debt	(80,555,000)	(143,620,000)
Interest paid on long-term debt	(27,049,829)	(34,286,420)
Other receipts	65,200	55,128
Acquisition and construction of fixed assets (including allowance for funds used during construction)	(145,450,660)	(93,100,494)
Proceeds from new debt and commercial paper	257,000,000	139,505,000
Cash received for connection charges	4,436,762	3,143,418
Net cash provided by (used in) capital and related financing activities	8,446,473	(128,303,368)
Investing activities		
Interest received	5,605,430	5,268,057
Purchase of investments	(924,502,246)	(441,486,603)
Investment in The Energy Authority	(1,200,000)	(1,200,000)
Distributions from The Energy Authority	1,266,057	1,215,070
Proceeds from investment maturities	836,699,000	499,350,520
Net cash (used in) provided by investing activities	(82,131,759)	63,147,044
Net change in cash and cash equivalents	11,331,742	(14,432,324)
Cash and cash equivalents, beginning of year	2,107,030	16,539,354
Cash and cash equivalents, end of year	\$ 13,438,772	\$ 2,107,030

Continued on next page.

Gainesville Regional Utilities

Statements of Cash Flows (continued)

	Year Ended September 30	
	2008	2007
Reconciliation of operating income to net cash provided by operating activities		
Operating income	\$ 64,138,817	\$ 50,970,660
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	44,724,361	40,197,132
Operating lease – lease/leaseback revenue	(1,774,203)	(1,774,203)
Increase (decrease) in cash attributable to change in assets and liabilities:		
Receivables	(2,446,447)	(8,006,410)
Fuel contracts	1,586,349	(847,466)
Inventories	3,497,265	(612,892)
Deferred charges	2,993,347	3,590,270
Accounts payable and accrued liabilities	10,827,507	5,761,328
Due to other funds	441,747	204,456
Utility deposits	921,007	398,288
Other liabilities and deferred credits	(8,440,837)	(8,759,635)
Net cash provided by operating activities	\$116,468,913	\$ 81,121,528

Noncash, investing, capital and financing activities

Utility plant contributed by developers in aid of construction was \$4,481,977 and \$14,139,286

See accompanying notes.

Gainesville Regional Utilities

Notes to Financial Statements

Years Ended September 30, 2008 and 2007

1. Summary of Significant Accounting Policies

Organization

Gainesville Regional Utilities (GRU or the Utility) is a combined municipal utility system operating electric, natural gas, water, wastewater, and telecommunications (GRUCom) utilities. GRU consists of the combined Utility Funds of the City of Gainesville, Florida (City). GRU is a unit of the City and, accordingly, the financial statements of GRU are included in the annual financial reports of the City.

Basis of Accounting

The financial statements are presented on the accrual basis of accounting. Under this basis, revenues are recognized in the period earned and expenses are recognized in the period incurred. GRU applies all applicable Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, in accounting for and reporting its operations. In accordance with government accounting standards, GRU has elected not to apply FASB pronouncements issued after that date. In accordance with the Utilities System Revenue Bond Resolution as Supplemented and Amended (Bond Resolution), rates are designed to cover operating and maintenance expense, debt service and other revenue requirements, which exclude depreciation expense and other noncash expense items. This method of rate setting results in costs being included in the determination of rates in different periods than when these costs are recognized for financial statement purposes. The effects of these differences are recognized in the determination of net income in the period that they occur, in accordance with GRU's accounting policies. GRU has adopted the uniform system of accounts prescribed by the Federal Energy Regulatory Commission (FERC) and substantially all provisions of the National Association of Regulatory Utility Commissioners (NARUC). Rates are approved annually by the City Commission.

Gainesville Regional Utilities reports net assets in the following classifications:

- Invested in capital assets, net of related debt – This component of net assets consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, or other long-term borrowings that are attributable to the acquisition, construction, or improvement of those assets. If there are significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of “invested in capital assets, net of related debt.” Rather, that portion of the debt is included in the same net assets component as the unspent proceeds. The costs of capital assets include material, labor, vehicle and equipment usage, related

Gainesville Regional Utilities

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

overhead items, capitalized interest, and certain administrative and general expenses. Maintenance and replacements of minor items are charged to operating expenses. When units of depreciable property are retired, the original cost and removal cost, less salvage, are charged to accumulated depreciation.

- Restricted – This component of net assets consists of net assets subject to external constraints on their use imposed by creditors (such as through debt covenants), contributors, or laws or regulations of other governments or constraints imposed by law through constitutional provisions or enabling legislation.
- Unrestricted net assets – This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amount of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Investments

Investments are reported at fair value in the balance sheets based on quoted market prices. All short-term commercial paper with maturities less than one year have been reported at cost which approximates fair value. More information is provided in Note 5, “Deposits and Investments.”

Risk Management/Futures and Options Contracts

GRU conducts a risk management program with the intent of reducing the impact of fuel price spikes for its customers. The program utilizes futures and options contracts that are traded on the New York Mercantile Exchange (NYMEX) so that prices may be fixed or reduced for given volumes of gas that the utility projects to consume during a given production month. Based on feedback and direction from GRU’s Risk Oversight Committee, consultation and recommendations from reputable risk management sources, and close monitoring of the market on a daily basis, GRU makes every effort to take reasonable steps to minimize the customers’ exposure to fuel spikes while, at the same time, attempting to reduce costs.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

The information below provides a summary of results based on GRU's risk management activity during fiscal years 2008 and 2007.

	September 30	
	2008	2007
Deposits	\$ 2,973,066	\$ 4,961,685
Unrealized gain/(loss)	(1,805,480)	(2,207,750)
Net Investment in derivatives	\$ 1,167,586	\$ 2,753,935

Gains or losses from hedging transactions are applied to GRU's monthly fuel expenses as an offset to fuel cost when recognized. Realized gains and losses related to hedging positions are deferred under the rate-setting policy. During fiscal years 2008 and 2007, GRU recognized losses of \$1 million and \$5.4 million, respectively. Realized, but unrecognized, losses of \$3.1 million and \$3.0 million have been deferred at September 30, 2008 and September 30, 2007, respectively.

Inventories

Inventories are stated at cost using the weighted average unit cost method for materials, and the last-in, first-out (LIFO) method for fuel. Obsolete and unusable items are reduced to estimated salvage values. The cost of fuel used for electric generation is charged to expense as consumed.

Capital Assets

Property and equipment are recorded at cost. Maintenance and repairs are charged to operating expense as incurred. The average cost of depreciable plant retired is eliminated from the plant accounts and charged to accumulated depreciation. Associated cost of removal net of salvage is charged to depreciation expense as incurred. Currently, GRU has a capitalization threshold of \$1,000 for general plant assets.

Plant unclassified includes property and equipment related to projects placed into service that have not been classified in the related asset category within utility plant in service.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Depreciation and Nuclear Generating Plant Decommissioning

An independent evaluation of GRU's depreciation rates and accumulated reserve was performed by an outside consultant in 2004. The study recommended an update to depreciation rates and allowance reserve balances. Depreciation of utility plant is computed using the straight-line method over estimated service lives ranging from 6 to 50 years. GRU implemented the recommended rates in fiscal 2005. The overall depreciation rate was 3.40% in fiscal 2008 and 3.29% in fiscal 2007. Depreciation expense includes a provision for decommissioning costs related to the jointly-owned nuclear power plant (see Note 6).

The cost of nuclear fuel, including estimated disposal cost, is amortized to fuel expense based on the quantity of heat produced for the generation of electric energy in relation to the quantity of heat expected to be produced over the life of the nuclear fuel core. These costs are charged to customers through the fuel adjustment clause.

Revenue Recognition

Revenue is recorded as earned. GRU accrues for services rendered but unbilled, which amounted to approximately \$14,171,000 and \$14,390,000 for 2008 and 2007, respectively. Fuel adjustment revenue is recognized based on the actual fuel costs. Amounts charged to customers for fuel are based on estimated costs, which are adjusted for any differences between the actual and estimated costs once actual fuel costs are known. If the amount recovered through billings exceeds actual fuel costs, GRU records deferred fuel as a liability. If the amount recovered through billings is less than the actual fuel costs, GRU records deferred fuel as an asset, for amounts to be collected through future rates. As of September 30, deferred fuel costs were a receivable of \$3,144,000 and \$5,523,000 in 2008 and 2007, respectively. The deferred fuel balances are reported as part of current deferred charges on the balance sheets.

Transactions with the City of Gainesville

As an enterprise fund of the City of Gainesville, transactions occur between GRU and the City's governmental funds throughout the year in the ordinary course of operations. Below is a summary of significant transactions:

- Administrative Services – GRU is billed monthly for various administrative and insurance services provided by the City's governmental functions. In FY2008, GRU paid \$1.6 million for joint services.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

- Nonmetered and Metered Service Charges – GRU bills the City’s governmental funds on a monthly basis for all nonmetered, metered and other administrative services. In FY2008, GRU billed the City \$4.7 million for these services.
- Transfers to the general fund – GRU budgets an annual transfer to the general fund based on a City Commission approved formula. See Note 11 for details.

Funds in Accordance with Bond Resolutions

Certain restricted funds of GRU are administered in accordance with bond resolutions. These funds are as follows:

- Debt Service Fund
- Subordinated Indebtedness Fund
- Rate Stabilization Fund
- Construction Fund
- Utility Plant Improvement Fund

The Debt Service Fund accounts for funds accumulated to provide payment of principal and interest on or redeem outstanding debt.

The Subordinated Indebtedness Fund, grouped in the Debt Service Fund for financial reporting purposes, accounts for funds accumulated to pay principal and interest on subordinated indebtedness.

The Rate Stabilization Fund accounts for funds accumulated to stabilize rates over future periods through the transfer of funds to and from operations as necessary and to provide operating reserves for the Utility.

The Construction Fund accounts for funds accumulated for the cost of acquisition and construction of the system.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

The Utility Plant Improvement Fund accounts for funds used to pay for certain capital projects or debt service, the purchase or redemption of bonds, or otherwise provide for the repayment of bonds.

When both restricted and unrestricted resources are available for use, it is GRU's policy to use restricted resources first, then unrestricted resources as they are needed.

Operating, Non-operating Revenues

GRU has defined operating revenue as that revenue which is derived from customer sales or service while non-operating revenues include interest on investments and any gain from the sale of such investments. Substantially all of GRU's revenues are pledged to the repayment of revenue bonds.

Allowance for Funds Used During Construction (AFUDC)

An allowance for interest on borrowed funds used during construction of \$2,599,000 and \$359,000 in 2008 and 2007, respectively, is included in construction in progress and as a reduction of interest expense. These amounts are computed by applying the effective interest rate on the funds borrowed to finance the projects to the monthly balance of projects under construction. The effective interest rate was approximately 4.37%.

Contributions in Aid of Construction

GRU recognizes capital contributions to the water, wastewater and GRUCom divisions, from developers and other third parties as revenues in the period received. Contributions to the electric and gas divisions are also reported as capital contribution revenues; however, the related capital asset amounts are also expensed in the same period consistent with the requirements of the FERC Uniform System of Accounts.

Cash and Cash Equivalents

For purposes of reporting cash flows, cash and cash equivalents include cash on hand, bank demand accounts, and overnight repurchase agreements.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

1. Summary of Significant Accounting Policies (continued)

Unamortized Loss on Refinancing

Losses resulting from the refinancing of bonds are deferred and amortized over the remaining life of the old debt or the life of the new debt, whichever is shorter.

2. Rates and Regulation

GRU's rates are established in accordance with the Utilities System Bond Resolution and the Utilities System Subordinated Bond Resolution as adopted and amended. Under these documents, rates are set to recover Operation and Maintenance Expenses, Debt Service, Utility Plant Improvement Fund contributions, and costs for any other lawful purpose such as the General Fund Transfer.

Each year during the budgeting process, and at any other time necessary, the City Commission approves rate changes and other changes to GRU's charges.

GRU's cost of fuel for the electric and natural gas systems is passed directly through to its customers. Each month, GRU staff estimates the cost of fuel and consumption for both the electric and natural gas systems. These estimates are combined with a true-up for actual costs from previous months into a current-month electric fuel adjustment and natural gas purchased gas adjustment. Amounts overbilled or underbilled are passed along to customers and are either accrued or deferred at year-end.

The Florida Public Service Commission does not regulate rate levels in any of GRU's utilities. They do, however, have jurisdiction over rate structure for the electric system.

Currently, GRU prepares its financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 71, and records various regulatory assets and liabilities. For a company to report under SFAS No. 71, the company's rates must be designed to recover its costs of providing services, and the company must be able to collect those rates from customers. If it were determined, whether due to competition or regulatory action, that these standards no longer applied, GRU could be required to write off its regulatory assets and liabilities. Management believes that GRU currently meets the criteria for continued application of SFAS No. 71, but will continue to evaluate significant changes in the regulatory and competitive environment to assess continuing applicability of the criteria.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

3. Capital Assets and Changes in Accumulated Depreciation

A summary of capital assets, changes in accumulated depreciation and related depreciation provisions expressed as a percentage of average depreciable plant follows:

	Plant in Service					CWIP/Plant held for Future Use	Combined
	Treatment	Generation	Transmission, Distribution and Collection	General	Unclassified		
Balance, October 1, 2007	\$ 111,305,936	\$ 360,815,534	\$ 573,771,771	\$ 83,796,119	\$ 9,636,128	\$ 191,835,728	\$ 1,331,161,216
Capital additions and transfers	3,278,716	839,222	39,445,779	3,979,923	38,020,397	156,484,960	242,048,997
Sales, retirements and transfers	756,311	3,051,270	774,715	-	46,361,835	41,171,952	92,116,083
Balance, September 30, 2008	<u>\$ 113,828,341</u>	<u>\$ 358,603,486</u>	<u>\$ 612,442,835</u>	<u>\$ 87,776,042</u>	<u>\$ 1,294,690</u>	<u>\$ 307,148,736</u>	<u>\$ 1,481,094,130</u>
Accumulated depreciation, October 1, 2007	\$ 48,464,065	\$ 198,202,248	\$ 205,424,695	\$ 38,971,168	\$ 677,023	n/a	\$ 491,739,199
Depreciation expense	3,948,871	9,926,731	18,817,722	6,575,999	56,758	n/a	39,326,081
Retirements/adjustments	756,311	-	3,825,807	(65,200)	215,013	n/a	4,731,931
Accumulated depreciation, September 30, 2008	<u>\$ 51,656,625</u>	<u>\$ 208,128,979</u>	<u>\$ 220,416,610</u>	<u>\$ 45,612,367</u>	<u>\$ 518,768</u>	n/a	<u>\$ 526,333,349</u>
Average depreciation rate	<u>3.51%</u>	<u>2.76%</u>	<u>3.17%</u>	<u>7.67%</u>	<u>1.04%</u>	n/a	<u>3.40%</u>

	Plant in Service					CWIP/Plant held for Future Use	Combined
	Treatment	Generation	Transmission, Distribution and Collection	General	Unclassified		
Balance, October 1, 2006	\$ 109,677,811	\$ 354,276,054	\$ 553,684,313	\$ 66,584,468	\$ 9,063,632	\$ 130,635,433	\$ 1,223,921,711
Capital additions and transfers	1,730,760	8,136,708	21,455,959	21,301,766	52,495,380	115,037,440	220,158,013
Sales, retirements and transfers	102,635	1,597,227	1,368,501	4,090,115	51,922,884	53,837,145	112,918,507
Balance, September 30, 2007	<u>\$ 111,305,936</u>	<u>\$ 360,815,536</u>	<u>\$ 573,771,771</u>	<u>\$ 83,796,119</u>	<u>\$ 9,636,128</u>	<u>\$ 191,835,728</u>	<u>\$ 1,331,161,218</u>
Accumulated depreciation, October 1, 2006	\$ 44,753,789	\$ 189,863,548	\$ 189,280,483	\$ 38,124,845	\$ 359,878	n/a	\$ 462,382,543
Depreciation expense	3,812,913	9,828,319	17,512,093	4,879,748	677,023	n/a	36,710,096
Retirements/adjustments	102,635	1,489,620	1,367,882	4,033,425	359,878	n/a	7,353,440
Accumulated depreciation, September 30, 2007	<u>\$ 48,464,067</u>	<u>\$ 198,202,247</u>	<u>\$ 205,424,694</u>	<u>\$ 38,971,168</u>	<u>\$ 677,023</u>	n/a	<u>\$ 491,739,199</u>
Average depreciation rate	<u>3.45%</u>	<u>2.75%</u>	<u>3.11%</u>	<u>6.49%</u>	<u>7.24%</u>	n/a	<u>3.29%</u>

Gainesville Regional Utilities

Notes to Financial Statements (continued)

4. Long-Term Debt

Long-term debt outstanding at September 30, 2008 and 2007, consisted of the following:

	September 30	
	2008	2007
<u>Utilities System Revenue Bonds:</u>		
Series 1983 (1983 Bonds) – interest payable semi-annually to October 1, 2014 at a rate of 6.00%	\$ 4,675,000	\$ 4,675,000
1992 Series B (1992 B Bonds) – interest payable semi-annually to October 1, 2013 at various rates between 6.50% and 7.50%	24,630,000	24,630,000
1996 Series A (1996 A Bonds) – interest payable semi-annually to October 1, 2009 at rates between 5.00% and 5.75%	7,720,000	10,595,000
2002 Subordinated Series A (2002 Series A) – interest at variable rates; 2.80% at April 30, 2008 (Date of Redemption)	–	25,300,000
2002 Subordinated Series B (2002 Series B) – interest at variable rates; 2.83% at May 7, 2008 (Date of Redemption)	–	40,000,000
2003 Series A (2003 A Bonds) – interest payable semi-annually to October 1, 2023 at rates between 4.625% and 5.25%	7,525,000	7,525,000
2003 Series B (2003 B Bonds) – interest payable semi-annually to October 1, 2013 at a 4.4% interest rate (Federally Taxable)	4,960,000	5,670,000
2003 Series C (2003 C Bonds) – interest payable semi-annually to October 1, 2013 at rates between 4.00% and 5.00%	85,380,000	96,300,000
2005 Series A (2005 A Bonds) – interest payable semi-annually to October 1, 2036 at rates between 4.75% and 5.00%	91,820,000	91,820,000
2005 Series B (2005 B Bonds) – interest payable semi-annually to October 1, 2021 at rates between 5.14% and 5.31%	60,840,000	61,590,000
2005 Series C (2005 C Bonds) – interest payable semi-annually to October 1, 2026, interest at variable market rates; 4.25% at September 30, 2008	55,135,000	55,135,000
2006 Series A (2006 A Bonds) – interest payable semi-annually to October 1, 2026, interest at variable market rates; 4.30% at September 30, 2008	53,305,000	53,305,000
2007 Series A (2007 A Bonds) – interest payable semi-annually to October 1, 2036, interest at variable market rates; 7.91% at September 30, 2008	139,505,000	139,505,000
2008 Series A (2008 A Bonds) – interest payable semi-annually to October 1, 2020 at rates between 2.98% and 5.27%	105,000,000	–
2008 Series B (2008 B Bonds) – interest payable semi-annually to October 1, 2038, interest at variable market rates; 8.00% at September 30, 2008	90,000,000	–
Utilities System Commercial Paper Notes, Series C (C Notes), interest at variable market rate; 4.75% at September 30, 2008	62,000,000	–
Current portion of long-term debt	(21,984,991)	(18,555,000)
Unamortized loss on refinancing	(28,600,928)	(31,167,400)
Unamortized premium discount	6,693,973	7,836,301
Total long-term debt	\$ 748,603,054	\$ 574,163,901

Gainesville Regional Utilities

Notes to Financial Statements (continued)

4. Long-Term Debt (continued)

The 1983 Bonds mature on October 1, 2014. Those Bonds are subject to redemption at the option of the City as a whole at any time or in part on any interest payment date, at a redemption price of 100% plus accrued interest to the date of redemption.

The 1992B Bonds mature at various dates from October 1, 2001 to October 1, 2013. Those bonds maturing on or after October 1, 2004 to October 1, 2007, amounting to \$14.3 million were redeemed at the option of the City on October 1, 2002.

The 1996A Bonds matured at various dates through October 1, 2026. Those Bonds maturing on or after October 1, 2010 were subject to redemption at the option of the City on or after October 1, 2006 as a whole or in part at any time at a redemption price of 102% in 2006, 101% in 2007, and 100% thereafter. In August 2003, the 2003C Utility System Revenue Bonds were issued to advance-refund to the maturity dates a portion of the bonds maturing from October 1, 2004 through October 1, 2008 (\$6.235 million). The bonds were defeased, in substance, and will be paid from escrowed funds. There were \$1,390,000 in defeased bonds outstanding as of September 30, 2008. In November 2005, the 2005 Series C Bonds were issued to advance-refund to the maturity dates a portion (\$53,190,000) of the bonds maturing from October 1, 2010 to October 1, 2026. In July 2006, the 2006 Series A Bonds were issued to refund to the maturity dates the remainder (\$51,675,000) of the bonds maturing from October 1, 2010 to October 1, 2026. The proceeds related to the refunded Bonds for both series were deposited into an escrow account to refund the Bonds on October 1, 2006 at 102% of par.

The 2002A Subordinated Utilities System Revenue Bonds mature on October 1, 2017. The 2002B Subordinated Utility System Revenue Bonds mature on October 1, 2032. The 2002A and 2002B Series Bonds were issued as multi-modal variable interest-rate bonds, initially issued as variable-rate auction notes. In April 2008, the Utilities System Commercial Paper Notes, Series C, were issued to refund the 2002 Series A Bonds (\$22,000,000) and 2002 Series B Bonds (\$40,000,000). This refunding is anticipated to result in approximately \$888,000 of net present value savings for GRU, with yearly cash savings from approximately \$5,000 to \$110,000.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

4. Long-Term Debt (continued)

The 2003A Utilities System Revenue Bonds mature on various dates from October 1, 2015 through October 1, 2033. The 2003B Bonds mature on various dates from October 1, 2005 through October 1, 2013. The 2003A Bonds maturing on or after October 1, 2013 are subject to redemption at the option of the City on or after October 1, 2013 at 100%. In March 2007, the 2007 Series A Bonds (\$139,505,000) were issued to advance-refund to the maturity dates a portion of the bonds maturing from October 1, 2020 to October 1, 2033. The proceeds related to the refunded Bonds were deposited into an escrow account to refund the Bonds on October 1, 2013 at 100% of par. The 2003B Bonds maturing are not subject to redemption prior to maturity. The 2003C Utilities System Revenue Bonds mature at various dates from October 1, 2004 to October 1, 2013. The 2003C bonds are not subject to redemption prior to maturity.

On November 16, 2005, the City issued Utilities System Revenue Bonds, Series 2005A, 2005B, and 2005C in the amounts of \$196,950,000, \$61,590,000, and \$55,135,000 respectively. The 2005A Bonds were issued to (a) pay a portion of the cost of acquisition and construction of certain improvements to the City's electric, natural gas, water, wastewater and telecommunications systems and (b) to refund the City's Utilities System Commercial Paper Notes, Series C. The 2005B Bonds were issued to (a) pay a portion of the cost of acquisition and construction of certain improvements to the System and (b) to refund the City's Utilities System Commercial Paper Notes, Series D. The 2005C Bonds were issued to refund a portion of the City's outstanding Utilities System Revenue Bonds, 1996 Series A. The 2005A Bonds mature on various dates from October 1, 2021 to October 1, 2036. The 2005B Bonds mature on various dates from October 1, 2015 to October 1, 2021. The 2005C Bonds mature on various dates from October 1, 2010 to October 1, 2026. The 2005A Bonds will be subject to redemption at the option of the City on and after October 1, 2015 as a whole or in part at any time, at a redemption price of 100% of the principal amount, plus accrued interest to the date of redemption. In March 2007, the 2007 Series A Bonds (\$139,505,000) were issued to advance-refund to the maturity dates a portion of the 2005A bonds maturing from October 1, 2030 to October 1, 2036. The proceeds related to the refunded Bonds were deposited into an escrow account to refund the Bonds on October 1, 2015 at 100% of par. The 2005B Bonds will be subject to redemption prior to maturity at the option of the City, in whole or in part, on any date, at a redemption price equal to the greater of: (i) 100% of the principal amount of the Bonds to be redeemed, plus accrued and unpaid interest on the Bond; or (ii) the sum of the present values of the remaining scheduled payments of principal and interest on the Bonds to be redeemed discounted to the date of redemption on a semiannual basis plus 12.5 basis points. The 2005C Bonds will be subject to redemption prior to maturity at the election of the City at a redemption price of 100 percent of the principal amount plus accrued interest. The 2005C Bonds created a net present value savings of over \$6,700,000, with yearly cash savings ranging from approximately \$370,000 to over \$1,085,000.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

4. Long-Term Debt (continued)

On July 6, 2006, the City issued Utilities System Revenue Bonds, Series 2006A in the amount of \$53,305,000. The 2006A Bonds mature on various dates from October 1, 2010 to October 1, 2026. The 2006A Bonds were issued to refund a portion of the City's outstanding Utilities System Revenue Bonds, 1996 Series A and to pay costs of acquisition and construction of the City's utilities system. The 2006A Bonds will be subject to redemption prior to maturity at the election of the City as follows, in whole or in part, at a redemption price of 100 percent of the principal amount plus accrued interest to the redemption date. The 2006A Bonds created a net present value savings of over \$6,200,000, with yearly cash savings ranging from approximately \$371,000 to over \$890,000.

On February 13, 2008, the City issued Utilities System Revenue Bonds, Series 2008A in the amount of \$105,000,000 and Utilities System Revenue Bonds, Series 2008B in the amount of \$90,000,000. The 2008A Bonds mature on various dates from October 1, 2009 to October 1, 2020. The 2008B Bonds mature on various dates from October 22, 2022 to October 1, 2038. The 2008A Bonds and the 2008B Bonds were issued to pay costs of acquisition and construction of the City's utilities system. The 2008A Bonds will be subject to redemption prior to maturity at the election of the City as follows, in whole or in part, at a redemption price of 100 percent of the principal amount plus accrued interest to the redemption date. The 2008B Bonds will be subject to redemption prior to maturity at the election of the City as follows, in whole or in part, at a redemption price of 100 percent of the principal amount plus accrued interest to the redemption date.

Utilities System Commercial Paper Notes, Series C Notes (tax-exempt) in a principal amount not to exceed \$85 million may continue to be issued to refinance maturing Series C Notes or provide for other costs. Liquidity support for the Series C Notes is provided under a long-term credit agreement dated as of March 1, 2000 with Bayerische Landesbank Girozentrale. This agreement has been extended to November 30, 2015. The obligation of the bank may be substituted by another bank which meets certain credit standards and which is approved by GRU and the Agent. Under the terms of the agreement, GRU may borrow up to \$85 million with same day availability ending on the termination date, as defined in the agreement. There are \$62,000,000 of Series C Notes outstanding as of September 30, 2008 and no Series C Notes outstanding as of September 30, 2007.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

4. Long-Term Debt (continued)

In June 2000, a Utilities System Commercial Paper Note Program, Series D (taxable) was established in a principal amount not to exceed \$25 million. Liquidity support for the Series D Notes was provided under a long-term credit agreement dated June 1, 2000 with SunTrust Bank. This agreement has been extended to September 14, 2009. The obligation of the bank may be substituted by another bank that meets certain credit standards and is approved by GRU. Under the terms of the agreement, GRU may borrow up to \$25 million with same day availability ending on the termination date, as defined in the agreement. There are no Series D Notes outstanding as of September 30, 2008 or September 30, 2007.

GRU is required to make monthly deposits into separate accounts for an amount equal to the required share of principal and interest becoming payable for the revenue bonds on the payment dates of April 1 and October 1.

The following table lists the Debt Service requirements (principal and interest) on long-term debt outstanding at September 30, 2008:

Period ending September 30	Principal	Interest	Total Debt Service Requirements ⁽¹⁾
2009	\$ 21,985,000	\$ 26,814,925	\$ 48,799,925
2010	29,875,000	44,164,050	74,039,050
2011	31,245,000	42,786,530	74,031,530
2012	32,650,000	41,306,456	73,956,456
2013	34,140,000	39,741,600	73,881,600
2014 – 2018	167,460,000	173,635,240	341,095,240
2019 – 2023	125,765,000	135,719,676	261,484,676
2024 – 2028	112,845,000	105,028,542	217,873,542
2029 – 2033	139,535,000	68,045,558	207,580,558
2034 – 2038	96,995,000	21,630,168	118,625,168
	<u>\$ 792,495,000</u>	<u>\$ 698,872,745</u>	<u>\$ 1,491,367,745</u>

(1) Interest rates on variable-rate long-term debt were valued to be equal to 4.25% for the 2005C Series Bonds, 4.30% for the 2006A Series Bonds, 7.91% for the 2007A Series Bonds, 8.00% for the 2008B Series Bonds and 4.75% for the 2008 TECP. These are the rates in effect as of September 30, 2008.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

4. Long-Term Debt (continued)

The interest rates used in this table are per GASB 38, which requires the rate used in the calculations be that in effect as of September 30, 2008. At that time there was significant market unrest driving rates high for a short time. Rates are considerably lower now. Management believes these future debt service requirements are substantially overstated.

The table below shows the changes in net long-term debt balances that occurred during the years ended September 30, 2008 and 2007.

	September 30	2008	2007
Long-term debt outstanding at beginning of year	\$574,163,901	\$ 592,314,742	
Changes in long-term debt:			
Series 2007A issued	–	139,505,000	
Series 2008A issued	105,000,000	–	
Series 2008B issued	90,000,000	–	
TECP issued during the year	62,000,000	–	
Fixed rate debt redeemed – Senior Lien and Subordinated	(21,984,991)	(18,555,000)	
Series 2002A refunded	(22,000,000)	–	
Series 2002B refunded	(40,000,000)	–	
Series 2003A refunded (partial)	–	(25,475,000)	
Series 2005A refunded (partial)	–	(105,130,000)	
Change in unamortized loss/bond discount	1,424,144	(8,495,841)	
Long-term debt outstanding at end of year	\$748,603,054	\$ 574,163,901	
Current portion of long-term debt	\$ 21,984,991	\$ 18,555,000	

Under the terms of the Bond Resolution relating to the sale of the Utilities System Revenue Bonds, payment of the principal and interest is secured by an irrevocable lien on GRU's net revenue (exclusive of any funds which may be established pursuant to the Bond Resolution for decommissioning and certain other specified purposes), including any investments and income thereof.

The Bond Resolution contains certain restrictions and commitments, including GRU's covenant to establish and maintain rates and other charges to produce revenue sufficient to pay operation and maintenance expenses, amounts required for deposit in the debt service fund, and amounts required for deposit into the utility plant improvement fund.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

4. Long-Term Debt (continued)

Derivatives

GRU is a party to certain interest rate swap agreements, which are not recorded in the financial statements. Following is a disclosure of key aspects of the agreements.

Objective of the interest rate swap. To protect against the potential of rising interest rates, the City has entered into three separate floating-to-fixed interest rate swap transactions.

Terms, fair values and credit risk. The terms, fair values and credit ratings of the outstanding swaps as of September 30, 2008, were as follows. The notional amounts of the swaps match the principal amounts of the associated debt.

Associated Bond Issue	2008CP*	2005B*	2005C *
Notional Amounts	\$ 25,300,000	\$ 45,000,000	\$ 55,135,000
Effective Date	7/3/2002	11/16/2005	11/16/2005
Fixed Payer Rate	4.100%	BMA	3.200%
Variable Receiver Rate	BMA	77.14% of LIBOR	68% of LIBOR
Fair Value	\$ (1,263,770)	\$ (642,806)	\$ (359,645)
Termination Date	10/1/2017	10/1/2021	10/1/2026
Counterparty Credit Rating	A2/A/A+	Aaa/AAA	Aaa/AAA
Associated Bond Issue	2006A *	2008B *	2008B *
Notional Amounts	\$ 53,305,000	\$ 58,500,000	\$ 31,500,000
Effective Date	7/6/2006	2/1/2008	2/1/2008
Fixed Payer Rate	3.224%	4.222%	4.222%
Variable Receiver Rate	68% of 10 YR LIBOR	BMA	BMA
Fair Value	\$ (327,021)	\$ (3,799,930)	\$ (2,076,216)
Termination Date	10/1/2026	10/1/2038	10/1/2038
Counterparty Credit Rating	Aaa/AAA	Aaa/AAA	Aaa/AA/AA-

Gainesville Regional Utilities

Notes to Financial Statements (continued)

4. Long-Term Debt (continued)

Associated Bond Issue	2007A*
Notional Amounts	\$ 139,505,000
Effective Date	3/1/2007
Fixed Payer Rate	3.944%
Variable Receiver Rate	BMA
Fair Value	\$ (3,387,603)
Termination Date	10/1/2036
Counterparty Credit Rating	Aaa/AAA

* See “basis risk” in Note 4, Long-Term Debt.

Fair Value. All seven of the swap agreements currently have a negative fair value as of September 30, 2008. Due to the low interest rate environment, as compared to the period when the swaps were entered into, our fixed payer rates currently exceed the variable receiver rates. This is anticipated to be a short term event. These swaps are based on a different variable receiver rate, which is partially responsible for the difference in performance.

Swap payments and associated debt. Assuming interest rates remain the same at September 30, 2008, debt service requirements on the auction rate notes and the interest rate swap would be as follows:

Fiscal Year Ending Sept 30	Variable Rate		Fixed Rate		Interest Rate Swaps, Net	Total
	Principal	Interest	Principal	Interest		
2009	\$ 245,000	\$ 16,752,883	\$ 790,000	\$ 3,186,773	\$ 461,739	\$ 21,436,395
2010	255,000	25,785,741	830,000	3,145,139	461,295	30,477,175
2011	6,155,000	25,639,290	875,000	3,101,320	425,969	36,196,579
2012	6,360,000	25,361,995	920,000	3,055,189	389,469	36,086,653
2013	6,580,000	25,075,161	965,000	3,006,745	351,730	35,978,636
2014-2018	62,205,000	118,021,680	25,395,000	12,699,640	1,733,490	220,054,810
2019-2023	47,045,000	105,290,272	31,065,000	2,933,111	3,367,149	189,700,532
2024-2028	59,570,000	89,285,861	-	-	2,724,254	151,580,115
2029-2033	114,880,000	62,150,226	-	-	1,749,638	178,779,864
2034-2038	96,650,000	17,728,698	-	-	505,653	114,884,351
Total	\$ 399,945,000	\$ 511,091,807	\$ 60,840,000	\$ 31,127,917	\$ 12,170,386	\$ 1,015,175,110

Gainesville Regional Utilities

Notes to Financial Statements (continued)

4. Long-Term Debt (continued)

The interest rates used in this table are per GASB Technical Bulletin 2003-1, which requires the rate used in the calculations be that in effect as of September 30, 2008. At that time there was significant market unrest driving rates high for a short time. Rates are considerably lower now. Thus management believes these future debt service requirements are substantially overstated.

Credit Risk. As of September 30, 2008, the fair value of all of the swaps were negative, therefore the City is not subject to credit risk. To mitigate the potential for credit risk, the City has negotiated additional termination event and collateralization requirements in the event of a ratings downgrade. Failure to deliver the Collateral Agreement to the City as negotiated and detailed in the Schedule to the International Swap and Derivative Agreement (ISDA) for each counterparty would constitute an event of default with respect to that counterparty.

Basis Risk. The swaps expose the City to basis risk. The 2008 swap (formerly the 2002A swap) is exposed to the difference between the weekly BMA index and a 35-day rollover based on current market conditions. As a result, savings may not be realized. As of September 30, 2008, BMA/SIFMA was 7.96%. The 2005B Swap is exposed to basis risk through the potential mismatch of 77.14% of LIBOR and the BMA rate. The swap for the 2005C Series is exposed to basis risk through the potential mismatch of 68% of 1-month LIBOR and the BMA rate. As of September 30, 2008, the one-month LIBOR rate was at 3.92%, which places the BMA at approximately 203.00% of LIBOR on that date. The swap for the 2006A Series is exposed to basis risk through the potential mismatch of 68% of 10-year LIBOR less .365% and the BMA rate. As of September 30, 2008, the 10-year LIBOR rate was 4.37%, while the BMA traded at approximately 182.21% of this rate. The 2007A swap is exposed to the difference between the BMA index and a 31-day rollover.

Termination Risk. The swap agreement will be terminated at any time if certain events occur that result in one party not performing in accordance with the agreement. The swap can be terminated due to illegality, a credit event upon merger, or an event of default and illegality. The swap can also be terminated if credit ratings fall below established levels.

5. Deposits and Investments

Deposits are held in qualified public depository institutions insured by the Federal Depository Insurance Corporation up to the applicable limits and, as required by the Bond Resolution, in banks, savings and loan associations, trust companies of the United States or national banking associations having capital stock, surplus and undivided earnings aggregating at least \$10 million.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

5. Deposits and Investments (continued)

In accordance with state laws and the Bond Resolution, GRU is authorized to invest in obligations which are unconditionally guaranteed by the United States of America or its agencies or instrumentalities, repurchase agreement obligations unconditionally guaranteed by the United States of America or its agencies, corporate indebtedness, direct and general obligations of any state of the United States of America or of any agency, instrumentality or local governmental unit of any such state (provided such obligations are rated by a nationally recognized bond rating agency in either of its two highest rating categories), public housing bonds, and certain certificates of deposit. Investments in corporate indebtedness must be rated in the highest rating category of a nationally recognized rating agency and in one of the two highest rating categories of at least one other nationally recognized rating agency.

As of September 30, 2008, GRU had the following investments and maturities (amounts are in thousands).

Investment Type	Maturities in Years		
	Fair Value	Less than 1	1-5
Commercial Paper	\$ 98,025	\$ 98,025	\$ —
U.S. Agencies	155,539	3,952	151,587
Total	\$ 253,564	\$ 101,977	\$ 151,587

Interest Rate Risk: GRU's investment policy limits its investments to securities with terms of ten years or less to reduce exposure to rising interest rates, unless investments are matched to meet specific cash flow needs. Additionally, the average portfolio term is not to exceed seven years. GRU's Bond Resolution further limits investments in the Utility Plant Improvement Fund and Rate Stabilization Fund to five years.

Credit Risk: GRU's investment policy and Bond Resolution limits investments in state and local taxable or tax exempt debt, corporate fixed income securities and other corporate indebtedness to investments that are rated by a nationally recognized rating agency in its highest rating category, and at least one other nationally recognized rating agency in either of its two highest rating categories. As of September 30, 2008, all of GRU's commercial paper investments were rated P-1 or better by Moody's Investor Services and/or A-1 or better by Standard and Poor's and/or F1 or better by Fitch.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

5. Deposits and Investments (continued)

Concentration of Credit Risk: State law does not limit the amount that may be invested in any one issuer. It does require, however, that investments be diversified to control risk of loss from over concentration of assets. As of September 30, 2008, GRU had more than 5% of the investment portfolio of the following:

	Percent of Total Investments
Issuer:	
Federal National Mortgage Association	10.94%
Federal Home Loan Bank	23.37%
Federal Home Loan Mortgage Corporation	19.22%

Cash and investments are contained in the following balance sheet accounts as of September 30:

	2008	2007
Restricted assets	\$274,193,044	\$ 180,209,143
Current assets:		
Cash and cash equivalents	4,568,881	497,495
Total cash and investments	278,761,925	180,706,638
Less cash and cash equivalents	(13,438,772)	(2,107,030)
Less Investment in TEA	(2,447,440)	(2,513,497)
Less CR3 Decommissioning Reserve	(8,529,188)	(7,594,434)
Less accrued interest receivable and accounts receivable	(782,299)	(132,996)
Total investments	<u>\$253,564,226</u>	<u>\$ 168,358,681</u>

6. Jointly Owned Electric Plant

GRU-owned resources for supplying electric power and energy requirements include its 1.4079% undivided ownership interest in Crystal River Unit 3 (CR3) nuclear power plant operated by Progress Energy. GRU's net investment in CR3 at September 30, 2008 and 2007 is approximately \$10,942,500 and \$9,971,000 respectively. CR3 operation and maintenance costs, which represent GRU's part of expenses attributable to operation of CR3, are recorded in accordance with the instructions as set forth in the FERC uniform system of accounts. Payments are made to Progress Energy in accordance with the CR3 participation agreement.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

6. Jointly Owned Electric Plant (continued)

GRU, as a part of this participation agreement, is responsible for its share of future decommissioning costs. Decommissioning costs are funded and expensed annually and are recovered through rates charged to customers. The most recent decommissioning cost estimates provided by Progress Energy in September 2006, estimated GRU's share of the total projected decommissioning funding requirements to be \$7,744,000 of which \$4,874,000 has already been deposited. This \$7,744,000 is expected, with reinvestment and interest earnings, to reach \$24,654,207 in total which will be used in 2041 to pay for the projected costs of decommissioning the plant. The market value of the funds on deposit as of September 30, 2008 is \$8,529,000.

7. Restricted Net Assets

Certain assets are restricted by bond resolution and other external requirements. Following is a summary of the computation of restricted net assets at September 30, 2008 and 2007, and the restricted purposes of the net asset balances:

	2008	2007
Restricted net assets:		
Total restricted assets	\$ 274,193,044	\$ 180,209,143
Unspent debt proceeds	(131,330,393)	(66,740,573)
Payable from restricted assets	(96,001,616)	(75,607,022)
Restricted net assets	\$ 46,861,035	\$ 37,861,548

Net assets are restricted as follows:

	2008	2007
Debt covenants:		
Debt service	\$ 11,389,236	\$ 11,682,233
Utility plant improvement	24,495,171	16,071,384
Total restricted pursuant to debt covenants	35,884,407	27,753,617
Other restrictions:		
Investment in The Energy Authority	\$ 2,447,440	\$ 2,513,497
Nuclear decommissioning reserve	8,529,188	7,594,434
Total other restrictions	10,976,628	10,107,931
Restricted net assets	\$ 46,861,035	\$ 37,861,548

Gainesville Regional Utilities

Notes to Financial Statements (continued)

8. Retirement Plans

The City sponsors and administers one defined benefit pension plan and two defined contribution plans (collectively, the Plans) that include GRU and other City employees. The Plans do not make separate measurements of assets and pension benefit obligations for individual units of the City. Such information is presented in the City of Gainesville, Florida, September 30, 2008, Comprehensive Annual Financial Report.

The General Employees Pension Plan (Employees Plan), a contributory defined benefit pension plan, covers all employees of GRU, except certain limited personnel who elect to participate only in a defined contribution plan.

The City accounts for and funds the costs of the Employee Plan as they accrue. Such costs are based on contribution rates determined by the most recent actuarial valuation. The total contributions by GRU, including amortization of prior service costs, were \$2,206,600 and \$1,826,200 for the years ended September 30, 2008 and 2007, respectively.

Certain limited employees are eligible to participate in defined contribution plans managed by outside fiscal agents for the City. Under the first plan, the City contributes a percentage of an employee's annual salary and employees contribute a specified percentage. All employees have the option to participate in the second defined contribution plan. The total defined contribution cost for GRU for the years ended September 30, 2008 and 2007, was \$108,900 and \$101,600, respectively.

9. Postretirement Benefits

In addition to providing pension benefits, the City provides certain health care insurance benefits for retired employees of the City and GRU. The City also permits retirees to participate in the life insurance program. Most permanent full and part-time employees who are eligible for normal, early, or disability retirement are eligible for these benefits. Individual benefits are the same for all employees, but the cost to the City may vary. Contributions by the City to fund these benefits are neither mandated nor guaranteed. The actuarial costs of these plans are determined and funded by the City. A portion of this funding comes from bonds issued by the City to cover Post Employment Benefits. GRU contributes 0.5% of payroll to fund the remaining portion. The cost of providing these benefits for the GRU retirees for the fiscal years ended September 30, 2008 and 2007 was \$256,100 and \$236,000, respectively.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

10. Disaggregation of Receivables and Payables

Receivables

For the years ended September 30, 2008 and 2007 respectively, net accounts receivable represent 82.8% and 88.8% from customers for billed and unbilled utility services, and 17.2% and 11.2% from other receivables. There are no receivables expected to take longer than one year to collect.

Payables

As of September 30, 2008 and 2007 respectively, payable balances represent 23.0% and 25.6% related to fuels payable, 53.9% and 47.1% to standard vendor payables, 8.7% and 10.9% to accrued vacation payable, 9.1% and 11.1% to intergovernmental payables and 5.3% and 5.3% to other payables.

11. Transfers to General Fund

GRU makes transfers to the City's general government based on a pre-defined formula that predominantly ties the transfer directly to the financial performance of the system. The transfer to the general fund may be made only to the extent such moneys are not necessary to pay operating and maintenance expenses and to pay debt service on the outstanding bonds and subordinated debt or to make other necessary transfers under the Bond Resolution. The formula-based fund transfer to the general fund for the years ended September 30, 2008 and 2007 was \$31,451,885 and \$30,397,527, respectively.

12. Deferred Charges

Deferred charges are presented on the balance sheets under current assets, other noncurrent assets, current liabilities and other noncurrent liabilities.

The deferred charge for estimated environmental costs is \$15,908,000 and \$8,423,000 at September 30, 2008 and 2007, respectively. See Note 13 for details on the manufactured gas plant remediation portion of this item.

Also included in deferred charges is unamortized bond issuance costs of approximately \$6,750,000 and \$6,314,000, respectively, at September 30, 2008 and 2007. These costs are being amortized straight-line over the life of the bonds, which approximates the effective interest method.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

12. Deferred Charges (continued)

Unrecognized hedge adjustments were \$3,082,000 at September 30, 2008 and \$3,005,000 at September 30, 2007.

Accrued fuel adjustment was a deferred debit of \$3,144,000 and \$5,523,000 at September 30, 2008 and 2007, respectively. See Note 1, Revenue Recognition for details on GRU's policy regarding fuel adjustment.

Also included in deferred charges as a current liability is a temporary transfer from the Rate Stabilization reserve of \$3,950,000 and \$20,200,000 at September 30, 2008 and 2007, respectively. This transfer is made in accordance with our bond resolution for the purpose of meeting temporary cash requirements, primarily due to timing differences.

Electric distribution plant acquisition costs of \$2,957,000 and \$3,167,000 for September 30, 2008 and 2007, respectively, are being amortized over the expected life of the acquired assets.

Remaining smaller items make up the balance of the deferred charges.

13. Environmental Liabilities

GRU is subject to numerous federal, state and local environmental regulations. Under the Comprehensive Environmental Response Compensation and Liability Act, commonly known as "Superfund," GRU has been named as a potentially responsible party at several hazardous waste sites; however, GRU does not anticipate any more than "de minimus" liability at any of these sites. In January 1990, GRU purchased the natural gas distribution assets of a company and pursuant to the related purchase agreement, assumed responsibility for the investigation and remediation of environmental impacts related to the operation of the former manufactured gas plant. Based upon GRU's analysis of the cost to clean up these sites, GRU has accrued a liability to reflect the costs associated with the cleanup effort. Fiscal year 2008 and 2007 expenditures which reduce the liability balance were \$1,141,548 and \$169,000, respectively.

During fiscal year 2008, soil samplings from the site were collected and analyzed in order to determine alternatives to complete the remediation. On November 6, 2008, the City Commission voted to approve staff's recommendation to remove the soil to landfill. The estimate to complete the work is \$13.3 million. Based on this estimate, the reserve balance was increased by \$8.15 million on September 30, 2008, in accordance with GASB 49.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

13. Environmental Liabilities (continued)

The reserve balance at September 30, 2008 and 2007 is \$13,304,000 and \$6,296,000, respectively. GRU is recovering the costs of this clean-up through customer charges. A regulatory asset was established as a deferred charge in the accompanying balance sheets to represent the balance of customer charges. Fiscal 2008 and 2007 billings were \$665,000 and \$726,000, respectively. This reduced the deferred asset balance to \$13,658,000 and \$6,173,000 as of September 30, 2008 and 2007.

Although some uncertainties associated with environmental assessment and remediation activities remain, GRU believes that the current provision for such costs is adequate and additional costs, if any, will not have a material adverse effect on GRU's financial position, results of operations or liquidity.

GRU currently carries a reserve balance of \$2.25 million, primarily for possible liability related to the oil contamination at the Kelly Generating Station. In July of 2006, GRU was notified by the Florida Department of Environmental Protection, FDEP, that provisions of Chapter 62-780, F.A.C. must be complied with on this site. This Rule is currently being utilized to establish a process and time schedule for assessment and remediation of the site. GRU's liability utilizing this Rule is unknown and cannot be reasonably estimated at this time. Therefore, GRU will make no changes to the reserve balance until further information is received and a reasonable estimate can be established.

14. Lease/Leaseback

On December 10, 1998, GRU entered into a lease/leaseback transaction for all of the Deerhaven Unit 1 and a substantial portion of the Deerhaven Unit 2 generating facilities. Under the terms of the transaction, GRU entered into a 38-year lease and simultaneously a 20-year leaseback. At the end of the leaseback period term, GRU has an option to buy out the remainder of the lease for a fixed purchase option amount.

Under the terms of the transaction, GRU continues to own, operate, maintain and staff the facilities.

The proceeds received by GRU from this transaction were approximately \$249 million. From these proceeds, GRU deposited \$142 million as a payment undertaking agreement and a second deposit of \$72 million in the form of a collateralized Guaranteed Investment Contract (GIC), both with Ambac Assurance Corporation (Ambac), a financial guaranty insurance company that

Gainesville Regional Utilities

Notes to Financial Statements (continued)

14. Lease/Leaseback (continued)

also provided credit enhancement for the transaction. The deposit instruments will mature in amounts sufficient to meet the annual payment obligations under the leaseback including the end of term fixed purchase option if elected by GRU.

The net benefit of this transaction, after payment of transaction expenses, was approximately \$35 million and resulted in a deferred gain, which is being amortized as income on a straight-line basis over the leaseback period of 20 years.

Amortization of the net benefit was \$1,775,000 in both 2008 and 2007, respectively, and was reported as a component of other operating revenue.

On May 17, 2006, President Bush signed into law an act entitled the “Tax Increase Prevention and Reconciliation Act of 2005” (the Act). Among other provisions, the Act imposes an excise tax on certain types of leasing transactions entered into by tax-exempt entities, including states and their political subdivisions (including the City). Based on regulations released by the Internal Revenue Service in 2007, GRU currently anticipates that it will owe little, if any, excise tax under the Act, but this result is not certain given the interpretive questions that still remain with respect to the excise tax.

In November, 2008, Moody’s Investors Service and Standard & Poor’s downgraded their respective credit ratings of Ambac. Under the terms of the lease/leaseback transaction documents, the City is required to provide substitute credit enhancement within 30 days of the occurrence of Ambac’s ratings downgrades. GRU currently is working with its financial advisor and legal counsel to evaluate its options. Based on that evaluation, GRU has determined that the termination of the LILO transaction is the most appropriate action. GRU staff has negotiated the termination price with BNY and has worked with Ambac to value the GIC. The difference between the two amounts is approximately \$13.2 million, and is an obligation of the City. This difference will be paid by GRU upon the closing of the LILO termination scheduled in late February.

15. Investment in the Energy Authority

In May 2000, GRU became an equity member of The Energy Authority (TEA), a power marketing joint venture. In May 2002, TEA began trading natural gas on behalf of GRU. As of September 30, 2005, this joint venture was comprised of six municipal utilities across the nation, all of which are participating in the electric marketing and five of which participate in the gas program. GRU’s ownership interest was 7.1% in the electric venture and 7.7% in the gas

Gainesville Regional Utilities

Notes to Financial Statements (continued)

15. Investment in the Energy Authority (continued)

venture, and it accounted for this investment using equity accounting. To become a member, GRU paid an initial capital contribution of \$1,000,000 and a membership fee of \$867,360. The membership fee was amortized over 24 months and, consequently, eliminated at September 30, 2002. GRU has reflected the capital contribution as an investment in TEA. The investment balance has been adjusted for GRU's subsequent share of TEA's net income or loss. In calculating GRU's share of net income or loss, profit on transactions between GRU and TEA have been eliminated. Such transactions primarily relate to purchases and sales of electricity between GRU and TEA.

GRU had electric purchases transactions with TEA of \$29,587,919 and \$17,479,607 and sales transactions of \$8,052,411 and \$1,882,999 in fiscal years 2008 and 2007, respectively. TEA's profit on these transactions has been reflected as a reduction to GRU's reported revenue or expense.

As of September 30, 2008, GRU's investment in TEA was \$2,447,440 verses \$2,513,500 on September 30, 2007.

GRU provides guarantees to TEA and to TEA's bank to secure letters of credit issued by the bank to cover purchase and sale contracts for electric energy, natural gas and related transmission. In accordance with the membership agreement between GRU and its joint venture members and with the executed guaranties delivered to TEA and to TEA's bank, GRU's aggregate obligation for electric energy marketing transactions entered into by TEA on behalf of its members is \$9,600,000 as of September 30, 2008. GRU's aggregate obligation for TEA's natural gas marketing transactions, under similar agreements and executed guaranties, is \$18,800,000 as of September 30, 2008.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

15. Investment in the Energy Authority (continued)

The following is a summary of the unaudited financial information of TEA for the twelve month periods ended September 30, 2008 and 2007:

	2008	2007
Condensed statement of operations:		
Total revenue	\$ 1,693,794,000	\$ 1,626,802,000
Total cost of sales and expenses	1,531,232,000	1,495,487,000
Operating income	162,562,000	131,315,000
Net revenue	\$ 162,928,000	\$ 133,969,000
Condensed balance sheet:		
Assets:		
Current assets	\$ 169,877,000	\$ 185,384,000
Noncurrent assets	12,907,000	12,533,000
Total assets	\$ 182,784,000	\$ 197,917,000
Liabilities:		
Current liabilities	\$ 144,639,000	\$ 163,218,000
Noncurrent liabilities	2,447,000	419,000
Total liabilities	147,086,000	163,637,000
Members' capital	35,698,000	34,280,000
Total equity and liabilities	\$ 182,784,000	\$ 197,917,000

TEA issues separate audited financial statements on a calendar-year basis.

Gainesville Regional Utilities

Notes to Financial Statements (continued)

16. Risk Management

GRU is exposed to various risks of loss related to theft of, damage to, and destruction of assets, errors and omissions, injuries to employees, and natural disasters and insures against these losses. GRU purchases plant and machinery insurance from a commercial carrier. There have been no significant reductions in insurance coverage from that in the prior year, and settlements have not exceeded insurance coverage for the past three fiscal years. The City is self-insured for workers' compensation, auto liability, and general liability but carries excess workers' compensation coverage. These risks are accounted for under the City of Gainesville's General Insurance Fund. GRU reimburses the City for premiums and claims paid on its behalf, recording the appropriate expense. However, GRU does maintain its own insurance reserve, for the self-insured portion. An actuarial study completed during the fiscal year resulted in an increase to a balance of \$3,337,000. The present value calculation assumes a rate of return of 4.5% with a confidence level of 75%. This reserve is recorded as a fully amortized deferred credit. All claims for fiscal 2008 and 2007 were paid from current year's revenues.

Changes in the claims liability for the last two years are as follows:

Fiscal Year	Beginning Balance	Claims	Payments	Increase to Reserve	Ending Balance
2006-2007	\$ 2,106,000	\$ 957,216	\$ 957,216	\$ -	\$ 2,106,000
2007-2008	\$ 2,106,000	\$ 908,677	\$ 908,677	\$ 1,231,000	\$ 3,337,000

17. Subsequent Event

On November 19, 2008, Standard & Poor's lowered its rating on Ambac Assurance Corporation ("Ambac"), which either directly or through affiliates had provided the Equity Swap Guarantee, GIC Guarantee and Surety Bond under the terms of the Participation and Lease Agreements ("the Lease") with GRU (the "Lessee") of its Deerhaven Station and closed on December 10, 1998. As a result of the Ambac downgrade and as required in Section 11(c) of the Participation agreement, GRU must provide additional credit support for the equity investor, which was BNY Gator LLC and affiliate of the Bank of New York ("BNY"). Upon the downgrade to "A" level, GRU would have 30 days under which to provide such additional credit support. BNY provided GRU with several extensions of time to evaluate the options for securing such enhancement or to consider a buyout of the Lease transaction. GRU canvassed the market for replacement enhancement providers and at the same time commenced negotiations with Ambac and BNY to determine the buyout price under the Lease. The only bona fide proposal came from Berkshire

Gainesville Regional Utilities

Notes to Financial Statements (continued)

17. Subsequent Event (continued)

Hathaway at an expense of 1% of the outstanding exposure per annum which was equivalent to a present value cost of approximately \$15.2 million. Based upon the additional expense and considering GRU would retain ongoing credit exposure to Ambac under the GIC contract, which were used to defease the payment obligations to BNY, GRU has determined that the termination of the Lease is the most appropriate action. GRU has negotiated with BNY to reduce the equity portion of the termination price down from approximately \$214 million to \$138.4 million assuming the buyout occurs in February of 2009. At the same time, the Ambac GIC has an accreted value which is still being determined at this time but is approximately \$122.5 million. The difference in such amounts with an approximate shortfall of \$13.2 million is an obligation of GRU and will be paid by GRU upon the settlement of the liquidation. Included in the buyout will be a payoff of a loan provided originally by Ambac, which was defeased by a separate deposit with another affiliate of Ambac. This loan, which has a current balance of approximately \$58 million, will not require any additional payment from GRU in order to pay it off upon the termination of the Lease. It is anticipated that subject to its City Council approval, GRU will terminate the lease on or about February 24, 2009.

Supplemental Schedules

Gainesville Regional Utilities

Schedules of Combined Net Revenues in Accordance with Bond Resolution

	2008	2007	2006	2005	2004
Revenue					
Electric fund:					
Sales of electricity	\$ 238,595,628	\$ 206,552,756	\$ 207,023,570	\$ 174,046,209	\$ 159,117,761
Other electric revenue	3,871,838	3,878,187	2,614,880	2,692,565	2,887,861
Transfers from (to) rate stabilization	6,532,390	(4,372,298)	(2,047,553)	(134,672)	6,451,678
Interest investment income	2,859,539	3,597,057	2,837,575	2,326,225	4,161,700
Total electric fund revenue	<u>251,859,395</u>	<u>209,655,702</u>	<u>210,428,472</u>	<u>178,930,327</u>	<u>172,619,000</u>
Gas fund:					
Gas sales	29,842,601	27,614,405	31,148,518	26,044,659	24,500,658
Other gas revenue (expenses)	(63,412)	(8,750)	1,138	(25,177)	(19,825)
Transfers from (to) rate stabilization	1,987,360	1,160,544	(465,695)	761,130	(1,130,506)
Interest investment income	635,757	561,892	584,699	429,646	219,627
Total gas fund revenue	<u>32,402,306</u>	<u>29,328,091</u>	<u>31,268,660</u>	<u>27,210,258</u>	<u>23,569,954</u>
Water fund:					
Sales of water	25,094,181	22,970,588	17,987,383	13,826,209	13,998,249
Other water revenue	2,899,253	1,852,072	2,184,786	1,549,635	1,156,849
Transfers from (to) rate stabilization	(1,074,205)	(1,274,108)	(878,017)	1,534,938	3,065,791
Interest investment income	206,230	95,439	172,476	279,053	328,649
Total water fund revenue	<u>27,125,459</u>	<u>23,643,991</u>	<u>19,466,628</u>	<u>17,189,835</u>	<u>18,549,538</u>
Wastewater fund:					
Wastewater billing	29,819,878	25,554,311	20,474,546	17,418,564	16,933,546
Other wastewater revenue	2,840,164	2,200,469	3,693,161	2,351,726	1,512,204
Transfers from/(to) rate stabilization	(1,271,208)	(581,471)	(1,157,713)	1,816,821	3,362,600
Interest investment income	408,455	207,121	429,598	555,058	471,352
Total wastewater fund revenue	<u>31,797,289</u>	<u>27,380,430</u>	<u>23,439,592</u>	<u>22,142,169</u>	<u>22,279,702</u>
GRUCom fund:					
Sales to customers	10,277,819	9,275,122	8,722,084	8,565,405	8,081,031
Transfers from (to) rate stabilization	(1,085,755)	(1,691,798)	(1,036,283)	(5,391)	(688,811)
Interest investment income	239,050	155,735	133,002	79,455	90,022
Total GRUCom fund revenue	<u>9,431,114</u>	<u>7,739,059</u>	<u>7,818,803</u>	<u>8,639,469</u>	<u>7,482,242</u>
Total revenue	<u>\$ 352,615,563</u>	<u>\$ 297,747,273</u>	<u>\$ 292,422,154</u>	<u>\$ 254,112,058</u>	<u>\$ 244,500,436</u>

Continued on next page.

Gainesville Regional Utilities

Schedules of Combined Net Revenues in Accordance with Bond Resolution (continued)

	2008	2007	2006	2005	2004
Operation, maintenance and administrative					
Electric fund:					
Fuel expense	\$ 127,233,223	\$ 104,940,526	\$ 116,303,116	\$ 89,398,658	\$ 76,259,729
Operation and maintenance	36,753,083	32,076,530	33,715,716	30,539,416	32,132,279
Administrative and general	20,654,480	15,913,731	12,585,157	12,320,230	11,466,706
Total electric fund expense	184,640,786	152,930,787	162,603,989	132,258,304	119,858,714
Gas fund:					
Fuel expense	20,107,903	18,514,704	21,919,984	16,881,895	14,593,903
Operation and maintenance	1,606,831	1,571,781	1,342,257	1,388,368	1,166,824
Administrative and general	4,504,748	4,200,069	3,427,848	3,107,252	2,919,393
Total gas fund expense	26,219,482	24,286,554	26,690,089	21,377,515	18,680,120
Water fund:					
Operation and maintenance	7,074,992	6,711,674	6,176,450	5,497,667	5,235,332
Administrative and general	5,120,270	3,994,430	3,629,681	3,590,193	3,688,337
Total water fund expense	12,195,262	10,706,104	9,806,131	9,087,860	8,923,669
Wastewater fund:					
Operation and maintenance	7,273,610	6,316,884	6,701,627	6,174,582	5,842,395
Administrative and general	5,773,158	4,817,270	4,603,576	4,212,466	4,224,198
Total wastewater fund expense	13,046,768	11,134,154	11,305,202	10,387,048	10,066,593
GRUCom fund:					
Operation and maintenance	2,632,075	2,313,343	2,489,099	2,365,838	2,321,615
Administrative and general	2,349,715	2,294,882	2,255,465	2,142,330	1,651,046
Total GRUCom fund expense	4,981,790	4,608,225	4,744,565	4,508,168	3,972,661
Total operation, maintenance and administrative	241,084,088	203,665,825	215,149,976	177,618,895	161,501,757
Net revenue in accordance with bond resolution					
Electric	67,218,609	56,724,915	47,824,483	46,672,023	52,760,286
Gas	6,182,824	5,041,537	4,578,570	5,832,743	4,889,834
Water	14,930,197	12,937,887	9,660,498	8,101,975	9,625,869
Wastewater	18,750,521	16,246,276	12,134,389	11,755,121	12,213,109
GRUCom	4,449,324	3,130,834	3,074,238	4,131,301	3,509,581
Total net revenue in accordance with bond resolution	\$ 111,531,475	\$ 94,081,449	\$ 77,272,178	\$ 76,493,163	\$ 82,998,679
Aggregate bond debt service	\$ 47,127,033	\$ 40,545,456	\$ 34,107,669	\$ 24,876,978	\$ 26,673,276
Aggregate bond debt service coverage ratio	2.37	2.32	2.27	3.07	3.11
Total debt service	\$ 52,626,846	\$ 45,942,353	\$ 41,050,956	\$ 35,476,481	\$ 33,554,604
Total debt service coverage ratio	2.12	2.05	1.88	2.16	2.47

Gainesville Regional Utilities

Schedules of Net Revenues in Accordance with Bond Resolution – Electric Utility Fund

	2008	2007
Revenue		
Sales of electricity:		
Residential sales	\$ 52,464,529	\$ 50,908,035
General service and large power	50,931,403	45,894,630
Fuel adjustment	111,127,690	89,624,417
Street and traffic lighting	4,885,527	4,503,222
Utility surcharge	3,460,602	2,828,347
Sales for resale	7,679,975	7,140,373
Interchange sales	8,045,902	5,653,732
Total sales of electricity	238,595,628	206,552,756
Other electric revenue:		
Service charges	2,415,365	2,308,671
Pole rentals	582,895	1,183,047
Miscellaneous	873,578	386,469
Total other electric revenue	3,871,838	3,878,187
Transfers to rate stabilization	6,532,390	(4,372,298)
Interest income	2,859,539	3,597,057
Total revenue	251,859,395	209,655,702
Operation, maintenance and administrative expense		
Operation and maintenance:		
Fuel expense:		
Retail and purchased power	121,077,624	101,310,097
Interchange	6,155,599	3,630,429
Total fuel expense	127,233,223	104,940,526
Power production	23,774,403	20,015,804
Transmission	1,162,906	1,024,280
Distribution	11,815,774	11,036,446
Total operation and maintenance	163,986,306	137,017,056

Continued on next page.

Gainesville Regional Utilities

Schedules of Net Revenues
in Accordance with Bond Resolution –
Electric Utility Fund (continued)

	<u>2008</u>	<u>2007</u>
Administrative and general:		
Customer accounts	\$ 8,007,249	\$ 5,871,016
Administrative and general	<u>12,647,231</u>	<u>10,042,715</u>
Total administrative and general	<u>20,654,480</u>	<u>15,913,731</u>
Total operation, maintenance and administrative expense	<u>184,640,786</u>	<u>152,930,787</u>
Net revenue in accordance with bond resolution		
Retail	65,328,306	54,701,612
Interchange	1,890,303	2,023,303
Total net revenue in accordance with bond resolution	<u>\$ 67,218,609</u>	<u>\$ 56,724,915</u>

Gainesville Regional Utilities

Schedules of Net Revenues in Accordance with Bond Resolution – Gas Utility Fund

	2008	2007
Revenue		
Sales of gas:		
Residential	\$ 13,238,530	\$ 14,016,737
Interruptible/commercial	16,062,893	13,194,451
Other sales	541,178	403,217
Total sales of gas	29,842,601	27,614,405
Other gas revenue (expense)	(63,412)	(8,750)
Transfers (to) from rate stabilization	1,987,360	1,160,544
Interest income	635,757	561,892
Total revenue	32,402,306	29,328,090
 Operation, maintenance and administrative expense		
Operation and maintenance:		
Fuel expense	20,107,903	18,514,704
Operation and maintenance	1,606,831	1,571,781
Total operation and maintenance	21,714,734	20,086,485
Administrative and general:		
Customer accounts	2,176,975	2,164,294
Administrative and general	2,327,773	2,035,774
Total administrative and general	4,504,748	4,200,068
Total operation, maintenance and administrative expense	26,219,482	24,286,553
Total net revenue in accordance with bond resolution	\$ 6,182,824	\$ 5,041,537

Gainesville Regional Utilities

Schedules of Net Revenues in Accordance with Bond Resolution – Water Utility Fund

	2008	2007
Revenue		
Sales of water:		
General customers	\$ 21,662,066	\$ 19,898,854
University of Florida	1,216,708	951,324
Fire protection	–	3,122
Generating stations	–	13,549
Utility surcharge	2,215,407	2,103,739
Total sales of water	25,094,181	22,970,588
Other water revenue:		
Connection charges	2,630,509	1,652,098
Miscellaneous	268,744	199,974
Total other water revenue	2,899,253	1,852,072
Transfers from rate stabilization	(1,074,205)	(1,274,108)
Interest income	206,230	95,439
Total revenue	27,125,459	23,643,991
Operation, maintenance and administrative expense		
Operation and maintenance:		
Source of supply	18,790	13,868
Pumping	1,891,732	1,561,803
Water treatment	3,318,548	3,282,644
Transmission and distribution	1,845,922	1,853,359
Total operation and maintenance	7,074,992	6,711,674
Administrative and general:		
Customer accounts	1,293,922	1,155,815
Administrative and general	3,826,348	2,838,615
Total administrative and general	5,120,270	3,994,430
Total operation, maintenance and administrative expense	12,195,262	10,706,104
Total net revenue in accordance with bond resolution	\$ 14,930,197	\$ 12,937,887

Gainesville Regional Utilities

Schedules of Net Revenues in Accordance with Bond Resolution – Wastewater Utility Fund

	2008	2007
Revenue		
Wastewater billings:		
Billings	\$ 26,833,136	\$ 23,500,197
Utility surcharge	2,986,742	2,054,114
Total wastewater billings	29,819,878	25,554,311
Other wastewater revenue:		
Connection charges	2,269,836	1,662,669
Miscellaneous	570,328	537,800
Total other wastewater revenue	2,840,164	2,200,469
Transfers from rate stabilization	(1,271,208)	(581,471)
Interest income	408,455	207,121
Total revenue	31,797,289	27,380,430
Operation, maintenance and administrative expense		
Operation and maintenance:		
Collection	1,475,925	1,363,521
Treatment and pumping	5,797,685	4,953,363
Total operation and maintenance	7,273,610	6,316,884
Administrative and general:		
Customer accounts	1,152,713	991,642
Administrative and general	4,620,445	3,825,628
Total administrative and general	5,773,158	4,817,270
Total operation, maintenance and administrative expense	13,046,768	11,134,153
Total net revenue in accordance with bond resolution	\$ 18,750,521	\$ 16,246,277

Gainesville Regional Utilities

Schedules of Net Revenues in Accordance with Bond Resolution – GRUCom Utility Fund

	2008	2007
Revenue		
Sales to customers	\$ 10,277,819	\$ 9,275,122
Transfers to rate stabilization	(1,085,755)	(1,691,798)
Interest income	239,050	155,735
Total revenue	9,431,114	7,739,059
 Operation, maintenance and administrative expense		
Operation and maintenance	2,632,075	2,313,343
Total operation and maintenance	2,632,075	2,313,343
 Administrative and general:		
Customer accounts	429,351	379,636
Administrative and general	1,920,364	1,915,246
Total administrative and general	2,349,715	2,294,882
Total operation, maintenance and administrative expense	4,981,790	4,608,225
Total net revenue in accordance with bond resolution	\$ 4,449,324	\$ 3,130,834

Gainesville Regional Utilities

Notes to Schedules of Net Revenues in Accordance with Bond Resolution

September 30, 2008

“Net revenue in accordance with bond resolution” differs from “Net income,” which is determined in accordance with generally accepted accounting principles. Following are the more significant differences:

- Interest income does not include interest earned on construction funds.
- Operation and maintenance expense does not include depreciation, amortization or interest expense.
- Other water and wastewater revenue include fees for connection, installation, and backflow prevention.
- Transfers to the general fund are excluded.
- Revenue from lease/leaseback transaction is excluded (see financial statement Note 14).

Gainesville Regional Utilities

Combining Balance Sheet

September 30, 2008

	Electric	Gas	Water	Wastewater	GRUCom	Combined
Assets						
Current assets:						
Cash and cash equivalents	\$ 3,148,075	\$ 642,253	\$ 619,667	\$ 98,433	\$ 60,453	\$ 4,568,881
Accounts receivable, net	38,558,481	2,713,855	4,182,714	4,194,055	1,779,787	51,428,892
Prepaid rent – LILO	10,686,909	–	–	–	–	10,686,909
Deferred charges	6,763,252	1,423,376	139,914	230,994	112,693	8,670,229
Prepaid expenses	742,807	424,779	–	–	–	1,167,586
Inventories:						
Fuel	5,961,105	–	–	–	–	5,961,105
Materials and inventories	8,421,021	384,469	498,112	–	631,874	9,935,476
Total current assets	74,281,650	5,588,732	5,440,407	4,523,482	2,584,807	92,419,078
Restricted assets:						
Utility deposits – cash and investments	5,100,795	185,535	213,728	321,349	–	5,821,407
Debt service fund – cash and investments	24,730,064	1,497,940	4,086,939	6,100,757	1,267,548	37,683,248
Rate stabilization – cash and investments	51,063,296	3,604,515	1,142,222	3,490,992	4,585,172	63,886,197
Construction fund – cash and investments	101,988,134	1,637,017	3,585,994	15,815,285	8,303,963	131,330,393
Utility plant improvement fund – cash and investments	1,059,048	6,035,841	4,189,132	9,438,011	3,773,139	24,495,171
Decommission reserve – cash and investments	8,529,188	–	–	–	–	8,529,188
Investment in The Energy Authority	2,447,440	–	–	–	–	2,447,440
Total restricted assets	194,917,965	12,960,848	13,218,015	35,166,394	17,929,822	274,193,044
Prepaid rent – LILO	97,963,332	–	–	–	–	97,963,332
Other noncurrent assets	9,405,913	10,894,939	565,380	644,872	371,875	21,882,979
Capital assets:						
Utility plant in service	685,572,485	53,844,001	171,154,206	223,969,939	38,110,073	1,172,650,704
Plant unclassified	604,609	287,905	118,742	166,063	117,371	1,294,690
Less: accumulated depreciation and amortization	328,634,926	25,852,758	65,103,289	87,384,384	19,357,992	526,333,349
	357,542,168	28,279,148	106,169,659	136,751,618	18,869,452	647,612,045
Plant held for future use	6,053,926	–	–	–	–	6,053,926
Construction in progress	236,520,133	5,185,572	30,109,435	21,484,450	7,795,220	301,094,810
Net capital assets	600,116,227	33,464,720	136,279,094	158,236,068	26,664,672	954,760,781
Total assets	\$ 976,685,087	\$ 62,909,239	\$ 155,502,896	\$ 198,570,816	\$ 47,551,176	\$ 1,441,219,214

Continued on next page.

Gainesville Regional Utilities

Combining Balance Sheet (continued)

September 30, 2008

	Electric	Gas	Water	Wastewater	GRUCom	Combined
Liabilities and net assets						
Current liabilities:						
Fuels payable	\$ 8,262,552	\$ 1,034,596	\$ -	\$ -	\$ -	\$ 9,297,148
Accounts payable and accrued liabilities	14,824,260	(361,966)	855,733	1,324,620	362,599	17,005,247
Operating lease – LILO	12,461,916	-	-	-	-	12,461,916
Deferred charges	(42,120)	2,291,418	2,260,414	889,432	1,053,383	6,452,527
Due to other funds	3,471,237	(31,856)	1,225,118	(317,664)	(688,522)	3,658,313
Total current liabilities	38,977,845	2,932,192	4,341,265	1,896,388	727,461	48,875,151
Payable from restricted assets:						
Utility deposits	5,100,796	185,535	213,728	321,349	-	5,821,408
Rate stabilization deferred credit	51,063,297	3,604,515	1,142,222	3,490,992	4,585,171	63,886,197
Construction fund:						
accounts payable and accrued liabilities	8,926,233	29,938	142,938	1,196,057	91,316	10,386,482
Debt payable – current portion	13,409,263	1,281,970	2,771,210	3,563,642	958,906	21,984,991
Accrued interest payable	10,384,241	741,541	1,769,433	2,095,259	917,054	15,907,528
Total payable from restricted assets	88,883,830	5,843,499	6,039,531	10,667,299	6,552,447	117,986,606
Long-term debt:						
Utilities system revenue bonds	449,316,806	30,523,002	87,332,205	99,056,556	42,281,442	708,510,011
Subordinated utilities system revenue bonds	-	-	-	-	-	-
Commercial paper notes	32,907,630	10,540,120	5,337,350	13,214,900	-	62,000,000
Unamortized loss on refunding	(17,668,585)	(1,648,969)	(4,260,244)	(4,783,439)	(239,691)	(28,600,928)
Unamortized bond prem disc	4,504,922	193,344	910,441	1,043,905	41,361	6,693,973
Total long-term debt	469,060,773	39,607,497	89,319,752	108,531,922	42,083,112	748,603,056
Operating lease – LILO	114,225,173	-	-	-	-	114,225,173
Other noncurrent liabilities	13,319,991	12,741,042	603,595	551,547	5,295	27,221,470
Total liabilities	724,467,612	61,124,230	100,304,143	121,647,156	49,368,315	1,056,911,456
Net assets:						
Invested in capital assets, net of related debt	224,421,033	(5,589,606)	48,409,625	62,688,085	(7,675,860)	322,253,277
Restricted	17,455,264	6,762,302	6,363,699	12,247,452	4,032,318	46,861,035
Unrestricted	10,341,178	612,313	425,429	1,988,123	1,826,403	15,193,446
Total net assets	252,217,475	1,785,009	55,198,753	76,923,660	(1,817,139)	384,307,758
Total liabilities and net assets	\$ 976,685,087	\$ 62,909,239	\$ 155,502,896	\$ 198,570,816	\$ 47,551,176	\$ 1,441,219,214

Gainesville Regional Utilities

Combining Statement of Revenues, Expenses and Changes in Net Assets

Year Ended September 30, 2008

	Electric	Gas	Water	Wastewater	GRUCom	Combined
Operating revenue:						
Sales and service charges	\$ 238,595,628	\$ 29,583,927	\$ 25,094,180	\$ 29,819,878	\$ 10,277,819	\$ 333,371,432
Transfers from (to) rate stabilization	6,532,390	1,987,360	(1,074,205)	(1,271,208)	(1,085,755)	5,088,582
Other operating revenue	5,646,041	193,331	2,899,253	2,840,164	(69,207)	11,509,582
Total operating revenue	<u>250,774,059</u>	<u>31,764,618</u>	<u>26,919,228</u>	<u>31,388,834</u>	<u>9,122,857</u>	<u>349,969,596</u>
Operating expenses:						
Operation and maintenance	164,008,637	21,714,734	7,074,992	7,273,610	2,632,075	202,704,048
Administrative and general	20,654,479	4,504,748	5,120,270	5,773,158	2,349,715	38,402,370
Depreciation and amortization	26,577,333	1,677,870	5,416,410	8,357,446	2,695,302	44,724,361
Total operating expenses	<u>211,240,449</u>	<u>27,897,352</u>	<u>17,611,672</u>	<u>21,404,214</u>	<u>7,677,092</u>	<u>285,830,779</u>
Operating income	39,533,610	3,867,266	9,307,556	9,984,620	1,445,765	64,138,817
Non-operating income (expense):						
Interest income	7,027,092	651,917	234,733	471,345	887,163	9,272,250
Interest expense	(15,289,145)	(1,802,986)	(3,688,103)	(4,646,542)	(2,768,067)	(28,194,844)
Gain on sale of investments	92,615	3,101	23	397	913	97,050
Total non-operating income (expense)	<u>(8,169,438)</u>	<u>(1,147,968)</u>	<u>(3,453,347)</u>	<u>(4,174,800)</u>	<u>(1,879,991)</u>	<u>(18,825,544)</u>
Income before contributions and transfers	<u>31,364,172</u>	<u>2,719,298</u>	<u>5,854,209</u>	<u>5,809,820</u>	<u>(434,226)</u>	<u>45,313,273</u>
Capital contributions:						
Contributions from developers	323,300	-	2,442,142	2,039,835	-	4,805,277
Reduction of plant cost recovered from contributions	(323,300)	-	-	-	-	(323,300)
Net capital contributions	<u>-</u>	<u>-</u>	<u>2,442,142</u>	<u>2,039,835</u>	<u>-</u>	<u>4,481,977</u>
Operating transfer to City of Gainesville general fund	<u>(19,500,376)</u>	<u>(1,510,761)</u>	<u>(4,610,724)</u>	<u>(5,495,500)</u>	<u>(334,524)</u>	<u>(31,451,885)</u>
Change in net assets	11,863,796	1,208,537	3,685,627	2,354,155	(768,750)	18,343,365
Net assets - beginning of year	<u>240,353,679</u>	<u>576,472</u>	<u>51,513,126</u>	<u>74,569,505</u>	<u>(1,048,389)</u>	<u>365,964,393</u>
Net assets - end of year	<u>\$ 252,217,475</u>	<u>\$ 1,785,009</u>	<u>\$ 55,198,753</u>	<u>\$ 76,923,660</u>	<u>\$ (1,817,139)</u>	<u>\$ 384,307,758</u>

Independent Certified Public Accountants' Report on Internal Control
Over Financial Reporting and on Compliance and Other Matters Based on an
Audit of the Financial Statements Performed in Accordance With
Government Auditing Standards

The Honorable Mayor and
Members of the City Commission
City of Gainesville, Florida

We have audited the financial statements of Gainesville Regional Utilities (a department of the City of Gainesville, Florida) as of and for the year ended September 30, 2008, and have issued our report thereon dated February 10, 2009. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Gainesville Regional Utilities' internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Gainesville Regional Utilities' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Gainesville Regional Utilities' internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Gainesville Regional Utilities' financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We also noted certain additional matters that we reported to management of Gainesville Regional Utilities in a separate letter dated February 10, 2009.

This report is intended solely for the information and use of the City Commission and management and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

February 10, 2009

Gainesville Regional Utilities

Schedule of Utility Plant Properties – Combined Utility Fund

September 30, 2008

	Balance September 30, 2007	Additions	Sales, Retirements and Transfers	Balance September 30, 2008
Plant in service				
Electric utility fund:				
Production plant	\$ 358,677,013	\$ 119,704	\$ 3,051,270	\$ 355,745,447
Nuclear fuel	2,138,521	719,518	–	2,858,039
Transmission and distribution plant	244,136,017	9,994,634	–	254,130,651
General and common plant	69,435,727	3,402,624	–	72,838,351
Plant unclassified	2,255,383	11,404,174	13,054,948	604,609
Total electric utility fund	<u>676,642,661</u>	<u>25,640,654</u>	<u>16,106,806</u>	<u>686,177,097</u>
Gas utility fund:				
Distribution plant	41,943,104	4,461,634	132,428	46,272,310
General plant	2,836,801	84,254	–	2,921,055
Plant acquisition adjustment	4,650,635	–	–	4,650,635
Plant unclassified	1,313,360	3,520,160	4,545,615	287,905
Total gas utility fund	<u>50,743,900</u>	<u>8,066,048</u>	<u>4,678,043</u>	<u>54,131,905</u>
Water utility fund:				
Supply, pumping and treatment plant	27,730,186	810,500	37,254	28,503,432
Transmission and distribution plant	127,124,803	11,414,685	364,836	138,174,652
General plant	4,323,387	152,734	–	4,476,121
Plant unclassified	3,285,965	9,210,696	12,377,919	118,742
Total water utility fund	<u>162,464,341</u>	<u>21,588,615</u>	<u>12,780,009</u>	<u>171,272,947</u>
Wastewater utility fund:				
Pumping and treatment plant	83,575,750	2,468,216	719,057	85,324,909
Collection plant	113,835,431	10,956,947	277,451	124,514,927
Reclaimed water plant	6,834,773	696,874	–	7,531,647
General plant	6,378,790	219,666	–	6,598,456
Plant unclassified	2,477,080	12,030,686	14,341,703	166,063
Total wastewater utility fund	<u>213,101,824</u>	<u>26,372,389</u>	<u>15,338,211</u>	<u>224,136,002</u>
GRUCom utility fund:				
Distribution plant	35,247,008	1,921,005	–	37,168,013
General plant	821,414	120,645	–	942,059
Plant unclassified	304,340	1,854,681	2,041,650	117,371
Total GRUCom utility fund	<u>36,372,762</u>	<u>3,896,331</u>	<u>2,041,650</u>	<u>38,227,443</u>
Total plant in service	<u>\$ 1,139,325,488</u>	<u>\$ 85,564,037</u>	<u>\$ 50,944,131</u>	<u>\$ 1,173,945,394</u>
Plant held for future use – electric	<u>\$ 6,053,926</u>	<u>\$ –</u>	<u>\$ –</u>	<u>\$ 6,053,926</u>
Construction in progress				
Electric utility fund	\$ 122,695,973	\$ 126,790,627	\$ 12,966,467	\$ 236,520,133
Gas utility fund	5,454,333	3,180,999	3,449,760	5,185,572
Water utility fund	26,995,846	12,010,834	8,897,245	30,109,435
Wastewater utility fund	23,377,819	12,066,011	13,959,380	21,484,450
GRUCom utility fund	7,257,831	2,436,489	1,899,100	7,795,220
Total construction in progress	<u>\$ 185,781,802</u>	<u>\$ 156,484,960</u>	<u>\$ 41,171,952</u>	<u>\$ 301,094,810</u>

Gainesville Regional Utilities

Schedule of Accumulated Depreciation and Amortization – Combined Utility Fund

September 30, 2008

	Balance September 30, 2007	Additions	Sales, Retirements and Transfers	Balance September 30, 2008
Electric utility fund:				
Production plant	\$ 196,544,830	\$ 9,552,068	\$ –	\$ 206,096,898
Nuclear fuel	1,657,418	374,663	–	2,032,081
Transmission and distribution plant	80,501,098	7,626,954	3,051,092	85,076,960
General and common plant	29,092,969	5,788,477	(52,100)	34,933,546
Plant unclassified	398,769	33,431	(63,241)	495,441
Total electric utility fund	<u>308,195,084</u>	<u>23,375,593</u>	<u>2,935,751</u>	<u>328,634,926</u>
Gas utility fund:				
Distribution plant	18,724,292	1,297,568	132,428	19,889,432
General plant	1,103,597	202,158	(4,700)	1,310,455
Plant acquisition adjustment	4,650,637	–	–	4,650,637
Plant unclassified	26,646	2,234	26,646	2,234
Total gas utility fund	<u>24,505,172</u>	<u>1,501,960</u>	<u>154,374</u>	<u>25,852,758</u>
Water utility fund:				
Supply, pumping and treatment plant	12,353,730	911,562	37,254	13,228,038
Transmission and distribution plant	44,829,187	3,678,334	364,836	48,142,685
General plant	3,504,916	219,525	(1,100)	3,725,541
Plant unclassified	83,807	7,026	83,807	7,026
Total water utility fund	<u>60,771,640</u>	<u>4,816,447</u>	<u>484,797</u>	<u>65,103,290</u>
Wastewater utility fund:				
Pumping and treatment plant	36,110,335	3,037,309	719,057	38,428,587
Collection plant	39,637,800	3,318,690	277,451	42,679,039
Reclaimed water plant	894,410	266,369	–	1,160,779
General plant	4,797,345	301,128	(7,300)	5,105,773
Plant unclassified	121,732	10,205	121,732	10,205
Total wastewater utility fund	<u>81,561,622</u>	<u>6,933,701</u>	<u>1,110,940</u>	<u>87,384,383</u>
GRUCom utility fund:				
Distribution plant	16,187,271	2,629,807	–	18,817,078
General plant	472,341	64,711	–	537,052
Plant unclassified	46,069	3,862	46,069	3,862
Total GRUCom utility fund	<u>16,705,681</u>	<u>2,698,380</u>	<u>46,069</u>	<u>19,357,992</u>
Total	<u>\$ 491,739,199</u>	<u>\$ 39,326,081</u>	<u>\$ 4,731,931</u>	<u>\$ 526,333,349</u>