



Honorable Mayor and City Commissioners
City of Gainesville, Florida

We have audited the financial statements of Gainesville Regional Utilities (GRU or the Utility) of the City of Gainesville, Florida (the City) for the year ended September 30, 2016. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated July 11, 2016. Professional standards also require that we communicate to you the following information related to our audit:

Qualitative Aspects of Accounting Practices

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the Utility are described in Note 1 to the financial statements. During the year, the Utility implemented GASB Statement No. 72, *Fair Value Measurement and Application*. This statement clarifies the definition of fair value and requires disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques. This statement also provides guidance for applying fair value to certain investments. We noted no transactions entered into by the Utility during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting Estimates

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the Utility's financial statements were:

- **Capitalization of Leased Asset and Related Liability**

The Gainesville Renewable Energy Center (GREC) Biomass-Fired Power Production Facility (the Facility) began commercial operations on December 17, 2013. The related Power Purchase Agreement (PPA) includes an embedded capital lease of the Facility to GRU. As such, GRU recorded the Facility as a capital lease asset and a related long-term obligation to GREC. The basis for determining the initial carrying amount of the Facility and related capital lease obligation was a present value analysis of anticipated payments to GREC under the PPA. For purposes of that analysis, the Non-Fuel Energy Charge and the Fixed O&M Charge were deemed to be payments for the Facility and related products and form the basis for calculating the lease asset and related obligation, while the Variable O&M Charge was deemed to be executory in nature and not capitalized. Future payments were estimated

Certified Public Accountants

P.O. Box 141270 • 222 N.E. 1st Street • Gainesville, Florida 32614-1270 • (352) 378-2461 • FAX (352) 378-2505
 Laurel Ridge Professional Center • 2347 S.E. 17th Street • Ocala, Florida 34471 • (352) 732-3872 • FAX (352) 732-0542
 443 East College Avenue • Tallahassee, Florida 32301 • (850) 224-7144 • FAX (850) 224-1762
 5001 Lakewood Ranch Blvd. N., Suite 101 • Sarasota, Florida 34240 • (941) 907-0350 • FAX (941) 907-0309
MEMBERS OF AMERICAN AND FLORIDA INSTITUTES OF CERTIFIED PUBLIC ACCOUNTANTS
 MEMBER OF AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS PRIVATE COMPANIES AND S.E.C. PRACTICE SECTIONS

Qualitative Aspects of Accounting Practices (Continued)

Accounting Estimates (Continued)

■ **Capitalization of Leased Asset and Related Liability (Concluded)**

based upon Available Energy levels realized at the Facility during fiscal year 2014. As a result of these calculations, GRU recorded a capital asset and related lease obligation of \$1,006,808,754 which will be amortized and repaid over the 30-year term of the PPA. As permitted under regulatory accounting, GRU has also recognized a related future recoveries revenue and an asset for net cost recoverable in future years.

As required under GAAP, GRU has recorded imputed interest expense on the capital lease obligation related to the GREC PPA. As allowed under regulatory accounting and industry practice, GRU has presented interest expense related to the GREC capital lease obligation as O&M Expense in the statement of revenues, expenses, and changes in net position rather than as Non-Operating Interest Expense.

■ **Costs Recoverable in Future Years**

As discussed in Note 1 to the financial statements, the Utility prepares its financial statements in accordance with GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. This accounting treatment results in costs and revenues being recognized in different periods for financial reporting purposes in order to reflect the economics of rate regulation. For the Utility to report under GASB Statement No. 62, its rates must be designed to recover the cost of services and the Utility must be able to collect those rates from its customers. If through competition, regulation, or other actions it was determined the Utility no longer met these criteria, it could be required to write-off its regulatory assets.

■ **Allowance for Doubtful Accounts and Bad Debt Expense**

Management's estimate of the allowance for doubtful accounts reduces the Utility's accounts receivable balances to the net realizable value in the statement of net position and increases the bad debt expense in the statement of revenues, expenses, and changes in net position in accordance with generally accepted accounting principles. Management's estimate is based on historical revenues, loss levels, and analysis of the collectability of accounts.

■ **Net Pension Liability and Pension-Related Deferred Outflows and Inflows of Resources**

The Utility's share of the net pension liability and pension-related deferred outflows and inflows of resources of the City's Employee Pension Plan, a contributory defined benefit single-employer plan, is an estimate based on actuarial studies performed by a qualified actuary retained by the City. The actuarial valuation is based upon actuarial methods and assumptions which are selected based on risk and market factors affecting governmental entities of similar sizes, pension plan policies, and employee census information. The net pension liability and deferred outflows and inflows of resources are allocated to the Utility based on retirement contributions made. This allocation is also considered a significant estimate.

■ **Unbilled Revenue Receivable and Revenues**

Management's estimate of the unbilled revenue receivable on the statement of net position consists of actual cycle billings that are billed subsequent to year-end for consumption prior to September 30, 2016, multiplied by the average daily usage for the meter read period.

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Qualitative Aspects of Accounting Practices (Concluded)

Accounting Estimates (Concluded)

■ **Accumulated Depreciation and Depreciation Expense**

Management estimates accumulated depreciation and depreciation expense for capital assets using the straight-line method of depreciation and by determining estimated useful lives based on the classes of depreciable property described in the notes to the financial statements.

■ **Fair Market Value of Financial and Derivative Instruments**

As discussed in the notes to the financial statements, the Utility uses third party valuations for determining the fair market value of its financial and derivative instruments.

We evaluated the key factors and assumptions used to develop the significant estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

Financial Statement Disclosures

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements were:

■ **Capital Lease**

Note 6 to the financial statements more fully describes the capital lease accounting of GRU's PPA with GREC, including significant terms of the agreement and contingent collateral requirement.

■ **Fuel and Purchased Gas Adjustment Levelization**

A fuel and purchased gas adjustment levelization fund is used to stabilize the monthly impact of the cost of fuel and purchased gas. The fuel and purchased gas adjustment charge is based on ordinances approved by the City Commission. Note 7 to the financial statements describes the total revenues and expenses associated with the fuel and purchased gas adjustment and the subsequent impact on the fuel and purchased gas levelization balance as of September 30, 2016.

■ **Commitments and Contingencies**

As more fully described in Note 14 to the financial statements, various environmental and other regulations could result in increased future costs. Additionally, the note describes a contingency related to arbitration filed by GREC during the year and a counterclaim filed by GRU.

The financial statement disclosures are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

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Disagreements with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditors' report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated March 6, 2017.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to GRU's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the Utility's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Matters

We applied certain limited procedures to management's discussion and analysis, which is required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on the schedules of net revenues in accordance with bond resolution, combining statements, and schedules of utility plant properties and accumulated depreciation and amortization, which accompany the financial statements but are not RSI. With respect to this supplementary information, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

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Restriction on Use

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

Purvis, Gray and Company, LLP

March 6, 2017
Gainesville, Florida