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OUC 
The Reliable One®

**2018 AUDITED
FINANCIAL STATEMENTS**

LETTER FROM THE GENERAL MANAGER AND COMMISSION PRESIDENT

For nearly a century, Orlando Utilities Commission (OUC – The *Reliable One*) has kept the lights on and the water flowing in the City Beautiful. And, with the selection of Clint Bullock as General Manager & CEO in February 2018, the Board and management is poised to continue moving forward, ensuring OUC remains focused on diversifying its services to meet the needs of our customers, employees and community. A second generation employee with more than 29 years of service, Bullock follows in the footsteps of OUC's progressive past leadership with a strong focus on achieving our vision of being *The Best Utility in the Nation*.

Building upon our reputation for industry-leading responsiveness and reliability, OUC is expanding its business partnerships beyond traditional electric and water services. The *OUCooling* chilled water business is poised to double its capacity as we work side-by-side with our top commercial customers. *OUConvenient Lighting* is also growing with innovative LED-lighting and smart-city solutions to enhance the safety of our community and leverage OUC's advanced digital infrastructure.

This year, OUC continued supporting the City of Orlando being recognized as the *Greenest City* in the Southeast by spearheading the execution of a solar purchase power agreement with the Florida Municipal Power Agency. The agreement provides for three new solar farms delivering 225 megawatts of solar energy throughout the state. While OUC will retain the majority stakeholder position with its purchase of 108.5 megawatts, the project enables many smaller utilities throughout Florida to bring solar energy to their customers. This year we have also set in motion the establishment of an Electric Integrated Resource Plan designed to help OUC navigate the transition of energy resources into the future.

Our sustainability initiatives grew in 2018 with the start of the 13-megawatt Kenneth P. Ksionek Community Solar Farm's commercial operations, allowing our residential and commercial customers to receive a portion or all of their energy from solar. We launched the *OUCollective Solar* aggregation program in 2018, making residential rooftop solar more affordable.

In addition, we led the charge to promote the use of electric vehicles with an Electric Car Guest Drive event where residential and commercial customers had the opportunity to test drive a variety of electric vehicle models.

Across all aspects of OUC, reliability remains a core value, and we continued to be recognized as one of the most reliable electric utilities in the nation – #1 in Florida for the 20th year in a row. To maintain this rating, we are building a smarter, self-healing grid with technology initiatives to enhance the identification of fault locations, reducing outages and shortening restoration times.

Being reliable extends to water operations as well – and our commitment to providing clean, great-tasting water has never been stronger, as we're moving forward with a plan to replace aging water lines in downtown Orlando. Conservation is also a key area of focus for our water initiatives with continued customer communication to encourage reduced water usage. Our water sustainability initiatives are far reaching and innovative, as OUC partners with state agencies and peer utilities to evaluate alternative water resources to ensure there is an adequate supply of clean, safe drinking water well into the future.

In both water and electric operations, OUC has always strived to keep prices affordable. In 2018, fuel prices were reduced 7.7 percent with offsetting customer and energy price increases allowing the average bill for a residential customer using 1,000 kWh per month to remain the same. Water prices increased in 2018 as part of a phased-in four-year price plan with the average residential and commercial customer bill increasing by 4.0 percent while still keeping water prices among the lowest in the state. A Pricing Platform program was also initiated to provide residential customers with alternative pricing options to support the changing landscape of electric services.

As a community partner and good neighbor, OUC stays connected with its peer utilities and agencies throughout the state to provide support during times of emergency. To facilitate the effectiveness of the response needed during



OUC Commission 2018

*front row; left to right: Mayor Buddy Dyer | Gregory D. Lee, Commission President | Cesar Calvet, First Vice President
back row; left to right: Larry Mills, Th.D., Commissioner | Clint Bullock, General Manager & CEO |
Britta Gross, Second Vice President*

these events, OUC hosted the 2018 Florida Mutual Aid Assistance Workshop for the second consecutive year. The workshop provided a forum for emergency managers, communicators and others to discuss best practices to restore services as quickly and safely as possible for all customers in the state.

Safety for our employees and customers is paramount but this mindset is far-reaching with vigilant measures to protect our systems and customers from cyber security breaches.

To ensure we are sharp in this area, OUC continually manages this risk with system stress-tests, consultations with industry experts and business continuity and table top exercises.

Whether providing traditional or non-traditional utility services or safeguarding our employees, customers and system assets, OUC is committed to its vision to be recognized as *The Best Utility in the Nation* delivering electric and water services to the *Greenest City in the Southeast* today and into the future.

Clint Bullock
General Manager & CEO

Gregory D. Lee
Commission President

AUDITED FINANCIAL STATEMENTS

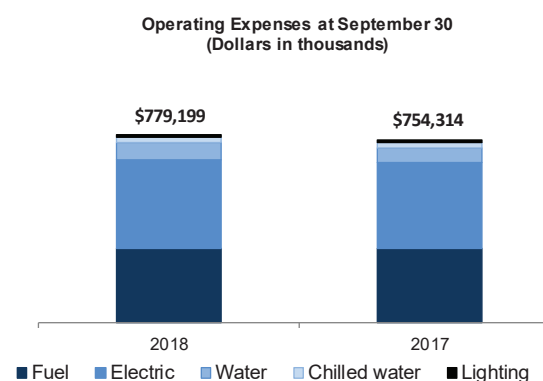
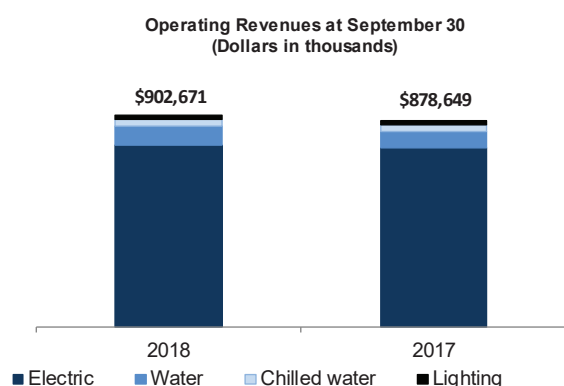
FINANCIAL HIGHLIGHTS

(Dollars in thousands)	2018	2017	% Increase / -Decrease
Operating revenues	\$ 902,671	\$ 878,649	2.7%
Operating revenues excluding fuel revenue	\$ 629,407	\$ 602,528	4.5%
Operating expenses	\$ 775,199	\$ 754,314	2.8%
Fuel for generation and purchased power	\$ 306,255	\$ 308,844	-0.8%
Interest, gain and net other income	\$ 25,116	\$ 23,722	5.9%
Interest expense	\$ 54,813	\$ 51,896	5.6%
Income before contributions	\$ 97,775	\$ 96,160	1.7%
City of Orlando dividend and revenue-based payments	\$ 90,008	\$ 87,400	3.0%
Utility plant, net	\$ 2,489,456	\$ 2,451,068	1.6%
Total assets and deferred outflows of resources	\$ 3,718,502	\$ 3,621,202	2.7%
Long-term debt, net and other bonds payable	\$ 1,564,637	\$ 1,477,363	5.9%
Net position	\$ 1,394,846	\$ 1,341,123	4.0%
Current debt service coverage	2.49	2.71	-8.1%
Senior bond ratings (1)	AA, Aa2, AA	AA, Aa2, AA	

(1) Bond Rating Agencies: Fitch Ratings, Moody's Investors Service and Standard & Poor's, respectively.

STATISTICAL HIGHLIGHTS

Electric metered services	242,971	238,051	2.1%
Electric sales (MWH)	8,112,279	7,857,609	3.2%
Average annual residential usage (KWH)	11,570	11,378	1.7%
Average residential revenue per KWH	\$ 0.1134	\$ 0.1146	-1.0%
Water metered services	142,044	140,592	1.0%
Water sales (MGAL)	28,847	28,711	0.5%
Average annual residential usage (KGAL)	80	82	-2.4%
Average residential revenue per KGAL	\$ 2.8112	\$ 2.7005	4.1%



ORLANDO UTILITIES COMMISSION

September 30, 2018

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COMMISSION MEMBERS and OFFICERS

Gregory D. Lee
President

Cesar Calvet
First Vice President

Britta Gross
Second Vice President

Larry Mills, Th.D.
Commissioner

Buddy H. Dyer
Mayor – Commissioner

Clint Bullock
Secretary

Mindy Brenay
W. Christopher Browder
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Report of Independent Auditors

To Management and the Commissioners of Orlando Utilities Commission

Report on the Financial Statements

We have audited the accompanying financial statements of Orlando Utilities Commission (OUC), as of and for the years ended September 30, 2018 and 2017, and the related notes to the financial statements, which collectively comprise OUC's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

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.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.



Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of OUC as of September 30, 2018 and 2017, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Required Supplementary Information

U.S. generally accepted accounting principles require that the management's discussion and analysis on pages 6-14, the schedules of changes in net Pension and OPEB liability and related ratios, the schedules of funding progress for Pension and OPEB, the schedules of employer contributions to the Pension and OPEB plans, and the schedules of investment returns for Pension and OPEB on pages 56-59 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board which considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States, which consisted of inquiries of management about 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 do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we also have issued our report dated December 3, 2018 on our consideration of OUC's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely 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 effectiveness of OUC's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering OUC's internal control over financial reporting and compliance.

December 3, 2018

MANAGEMENT’S DISCUSSION AND ANALYSIS

This discussion should be read in conjunction with the Financial Statements and Notes to the Financial Statements.

Management’s Report

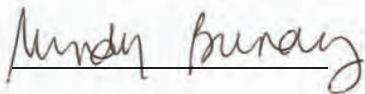
The management of Orlando Utilities Commission (OUC) has prepared — and is responsible for — the integrity of the financial statements and related information included in this report. The financial statements have been prepared in accordance with generally accepted accounting principles and follow the standards outlined by the Governmental Accounting Standards Board.

To ensure the integrity of our financial statements, OUC maintains a system of internal accounting controls that is supported by written policies and procedures and an organizational structure that appropriately assigns responsibilities to mitigate risks. These controls have been put in place to ensure OUC’s assets are properly safeguarded and the books and records reflect only those transactions that have been duly authorized. OUC’s controls are evaluated on an ongoing basis by both management and OUC’s internal auditors.

Based on the statements above, it is management’s assertion that the financial statements do not omit any disclosures necessary for a fair presentation of the information, nor do they improperly include untrue statements of a material fact or statements of a misleading nature.



Clint Bullock
General Manager &
Chief Executive Officer



Mindy Brenay
Chief Financial Officer



Matthew Lopez
Director of Accounting

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to OUC's financial statements. It defines the basic financial statements and summarizes OUC's general financial condition and results of operations, and should be read in conjunction with OUC's financial statements and accompanying notes, which follow this section.

Background

OUC was created in 1923 by a Special Act of the Florida Legislature as a statutory commission of the State of Florida and is governed by a Board (the Board) consisting of five members including the Mayor of the City of Orlando. The Act confers upon OUC the rights and powers to set prices for electric and water services. OUC is responsible for a portfolio of utility services including the acquisition, generation, transmission and distribution of electric and water services to its customers within Orange and Osceola counties as well as chilled water, lighting, back-up generation, electric vehicle charging and solar solution services.

Setting of Prices

The setting of electric and water prices are the responsibility of the Board. Price changes are implemented after public workshops are held and approved by the Board. In February 2018, a phased-in four-year water price plan was implemented, which at the first year of implementation, increased the average residential and commercial customer water bill by 4.0 percent. In July 2018, in conjunction with the 2019 Annual Budget and Rate Workshop, electric price neutral changes were approved lowering fuel prices 7.7 percent across all customer classes and increasing customer and energy prices effective October 1, 2018. This change allows the average residential electric customer using 1,000 kWh per month to retain the current price of \$106.00. The Board also approved the second year of the phased-in water price plan, which will increase water revenues 3.4 percent in January 2019. No electric or water price increases were implemented in 2017.

Financial Reporting

OUC's financial statements are presented in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The accounting records are maintained in accordance with the accounting principles and methods prescribed by the Federal Energy Regulatory Commission (FERC) with the exception of contributions in aid of construction, which are recorded in accordance with the standards prescribed by GASB.

OUC is a regulated enterprise and applies the Regulated Operations provision of GASB Statement No. 62 "*Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.*" In accordance with these principles, the Board has taken various regulatory actions for ratemaking purposes that have resulted in the deferral or recognition of certain revenues or expenses. In 2018, regulatory actions taken by the Board resulted in the recognition of \$13.8 million of electric and water reserves to offset annual financing costs associated with the issuance of the Series 2018A Bonds, the revenue requirement associated with the 4-year phased-in water rate plan, the acceleration of fossil fuel generation facilities and one-time post implementation costs for the new customer care and billing (CC&B) system. Also in 2018, the Board approved the deferral of unrealized investment valuations, which in 2018 were \$4.7 million lower than book value. In 2017, regulatory actions taken by the Board resulted in the recognition of \$7.3 million of electric and water reserves to offset one-time storm restoration costs included in unit/department expenses and implementation costs for the CC&B system, offset by the deferral of \$1.5 million of water revenues as a result of favorable weather conditions. Additionally in 2017, the Board approved the deferral of \$20.9 million of storm restoration costs expected to be recovered from the Federal Emergency Management Agency (FEMA) for Hurricanes Matthew and Irma. See Note G for additional information.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Basic Financial Statements

Three basic financial statements were prepared to provide the reader with a comprehensive overview of OUC's financial position, results of operations and cash flows.

- **Statement of Net Position:** The Statement of Net Position was prepared using the accrual method of accounting distinguishing current and long-term assets and liabilities, deferred inflows and outflows of resources, as well as the nature and amount of resources and obligations at a point in time.
- **Statement of Revenues, Expenses and Changes in Net Position:** This statement presents current period revenues and expenses. In addition, included in this statement is the presentation of operating income, which was reported separately from net non-operating expenses, contributions in aid of construction and annual dividend.
- **Statement of Cash Flows:** This statement was presented using the direct method and outlines the sources and uses of cash resulting from operations, non-capital related financing, capital related financing, and investing activities.

Condensed Statements of Net Position

As of September 30

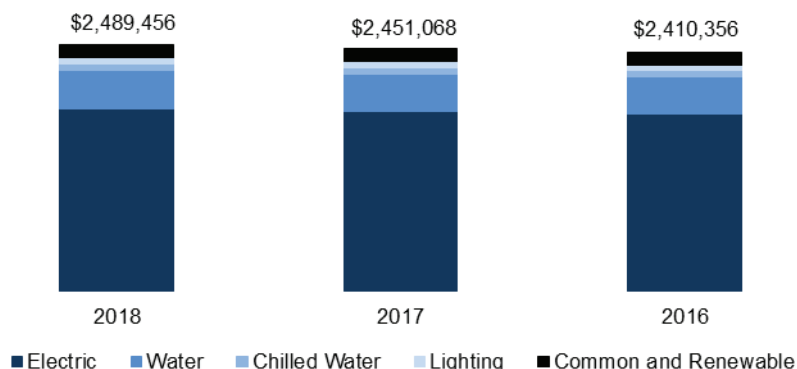
(Dollars in thousands)	2018	2017	2016
Assets			
Utility plant, net	\$ 2,489,456	\$ 2,451,068	\$ 2,410,356
Restricted and internally designated assets	657,489	539,295	625,270
Current assets	261,150	268,545	249,866
Other assets	209,141	241,555	222,503
Total assets	3,617,236	3,500,463	3,507,994
Deferred outflows of resources	101,266	120,739	178,987
Total assets and deferred outflows of resources	\$ 3,718,502	\$ 3,621,202	\$ 3,686,981
Liabilities			
Long-term debt, net	\$ 1,564,637	\$ 1,477,363	\$ 1,476,091
Current liabilities	258,339	260,483	333,935
Other liabilities and credits	207,717	250,413	299,216
Total liabilities	2,030,693	1,988,259	2,109,242
Deferred inflows of resources	292,963	291,820	292,357
Net position			
Net investment in capital assets	1,071,359	1,048,799	945,883
Unrestricted	323,487	292,324	339,499
Total net position	1,394,846	1,341,123	1,285,382
Total liabilities, deferred inflows of resources and net position	\$ 3,718,502	\$ 3,621,202	\$ 3,686,981

2018 Compared to 2017

Assets

Utility plant, net: Utility plant, net increased \$38.4 million inclusive of accumulated depreciation. Current year plant additions were \$184.7 million. The increase was primarily due to capital spending for major projects including several multi-year transmission line upgrades to improve system reliability and capacity, water system upgrades and fossil fuel generation facility upgrade projects inclusive of the Stanton Energy Center (SEC) Unit A and Unit B major outages. Capital additions were offset by systematic depreciation charges of \$141.1 million.

Utility Plant, net at September 30
(Dollars in thousands)



Restricted and internally designated assets: Restricted and internally designated assets of \$657.5 million were \$118.2 million higher than prior year. Restricted assets increased \$89.6 million due to the timing of construction fund reimbursements associated with the Series 2018A Bonds and increases in the debt service fund of \$12.6 million. Internally designated funds increased \$28.6 million for the funding of the capital reserves of \$22.0 million and increased customer-provided system development funds of \$5.0 million. These increases were offset by the use of electric and water reserves of \$13.8 million.

Current assets: Current assets of \$261.1 million were \$7.4 million lower than prior year. Customer accounts receivable decreased \$14.4 million due to the timing of the implementation of the CC&B system in 2017 and a change in the timing of billings for customers with consolidated bills. Additionally, fuel for generation inventories decreased \$6.6 million and derivative collateral deposits decreased \$1.9 million as a result of decreases in interest rate swap collateral deposits of \$2.9 million coupled with favorable market valuation changes of \$1.0 million for outstanding fuel hedges. These changes were offset by a \$4.2 million increase in outstanding participant receivables and an increase in cash and investments of \$7.7 million.

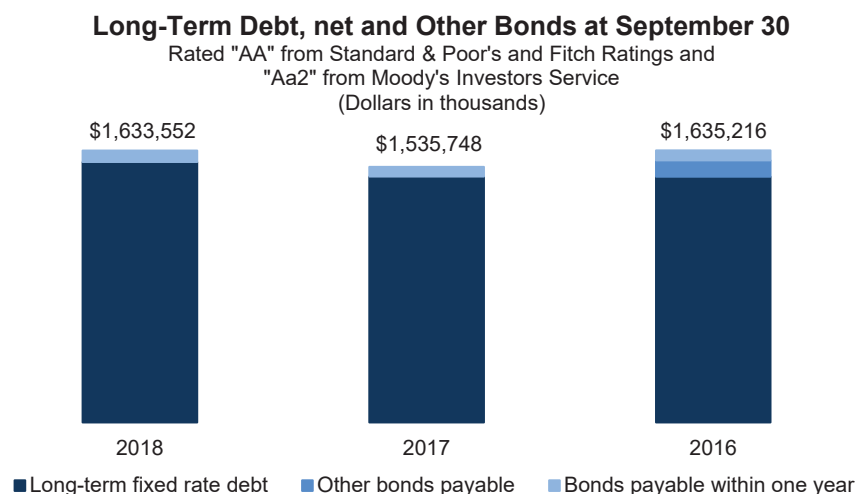
Other assets: Other assets decreased \$32.4 million from the prior year primarily due to a decrease in prepaid expenses and investment valuation changes. Prepaid expenses decreased \$18.9 million for the recognition of deferred major outage costs at SEC Unit A and Unit B generation facilities. Investment valuation changes along with actuarial assumption changes lowered unrecognized pension and other post-employment benefit (OPEB) costs \$11.7 million and \$6.8 million, respectively. Investment valuation changes decreased the unrecognized valuation on interest rate swap derivatives \$2.8 million. Effective beginning October 1, 2017, the Board approved a regulatory action to defer unrealized investment valuations to mitigate market driven timing differences and cost recovery through the rate-making model. Unrealized losses deferred in 2018 were \$4.7 million.

Deferred outflows of resources: In 2018, deferred outflows of resources decreased by \$19.5 million. The change was due to the systematic amortization of OPEB, pension and refunded bond costs of \$7.0 million, \$5.8 million, and \$6.1 million, respectively.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Liabilities

Long-term debt, net: In 2018, long-term debt increased \$87.3 million as compared to 2017. The primary driver of this change was the issuance of the Series 2018A Bonds in the amount of \$180.0 million. These increases were offset by scheduled bond maturities of \$68.9 million and the systematic amortization of bond-related premiums of \$17.9 million. In addition, the fair value of the interest rate swap derivatives decreased \$7.0 million.



Current liabilities: Current liabilities decreased \$2.1 million in 2018 as compared to 2017. Accounts payable and accrued expenses decreased \$16.5 million as a result of prior year accrued storm restoration costs and lower fuel related costs. These decreases were offset by increases in current bonds payable of \$10.5 million. Additionally, there were increases in accrued interest and customer deposits of \$2.1 million and \$1.2 million, respectively.

Other liabilities and credits: Other liabilities were \$42.7 million lower than that of 2017. The change was primarily driven by decreases in the net pension and OPEB liabilities of \$26.4 million and \$20.4 million, respectively, as a result of favorable market valuations and the systematic recognition of unfunded actuarial liabilities. These variances were offset by an increase in the asset retirement liability related to St. Lucie Unit 2 (SL2) of \$1.7 million.

Deferred inflows of resources: Deferred inflows of resources increased \$1.1 million in 2018. The change was primarily due to increases in the unrealized pension and OPEB gains of \$12.6 million and \$3.4 million, respectively, resulting from market valuation changes. Additionally, there was an increase in the valuation of unrecognized interest rate swap derivatives related to the Series 2015B Bonds of \$4.3 million. These increases were offset by the use of electric and water reserves of \$13.8 million. Additionally, there was a decrease due to the continued systematic recognition of deferred gains on sale to offset generation facility depreciation expenses for SEC Unit A of \$5.3 million.

2017 Compared to 2016

Assets

Utility plant, net: Utility plant, net increased \$40.7 million inclusive of accumulated depreciation. Current year plant additions were \$185.6 million. The increase was primarily due to capital spending for major projects including several multi-year transmission line upgrades to improve system reliability and capacity, a turbine electric production upgrade at SEC Unit 1 and pond liner replacement upgrades. Additionally, the CC&B system upgrade transitioned from development to operational status in July 2017. Capital additions were offset by systematic depreciation charges of \$128.9 million.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Restricted and internally designated assets: Restricted and internally designated assets of \$539.3 million were \$86.0 million lower than prior year. Internally designated funds decreased due to the planned release of \$69.5 million from the capital reserve to fund utility plant additions. Renewal and replacement and electric and water reserves decreased \$14.5 million and \$5.9 million, respectively, due to unanticipated storm restoration costs resulting from Hurricanes Matthew and Irma for which OUC filed for reimbursement from FEMA in 2018. Additionally, designated assets decreased \$3.8 million due to the planned utilization of fuel reserves to mitigate rising fuel prices. These usages were offset by increased customer-provided system development funds and deposits of \$4.9 million and \$0.9 million, respectively.

Current assets: Current assets of \$268.5 million were \$18.7 million higher than prior year. A portion of this increase was driven by the implementation of the new CC&B system which changed the timing of billings for customers with consolidated bills and increased customer receivables \$36.2 million. Additionally, miscellaneous receivables increased \$5.0 million as a result of billings from conservation lighting projects and outstanding participant receivables. Fuel for generation and materials and supplies inventories increased \$9.4 million and \$2.1 million, respectively. These changes were offset by decreased derivative collateral deposits of \$16.8 million as a result of the partial interest rate swap termination and lower fuel hedge collateral deposits of \$4.1 million from rising natural gas costs. Cash and investments decreased \$8.6 million due to billing in arrears for customers with consolidated bills offset by favorable current year operations.

Other assets: Other assets increased \$19.1 million from the prior year due to the deferral of \$20.9 million for FEMA storm restoration receivables from Hurricanes Matthew and Irma. In April 2017, the Board approved a regulatory action to defer a portion of the residual interest rate swap valuation of \$11.9 million to align with the life of the outstanding bonds and the maturity period of the interest rate swap. These increases were offset by the planned recognition of deferred pension and OPEB costs of \$18.5 million.

Deferred outflows of resources: In 2017, deferred outflows of resources decreased by \$58.2 million. The change was due to investment valuations and a partial termination of an interest rate swap of \$33.1 million. In addition, systematic recognition of other regulatory assets and fuel hedge valuations of \$20.3 million and \$3.9 million, respectively, contributed to the change.

Liabilities

Long-term debt, net: In 2017, long-term debt increased \$1.3 million as compared to 2016. The primary driver of this change was the issuance of the Series 2017A Bonds in the amount of \$98.4 million, refunding the Series 2011A *Windows* Bonds previously recognized as a current liability under the heading of payable from current assets. These increases were offset by scheduled bond maturities of \$58.4 million and systematic amortization of bond-related premiums of \$17.4 million. In addition, fair valued derivative instruments decreased \$11.7 million due to market valuation changes and \$9.6 million due to the partial termination of the interest rate swap agreement underlying the Series 2011A *Windows* Bonds.

Current liabilities: Current liabilities decreased \$73.5 million in 2017 as compared to 2016. In February 2017, the Series 2011A *Windows* Bonds in the amount of \$98.4 million, were refunded with the Series 2017A Bonds, included under the heading of long-term debt, net. In addition, there was a decrease in short-term fuel hedge derivative losses of \$1.7 million. Offsetting these decreases were higher supplier payables of \$26.4 million, as a result of accrued Hurricane Irma storm restoration expenses.

Other liabilities and credits: Other liabilities were \$48.8 million lower than that of 2016. The change was primarily driven by a decrease in the pension and OPEB liabilities and long-term fuel hedge derivatives of \$47.7 million as a result of market valuation fluctuations. Additionally, unapplied contributions in aid of construction decreased \$3.5 million. These variances were offset by an increase in the asset retirement liability related to SL2 of \$1.1 million.

Deferred inflows of resources: Deferred inflows of resources decreased \$0.5 million in 2017. The change was due to the continued systematic recognition of deferred gains on sale to offset depreciation expenses for SEC Unit A of \$8.3 million and the planned use of fuel reserves of \$4.1 million. In addition, the Board approved the recognition of regulatory credits to mitigate one-time costs associated with the implementation of the CC&B system and unanticipated Hurricanes Matthew and Irma storm restoration costs of \$1.4 million and \$5.9 million, respectively. These decreases were offset by an increase in unrealized pension and OPEB gains of \$18.8 million due to investment valuations. Additionally, higher than expected water revenues of \$1.5 million were deferred in 2017 to mitigate the impact of future water reserve usage.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Condensed Statements of Revenues, Expenses and Changes in Net Position Years ended September 30

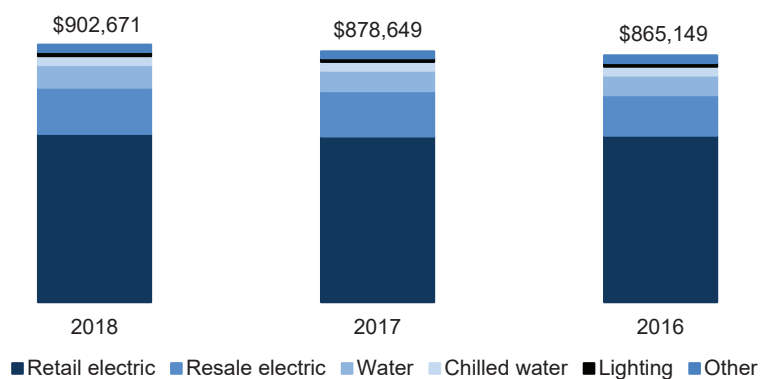
(Dollars in thousands)	2018	2017	2016
Operating revenues	\$ 902,671	\$ 878,649	\$ 865,149
Operating expenses	775,199	754,314	728,978
Operating income	127,472	124,335	136,171
Net non-operating expenses	29,697	28,174	38,015
Income before contributions	97,775	96,161	98,156
Contributions in aid of construction	16,564	18,642	16,584
Annual dividend	(60,616)	(59,061)	(55,719)
Increase in net position	53,723	55,742	59,021
Net position - beginning of year	1,341,123	1,285,382	1,226,361
Net position - end of year	\$ 1,394,846	\$ 1,341,123	\$ 1,285,382

2018 Compared to 2017

Changes in Net Position

Operating revenues: Operating revenues increased \$24.0 million, or 2.7 percent, compared to 2017. Retail energy revenues were \$11.2 million higher than prior year due to customer growth and the use of \$9.0 million of electric reserves. Water revenues were \$7.8 million higher than prior year due to customer growth, the mid-year rate increase and the use of \$4.8 million of water reserves. Resale revenues were \$3.6 million higher due to strong customer growth in the St. Cloud service territory and wholesale sales. Other revenues increased by \$4.3 million primarily due to a \$1.9 million increase in service fees, a \$1.7 million increase in OUConvenient lighting revenues and a \$0.6 million increase in chilled water revenues. Offsetting these increases were lower fuel revenues of \$2.9 million as a result of renegotiated transportation savings and lower commodity market pricing. See Note G for information related to the Board approved regulatory actions.

Operating Revenues at September 30 (Dollars in thousands)



Operating expenses: In 2018, operating expenses were \$20.9 million, or 2.8 percent, higher than 2017. The increase was primarily due to higher depreciation and amortization, unit/departments expenses and payments to other governments and taxes, offset by lower fuel for generation and purchased power costs due to lower transportation and commodity costs.

Depreciation and amortization expenses were \$12.2 million higher than 2017 primarily from the depreciation of major outage costs at SEC Unit A and Unit B and the go-live impact of the CC&B system.

Unit/departments expenses were \$8.4 million higher than 2017, inclusive of \$8.6 million of one-time storm restoration expenses incurred in 2017. The increase was driven by higher planned generation and distribution reliability costs, as well as overall cost increases associated with inflation and economic growth in the Central Florida area.

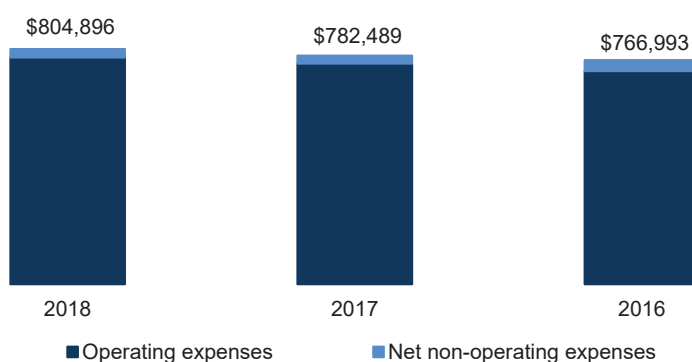
MANAGEMENT'S DISCUSSION AND ANALYSIS

Payments to other governments were \$55.3 million, an increase of \$2.9 million, as a result of increased sales.

Net non-operating expenses: Total net non-operating expenses for 2018 were \$1.5 million higher than 2017. The increase was driven by a \$3.0 million increase in net interest expense due to the issuance of the Series 2018A Bonds and a \$2.3 million decrease in the deferred gain on sale amortization to offset the planned depreciable asset life of SEC Unit A. This change was offset by the Board approved action to defer unrealized investment valuations consistent with the rate-making model which, in 2017, included a valuation loss of \$3.8 million.

Contributions in aid of construction: Contributions in aid of construction of \$16.6 million for 2018 were \$2.1 million lower than 2017.

Operating and Non-operating Expenses at September 30
(Dollars in thousands)



2017 Compared to 2016

Changes in Net Position

Operating revenues: Operating revenues increased \$13.5 million or 1.6 percent as compared to 2016. Fuel revenues were \$7.5 million higher than prior year due to rising natural gas costs offset by the annualized impact of the 9.0 percent fuel rate decrease implemented in July 2016. Water revenues were \$3.4 million higher than prior year due to lower rainfall and a 1.0 percent increase in customer growth. Offsetting these increases were lower service fee revenues and retail energy revenues of \$3.0 million and \$2.7 million, respectively, as a result of milder weather in 2017 and impacts from the implementation of the CC&B system, partially mitigated by a 2.0 percent increase in customer growth. In 2017, the Board approved several regulatory actions for rate-making purposes that resulted in an overall increase in operating revenues of \$5.8 million. See Note G for further information.

Operating expenses: In 2017, operating expenses were \$25.3 million, or 3.5 percent, higher than in 2016. The increase was due to higher unit/department expenses and fuel for generation and purchased power costs of \$11.4 million and \$7.4 million, respectively. The primary driver of the higher unit/department expenses were the unexpected costs related to Hurricanes Matthew and Irma of \$8.6 million. Fuel for generation and purchased power costs were higher than prior year primarily due to increased commodity costs, particularly for natural gas resources.

Depreciation and amortization expenses were \$128.9 million, an increase of \$7.9 million or 6.5 percent as compared to 2016. This change resulted from incremental year-over-year systematic depreciation related to the capitalization of new assets and the acceleration of the fossil fuel generation assets to align with OUC's clean energy initiatives.

Payments to other governments and taxes were \$1.4 million lower in 2017 as compared to 2016 as a result of decreased retail electric sales.

Net non-operating expenses: Total net non-operating expenses for 2017 were \$9.8 million lower than 2016. The decrease was driven by lower interest expense as a result of bond refunding activity and debt maturities. In addition, the amortization of the deferred gain on sale increased by \$4.8 million to offset the impact of the acceleration of the fossil fuel generation assets.

Contributions in aid of construction: Contributions in aid of construction of \$18.6 million for 2017 were \$2.1 million higher than 2016.

MANAGEMENT'S DISCUSSION AND ANALYSIS

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

Legislative and Regulatory:

As OUC's electric operations are subject to legislative and regulatory mandates, rulings regarding environmental matters can have a significant impact on operational and financial results. OUC's intentions are to ensure compliance with any rule requirements and also allow a "glide path" that would ensure price stability and equity for its customers and OUC and allow for the full depreciation of OUC's impacted assets. See Note J for further information.

OUC water resources are governed by its consumptive use permit (CUP) with key requirements to supply reclaimed water to customers inside the City limits and areas outside the OUC service area for irrigation to conserve groundwater resources and offset environmental impacts due to groundwater pumping and partner with other utilities to provide regional solutions to water supply constraints and develop alternative water supply resources.

Operations

Plans are underway to expand residential customer pricing options from the current one-size fits all model to more flexible models that complement advancing home energy technologies, electrification of transportation, and conservation and community sustainability efforts. In addition, traditional pricing changes are being evaluated to enable enhanced cost alignment and reduce the seasonal variability of customer billings and OUC's electric retail revenues.

Overall, the 2019 Operating Budget reflects a 2.8 percent increase in revenues driven by projected and sustainable customer growth throughout OUC's portfolio of utility services.

OUC remains focused on achieving the City of Orlando's goal to transition to renewable energy by 2050 and has initiated a comprehensive Electric Integrated Resource Plan (EIRP) beginning in 2019 with an expected completion date of 2020. Results of the EIRP will provide guidance and alternatives to enable OUC to identify future generation needs and emerging technologies to transition from fossil fuels to renewable energy. Aligned with this initiative, OUC is also launching a rooftop solar feasibility assessment to evaluate the potential for this source of renewable energy in its service territory.

In 2018, OUC and the Greater Orlando Aviation Authority (GOAA) agreed to broaden the scope of their relationship beyond traditional electric and water services with a Comprehensive Partnership - Letter of Intent agreement for OUC to provide chilled water, backup generation, electric vehicle charging and on-site solar energy. The Letter of Intent was approved by GOAA and OUC subsequent to September 30, 2018.

In 2018, OUC entered into an extension of the power purchase agreement (PPA) with Southern Company for the generation output of SEC Unit A through 2031. Subsequent to the execution of this extension, Southern Company announced that it had agreed to sell its equity interest in SEC Unit A to NextEra Energy, Inc. as part of a larger sale that is expected to close in the first quarter of 2019. OUC is currently evaluating the impact of this transaction.

Financing Opportunities

In November 2018, OUC's Finance Committee approved for recommendation to the Board a resolution to issue the Series 2019A Utility System Revenue Refunding Bonds in the par value of \$57.3 million. The bonds will be issued by March 2019 as fixed rate debt with the proceeds used to refund the Series 2009B Utility System Revenue Refunding Bonds.

Also at the November Finance Committee meeting, the Committee approved for recommendation to the Board a resolution to authorize prepaid natural gas opportunities for up to 30,000 MMBtu per day. These agreements are not anticipated to be executed until the second quarter of fiscal year 2019.

Requests for information should be emailed to recordscustodian@ouc.com or (407) 434-2727.



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STATEMENTS OF NET POSITION

(Dollars in thousands)	As of September 30	
	2018	2017
Assets		
Utility plant, net		
Utility plant in service	\$ 4,313,625	\$ 4,159,316
Allowances for depreciation and amortization	(2,061,635)	(1,940,364)
Utility plant in service, net	2,251,990	2,218,952
Land	73,253	73,091
Construction work in progress	164,213	159,025
Total utility plant, net	2,489,456	2,451,068
Restricted and internally designated assets		
Restricted assets	131,796	42,176
Internally designated assets	525,693	497,119
Total restricted and internally designated assets	657,489	539,295
Current assets		
Cash and investments	47,099	39,408
Customer receivables, net	97,287	111,731
Miscellaneous receivables, net	9,889	5,728
Accrued utility revenue	38,003	35,880
Fuel for generation	18,223	24,829
Materials and supplies inventory, net	38,479	37,499
Accrued interest receivable	2,127	2,049
Prepaid and other expenses	9,698	10,772
Hedging derivative instruments maturing within one year	345	649
Total current assets	261,150	268,545
Other assets		
Regulatory assets	178,987	194,863
Other long-term assets	30,154	46,511
Hedging derivative instruments	-	181
Total other assets	209,141	241,555
Total assets	3,617,236	3,500,463
Deferred outflows of resources		
Accumulated decrease in fair value of hedging derivatives	2,536	2,098
Fair value retirement obligation asset	6,319	6,576
Unrealized pension contributions and losses	40,500	46,313
Unrealized other post-employment benefits contributions and losses	10,762	17,777
Goodwill	368	1,101
Unamortized loss on refunded bonds	40,781	46,874
Total deferred outflows of resources	101,266	120,739
Total assets and deferred outflows of resources	\$ 3,718,502	\$ 3,621,202

See Notes to the Financial Statements for additional information.

STATEMENTS OF NET POSITION

(Dollars in thousands)	As of September 30	
	2018	2017
Liabilities		
Current liabilities		
Payable from restricted and designated assets		
Current portion of long-term debt	\$ 68,915	\$ 58,385
Accrued interest payable on notes and bonds	30,883	28,790
Customer meter deposits	58,156	56,991
Total payable from restricted and designated assets	157,954	144,166
Payable from current assets		
Accounts payable and accrued expenses	62,327	78,860
Billings on behalf of state and local governments	19,693	19,032
Compensated absences and accrued wages	14,298	14,004
Accrued governmental payments	2,973	2,901
Accrued swap payables	59	125
Hedging derivative instruments maturing within one year	1,035	1,395
Total payable from current assets	100,385	116,317
Total current liabilities	258,339	260,483
Other liabilities and credits		
Pension liability	97,623	124,057
Net other post-employment benefits liability	25,146	45,545
Asset retirement obligation and other liabilities	83,446	80,108
Hedging derivative instruments	1,502	703
Total other liabilities and credits	207,717	250,413
Long-term debt, net		
Bond and note principal	1,459,945	1,378,640
Unamortized premium	99,868	86,858
Fair value of derivative instruments	4,824	11,865
Total long-term debt, net	1,564,637	1,477,363
Total liabilities	2,030,693	1,988,259
Deferred inflows of resources		
Unrealized pension gains	22,609	10,047
Unrealized other post-employment benefits gains	25,806	22,399
Accumulated increase in fair value of hedging derivatives	5,519	1,713
Regulatory credits	237,817	256,271
Unamortized gain on refunded bonds	1,212	1,390
Total deferred inflows of resources	292,963	291,820
Net position		
Net investment in capital assets	1,071,359	1,048,799
Unrestricted	323,487	292,324
Total net position	1,394,846	1,341,123
Total liabilities, deferred inflows of resources and net position	\$ 3,718,502	\$ 3,621,202

See Notes to the Financial Statements for additional information.

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

(Dollars in thousands)	Years ended September 30	
	2018	2017
Operating revenues		
Retail electric revenues	\$ 589,455	\$ 580,361
Resale electric revenues	161,468	158,577
Water revenues	79,154	71,371
Chilled water revenues	31,397	30,752
Lighting revenues	14,749	13,067
Other revenues	26,448	24,521
Total operating revenues	902,671	878,649
Operating expenses		
Fuel for generation and purchased power	306,255	308,844
Unit/department expenses	272,559	264,138
Depreciation and amortization	141,101	128,944
Payments to other governments and taxes	55,284	52,388
Total operating expenses	775,199	754,314
Operating income	127,472	124,335
Net non-operating expenses		
Interest income	8,318	4,551
Other income, net	10,726	10,784
Amortization of gain on sale of assets	6,072	8,386
Interest expense	(54,813)	(51,896)
Total net non-operating expenses	(29,697)	(28,175)
Income before contributions	97,775	96,160
Contributions in aid of construction	16,564	18,642
Annual dividend	(60,616)	(59,061)
Increase in net position	53,723	55,741
Net position - beginning of year	1,341,123	1,285,382
Net position - end of year	\$ 1,394,846	\$ 1,341,123

See Notes to the Financial Statements for additional information.

STATEMENTS OF CASH FLOWS

(Dollars in thousands)	Years ended September 30	
	2018	2017
Cash flows from operating activities		
Cash received from customers	\$ 908,504	834,122
Cash paid for fuel and purchased power	(299,910)	(308,101)
Cash paid for unit/department expenses excluding salaries and benefits	(67,009)	(62,124)
Cash paid for salaries and benefits	(173,994)	(174,890)
Cash paid for storm recovery	(17,479)	(14,365)
Cash paid to other governments and taxes	(55,213)	(52,390)
Net cash provided by operating activities	294,899	222,252
Cash flows from non-capital related financing activities		
Dividend payment	(60,616)	(59,061)
Pension bond interest payments	(391)	(636)
Pension bond principal payments	(4,755)	(4,515)
Build America Bond interest subsidy received	3,708	3,732
Net cash used in non-capital related financing activities	(62,054)	(60,480)
Cash flows from capital related financing activities		
Utility plant net of contributions in aid of construction	(160,391)	(164,715)
Debt interest payments	(61,264)	(55,917)
Collateral deposits	2,900	16,800
Principal payments and refunding costs on long-term debt	(53,630)	(164,913)
Debt issuances	180,000	108,663
Debt issuance expense	(1,039)	(1,376)
Net cash used in capital related financing activities	(93,424)	(261,458)
Cash flows from investing activities		
Proceeds from sales and maturities of investment securities	334,838	570,050
Purchases of investment securities	(436,079)	(413,663)
Investments and other income received	(8,519)	7,345
Net cash (used in)/provided by investing activities	(109,760)	163,732
Net increase in cash and cash equivalents	29,661	64,046
Cash and cash equivalents - beginning of year	179,779	115,733
Cash and cash equivalents - end of year	\$ 209,440	\$ 179,779
Reconciliation of operating income to net cash provided by operating activities		
Operating income	\$ 127,472	\$ 124,335
Adjustments to reconcile operating income to net cash provided by operating activities		
Depreciation and amortization of plant charged to operations	141,101	128,944
Depreciation and amortization charged to fuel for generation and purchased power	4,219	4,711
Depreciation of vehicles and equipment charged to unit/department expenses	2,575	1,755
Changes in assets and liabilities		
Decrease/(Increase) in receivables and accrued revenue	1,722	(45,655)
Decrease/(Increase) in fuel and materials and supplies inventories	14,018	(3,745)
(Decrease)/Increase in accounts payable	(18,609)	13,445
Increase in deposits payable and liabilities	17,200	3,045
Increase/(Decrease) in stabilization and deferred credits	5,201	(4,583)
Net cash provided by operating activities	\$ 294,899	\$ 222,252
Reconciliation of cash and cash equivalents		
Restricted and internally designated cash and cash equivalents	\$ 173,645	\$ 134,419
Cash and investments	35,795	45,360
Cash and cash equivalents - end of year	\$ 209,440	\$ 179,779
Non-cash investing, capital and financing activities		
Increase in donated utility plant assets	\$ 4,839	\$ 4,019
Decrease in fair value of investments	\$ (4,677)	\$ (2,298)
Decrease/(Increase) in accounts payable related to utility plant purchases	\$ 770	\$ (6,580)

See Notes to the Financial Statements for additional information.

NOTES TO THE FINANCIAL STATEMENTS

Note A – The Organization

Orlando Utilities Commission (OUC) was created in 1923 by a Special Act of the Florida Legislature as a statutory commission of the State of Florida. The Act confers upon OUC the rights and powers to set rates and charges for electric and water. OUC provides a portfolio of utility services including the acquisition, generation, transmission and distribution of electric and water services to its customers within Orange and Osceola Counties as well as chilled water, lighting, back-up generation and electric vehicle charging and solar solution services.

OUC's governing Board (the Board) consists of five members including the Mayor of the City of Orlando. Members serve without compensation and with the exception of the Mayor, who is an ex-officio member of the Board, may serve no more than two full consecutive four-year terms.

Note B – Summary of Significant Accounting Policies

Basis of presentation: The financial statements are presented in conformity with generally accepted accounting principles for enterprise funds as prescribed by the Governmental Accounting Standards Board (GASB). The accounting records are maintained in accordance with the accounting principles and methods prescribed by the Federal Energy Regulatory Commission (FERC) with the exception of contributions in aid of construction which are recorded in accordance with the standards prescribed by GASB.

OUC is a regulated enterprise and, as such, applies GASB Statement No. 62 *"Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements"* (Statement No. 62). Under this guidance, certain revenues and expenses are recognized and deferred in accordance with rate actions of the Board.

Reporting entity: OUC meets the criteria of an "other stand-alone government" as defined in GASB Statement No. 14, *"The Financial Reporting Entity"* and GASB Statement No. 39, *"Determining Whether Certain Organizations are Component Units."*

OUC has undivided interests in several power generation facilities which are operated through participation agreements and are described in Note D. Title to the property is held in accordance with the terms defined in each agreement and, as such, each party is obligated for its contractual share of operations. There are no separate entities or organizations associated with these agreements.

Measurement focus, basis of accounting, and financial statement presentation: OUC reports operating revenues and expenses separately from net non-operating expenses and contributions in aid of construction. Operating revenues and expenses generally result from producing and delivering utility services. The principal operating revenues are charges to retail and wholesale customers and are recorded net of the provision for doubtful accounts. Operating expenses include fuel and purchased power, unit/department expenses, taxes, and depreciation on capital assets. Net non-operating expenses include financial and investment activities. Contributions in aid of construction are primarily comprised of impact fees assessed for the future expansion and development of OUC's water system and developer contributions to OUC's electric and water systems.

Setting of prices: According to the existing laws of the State of Florida, the five Board members of OUC act as the regulatory authority for the establishment of electric and water prices. Electric prices are set in accordance with the "rate structures" established by the Florida Public Service Commission (FPSC), as they have the jurisdiction to regulate the electric "rate structures" of municipal utilities in Florida. A "rate structure" is defined as the rate relationship between customer class and among customers within rate classes and is distinguishable from the total amount of revenue requirements a utility may receive from rates.

Periodically, OUC performs a rate adequacy study to determine the electric base and fuel revenue requirements. Based on this study, current cost-of-service studies, and regulations of the FPSC regarding electric rate structures, OUC develops the electric rate pricing. Prior to the implementation of any price change, OUC notifies customers individually, convenes a public workshop, presents the prices to the Board for approval and files with the FPSC. Water rate requirements are studied and prepared in a similar manner excluding filing a notification with the FPSC. Charges for other non-regulated utility services are contractually based.

NOTES TO THE FINANCIAL STATEMENTS

Note B – Summary of Significant Accounting Policies (continued)

In 2018 and 2017, there were no electric rate changes. In 2018, rate neutral changes were approved with an effective date of October 1, 2018. These changes reduce fuel prices 7.7 percent across all customer classes and increase energy demand and customer charges with the goal of reducing seasonal variability of customer bills and stabilizing electric retail revenues.

In August 2017, the Board approved a multi-year water price increase that transitions prices over four years. This action resulted in a 4.0 percent increase across all customer classes, effective March 2018. Effective January 2019, the second price increase of 3.4 percent will be implemented. There were no water price changes in 2017.

Budgets: Revenue and expense budgets are prepared on an annual basis in accordance with OUC's budget policy and bond resolutions and submitted to the Board for approval prior to the beginning of the fiscal year. OUC's annual operating budget and capital plan are approved and adopted, respectively, in the month of August preceding the budgeted fiscal year. The legal adoption of OUC's operating budget and capital plan are not required.

In accordance with OUC's budget policy and bond resolutions, actual revenues and expenses are compared to the approved budget by operating unit line item and reported to the Board monthly.

Utility plant: Utility plant is stated at historical cost with the exception of impaired assets recorded in accordance with GASB Statement No. 42, "Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries." See Note C for more information.

Historical utility plant costs include the costs of contract work, labor, materials and allocated indirect charges for equipment, supervision and engineering. Interest expense is not a component of OUC's historical utility plant costs. Utility plant costs also include nuclear fuel costs which are assembled and amortized to fuel for generation and purchased power over a period of at least two years.

Assets are subject to capitalization if they have a useful life of at least two years, a unit cost of at least \$1,000 with the exception of bulk asset purchases which must have a minimum per-unit cost of \$500 and a total purchase amount of at least \$75,000. Assets are depreciated systematically using the straight-line method over the estimated useful life, considering FERC guidelines or the license period of the asset. OUC periodically conducts a depreciation study with the last study completed in 2013.

The cost of retired electric or water utility plant assets, together with removal costs less salvage, are charged to accumulated depreciation. In addition, when a utility plant asset constituting an operating unit or system is sold or disposed of and the net proceeds are at least \$0.5 million, the gain on the sale or disposal is deferred and proceeds are placed in the renewal and replacement fund in accordance with the Board-approved Policy for Accounting Treatment of Disposal of Capital Assets.

The consolidated average annual depreciation rate, inclusive of impairment expense, was 3.4 percent and 3.3 percent for 2018 and 2017, respectively. Depreciation is calculated using the following estimated lives:

Electric	3 – 60 years
Water	3 – 75 years
Chilled Water	5 – 50 years
Lighting	20 years
Common and Renewable	3 – 40 years

Cash, cash equivalents and investments: Cash and cash equivalents are reported under the headings of restricted and internally designated assets and current assets. OUC's cash and cash equivalents include all authorized instruments purchased with an original maturity date of three months or less including all investments in money market funds. Premiums and discounts on investments are amortized using the effective interest method.

Investments having maturities of greater than one year at the time of purchase are reported at fair value and those with maturities of less than one year at the time of purchase are reported at amortized book value.

NOTES TO THE FINANCIAL STATEMENTS

Note B – Summary of Significant Accounting Policies (continued)

In 2017, realized and unrealized investment valuation changes except those executed in conjunction with a bond refunding were included in interest income on the Statements of Revenues, Expenses and Changes in Net Position. Beginning in 2018, in accordance with the Regulated Operations provision of Statement No. 62, unrealized valuation changes were deferred until realized. Realized valuation changes will continue to be recognized and included in interest income in the Statements of Revenues, Expenses and Changes in Net Position except for realized valuation changes associated with a bond refunding which are included as a component of the unamortized amount on refunding.

Realized investment losses in the amount of \$0.8 million, net of \$0.2 million of unrealized losses recognized in prior years, were incurred as of September 30, 2018 in conjunction with Treasury Policy guidance. Realized investment gains in the amount of \$0.3 million, net of \$0.2 million of unrealized gains recognized in prior years, were recognized as of September 30, 2017.

Restricted and internally designated assets: Funds classified as restricted assets represent cash, cash equivalents and investments which were designated by law, bond requirements or regulatory statutes. Funds classified as internally designated assets also represent cash, cash equivalents and investments for which OUC has a customer obligation or the Board has taken action to designate.

Accounts receivable: OUC recognizes revenue and the associated customer receivables, net of the allowance for doubtful accounts, on a cyclical basis in the period in which it was earned. The allowance for doubtful accounts was calculated based upon OUC's historical experience with collections and local economic market conditions. Bad debt expenses for estimated doubtful accounts were recorded as a reduction of operating revenues in the Statements of Revenues, Expenses and Changes in Net Position.

The net customer receivable balance of \$97.3 million and \$111.7 million at September 30, 2018 and 2017 includes an allowance for doubtful accounts of \$16.0 million and \$15.0 million, respectively. Included in net customer receivables were billings on behalf of the State and other local governments of \$11.5 million and \$14.7 million at September 30, 2018 and 2017, inclusive of an allowance for doubtful accounts of \$2.4 million and \$2.1 million, respectively. Agency billings are not reflected in the Statements of Revenues, Expenses and Changes in Net Position. Bad debt expenses were \$0.9 million and \$3.3 million for the years ended September 30, 2018 and 2017, respectively, with the primary driver of the decrease due to the 90-day suspension of collections activities during implementation of the customer care and billing (CC&B) system in 2017 and the exclusion of governmental agencies, subject to the Prompt Payment Act, from the bad debt calculation in 2018.

As of September 30, 2018 and 2017, miscellaneous receivables, including participation billing, were \$9.9 million and \$5.7 million, inclusive of an allowance for doubtful accounts of \$1.6 million and \$0.7 million for the years ended September 30, 2018 and 2017, respectively.

All receivables are anticipated to be collected within an operating cycle and are reported as current assets at September 30:

(Dollars in thousands)	2018	2017
Customer receivables, net		
Customer receivables	\$ 78,626	\$ 89,282
Agency receivables	11,467	14,686
Wholesale receivables	7,194	7,763
Total customer receivables, net	97,287	111,731
Miscellaneous receivables, net	9,889	5,728
Total accounts receivable, net	\$ 107,176	\$ 117,459

Accrued utility revenue: This amount represents utility services provided to retail customers but not billed at the end of the fiscal year. Accrued utility revenues were \$38.0 million and \$35.9 million at September 30, 2018 and 2017, respectively, including unbilled electric fuel revenues in the amount of \$10.3 million and \$10.5 million, respectively.

Fuel for generation: Fuel oil and coal were reported at current cost, based on market fuel indices. Fuel for generation at September 30, 2018 and 2017 was \$18.2 million and \$24.8 million, respectively.

NOTES TO THE FINANCIAL STATEMENTS

Note B – Summary of Significant Accounting Policies (continued)

Materials and supplies inventory: Materials and supplies were reported at current cost based on contractual material and supply agreements. Materials and supplies inventory at September 30, 2018 and 2017 was \$38.5 million and \$37.5 million, including an allowance for obsolescence of \$9.6 million for both years.

Prepaid and other expenses: Prepaid expenses represent costs that are anticipated to be recognized in the Statements of Revenues, Expenses and Changes in Net Position in the near future, including service agreement costs and derivative margin deposits resulting from unrealized market valuations. Prepaid expenses at September 30, 2018 and 2017 were \$9.7 million and \$10.8 million, respectively, for which collateral deposits related to fuel and interest rate hedge agreements were \$3.9 million and \$5.8 million, respectively.

Hedging derivative instruments: All effective derivative instruments were included in the Statements of Net Position as either an asset or liability measured at fair value. Changes in the fair value of the hedging derivative instruments during the year were deferred and recognized in the period in which the derivative was settled. The settlement of fuel and financial related hedging derivative instruments was included as part of fuel for generation and purchased power costs and interest expense, respectively, in the Statements of Revenues, Expenses and Changes in Net Position.

Fuel related derivative transactions for natural gas and crude oil are executed in accordance with OUC's internally established Energy Risk Management Oversight Committee (ERMOC) whose primary objective is to minimize exposure to energy price volatility for cash flow and budgetary purposes. ERMOC has a defined organizational structure and responsibilities, which include approving all brokerage relationships, counterparty credit worthiness and overall program compliance. In addition, the Energy Risk Management Program incorporates specific volume and financial limits for natural gas derivatives which begin at 40.0 percent of the approved fuel budget of the current year (the first year) and graduate down in 5.0 percent increments to 20.0 percent of the forecasted annual fuel budget for the fifth year. Oil derivatives are hedged based on the expected volume of oil consumed in conjunction with coal transportation costs.

Financial related derivatives are executed to modify interest rate risk on outstanding debt. These agreements are prepared in accordance with OUC's Treasury policy, presented to the Finance Committee and approved by the Board. Periodically, as defined by the underlying agreement, the net differential between the fixed and variable rate is exchanged with the counterparty and included as a component of interest expense. Financial-related derivatives terminated in conjunction with a bond refunding are deferred and included as a component of unamortized gain or loss on refunded bonds as a deferred inflow or outflow of resources, respectively. Financial-related derivatives, which are terminated prior to their original maturity date and are not terminated in conjunction with a bond refunding, are recognized as a component of interest expense unless otherwise authorized by Board action.

Current portion of long-term debt: Bonds payable within one year represent scheduled principal payments due within the upcoming year, in accordance with the serial requirements of the bond agreements. Funds to satisfy these scheduled principal payments are segregated and included as a component of internally designated assets.

Accounts payable and accrued expenses: Accounts payable and accrued expenses include liabilities incurred in conjunction with fuel and purchased power costs, supplier payables and accrued expenses for self-insurance. The following summarizes the significant payable balances included under this heading at September 30:

(Dollars in thousands)	2018	2017
Supplier payables	\$ 30,590	\$ 29,719
Hurricane related supplier payables	-	15,701
Fuel and purchased power payables	24,604	26,743
Accrued self-insurance expenses	3,044	2,856
Other accounts payable and accrued expenses	4,089	3,841
Total accounts payable and accrued expenses	\$ 62,327	\$ 78,860

Other accounts payable and accrued expenses under this heading include taxes billed on behalf of various governmental authorities and pollution remediation. Pollution remediation of \$1.7 million in both September 30, 2018 and 2017, was recorded in accordance with GASB Statement No. 49, "Accounting and Financial Reporting for Pollution Remediation Obligations."

NOTES TO THE FINANCIAL STATEMENTS

Note B – Summary of Significant Accounting Policies (continued)

Pension Plan: For purposes of measuring the pension liability, deferred outflows of resources and deferred inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the OUC Pension Plan and additions to/deductions from the plan's fiduciary net position were determined on the same basis as they were reported by the plan. For this purpose, the plan recognized benefit payments (including refunds of employee contributions) when due and payable in accordance with the benefit terms. Investments were reported at fair value, except for money market and alternative investments, which were reported at amortized cost.

Other Post-Employment Benefits Plan (OPEB): For purposes of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense, information about the fiduciary net position of the OUC OPEB Plan and additions to/deductions from the plan's fiduciary net position were determined on the same basis as they were reported by the plan. For this purpose, the plan recognized benefit payments when due and payable in accordance with the benefit terms. Investments were reported at fair value, except for money market and alternative investments, which were reported at amortized cost.

Compensated absences and accrued wages: OUC accrues vacation leave for all employees annually on January 1. Sick leave is earned annually on the employee's anniversary date and is accrued based on a ratio of sick leave taken to sick leave earned. This ratio is then used to determine an employee's payout at either the retirement rate of 50.0 percent or termination rate of 25.0 percent. No payout is accrued for employees with less than two years of employment. Compensatory time is also included in the liability and is accrued when earned. At September 30, 2018 and 2017, the estimated liability for compensated absences and accrued wages was \$14.3 million and \$14.0 million, respectively.

Other bonds payable: Variable rate bonds with final maturities extending past one year that are not supported by an underlying liquidity facility are classified as payable from current assets.

Asset retirement obligation and other liabilities: Included in this amount are the asset retirement obligation (ARO) costs associated with OUC's participant ownership interest in its nuclear generation facility, accrued closure and post-closure landfill costs and advances received from customers for construction commitments.

The ARO associated with the St. Lucie Unit 2 (SL2) facility was determined based on the December 2015 decommissioning report approved by the FPSC. OUC's minority share of the SL2 facility is 6.09 percent, and decommissioning closure costs are estimated to be \$52.9 million, in 2015 dollars. This liability continues to be systematically accreted over a life consistent with the plant's license period and at September 30, 2018 and 2017 was \$56.1 million and \$54.9 million, respectively. The operational license expiration date for SL2 is 2043. As of September 30, 2018 and 2017, nuclear generation facility decommissioning funds of \$41.8 million and \$42.2 million, respectively, were restricted to pay for OUC's minority share of the SL2 ARO.

The landfill closure and post-closure costs related to landfill sites at the Stanton Energy Center (SEC) are estimated to be \$3.2 million. Costs associated with the closing and future maintenance of these facilities were accrued in the amount of \$1.3 million and \$0.6 million as of September 30, 2018 and 2017, respectively, based on the capacity used to date of 41.5 percent and the remaining useful life of three years.

Unamortized discount/premium: Unamortized discount/premium on outstanding bonds was recorded in the year of issuance. Amortization of these amounts was recorded using the bonds outstanding method based on the individual serial maturities and was presented net of accumulated amortization.

Contributions in aid of construction: Developer and customer funds received for system development fees and assets were recorded as contributions in aid of construction in the period in which they were received on the Statements of Revenues, Expenses and Changes in Net Position.

Note B – Summary of Significant Accounting Policies (continued)

Net positions: OUC classifies net position into three components as follows:

- **Net investment in capital assets:** This component of net position consists of capital assets, net of accumulated depreciation reduced by the outstanding debt balances used to acquire or construct these assets.
- **Restricted:** This component consists of net position with external constraints placed on their use. Constraints include those by debt indentures, grants or laws and regulations of other governments and those established by law through constitutional provisions or enabling legislation.
- **Unrestricted:** This component of net position consists of net position that is not included in the definition of “net investment in capital assets” or “restricted.”

Subsequent events: Subsequent events for OUC have been evaluated through December 5, 2018, which is the date the financial statements were available to be issued.

Implementation of New GASB Accounting Standards

OUC early adopted GASB Statement No. 88, “*Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements,*” (Statement No. 88). The objective of this Statement is to improve the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt. This Statement requires that additional essential information related to debt be disclosed in notes to financial statements, including unused lines of credit; assets pledged as collateral for the debt; and terms specified in debt agreements related to significant events of default with finance-related consequences, significant termination events with finance-related consequences, and significant subjective acceleration clauses. This statement has no effect on the financial statements.

OUC early adopted GASB Statement No. 89, “*Accounting for Interest Cost Incurred before the End of a Construction Period,*” (Statement No. 89). The objective of this statement is to enhance the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period and to simplify accounting for interest costs incurred before the end of a construction period. This Statement requires that interest costs incurred before the end of a construction period be recognized as an expense in the period in which the cost is incurred for financial statements prepared using the economic resources measurement focus. As a result, interest costs incurred before the end of a construction period will not be included in the historical cost of a capital asset reported in a business-type activity or enterprise fund. This statement has no effect on the financial statements as OUC has historically expensed interest costs as incurred.

Future GASB Accounting Standard Implementations

In January 2017, GASB Statement No. 84, “*Fiduciary Activities,*” (Statement No. 84) was issued. Statement No. 84 establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on whether a government controls the assets of the fiduciary activity and the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and post-employment benefit arrangements that are fiduciary activities. Note disclosures and required supplementary information requirements about fiduciary activities are also addressed. This statement is under review and management has yet to determine the impact, if any, to the financial statements.

In June 2017, GASB Statement No. 87, “*Leases,*” (Statement No. 87) was issued. Statement No. 87 requires the recognition of certain lease assets and liabilities for leases that were previously classified as operating leases and recognized as deferred outflows or inflows of resources based on the payment provisions of the contract. This statement is under review and management has yet to determine the impact, if any, to the financial statements.

In August 2018, GASB Statement No. 90, “*Majority Equity Interests,*” (Statement No. 90) was issued. Statement No. 90 requires that a majority equity interest in a legally separate organization should be reported as an investment if a government’s holding of the equity interest meets the definition of an investment. A majority equity interest that meets the definition of an investment should be measured using the equity method, unless it is held by a special-purpose government engaged only in fiduciary activities, a fiduciary fund, or an endowment or a permanent fund. This statement is under review and management has yet to determine the impact, if any, to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

Note C – Utility Plant

Activities for the years ended September 30, 2018 and 2017 were as follows:

Net utility plant increased 1.6 percent and 1.7 percent in 2018 and 2017, respectively. In addition, OUC's depreciation recapture, included in the revenue requirement, represents 80.0 percent and 72.8 percent of the capital plan at September 30, 2018 and 2017, respectively.

Utility plant, net (Dollars in thousands)	2017	Additions	Transfers	Retirements/ reclassifications	2018
Utility plant					
Electric	\$ 3,110,900	\$ 16,406	\$ 125,779	\$ (10,624)	\$ 3,242,461
Water	599,592	5,248	13,009	(453)	617,396
Chilled Water	116,848	-	53	-	116,901
Lighting	88,191	-	3,100	(3,305)	87,986
Shared/Customer Service	243,785	1,356	11,387	(7,647)	248,881
Total utility plant	4,159,316	23,010	153,328	(22,029)	4,313,625
Accumulated depreciation					
Electric	(1,489,540)	(93,691)	-	3,441	(1,579,790)
Water	(235,156)	(15,812)	-	461	(250,507)
Chilled Water	(49,352)	(4,290)	-	713	(52,929)
Lighting	(41,843)	(4,494)	-	3,305	(43,032)
Shared/Customer Service	(124,473)	(18,393)	-	7,489	(135,377)
Total accumulated depreciation	(1,940,364)	(136,680)	-	15,409	(2,061,635)
Total depreciable utility plant, net	2,218,952	(113,670)	153,328	(6,620)	2,251,990
Land and other non-depreciable assets	73,091	177	-	(15)	73,253
Construction work in progress	159,025	161,539	(153,328)	(3,023)	164,213
Utility plant, net	\$ 2,451,068	\$ 48,046	\$ -	\$ (9,658)	\$ 2,489,456

Utility plant, net (Dollars in thousands)	2016	Additions	Transfers	Retirements/ reclassifications	2017
Utility plant					
Electric	\$ 3,027,391	\$ 17,233	\$ 82,268	\$ (15,992)	\$ 3,110,900
Water	575,682	4,385	19,621	(96)	599,592
Chilled Water	116,669	-	179	-	116,848
Lighting	79,009	-	9,840	(658)	88,191
Shared/Customer Service	214,262	1,523	42,192	(14,192)	243,785
Total utility plant	4,013,013	23,141	154,100	(30,938)	4,159,316
Accumulated depreciation					
Electric	(1,403,520)	(83,389)	-	(2,631)	(1,489,540)
Water	(220,349)	(14,904)	-	97	(235,156)
Chilled Water	(45,722)	(4,343)	-	713	(49,352)
Lighting	(37,552)	(4,217)	-	(74)	(41,843)
Shared/Customer Service	(122,299)	(16,283)	-	14,109	(124,473)
Total accumulated depreciation	(1,829,442)	(123,136)	-	12,214	(1,940,364)
Total depreciable utility plant, net	2,183,571	(99,995)	154,100	(18,724)	2,218,952
Land and other non-depreciable assets	72,569	542	-	(20)	73,091
Construction work in progress	154,216	161,880	(154,100)	(2,971)	159,025
Utility plant, net	\$ 2,410,356	\$ 62,427	\$ -	\$ (21,715)	\$ 2,451,068

NOTES TO THE FINANCIAL STATEMENTS

Note D – Power Generation Facility Operations

Jointly owned and owner operated generation facilities: OUC maintains fiscal, budgetary and operating control at four power generation facilities for which there are undivided participant ownership interests. These undivided ownership interests are with the Florida Municipal Power Agency (FMPA) and Kissimmee Utility Authority (KUA). Each agreement is limited to the generation facilities and excludes the external facilities. OUC also maintains operational control of a wastewater treatment facility at the SEC Unit 1 and Unit 2 sites through an agreement with Orange County.

Jointly owned and non-OUC operated: OUC maintains an undivided participant interest at the SEC Unit A located at OUC's SEC, SL2 and McIntosh 3 (MAC3) generation facility. In each of these agreements, fiscal, budgetary and operational controls are not maintained by OUC, with the exception of fuel-related services at SEC Unit A where OUC retains responsibility as fuel agent through the purchased power agreement term. Funds secured in this role as fuel agent are restricted on the Statements of Net Position and disclosed in Note E.

Wholly owned and OUC operated: OUC maintains fiscal, budgetary and operating control of SEC Unit B with no undivided participant ownership interests.

OUC and non-OUC-operated agreements and the related undivided interests are as follows:

Facility name	Operational year	Nameplate capacity	OUC undivided ownership interest	Net OUC megawatt capacity	Fuel Source
Indian River (IRP - A&B)	1989	76	48.80%	37	Natural gas
Indian River (IRP - C&D)	1992	224	79.00%	177	Natural gas
Stanton Unit A (SEC Unit A) ¹	2003	633	28.00%	177	Natural gas
Stanton Unit B (SEC Unit B)	2010	300	100.00%	300	Natural gas
McIntosh Unit 3 (MAC3) ²	1982	364	40.00%	146	Coal
Stanton Unit 1 (SEC Unit 1)	1987	425	68.55%	291	Coal
Stanton Unit 2 (SEC Unit 2)	1996	425	71.59%	304	Coal
St. Lucie Unit 2 (SL2)	1983	850	6.09%	52	Nuclear

¹ In May 2018, Southern Company announced the sale of its equity interest in SEC Unit A to NextEra Energy, Inc. as part of a larger sale that is expected to close in the first quarter of 2019.

² In December 2018, Lakeland Electric, owner operator of MAC3, announced the retirement of this generation facility between 2023 and 2025.

Asset valuation: Plant balances for SEC Unit 1, SEC Unit 2, MAC3 and IRP A-D include the cost of common and/or external facilities. At the other plants, participants pay user charges to the operating entity for the cost of common and/or external facilities. User charges paid for SEC Unit A are remitted back to OUC at their proportionate ownership interest of shared facilities.

Allowance for depreciation and amortization of utility plant is determined by each participant based on their proportionate ownership interest and depreciation methodology.

The following is a summary of OUC's recorded gross and net share of each jointly and wholly owned power generation facility at September 30:

(Dollars in thousands)	2018			2017		
	Utility plant	Accumulated depreciation	Net book value	Utility plant	Accumulated depreciation	Net book value
SEC Unit 2	\$ 493,221	\$ 262,868	\$ 230,353	\$ 485,171	\$ 248,144	\$ 237,027
SEC Unit 1	405,325	262,061	143,264	398,469	248,384	150,085
MAC3	200,492	142,298	58,194	197,478	132,580	64,898
SL2	199,111	93,431	105,680	197,229	91,397	105,832
SEC Unit A	88,350	48,534	39,816	84,979	51,061	33,918
IRP	59,320	48,011	11,309	59,043	46,508	12,535
SEC Unit B	298,126	88,331	209,795	284,771	75,090	209,681
Total	\$ 1,743,945	\$ 945,534	\$ 798,411	\$ 1,707,140	\$ 893,164	\$ 813,976

NOTES TO THE FINANCIAL STATEMENTS

Note E – Cash, Cash Equivalents and Investments

OUC maintains a portion of its cash, cash equivalents and investments in qualified public depository accounts with institutions insured by the Federal Deposit Insurance Corporation or collateralized by a pool of U.S. Governmental securities, per the Florida Security for Public Deposits Act, Chapter 280, of the Florida Statutes as well as other types authorized by the Treasury policy.

Unexpended funds from the sale of bonds, debt service funds, and other special funds are included in the restricted and internally designated assets section of the Statements of Net Position. The use of these funds is designated in accordance with applicable debt indentures, Board action, or any other laws and regulations established through legislation.

Securities are recorded at fair value with realized and unrealized gains and losses recorded as a component of interest income in the Statements of Revenues, Expenses and Changes in Net Position in 2017. Beginning in 2018, in accordance with Board approval, unrealized gains and losses were deferred and recorded as a component of regulatory assets in the Statement of Net Position.

The Treasury policy, inclusive of the maximum portfolio weighting, provides management with guidelines to ensure risks associated with these assets are mitigated. The following are the key controls which OUC utilizes to mitigate investment risk:

- **Interest rate risk:** To mitigate this risk, OUC limits maturities based on investment type and credit strength and executes transactions in accordance with the “prudent person” rule requiring the evaluation of current market conditions to ensure overall interest rate risks that might adversely affect the portfolio value are mitigated.
- **Custodial credit risk:** OUC views this type of risk as minimal due to its use of Qualified Public Depositories (QPD) of the State of Florida, Local government investment pools which are backed by securities allowed by law by the State of Florida or money market mutual funds rated at the highest available credit rating for this type of security with a stable net asset value but could be subject to daily mark to market and no later than next day liquidity. OUC had \$137.6 million and \$106.5 million of investments held in money market funds and QPD accounts that were exposed to this risk as of September 30, 2018 and 2017, respectively.
- **Credit risk:** To mitigate the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment, OUC limits investments to those rated, at a minimum, “A-1 / P-1 / F1” or equivalent for commercial paper and “A3 / A-” for medium-term corporate notes by nationally recognized rating agencies.
- **Foreign currency risk:** OUC is not authorized to invest in foreign currency and, as such, is not exposed to this risk.
- **Concentration risk:** This is the risk of loss associated with the extent of OUC’s investment in a single issuer. OUC places limits on the amounts invested in any one issuer for certain types of securities. The following were the investment concentrations greater than 5.0 percent for a single issuer as of September 30:

Investment type (Dollars in Thousands)	2018		2017	
U.S. Treasury notes	\$ 213,592	32%	\$ 129,953	24%
U.S. Agencies				
Federal Home Loan Banks	\$ 75,182	11%	\$ 102,953	19%
Federal National Mortgage Association (Fannie Mae) (1)	\$ 10,742	N/A	\$ 25,073	5%
Local government surplus funds investment pool				
Florida State Board of Administration	\$ 56,029	8%	\$ 31,971	6%
Money market mutual funds				
MSIFT Ultra Short Fund	\$ 44,000	7%	\$ 43,000	8%

(1) Federal National Mortgage Association was under the 5.0 percent threshold in 2018

NOTES TO THE FINANCIAL STATEMENTS

Note E – Cash, Cash Equivalents and Investments (continued)

The following table summarizes the investment criteria underlying the policy segregated by investment type, credit guidelines and maximum portfolio weighting.

Investment type	Credit guidelines	Maximum portfolio weighting	Portfolio weighting at September 30,	
			2018	2017
Certificates of deposit	Investments held by or purchased from institutions certified with the Florida Security of Public Deposits Act, Chapter 280 of the Florida Statutes.	5%	-	-
Corporate notes and multi-national sovereign debt	Minimum rating of "A3" / "A-" by at least two nationally recognized rating agencies.	35%	21%	21%
Municipal notes	Minimum "A" rating by a nationally recognized rating agency.	25%	2%	3%
Bankers acceptances	Inventory based with an unsecured, uninsured and unguaranteed obligation rating of at least "P-1" and "A", and "A-1" and "A" by Moody's and S&P, respectively. Bank must be ranked in the top 100 banks.	10%	-	-
Money market mutual funds	Limited to funds that meet a stable net asset value and have the highest available credit rating for this type of security.	30%	7%	8%
Commercial paper	Minimum rating of "A-1", "P-1" and "F1" by at least two nationally recognized rating agencies.	20%	9%	5%
Depository accounts	Investments held by or purchased from institutions certified with the Florida Security of Public Deposits Act, Chapter 280 of the Florida Statutes.	30%	2%	2%
Local government surplus funds investment pool (1)	Qualified under the laws of the State of Florida with no limitations or restrictions on withdrawals.	25%	11%	10%
U.S. Treasury notes	Direct obligations that are unconditionally guaranteed by the United States Government.	100%	32%	24%
U.S. Agencies	Indebtedness issued by government-sponsored enterprises (GSE), which are non-full faith and credited by the United States Government.	100%	16%	27%
Repurchase and reverse repurchase agreements	Secured transactions executed under a master repurchase agreement with collateral limited to direct governmental and agency obligations with terms of less than 10 years and held and maintained by a third-party trust at a market value of 102% of the cash value.	50% and 20%, respectively	-	-

(1) Financial Statements for the Florida Prime investment pool may be obtained by contacting the Chief Financial Officer, State Board of Administration of Florida, 1801 Hermitage Boulevard, Suite 101, Tallahassee, Florida 32308 and Financial Statements for the Florida Fixed Income Trust investment pool may be obtained by contacting the Administrator for Florida Fixed Income Trust, c/o Wertz York Capital Management Group, P.O. Box 9691, Tampa, FL 33674.

The following schedule discloses the weighted average maturity in years for each of the investment classifications at September 30:

Investment type	Credit ratings		
	Moody's Investors Service/Standard & Poor's/Fitch Ratings	2018	2017
Corporate notes and multi-national sovereign debt	Aaa - A3 / AAA - A- / AAA - A	2.13	1.91
Municipal notes	Aa2 - Aa3 / AA - AA- / AA - AA-	1.54	2.64
U.S. Agencies	Aaa / AA+ / AAA	1.42	1.66
U.S. Treasury notes	Aaa / AA / AAA	0.99	1.82
Commercial paper	A-1+ - A-1 / P-1 / F1+ - F1	0.00	0.07

NOTES TO THE FINANCIAL STATEMENTS

Note E – Cash, Cash Equivalents and Investments (continued)

The following schedule discloses cash, cash equivalents and investments at September 30:

(Dollars in thousands)	2018	2017
Cash	\$ 35,795	\$ 45,360
Cash equivalents		
Local government surplus funds investment pool	76,141	51,153
Money market mutual funds	44,977	43,000
Commercial paper	19,999	9,976
Depository accounts	16,529	12,302
U.S. Agencies	15,999	9,991
U.S. Treasury notes	-	7,997
Total cash equivalents	173,645	134,419
Total cash and cash equivalents	209,440	179,779
Investments		
U.S. Treasury notes	213,592	121,956
Corporate notes and multi-national sovereign debt	138,799	110,383
U.S. Agencies	89,451	134,146
Commercial paper	40,997	17,999
Municipal notes	11,798	14,228
Total investments	494,637	398,712
Total cash, cash equivalents and investments	\$ 704,077	\$ 578,491
Restricted and internally designated assets		
Restricted assets		
Construction funds	\$ 89,992	\$ -
Nuclear generation facility decommissioning funds	41,804	42,176
Total restricted assets	131,796	42,176
Internally designated assets		
Rate reserve funds	177,547	190,518
Deposits and advances	113,259	108,077
Debt service sinking funds and cost of issuance reserve funds	99,527	86,949
Capital reserve	71,468	49,468
Renewal and replacement fund	53,415	52,607
Self-insurance fund and excess pension plan fund	10,477	9,500
Total internally designated assets	525,693	497,119
Total restricted and internally designated assets	657,489	539,295
Cash and investments	47,099	39,408
Less accrued interest receivable from restricted and internally designated assets	(511)	(212)
Total cash, cash equivalents and investments	\$ 704,077	\$ 578,491

Note F – Fair Value Measurements

OUC categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based upon the observability of the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 inputs are significant unobservable inputs.

Investments

Investments are recorded at fair value as described above. The following are additional considerations used to categorize investments:

- **Depository accounts** include money market and other liquid funds which are classified as Level 1 since quoted prices in active markets are available. According to GASB Statement No. 72, “*Fair Value Measurement and Application*,” (Statement No. 72), money market investments and participating interest-earning investment contracts that have a remaining maturity at the time of purchase of one year or less and are held by governments other than external investment pools are measured at amortized cost.
- **Local government surplus funds investment pools** are classified as Level 2 because they are financial instruments held in co-mingled funds. According to Statement No. 72, an external investment pool is measured at the amortized cost per share determined by the pool.
- **Debt securities** classified as Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities. Debt securities classified in Level 2 of the fair value hierarchy are valued using a matrix pricing technique. Matrix pricing is used to value securities based on the securities’ relationship to benchmark quoted prices.

Derivative Instruments

The fair value of OUC’s interest rate swap agreements is based on a discounted cash flow model with Level 2 inputs including the value of the relevant market index upon which the swaps are based. The fair value of OUC’s debt is presented in Notes H and N.

Fuel derivatives are classified as Level 1 in the fair value hierarchy since quoted commodity prices in active markets are available. The fair value of OUC’s fuel rate hedges is presented in Note N.

Donated Capital Assets

Donated capital assets are measured at acquisition value. Acquisition value is the price that would be paid to acquire an asset with equivalent service potential in an orderly market transaction at the acquisition date, or the amount at which a liability could be liquidated with the counterparty at the acquisition date. The donated capital assets acquisition value for water infrastructure received from developers and customers were included as contributions in aid of construction in the Statements of Revenues, Expenses and Changes in Net Position was \$4.8 million and \$4.0 million for the years ended September 30, 2018 and 2017, respectively.

NOTES TO THE FINANCIAL STATEMENTS

Note F – Fair Value Measurements (continued)

OUC had the following fair value measurements by fair value level at September 30:

(Dollars in thousands)	2018	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Cash equivalents and investments				
Investments by fair value level:				
Debt securities				
U.S. Agencies	\$ 89,451	\$ -	\$ 89,451	\$ -
U.S. Treasury notes	118,662	118,662	-	-
Corporate notes and multi-national sovereign debt	106,361	-	106,361	-
Municipal notes	11,798	-	11,798	-
Total investments by fair value level	326,272	\$ 118,662	\$ 207,610	\$ -
Investments measured at the amortized cost:				
Debt securities				
Corporate notes and private placements	32,438			
U.S. Treasury notes	94,930			
Commercial paper	40,997			
Total investments measured at the amortized cost	168,365			
Cash equivalents measured at the amortized cost:				
Local government surplus funds investment pool	76,141			
Money market mutual funds	44,977			
Depository accounts	16,529			
Debt securities				
U.S. Agencies	15,999			
Commercial paper	19,999			
Total cash equivalents measured at the amortized cost	173,645			
Total cash equivalents and investments	\$ 668,282			
Derivatives:				
Interest rate swaps	\$ (4,824)	\$ -	\$ (4,824)	\$ -
Fuel hedges	(2,192)	(2,192)	-	-
Total derivatives	\$ (7,016)	\$ (2,192)	\$ (4,824)	\$ -

(Dollars in thousands)	2017	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)
Cash equivalents and investments				
Investments by fair value level:				
Debt securities				
U.S. Agencies	\$ 116,158	\$ -	\$ 116,158	\$ -
U.S. Treasury notes	95,963	95,963	-	-
Corporate notes and multi-national sovereign debt	76,404	-	76,404	-
Municipal notes	14,228	-	14,228	-
Total investments by fair value level	302,753	\$ 95,963	\$ 206,790	\$ -
Investments measured at the amortized cost:				
Debt securities				
Corporate notes and private placements	33,979			
U.S. Treasury notes	25,993			
Commercial paper	17,999			
U.S. Agencies	17,988			
Total investments measured at the amortized cost	95,959			
Cash equivalents measured at the amortized cost:				
Local government surplus funds investment pool	51,153			
Money market mutual funds	43,000			
Depository accounts	12,302			
Debt securities				
U.S. Agencies	9,991			
Commercial paper	9,976			
U.S. Treasury notes	7,997			
Total cash equivalents measured at the amortized cost	134,419			
Total cash equivalents and investments	\$ 533,131			
Derivatives:				
Interest rate swaps	\$ (11,865)	\$ -	\$ (11,865)	\$ -
Fuel hedges	(1,268)	(1,268)	-	-
Total derivatives	\$ (13,133)	\$ (1,268)	\$ (11,865)	\$ -

Note G – Regulatory Deferrals

Based on regulatory action taken by the Board, and in accordance with the Regulated Operations section within Statement No. 62, OUC has recorded the following regulatory assets and credits that will be included in the rate-making process and recognized as expenses and revenues, respectively, in future periods.

Regulatory Assets

Unrecognized long-term employee benefit costs: As a result of the implementation of GASB pronouncements related to defined benefit pensions and OPEB, the Board approved regulatory assets of \$118.8 million and \$65.1 million, respectively. These regulatory assets will be recognized in a method that will, at a minimum, match the expense to the related annual actuarial required funding amount. The planned recovery of these costs has been approved through 2025. The amount of the deferred long-term employee benefit costs at September 30, 2018 and 2017 was \$130.3 million and \$148.0 million, respectively.

Anticipated recovery of hurricane restoration costs: As a result of the impacts of Hurricanes Matthew and Irma, OUC incurred restoration costs of \$29.5 million. Based on Federal Emergency Management Agency (FEMA) eligibility guidelines, a significant portion of the costs associated with storm restoration are anticipated to be eligible for reimbursement through the FEMA cost reimbursement process. In 2017, the Board approved the establishment of a regulatory asset to ensure the recognition of these costs is consistent with the cost reimbursement process. In 2018, an additional \$0.3 million was incurred for restoration activities. The amount of the unrecognized hurricane restoration cost as of September 30, 2018 and 2017 was \$21.2 million and \$20.9 million, respectively.

Unrecognized fair value interest rate hedge costs: This amount represents the deferral of the suspended residual value of the interest rate swap valuation in association with the refunded Series 2011A *Windows* Bonds. The recognition of this deferred interest rate swap valuation is anticipated to be recovered, consistent with the Term Rate period of the Series 2017A Bonds, by October 1, 2020. The unrecognized fair value interest rate hedge costs at September 30, 2018 and 2017 were \$10.0 million and \$12.7 million, respectively.

Asset retirement obligation costs: This amount represents the deferral of the difference between retirement obligation expense and the amount recovered in the rates charged to customers. To date, retirement obligation expense exceeds the amount charged to customers, net of investment income earned from the associated restricted retirement obligation assets. As such, the asset retirement obligation regulatory asset at September 30, 2018 and 2017 was \$7.0 million and \$6.2 million, respectively.

Unrealized investment valuations: In 2018, unrealized investment valuations were deferred to ensure revenues and expenses were recovered consistent with the rate-making model. While changes in investment valuations have historically been recognized in the period in which they were incurred, these changes were abated as investments approached their maturity date. The amount of deferred unrealized investment valuation losses as of September 30, 2018 were \$4.7 million.

Unamortized issue costs: In conjunction with the implementation of GASB Statement No. 65. "*Items Previously Reported as Assets and Liabilities*", OUC established a regulatory asset for unrecognized debt issue costs. The regulatory asset will be collected in rates over a period of ten years. Future debt issue costs are expensed as incurred. The unrecognized issue cost at September 30, 2018 and 2017 was \$4.2 million and \$5.1 million, respectively.

Unamortized interest costs: This amount represents the deferral of interest costs incurred in association with the refunded Series 1993 and 1993B Bonds as a result of differing short-term and long-term rates at the time of bond issuance. Deferred charges are currently amortized to interest expense over the remaining period of the original bond series. The amount of deferred charges at September 30, 2018 and 2017 was \$1.6 million and \$2.0 million, respectively.

NOTES TO THE FINANCIAL STATEMENTS

Note G – Regulatory Deferrals (continued)

The following is a summary of OUC's regulatory assets at September 30:

(Dollars in thousands)	2018	2017
Unrecognized long-term employee benefit costs	\$ 130,280	\$ 147,957
Anticipated recovery of hurricane restoration costs	21,196	20,856
Unrecognized fair value interest rate hedge costs	9,998	12,747
Asset retirement obligation costs	6,956	6,165
Unrealized investment valuations	4,677	-
Unamortized issue costs	4,248	5,098
Unamortized interest costs	1,632	2,040
Total regulatory assets	\$ 178,987	\$ 194,863

Regulatory Credits

Fuel reserves: This account was established in accordance with guidelines from the Public Utilities Regulatory Policies Act of 1978 and represents the difference between the fuel costs charged to customers, inclusive of accrued utility revenue and fuel costs. The amount of fuel reserves at September 30, 2018 and 2017 was \$119.3 million and \$118.4 million, respectively, inclusive of \$40.0 million in both years to mitigate carbon constraint costs.

Electric and water reserves: The Board established the electric and water reserves for costs or revenues that are to be recovered by or used to reduce customer prices in periods other than when incurred or realized. The Board approved the recognition of \$13.8 million in 2018 to offset costs related to the issuance of the Series 2018A bonds, post-implementation CC&B activities, a delayed water rate increase, and additional depreciation for coal generation facilities. In 2017, the Board approved the use of \$5.9 million of reserves to mitigate unplanned hurricane restoration costs and the use of \$1.4 million for implementation costs of the customer billing system, offset by a deferral of \$1.5 million in unplanned water revenues. The electric and water reserves at September 30, 2018 and 2017 were \$52.6 million and \$66.7 million, respectively.

Deferred wholesale trading profits: This account represents a portion of profits generated from resale sales, net of funds used for approved regulatory actions. No funds were approved for deferral or usage in 2018 or 2017.

Deferred gain on sale and settlement of assets: In accordance with the Board's Capital Asset Disposal policy, gains and financial settlements related to the disposition of long-term assets are recognized as a regulatory liability on the Statements of Net Position and systematically recognized over a period consistent with the lives of the assets with which they are associated.

- In 2018, OUC sold the West Copeland property and recognized a deferred gain of \$0.8 million.
- In 2015, as part of the I-4 Ultimate Project, the FDOT imposed an eminent domain action on a portion of OUC's Gardenia property, resulting in a gain of \$0.8 million.
- In July 2005, the Florida Department of Transportation (FDOT) imposed an eminent domain action and took possession of OUC's administration building parking garage. In exchange for taking possession of OUC's garage and the underlying land, the FDOT provided OUC with an adjacent land parcel and a cash settlement of \$15.0 million. In association with this action, OUC constructed a new administration facility and utilized \$6.0 million of the gain on settlement for transition and relocation costs. In addition to the accrued transition and relocation amount, a residual gain on settlement amount of \$2.3 million was deferred. In 2012, the old administration building site was sold and the associated gain on the sale of \$0.9 million was deferred. The balance in the deferred gain on settlement related to the administration building remained \$2.3 million at September 30, 2018 and 2017.
- In 1999, OUC sold the steam units at IRP and recognized a gain of \$144.0 million. In 2012, this asset was repurchased and outstanding deferred rights associated with the original sale in the amount of \$10.4 million were reclassified to the deferred gain. Recognition of the gain is aligned with the utilization of the SEC Unit A generation facility. The balance in the deferred gain on sale of assets related to IRP was \$46.1 million and \$52.1 million at September 30, 2018 and 2017, respectively.

NOTES TO THE FINANCIAL STATEMENTS

Note G – Regulatory Deferrals (continued)

In conjunction with the recording of these regulatory credits, the Board internally designated funds in the amount of \$178.8 million and \$190.5 million at September 30, 2018 and 2017, respectively.

The following is a summary of OUC’s regulatory credits at September 30:

(Dollars in thousands)	2018	2017
Fuel reserves	\$ 119,310	\$ 118,352
Electric and water reserves	52,551	66,699
Deferred wholesale trading profits	16,000	16,000
Deferred gain on sale and settlement of assets	49,956	55,220
Total regulatory credits	\$ 237,817	\$ 256,271

Note H – Long-Term Debt

The following schedule summarizes the long-term debt activity for the years ended September 30:

Bond Series (Dollars in thousands)	Final principal payment	Interest rates (%)	2017	Additions during year	Decreases during year	2018	Current portion
2003T	2018	5.29%	\$ 9,765	\$ -	\$ 4,755	\$ 5,010	\$ 5,010
2009B	2033	5.00%	65,160	-	-	65,160	-
2009C	2017	3.50 - 5.00%	19,040	-	19,040	-	-
2010A	2040	5.662%	200,000	-	-	200,000	-
2010C	2022	4.00 - 5.25%	54,830	-	8,095	46,735	8,480
2011B	2023	3.00 - 5.00%	68,100	-	5,425	62,675	13,325
2011C	2027	4.00 - 5.00%	86,450	-	-	86,450	-
2012A	2027	4.00 - 5.00%	51,670	-	2,155	49,515	2,235
2013A	2025	3.00 - 5.00%	230,965	-	2,500	228,465	5,370
2015A	2035	5.00%	94,905	-	-	94,905	-
2016A	2033	4.00 - 5.00%	142,690	-	16,415	126,275	34,495
2017A	2027	3.00 - 5.00%	98,360	-	-	98,360	-
2018A	2038	5.00%	-	150,220	-	150,220	-
Total fixed rate debt			1,121,935	150,220	58,385	1,213,770	68,915
2008	2033	Variable rate (1)/(2)	200,000	-	-	200,000	-
2015B	2039	Variable rate (1)/(3)	115,090	-	-	115,090	-
Total variable rate debt			315,090	-	-	315,090	-
Total debt			1,437,025	\$ 150,220	\$ 58,385	1,528,860	\$68,915
Less current portion			(58,385)	\$ (68,915)	\$ 58,385	(68,915)	
Total long-term debt			\$ 1,378,640			\$ 1,459,945	

(1) Variable rates ranged from 0.88% to 1.85% for the year ended September 30, 2018.

(2) The Series 2008 Variable Rate Demand Obligation Bonds of \$200.0 million are supported by a Standby Bond Purchase Agreement (SBPA), which will expire on April 4, 2022.

(3) The Series 2015B Variable Rate Demand Obligation Bonds of \$115.1 million are supported by a SBPA, which will expire on October 1, 2020.

NOTES TO THE FINANCIAL STATEMENTS

Note H – Long-Term Debt (continued)

The following schedule summarizes the long-term debt activity for the years ended September 30:

Bond Series (Dollars in thousands)	Final principal payment	Interest rates (%)	2016	Additions during year	Decreases during year	2017	Current portion
2003T	2018	5.29%	\$ 14,280	\$ -	\$ 4,515	\$ 9,765	\$ 4,755
2006	2016	4.50 - 5.00%	11,785	-	11,785	-	-
2009B	2033	5.00%	65,160	-	-	65,160	-
2009C	2017	3.50 - 5.00%	37,230	-	18,190	19,040	19,040
2010A	2040	5.662%	200,000	-	-	200,000	-
2010C	2022	4.00 - 5.25%	62,575	-	7,745	54,830	8,095
2011B	2023	3.00 - 5.00%	69,675	-	1,575	68,100	5,425
2011C	2027	4.00 - 5.00%	86,450	-	-	86,450	-
2012A	2027	4.00 - 5.00%	52,935	-	1,265	51,670	2,155
2013A	2025	3.00 - 5.00%	233,255	-	2,290	230,965	2,500
2015A	2035	5.00%	94,905	-	-	94,905	-
2016A	2033	4.00 - 5.00%	142,690	-	-	142,690	16,415
2017A	2027	3.00 - 5.00% (3)	-	98,360	-	98,360	-
Total fixed rate debt			1,070,940	98,360	47,365	1,121,935	58,385
2007	2016	Variable rate (1)	13,400	-	13,400	-	-
2008	2033	Variable rate (1)/(2)	200,000	-	-	200,000	-
2011A	2027	Variable rate (1)/(3)	98,360	-	98,360	-	-
2015B	2039	Variable rate (1)/(4)	115,090	-	-	115,090	-
Total variable rate debt			426,850	-	111,760	315,090	-
Total debt			1,497,790	\$ 98,360	\$ 159,125	1,437,025	\$58,385
Less Bonds payable w ithin one year			(60,765)	\$ (58,385)	\$ 60,765	(58,385)	
Less Other bonds payable (3)			(98,360)	-	98,360	-	
Less current portion			(159,125)	\$ (58,385)	\$ 159,125	(58,385)	
Total long-term debt			\$ 1,338,665			\$ 1,378,640	

(1) Variable rates ranged from 0.54% to 0.95% for the year ended September 30, 2017.

(2) The Series 2008 Variable Rate Demand Obligation Bonds of \$200.0 million are supported by a SBPA, w hich w ill expire on April 4, 2022.

(3) The Series 2011A Bonds, of \$98.4 million w ere issued in the Window s mode as extendable debt excluding underlying liquidity facilities. As such, these bonds w ere classified as current but have since been refunded by the 2017A bonds.

(4) The Series 2015B Variable Rate Demand Obligation Bonds of \$115.1 million are supported by a SBPA, w hich w ill expire on October 1, 2020.

NOTES TO THE FINANCIAL STATEMENTS

Note H – Long-Term Debt (continued)

Debt service requirements: Aggregate annual debt service requirements at September 30 are presented below. The schedule includes net receipts and payments on outstanding effective hedging derivative instruments and interest subsidies anticipated on refundable tax credits. The Series 2008 and Series 2015B Bonds were reported according to the scheduled maturity dates as management anticipates these bonds will remain outstanding.

Variable interest rates are included based upon budgeted projections and are assumed to remain static until their maturity. As these rates vary, actual interest payments on variable rate bonds and effective hedging derivative instruments will vary in relation to these changes.

(Dollars in thousands)	Principal	Interest	Federal interest subsidy	Hedging derivative instrument	Total
2019	\$ 60,340	\$ 64,858	\$ (3,702)	\$ (202)	\$ 121,294
2020	73,930	62,698	(3,702)	(489)	132,437
2021	82,050	58,602	(3,702)	-	136,950
2022	80,240	55,097	(3,702)	-	131,635
2023	76,500	51,114	(3,702)	-	123,912
2024-2028	375,075	199,874	(18,510)	-	556,439
2029-2033	298,135	130,681	(18,510)	-	410,306
2034-2038	317,425	63,397	(14,087)	-	366,735
2039-2043	96,250	7,469	(2,305)	-	101,414
Long-term debt	1,459,945	693,790	(71,922)	(691)	2,081,122
Current portion	68,915	62,628	(3,702)	1,054	128,895
Total debt	\$ 1,528,860	\$ 756,418	\$ (75,624)	\$ 363	\$ 2,210,017

General bond resolution: All bonds outstanding were subject to the provision of this resolution for which some of the key provisions are as follows:

- **Rate covenant:** The net revenue requirement for annual debt service has been set at 100.0 percent of available funds plus net revenues at 125.0 percent of annual debt service.
- **Conditions precedent:** This test is limited to OUC's certification that it meets the rate covenant.
- **Flow of funds:** There are no funding requirements; however, consistent with prior resolutions, OUC can determine whether to fund a debt service reserve account on an issue-by-issue basis or internally designate funds.
- **System definition:** OUC's system definition has been modified to utility system. This definition is a more expansive definition to accommodate organizational changes and the expansion into new services.
- **Sale of assets:** System assets may be sold if the sale will not interfere with OUC's ability to meet rate covenants. The net benefit of capital asset dispositions in excess of \$0.5 million will be reinvested into the utility system or used to retire outstanding debt. As such, there are no assets pledged as collateral.
- **Finance-related consequences and acceleration:** There are no events of default or other termination events with finance-related consequences or subjective acceleration clauses.

Issued bonds: In January 2018, OUC issued the fixed rate Series 2018A Bonds at a par value of \$150.2 million and a premium of \$30.9 million with a fixed rate coupon of 5.0 percent, paid semiannually. Proceeds from the sale of the bonds are being used to finance capital spending through 2019. The bonds are scheduled to mature beginning October 1, 2023 with a final maturity of October 1, 2038.

Refunded bonds: Consistent with accounting guidance, all refunded and defeased bonds are treated as extinguished debt for financial reporting purposes and have been removed from the Statements of Net Position. The proceeds secured from refunding transactions are invested in United States Treasury obligations in irrevocable escrow deposit trust funds. Each escrow deposit trust is structured to mature at such time as to provide sufficient funds for the payment of maturing principal and interest on the refunded bonds. Interest earned or accrued on these escrow funds has been pledged and will be used for the payment of the principal and interest on each respective bond series.

NOTES TO THE FINANCIAL STATEMENTS

Note H – Long-Term Debt (continued)

On February 23, 2017, OUC issued the Series 2017A variable-rate bonds with a par amount of \$98.4 million and a premium of \$10.3 million. The proceeds were used for the refunding of the Series 2011A *Windows* Bonds of \$98.4 million and a payment to the interest rate swap counterparty to suspend cash flows on the 2011A interest rate swap. The Series 2017A Bonds have maturity dates between October 1, 2026 and October 1, 2027. The bonds were issued initially in the Term Rate Mode with fixed rate coupons of 3.0 and 5.0 percent until October 1, 2020.

Debt Issued (Dollars in thousands)	Month Issued	Par Amount Issued	Premium on Issuance	Par Amount Refunded	PV Savings	Accounting Loss	Savings % of Refunded Bonds	Debt Refunded
2017A	February 2017	\$ 98,360	\$ 10,303	\$ 98,360	\$ 97	\$ -	0.1%	2011A

The balance outstanding at September 30, 2018 and 2017 for defeased bonds was \$149.0 million for each year.

Interest rate swaps: OUC limits its execution of interest rate swap agreements to major financial institutions with a minimum credit rating of “A3” or “A-” by any two nationally recognized credit rating agencies. The ratings of all current swap counterparties met the minimum rating requirements as of the execution dates. Although some counterparty ratings have changed since the date of issuance, OUC does not anticipate nonperformance by a counterparty nor have any instances of this nature occurred. In the event of the termination of a swap agreement, OUC may be required to make or be subject to receive a termination payment, as shown in the swap schedule below.

In accordance with each interest rate swap agreement, collateral deposit thresholds have been established. These thresholds require OUC to remit deposits to mitigate the counterparty’s exposure to credit risk. If OUC were to experience a credit downgrade, established thresholds would be reduced, requiring additional collateral deposits. There were no collateral deposits held by OUC counterparties at September 30, 2018 and collateral deposits in the amount of \$2.9 million were held by OUC counterparties at September 30, 2017 due to market volatility and the fair value liability in excess of contractual thresholds of \$10.0 million.

The following schedule summarizes OUC’s fair value position, based on quoted market rates, for its outstanding swap agreements at September 30, 2018 and 2017. Costs associated with these agreements are deferred and amortized over the life of the underlying bond agreement. The notional amounts below are the basis for which interest is calculated; however, the notional amounts are not exchanged. Upon the refunding of the Series 2011A *Windows* Bonds by the Series 2017A Bonds, the Series 2017A Bonds became the series of bonds related to the 2017A Swap. Prior to October 1, 2020, there will be no periodic payments to or from OUC under the 2017A Swap and the Series 2017A Bonds will bear interest at fixed rates. On October 1, 2020 the Series 2017A Bonds will be subject to a mandatory tender after which OUC intends to remarket the bonds in a variable rate mode to offset the restart of cash flows from the 2017A Swap. See Note N for additional derivative instrument disclosures.

Bond Series	Notional amount (000)'s	OUC pays	Rate paid	Rate received	Initiation date	Termination date	2018 Fair value liability/ (asset) (000)'s	2017 Fair value liability/ (asset) (000)'s	Counterparty
2017A	\$ 100,000	Fixed	3.780%	67% of LIBOR	6/1/2011	10/1/2027	\$ 9,998	\$ 12,748	Morgan Stanley
2015B	\$ 115,090	Fixed	2.075%	67% of LIBOR	10/23/2015	10/1/2039	(5,174)	(883)	Goldman Sachs
Total							\$ 4,824	\$ 11,865	

Goldman Sachs counterparty credit rating - A1 / A+ / A+
Morgan Stanley counterparty credit rating - A3 / BBB+ / A

Unused lines of credits: There are no unused lines of credit at September 30, 2018 and 2017.

Note I – Insurance Programs and Claims

Insurance Programs

OUC was exposed to various risks of loss related to torts, theft and destruction of assets, errors and omissions and natural disasters. In addition, OUC was exposed to risks of loss due to injuries and illness of its employees. These risks were managed through OUC’s self-insurance and third-party claims administration programs, and recovery of eligible costs through FEMA public assistance grants.

Under the self-insurance program, OUC was liable for all claims up to certain maximum amounts per occurrence. At September 30, 2018, insurance coverage was available for claims in excess of \$0.25 million for healthcare coverage and \$2.0 million for general and automobile liability. As of September 30, 2018, coverage was available for workers’ compensation claims in excess of \$0.5 million.

The healthcare benefits program was administered by an insurance company (the Administrator). The Administrator was responsible for processing claims in accordance with OUC’s benefit specifications and was reimbursed regularly for claims paid. Incurred claims included current period payments and estimated incurred but not received claims based on actuarial information received in conjunction with OUC’s annual State of Florida self-insurance filing. Liabilities associated with the healthcare programs were determined based on actuarial studies and included amounts for claims that have been incurred but not reported. For workers’ compensation claims, liabilities were determined from estimates provided by OUC’s third-party administrator based on amounts already paid and the age and type of claim. Liabilities associated with general and automobile liability coverage were determined based on historic information in addition to estimated costs for current pending claims. The total of these liabilities is included in the Statements of Net Position under the heading of accounts payable and accrued expenses.

Self-insurance program liability at September 30 was as follows:

(Dollars in thousands)	2017	Payments, net	Incurred claims	2018
Workers' compensation	\$ 618	\$ (547)	\$ 628	\$ 699
General and automobile liability	377	(130)	122	369
Health and medical claims	1,861	(20,530)	20,645	1,976
Total	\$ 2,856	\$ (21,207)	\$ 21,395	\$ 3,044

(Dollars in thousands)	2016	Payments, net	Incurred claims	2017
Workers' compensation	\$ 518	\$ (214)	\$ 314	\$ 618
General and automobile liability	377	(156)	156	377
Health and medical claims	1,875	(17,777)	17,763	1,861
Total	\$ 2,770	\$ (18,147)	\$ 18,233	\$ 2,856

Claims

It is the opinion of OUC’s general counsel that OUC, as a statutory commission, may enjoy sovereign immunity in the same manner as a municipality, as allowed by Florida Court of Appeals rulings. Under said rulings, the Florida Statutes limit of liability for claims or judgments by one person for general liability or auto liability is \$0.2 million or a total of \$0.3 million for the same incident or occurrence; greater liability can result only through an act of the Florida Legislature. Furthermore, any defense of sovereign immunity shall not be deemed to have been waived or the limits of liability increased as a result of obtaining or providing insurance in excess of statutory limitations.

OUC’s transmission and distribution systems are not covered by property insurance, since such coverage is generally not available.

NOTES TO THE FINANCIAL STATEMENTS

Note I – Insurance Programs and Claims (continued)

Nuclear liability insurance: Liability for accidents at the SL2 nuclear power plant, for which OUC has a minority interest, is governed by the Price-Anderson Act which limits the public liability of nuclear reactor owners to the amount of insurance available from private sources and an industry retrospective payment plan. Florida Power and Light (FPL), for SL2, maintains private liability insurance for all participants owning an undivided interest in the nuclear generation facility of \$450.0 million per site and participates in a secondary financial protection system. In addition, FPL participates in nuclear mutual companies that provide limited insurance coverage for property damage, decontamination and premature decommissioning risks. Irrespective of the insurance coverage, should a catastrophic loss occur, the amount of insurance available may not be adequate to cover property damage and other expenses incurred. The majority owner of a nuclear power plant is subject to retrospective assessments of up to \$1,000.0 million per unit, per incident at any nuclear utility reactor in the United States, payable at a rate not to exceed \$152.0 million per incident, per year. In the case of SL2, FPL is contractually entitled to recover a proportionate share of any such assessment from the owners of minority interests in SL2 which, at the maximum level, approximates \$19.0 million plus applicable taxes per incident. Any such assessment to minority owners would be borne by each minority owner at their proportionate ownership share. See Note D for OUC's ownership interest in SL2.

On behalf of all the co-owners of SL2, FPL carries in excess of \$2,750.0 million of property damage insurance; however, substantially all insurance proceeds must first be used to satisfy decontamination and clean-up costs before they can be used for repair or restoration of plants.

Note J – Commitments and Contingent Liabilities

Fuel for Generation and Purchased Power Commitments

OUC has entered into fuel supply and transportation contracts which align with the ownership of SEC Unit 1, Unit 2 and Unit B, the IRP generation facilities and its fuel agent obligations for SEC Unit A. For those generation facilities in which there is participation ownership, each participant has a commitment proportionate to its ownership interest that is included in the schedule below for the years ended September 30:

(Dollars in thousands)	Fuel supply and transportation contracts	Purchased power capacity commitments
2019	\$ 33,470	\$ 23,353
2020	33,673	21,032
2021	32,843	19,138
2022	29,998	17,538
2023	28,459	18,159
2024-2028	63,261	86,130
2029 - thereafter	113,095	55,985
Total	<u>\$ 334,799</u>	<u>\$ 241,335</u>

OUC has also entered into five solar and three landfill gas renewable energy power purchase agreements (PPA). The solar and landfill gas PPAs have a total contract capacity of 32.3 megawatts. OUC purchases any and all energy that is produced at the sites and there are no demand payments related to these agreements.

Regulation

The electric utility industry continues to be affected by a number of legislative and regulatory factors. The following summarizes the key regulations impacting OUC.

Environmental Protection Agency (EPA)

Greenhouse Gas (GHG) Regulation: Following the guidance outlined in the memorandum provided by the President of the United States, the EPA announced in 2013 the development of new carbon dioxide (CO₂) emission rules for new power plants, setting a cap for the amount of CO₂ that is allowed to be emitted from any newly constructed power plant. The EPA also proposed the Clean Power Plan (CPP) on August 3, 2015 regulating GHG emissions from existing stationary sources through the development of guidance-setting carbon pollution reduction goals for each state, based on its ability to comply or achieve the goals.

Note J – Commitments and Contingent Liabilities (continued)

This rule was challenged and on February 9, 2016, the United States Supreme Court issued a stay of the CPP. On October 10, 2017, the EPA issued a Notice of Proposed Rulemaking proposing to repeal the CPP. On August 21, 2018, the EPA proposed a new rule, entitled the Affordable Clean Energy (ACE) Rule, to replace the CPP. It is expected that some or all of OUC's electric generating units may be subject to this new rule, however, because the rule is not yet final, the impact to OUC cannot be determined at this time.

Mercury and Air Toxics Standards (MATS) Rule: The EPA proposed the MATS rule to further regulate mercury and other hazardous air pollutant emissions from electric generating units. In April 2016, the EPA finalized their supplemental finding in order to fulfill the directives of the United States Supreme Court. Although litigation of the MATS rule continues, affected OUC generating units have operated under the requirements of the MATS rule since April 2015.

EPA Coal Combustion Residual (CCR) Regulations: On April 17, 2015, the EPA issued new rules regulating the disposal and beneficial use of CCRs. In late 2016, Congress passed the Water Infrastructure Improvements for the Nation Act (WIIN Act), which fundamentally changed the manner in which the CCR rules are to be implemented. Under the WIIN Act, the EPA is authorized to review and approve state CCR permit programs that are at least as protective as the federal CCR rules. Currently, environmental and industry groups are challenging the CCR rules in the D.C. Circuit Court of Appeals. At this time, OUC's future costs to comply with these regulations are not anticipated to be material and are primarily related to new groundwater monitoring and reporting requirements contained within the CCR rules.

Interstate Transport Rule: Based on current modeling, Florida is not significantly contributing to any other state's ozone compliance and as such is meeting its transport-related obligations. Therefore OUC's electric generating units are not currently impacted by this ruling, although subsequent modeling could impact this status and require subsequent compliance measures.

Federal Regulation Enforcement

The Federal Energy Regulatory Commission (FERC) has primary jurisdiction over investor-owned utilities including rulemaking authority for non-discriminatory open transmission system access requirements and wholesale PPAs. To ensure OUC operates in a manner that is aligned with FERC's non-discriminatory open transmission system access requirements, OUC has adopted a "safe harbor" Open Access Transmission Tariff (OATT). This OATT ensures that OUC will have access to all transmission-related services offered by public utilities through its offering of reciprocal services. OUC's contractual PPAs are not subject to FERC oversight.

FERC also has the authority to impose standards which enforce an acceptable level of reliability to the Bulk Electric System. OUC is subject to these standards including Critical Infrastructure Protection standards through FERC's delegated authority to the Florida Reliability Coordination Council (FRCC). Based on the results of recent audits, OUC remains fully compliant with these standards.

Florida State Regulation

Legislation under Sections 366.80 through 366.85, and 403.519, Florida Statutes (FS), are known collectively as the Florida Energy Efficiency and Conservation Act (FEECA). This Act provides the FPSC with the authority to establish goals every five years to encourage electric utilities to increase the efficiency of energy consumption, limit the growth of energy consumption and minimize weather-sensitive peak demands. OUC submitted its five-year Conservation Plan in March 2015 and final approval was submitted through a Consummating Order on September 8, 2015. The approved plan calls for OUC to achieve a reduced level of conservation. Pursuant to Section 366.82, FS, the FPSC must review a utility's conservation goals not less than every five years. The FPSC's review of OUC's conservation goals and the supporting demand-side management plan covers the period between 2015 and 2024.

NOTES TO THE FINANCIAL STATEMENTS

Note K – Major Agreements

City of Orlando: OUC pays to the City of Orlando (City) a revenue-based payment and an income-based dividend payment.

Beginning in 2008 and continuing through 2017, payments to the City were fixed based on projected revenues and income before contributions. Beginning in 2018, these payments were fixed through 2020 at a 3.0 percent annual escalation rate. Total revenue and income-based payments for the years ended September 30, 2018 and 2017 were \$90.0 million and \$87.4 million, respectively.

City of St. Cloud: In April 1997, OUC entered into an inter-local agreement with the City of St. Cloud (STC) to provide retail electric energy services to all STC customers and to maintain and operate STC's electric transmission, distribution and generation facility rights and ownership interests. The term of the agreement commenced May 1, 1997 and, as amended in April 2003, continues until September 30, 2032. In return, OUC's commitment is to pay STC 9.5 percent of gross retail electric billings from STC customers billed during the second preceding fiscal year.

Billed revenue for the years ended September 30, 2018 and 2017, subject to the inter-local agreement is included under the heading of resale electric revenues and was \$79.6 million and \$76.2 million, respectively. Revenue-based payments recorded under the heading of payments to other governments and taxes for the years ended September 30, 2018 and 2017 were \$7.3 million and \$6.9 million, respectively.

Orange County: OUC pays a revenue-based payment to Orange County (County) calculated at 1.0 percent of gross retail electric and chilled water billings to customers within the County but outside the city limits of the City of Orlando and other municipalities. This payment is recorded under the heading of payments to other governments and taxes on the Statements of Revenues, Expenses and Changes in Net Position. Revenue-based payments were \$1.5 million for each of the years ended September 30, 2018 and 2017.

City of Vero Beach: In April 2008, OUC and the City of Vero Beach (Vero Beach) executed a 20 year power supply agreement, with a 10 year extension option, whereby OUC supplements Vero Beach's electric capacity and energy requirements. On October 24, 2017, Vero Beach approved the sale of its city-owned utility system to FPL effective December 2018. Upon completion of the sale, OUC's contractual obligation to serve Vero Beach will terminate and OUC will receive a settlement amount of \$20.0 million. In addition, the termination and settlement agreement includes the execution of a power supply agreement with FPL to purchase 85 megawatts of capacity and energy from OUC for a two year period immediately following the sale effective date. Billed revenues under the current power supply agreement, included under the heading of resale electric revenues, were \$30.3 million and \$31.1 million for the years ended September 30, 2018 and 2017, respectively.

City of Bartow: In October 2010, OUC entered into an inter-local agreement with the City of Bartow (Bartow) to provide wholesale electric services sufficient to meet Bartow's load requirements. The term of the agreement was seven years with an effective date of January 1, 2011. In August 2017, a new long-term power supply agreement for capacity and energy was approved for a term of three years with an effective date of January 1, 2018. Billed revenues, included under the heading of resale electric revenues, were \$11.7 million and \$18.5 million for the years ended September 30, 2018 and 2017, respectively.

City of Lake Worth: In February 2013, OUC and the City of Lake Worth (Lake Worth) initiated an agreement whereby OUC would act as the administrator to provide wholesale electric and asset management services. The term of the agreement began January 1, 2014 for three years with an option for Lake Worth to extend the term for two additional one-year terms. As of September 2016, the City of Lake Worth exercised its option to extend the term of the agreement through December 31, 2018. An additional extension is pending OUC Board approval for an initial term of four years. Billed revenues, included under the heading of resale electric revenues, were \$14.3 million and \$12.1 million for the years ended September 30, 2018 and 2017, respectively.

City of Winter Park: In August 2013, OUC and the City of Winter Park (Winter Park) executed a power supply agreement whereby OUC supplements Winter Park's electric capacity and energy requirements. The service date of the agreement was January 1, 2014 with an initial term of six years. Billed revenues, included under the heading of resale electric revenues, were \$3.8 million and \$3.6 million for the years ended September 30, 2018 and 2017, respectively.

Note L – Pension Plans

OUC provides a Defined Benefit Pension Plan for employees hired prior to January 1, 1998 and a Hybrid Pension Plan, which includes a cash balance defined benefit and a defined contribution benefit, for employees hired on or after January 1, 1998. The defined benefit components of each plan are funded through the Defined Benefit Pension Trust and are disclosed together in accordance with GASB Statement No. 68, “Accounting and Financial Reporting for Pensions” (Statement No. 68), followed by disclosures related to the defined contribution benefit included in the Hybrid Pension Plan.

Defined Benefit

OUC is the administrator of the Orlando Utilities Commission Pension Plan (the Plan), a single-employer, defined benefit pension plan. As such, OUC has the authority to make changes subject to Board approval. Plan assets are segregated from OUC’s assets and are separately managed by the OUC Defined Benefit Pension Administrative Committee or Trustees. The Trustees are appointed by OUC.

The plan issues annual stand-alone financial statements, with the most recent report issued for the year ended September 30, 2017. This report may be obtained by writing to OUC Pension Plans, Reliable Plaza at 100 West Anderson Street, Orlando, Florida 32801 or from the OUC website at www.ouc.com/about-ouc/post-employment-benefit-reporting. The next available report will be issued during 2019 for the plan year ended September 30, 2018.

Benefits provided: Benefits are available to all employees who regularly work 20 or more hours per week and are detailed as follows:

- Traditional defined benefit offering:** This benefit offering was closed on December 31, 1997 and provides benefits to all employees hired prior to January 1, 1998 who did not elect to transition their pension plan interests to the defined contribution pension plan. Under the provisions of this closed offering, benefits vest after five years of service and are earned for up to a maximum service period of 30 years. Upon retirement, participants who have attained normal retirement age receive a pension benefit equal to 2.5 percent of the highest three consecutive years’ average base earnings times years of employment. The normal retirement age of a participant is the date at which the participant has attained age 62 and five years of participation in the plan. A participant may retire with a reduced benefit at age 55 with a minimum of ten years of service. The benefit reduction for early retirement is 1.0 percent per year for each year which precedes the normal retirement date. Benefit payments that exceed the Internal Revenue Service Section 415(b) limits are eligible for non-qualified trust benefits for which there were five active and three inactive participants currently receiving benefits and four active and three inactive participants currently receiving benefits as of the valuation date for the years ended September 30, 2018 and 2017, respectively.

Benefit terms provide for annual cost of living adjustments (COLA) to each employee’s retirement benefit subsequent to the employee’s retirement date. Future COLA increases, each January 1st, are based on the net return on plan investments for the previous fiscal year as follows:

<u>Net investment return</u>	<u>COLA rate</u>
Up to 4.0%	-
Greater than 4.0% up to 8.0%	1.0%
Greater than 8.0% up to 12.0%	1.5%
Greater than 12.0%	2.0%

NOTES TO THE FINANCIAL STATEMENTS

Note L – Pension Plans (continued)

- Hybrid plan cash balance defined benefit offering:** This benefit offering is provided to all employees participating in the Hybrid plan. The cash balance benefit is fully funded by OUC and includes a sliding pay credit scale based on the combination of an employee's age and years of service at September 30. Pay credits range from 5.0 percent to 12.0 percent and are earned annually. A service credit is earned if an employee has worked 1,000 hours or more in the fiscal year. Benefits vest after five years of service and normal retirement is available following the earlier of an employee reaching age 62 with a minimum of five years of service or 30 years of continuous service. Benefit payments that exceed the Internal Revenue Service Section 415(b) limits are eligible for non-qualified trust benefits. There were no participants in the non-qualified trust as of the valuation date for the years ended September 30, 2018 and 2017. Annually, pay credits earn interest based on the net return on plan investments for the previous fiscal year as follows:

<u>Net investment return</u>	<u>Interest credit</u>
Up to 4.0%	4.0%
Greater than 4.0% up to 8.0%	5.0%
Greater than 8.0% up to 12.0%	5.5%
Greater than 12.0%	6.0%

The following table presents information about plan participants covered by the benefit terms as of the valuation date for the years ended September 30:

	<u>2018</u>	<u>2017</u>
Qualified plan		
Active plan members	1,143	1,111
Inactive plan members currently receiving benefits	899	865
Inactive plan members entitled to deferred benefits	134	128
Total qualified plan	<u>2,176</u>	<u>2,104</u>

Funding policy: The pension plan agreement requires OUC to contribute, at a minimum, amounts actuarially determined. Required participant contribution obligations for the traditional defined benefit offering are 4.0 percent of earnings until the later of age 62 or completion of 30 years of service, with no required contributions thereafter. No participant contributions are required for the hybrid plan cash balance defined benefit offering.

The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. OUC is required to contribute the difference between the actuarially determined rate and the contribution rate of its employees. The required rate of contribution, based on annual covered payroll, for the years ended September 30, 2018 and 2017 was 25.4 percent and 27.1 percent, respectively.

In accordance with GASB Statement No. 73, "Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68" (Statement No. 73), the \$1.0 million contribution to the 415 Trust was recorded to internally designated assets in the Statements of Net Position as of September 30, 2018. The 415 Trust was not funded as of September 30, 2017.

Actuarial methods and assumptions used to measure total pension liability (TPL) and net pension liability (NPL): The TPL and NPL as of September 30, 2018 and 2017 were measured as of September 30, 2017 and 2016, respectively. Since the measurement date and valuation date are the same, no update procedures were used to roll forward the TPL from the valuation date to the measurement date.

The measurement of the TPL was determined by an independent actuary in accordance with the American Academy of Actuaries Interpretations, and there were no deviations from the guidance in the Actuarial Standards of Practice in the selection of assumptions used to determine the TPL and related measures. Annual actuarial amounts for reporting were calculated using the entry age normal cost method.

NOTES TO THE FINANCIAL STATEMENTS

Note L – Pension Plans (continued)

The assumptions used to measure the TPL for both the qualified and non-qualified plans as of September 30, 2017 included an inflation assumption of 2.25 percent per year, salary increases of 3.75 percent to 7.5 percent per year, depending on years of service, annual COLA of 2.0 percent per year, based on actual COLA granted for the year, and 1.0 percent per year, compounded annually for each year thereafter, for the traditional defined benefit offering, and an annual cash balance interest credit rate of 6.0 percent for the current year and 5.0 percent per year thereafter for active members and 4.0 percent per year for inactive members. Mortality assumptions were based on the RP-2000 Combined Healthy Participant Mortality Table for active members and the RP-2000 Mortality Table for Annuitants for non-disabled inactive members, with mortality improvements projected to all future years using Scale BB.

The assumptions used to measure the TPL for both the qualified and non-qualified plans as of September 30, 2016 included an inflation assumption of 2.25 percent per year, salary increases of 3.75 percent to 7.5 percent per year, depending on years of service, annual COLA of 1.5 percent per year, based on actual COLA granted for the year, and 1.0 percent per year, compounded annually for each year thereafter, for the traditional defined benefit offering, and an annual cash balance interest credit rate of 5.0 percent per year for active members and 4.0 percent per year for inactive members. Mortality assumptions were based on the RP-2000 Combined Healthy Participant Mortality Table for active members and the RP-2000 Mortality Table for Annuitants for non-disabled inactive members, with mortality improvements projected to all future years using Scale BB.

Employer contributions were assumed to be made at the end of each calendar quarter. Member contributions were assumed to be received continuously throughout the year based upon the computed percent of payroll and the actual payroll payable at the time contributions were made.

The projected long-term real rate of return on pension plan investments, valued as of September 30, 2017 and 2016, was determined using a building block method, which considers historical performance data and future expectations for each major asset class, while also reflecting current capital market conditions. These best-estimate ranges, net of assumed long-term inflation and investment expenses, were combined to produce the long-term expected rate of return.

The target allocation and best estimates of arithmetic real rates of return for each major asset class as of September 30, 2017 and 2016 are summarized in the following table:

<u>Asset class</u>	<u>Target allocation</u>	<u>Long-term expected real rate of return</u>
Domestic equity	43.0%	7.5%
International equity	15.0%	8.5%
Domestic bonds	17.0%	2.5%
International bonds	5.0%	3.5%
Real estate	10.0%	4.5%
Alternative assets	10.0%	6.2%
Total	100.0%	

In conjunction with the implementation of Statement No. 68 in 2015 and Statement No. 73 in 2017, the balance of the pension asset, as well as the future funding of the net pension liability, were classified as a regulatory asset as approved by the Board. Refer to Note G for further details.

Discount rate: The discount rate used to measure the TPL was 7.25 percent, valued as of September 30, 2017 and 2016. The projection of cash flows used to determine the discount rate assumed that employee contributions would be made at the current contribution rate and that future employer contributions would be made at rates equal to the difference between actuarially determined contribution rates and the employee rate. Based on these assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the TPL.

NOTES TO THE FINANCIAL STATEMENTS

Note L – Pension Plans (continued)

The TPL for the non-qualified plan as of September 30, 2017 and 2016 was calculated using a municipal bond rate of 3.50 percent and 3.06 percent, respectively, as reported in Fidelity's "20-Year Municipal GO AA Index" as of September 29, 2017 and 2016, respectively.

The following presents the sensitivity of the NPL and TPL calculations to a 1.0 percent increase and a 1.0 percent decrease in the discount rates used to measure the TPL at September 30:

(Dollars in thousands)	2017		2016		
	NPL		NPL		
Qualified plan					
1.0 percent decrease - 6.25%	\$	142,627	\$	170,035	
Current discount rate - 7.25%	\$	95,010	\$	122,795	
1.0 percent increase - 8.25%	\$	54,177	\$	82,366	
Non-qualified plan					
		Rate	TPL	Rate	TPL
1.0 percent decrease		2.50%	\$ 2,930	2.06%	\$ 1,432
Current discount rate		3.50%	\$ 2,613	3.06%	\$ 1,262
1.0 percent increase		4.50%	\$ 2,351	4.06%	\$ 1,123

Net pension liability (NPL): The following schedule presents the changes in NPL at September 30:

(Dollars in thousands)	2018		2017	
Total pension liability				
Service cost	\$	5,748	\$	5,539
Interest on the total pension liability		33,535		32,767
Benefit changes		408		-
Difference between expected and actual experience ⁽¹⁾		3,706		(106)
Assumption changes		-		171
Benefit payments, including refunds of plan member contributions		(28,663)		(27,324)
Net change in total pension liability		14,734		11,047
Total pension liability - beginning of year		471,131		460,084
Total pension liability - end of year	\$	485,865	\$	471,131
Plan fiduciary net position				
Contributions - employer	\$	21,876	\$	17,803
Contributions - plan members		660		748
Total investment income, net of investment expense		48,761		29,872
Benefit payments, including refunds of plan member contributions		(28,663)		(27,324)
Administrative expense		(115)		(36)
Net change in plan fiduciary net position		42,519		21,063
Plan fiduciary net position - beginning of year		348,336		327,273
Plan fiduciary net position - end of year	\$	390,855	\$	348,336
Net pension liability - beginning of year	\$	122,795	\$	132,811
Net pension liability - end of year	\$	95,010	\$	122,795

(1) The actual return on the market value of assets was 14.1 percent. The actuarial value of assets was 1.65 percent higher than the assumed rate of return, which contributed to this increase.

Pension plan fiduciary net position: Detailed information about the pension plan's fiduciary net position is available in the separately issued 2017 OUC Benefit Plan Reports for the years ended September 30, 2017 and 2016.

NOTES TO THE FINANCIAL STATEMENTS

Note L – Pension Plans (continued)

Total pension liability (TPL) for non-qualified plan: The following schedule presents the changes in TPL for excess pension benefits at September 30:

(Dollars in thousands)	2018	2017
Total pension liability		
Service cost	\$ 28	\$ 22
Interest on the total pension liability	38	41
Benefit changes	1,124	-
Difference between expected and actual experience	373	47
Assumption changes	(132)	97
Benefit payments, including refunds of plan member contributions	(80)	(51)
Net change in total pension liability	1,351	156
Total pension liability - beginning of year	1,262	1,106
Total pension liability - end of year	\$ 2,613	\$ 1,262

Pension liability: The following schedule presents the pension liability as reported in the Statements of Net Position for the years ended September 30:

(Dollars in thousands)	2018	2017
Qualified plan		
Total pension liability	\$ 485,865	\$ 471,131
Net position	390,855	348,336
Net pension liability	95,010	122,795
Non-qualified plan		
Total pension liability	2,613	1,262
Pension Liability	\$ 97,623	\$ 124,057

Pension expense, regulatory expense, deferred outflows of resources and deferred inflows of resources: OUC recorded \$13.4 million and \$17.5 million in pension expense and \$1.3 million and \$0.1 million in non-qualified pension plan expense for the years ended September 30, 2018 and 2017, respectively. In addition, \$11.7 million was recorded to pension regulatory expense for each year, resulting in a \$82.4 million and \$93.2 million regulatory pension asset at September 30, 2018 and 2017, respectively. See Note G for details.

The following schedule presents information about the pension-related deferred outflows of resources and deferred inflows of resources at September 30:

(Dollars in thousands)	2018	2017
Deferred outflows of resources		
Qualified plan		
Employer's contributions to the plan subsequent to the measurement of NPL	\$ 22,614	\$ 21,876
Changes in assumptions	14,418	19,389
Net difference between projected and actual earnings on pension plan investments	-	4,863
Differences between expected and actual experience	2,993	-
Subtotal qualified plan	40,025	46,128
Non-qualified plan		
Benefit payments	113	74
Changes in assumptions	54	75
Differences between expected and actual experience	308	36
Subtotal non-qualified plan	475	185
Total deferred outflows of resources	\$ 40,500	\$ 46,313

NOTES TO THE FINANCIAL STATEMENTS

Note L – Pension Plans (continued)

(Dollars in thousands)	2018	2017
Deferred inflows of resources		
Qualified plan		
Net difference between projected and actual earnings on pension plan investments	\$ 15,802	\$ -
Changes in assumptions	4,603	7,064
Differences between expected and actual experience	2,104	2,983
Subtotal qualified plan	22,509	10,047
Non-qualified plan		
Changes in assumptions	100	-
Subtotal non-qualified plan	100	-
Total deferred inflows of resources	\$ 22,609	\$ 10,047

The following schedule presents the future amortization of pension-related deferred outflows of resources and deferred inflows of resources, excluding the balance attributable to the employer's contribution to the plan in the current fiscal year and subsequent to the measurement date. The difference between projected and actual earnings on pension plan investments is recorded in pension expense over a five-year period. Changes in assumptions and the difference between expected and actual experience in the measurement of TPL are recorded in pension expense over a period equal to the average of the expected remaining service lives of all participants in the plan.

Amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense for the years ended September 30:

(Dollars in thousands)	Qualified plan	Non-qualified plan
2019	\$ (726)	\$ 91
2020	772	90
2021	(1,253)	75
2022	(4,034)	6
2023	143	-
Net deferred outflows of resources	\$ (5,098)	\$ 262

Defined Contribution Benefit

The Hybrid Plan also includes a defined contribution benefit. All employees who regularly work 20 or more hours per week and were hired on or after January 1, 1998, are required to participate in a defined contribution retirement plan established under section 401(a) of the Internal Revenue Code and administered by OUC. In addition, employees hired prior to January 1, 1998, were offered the option to convert their defined benefit pension account to this plan. On September 30, 2018 and 2017, the number of active employees enrolled in this pension plan were 1,037 and 972, respectively.

Under the plan, each eligible employee, at the start of their employment, is required to contribute 4.0 percent of their salary. This required contribution is matched equally by OUC. Eligible employees may also voluntarily contribute up to an additional 2.0 percent of their salary to the Trust. Beginning in March 2018, this additional 2.0 percent was also matched by OUC for employees completing seven years of service. Employees are fully vested after one year of employment. Total contributions for the years ended September 30, 2018 and 2017 were \$8.7 million (\$3.6 million employer and \$5.1 million employee) and \$7.6 million (\$2.8 million employer and \$4.8 million employee), respectively.

Note M – Other Post-Employment Benefits

Plan description: OUC is the administrator of the Orlando Utilities Commission Other Post-Employment Benefits Plan (the Plan), a single-employer, OPEB plan. As such, OUC has the authority to make changes subject to Board approval. Plan assets are segregated from OUC’s assets and are separately managed by the OUC OPEB Administrative Committee or Trustees. The Trustees are appointed by OUC and are comprised of the same membership as the OUC Defined Benefit Pension Administrative Committee.

Consistent with the defined benefit pension plan disclosed in Note L, the OPEB plan issues annual stand-alone financial statements, with the most recent report issued for the year ended September 30, 2017. This report may be obtained by writing to OUC OPEB Plans, Reliable Plaza at 100 West Anderson Street, Orlando, Florida 32801 or from the OUC website at www.ouc.com/about-ouc/post-employment-benefit-reporting. The next available report will be issued during 2019 for the plan year ended September 30, 2018.

Benefits provided: OUC offers medical and dental coverage, as well as life insurance coverage, to all employees upon their retirement. Post-employment benefits, in the form of utility discounts, are offered to employees hired prior to 1985. Consistent with the defined benefit pension offerings, two benefit offerings are available for health and medical coverage as follows:

- **Employees participating in the traditional defined benefit pension plan:** Under this health and medical benefit offering, which was closed on December 31, 1997, employees are provided continued access to medical, dental and life insurance coverage upon retirement on or after age 55 with at least ten years of service or at any age after completing 25 or more years of service. Secondary health coverage is also available for those retirees who are Medicare eligible. Costs associated with these benefits are fully subsidized for the employee and partially subsidized for their dependents.

Effective January 1, 2014, the plan was modified to transition over a five-year period the subsidized dependent coverage for Medicare-eligible retirees to 50.0 percent and to phase out the premium subsidy for dependent coverage provided to pre-Medicare-eligible retirees by December 31, 2018. Beginning January 1, 2016, OUC offered a new option for Medicare-eligible retirees to assume OUC subsidized coverage under a fully insured Medicare Advantage Program.

- **Employees participating in the hybrid plan:** Under this health and medical benefit offering, employees and their dependents are provided access to medical and dental coverage upon retirement on or after age 62 with at least five years of service or at any age after completing 30 years of service. Medical and dental benefits, inclusive of secondary health coverage for Medicare-eligible employees, are not directly subsidized. Participants are eligible for implicit subsidy benefits and, at retirement, access to an employer-funded health reimbursement account (HRA), indexed annually, which can be used to pay all eligible medical costs including medical premiums at retirement.

The following table presents information about plan participants covered by the benefit terms as of the valuation date for the years ended September 30:

	<u>2018</u>	<u>2017</u>
Active plan members	1,148	1,122
Inactive plan members currently receiving benefits	857	835
Total	<u>2,005</u>	<u>1,957</u>

Funding policy: No employee contributions are required for the OPEB plan. Funding for OPEB is established based on actuarial valuations and is approved annually by the Board in conjunction with the annual budget.

The annual actuarially determined contribution paid directly to the OPEB Trust (the Trust) for the years ended September 30, 2018 and 2017 was \$9.1 million and \$13.4 million, respectively. Since benefits were paid through operations, OUC was reimbursed by the Trust in 2018 and 2017, in the amounts of \$7.7 million and \$6.4 million, respectively. In 2018, reimbursements from the Trust were lower than OPEB expenses, resulting in a net OPEB reimbursement receivable of \$0.4 million.

The rate of contribution, based on annual covered payroll for the years ended September 30, 2018 and 2017 was 10.4 percent and 17.1 percent, respectively.

NOTES TO THE FINANCIAL STATEMENTS

Note M – Other Post-Employment Benefits (continued)

Actuarial methods and assumptions to measure net OPEB liability (NOL): OUC recognized annual OPEB expense and NOL in accordance with GASB Statement No. 75, “Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions” (Statement No. 75) and GASB Statement No. 85, “Omnibus 2017,” based on information obtained from the annual actuarial report. The NOL as of September 30, 2017 and 2016 was measured as of September 30, 2016 and 2015, respectively. Since the measurement date for the total OPEB liability (TOL) and valuation date for the plan fiduciary net position are the same, no update procedures were used to roll forward the TOL from the valuation date to the measurement date.

The measurement of the TOL was determined by an independent actuary in accordance with the American Academy of Actuaries Interpretations, and there were no deviations from the guidance in the Actuarial Standards of Practice in the selection of assumptions used to determine the TOL and related measures.

The assumptions used to measure the TOL as of September 30, 2017 included an inflation assumption of 2.25 percent per year, and salary increases of 3.75 percent to 7.5 percent per year depending on years of service, and an annual medical cash balance interest crediting rate of 5.0 percent per year for active members and 4.0 percent per year for inactive members. Health coverage assumptions included acceptance rates which were consistent with elections made by retiring employees in recent years (100.0 percent for traditional defined benefit participants, 30.0 percent for cash balance defined benefit participants at a retirement age before 65, and 9.0 percent for cash balance defined benefit participants at a retirement age of 65 and after). The mortality assumptions were based on the RP-2000 Combined Healthy Participant Mortality Table for active members and the RP-2000 Mortality Table for Healthy Annuitants for non-disabled inactive members, with mortality improvement projected to all future years using Scale BB. Annual actuarial amounts were calculated using the entry-age normal cost method with an increasing normal cost pattern consistent with the salary increase assumption. The healthcare cost trend assumptions are based on a trend rate starting at 7.0 percent and gradually decreasing to an ultimate trend rate of 4.97 percent for years ended September 30, 2040 and thereafter.

The assumptions used to measure the TOL as of September 30, 2016 included an inflation assumption of 2.25 percent per year for the first 10 years and 2.5 percent thereafter, and salary increases of 3.75 percent to 7.5 percent per year depending on years of service, and a medical cash balance interest crediting rate of 5.0 percent per year for active members and 4.0 percent per year for inactive members. Health coverage assumptions included acceptance rates which were consistent with elections made by retiring employees in recent years (100.0 percent for traditional defined benefit participants, 30.0 percent for cash balance defined benefit participants at a retirement age before 65, and 9.0 percent for cash balance defined benefit participants at a retirement age of 65 and after). The mortality assumptions were based on the RP-2000 Combined Healthy Participant Mortality Table for active members and the RP-2000 Mortality Table for Annuitants for non-disabled inactive members, with mortality improvement projected to all future years using Scale BB. Annual actuarial amounts were calculated using the entry-age normal cost method with an increasing normal cost pattern consistent with the salary increase assumption. The healthcare cost trend assumptions are based on a trend rate starting at 6.5 percent and gradually decreasing to an ultimate trend rate of 4.75 percent for years ended September 30, 2040 and thereafter.

Employer contributions were assumed to be made at the end of each calendar quarter.

The projected long-term real rates of return on OPEB plan investments, valued as of September 30, 2017 and 2016, was determined using a building block method, which considers historical performance data and future expectations for each major asset class, while also reflecting current capital market conditions. These best-estimate ranges, net of assumed long-term inflation and investment expenses, were combined to produce the long-term expected rate of return.

NOTES TO THE FINANCIAL STATEMENTS

Note M – Other Post-Employment Benefits (continued)

The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table for valuation dates at September 30:

Asset class	2017		2016	
	Target allocation	Long-term expected real rate of return	Target allocation	Long-term expected real rate of return
U.S. equity	48.0%	7.5%	50.0%	7.5%
International equity	15.0%	8.5%	15.0%	8.5%
Domestic bonds	17.0%	2.5%	20.0%	2.5%
International bonds	5.0%	3.5%	5.0%	3.5%
Alternative assets	10.0%	6.3%	5.0%	6.2%
Real estate	5.0%	4.5%	5.0%	4.5%
Total	100.0%		100.0%	

In conjunction with the implementation of Statement No. 75, the balance of the OPEB asset, as well as the establishment of the NOL, were classified as a regulatory asset as approved by the Board. Refer to Note G for further details.

The following schedules present the medical cost increase assumptions used to measure the NOL as of September 30, 2017 and 2016. The trend rate for the cost of benefits and premiums charged to retirees are based on the forecasting model built and published in *Modeling Long-Term Health Care Cost Trends* sponsored by the Society of Actuaries.

Year	Percentage increase, valued as of September 30,		Year	Percentage increase, valued as of September 30,	
	2017	2016		2017	2016
2017	-	6.50%	2029	5.81%	5.59%
2018	7.00%	6.25%	2030	5.81%	5.59%
2019	6.75%	6.00%	2031	5.64%	5.45%
2020	6.50%	5.85%	2032	5.53%	5.35%
2021	6.25%	6.23%	2033	5.45%	5.27%
2022	6.78%	6.10%	2034	5.39%	5.22%
2023	6.59%	5.97%	2035	5.34%	5.17%
2024	6.39%	5.84%	2036	5.31%	5.09%
2025	6.20%	5.72%	2037	5.22%	5.00%
2026	6.00%	5.59%	2038	5.14%	4.92%
2027	5.81%	5.59%	2039	5.06%	4.84%
2028	5.81%	5.59%	Thereafter	4.97%	4.75%

Discount rate: The discount rate used to measure the TOL was 7.25 percent, valued as of September 30, 2017 and 2016. The projection of cash flows used to determine the discount rate assumed that future employer contributions would be made at rates equal to the actuarially determined contribution rates. Based on these assumptions, the Plan's fiduciary net position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on Plan investments was applied to all periods of projected benefit payments to determine the TOL.

The following presents the sensitivity of the NOL calculation to a one percent increase and a one percent decrease in the discount rate used to measure the TOL at September 30:

(Dollars in thousands)	2017	2016
1.0 percent decrease - 6.25%	\$ 43,007	\$ 64,066
Current discount rate - 7.25%	\$ 25,146	\$ 45,545
1.0 percent increase - 8.25%	\$ 10,262	\$ 29,975

NOTES TO THE FINANCIAL STATEMENTS

Note M – Other Post-Employment Benefits (continued)

The following presents the sensitivity of the NOL calculation to a one percent increase and a one percent decrease in the medical cost assumptions used to measure the TOL at September 30:

(Dollars in thousands)	2017		2016	
1.0 percent decrease	6.00% decreasing to 3.97%	\$ 9,250	5.50% decreasing to 3.75%	\$ 29,958
Current assumption	7.00% decreasing to 4.97%	\$ 25,146	6.50% decreasing to 4.75%	\$ 45,545
1.0 percent increase	8.00% decreasing to 5.97%	\$ 44,230	7.50% decreasing to 5.75%	\$ 64,061

Net OPEB liability (NOL): The following schedule presents the changes in NOL at September 30:

(Dollars in thousands)	2017	2016
Total OPEB liability		
Service cost	\$ 1,331	\$ 1,346
Interest on the total OPEB liability	10,434	11,882
Difference between expected and actual experience	(3,285)	(23,970)
Assumption changes	(2,093)	(2,670)
Benefit payments, including refunds	(6,374)	(8,063)
Net change in total OPEB liability	13	(21,475)
Total OPEB liability - beginning of year	145,775	167,250
Total OPEB liability - end of year	\$ 145,788	\$ 145,775
Plan fiduciary net position		
Contributions - employer	\$ 13,384	\$ 12,628
Net investment income/(loss)	13,420	9,621
Benefit payments, including refunds	(6,374)	(8,062)
Administrative expense	(18)	(18)
Net increase in plan fiduciary net position	20,412	14,169
Plan fiduciary net position - beginning of year	100,230	86,061
Plan fiduciary net position - end of year	\$ 120,642	\$ 100,230
Net OPEB liability - beginning of year	\$ 45,545	\$ 81,189
Net OPEB liability - end of year	\$ 25,146	\$ 45,545

OPEB plan fiduciary net position: Detailed information about the OPEB plan's fiduciary net position is available in the separately issued 2017 OUC Benefit Plan Reports for the years ended September 30, 2017 and 2016.

OPEB expense, regulatory expense, deferred outflows of resources and deferred inflows of resources: OUC recorded (\$0.9 million) and \$3.8 million in OPEB expense for the years ended September 30, 2018 and 2017, respectively. In addition, \$6.8 million was recorded to OPEB regulatory expense for each year, resulting in a \$47.9 million and \$54.8 million regulatory OPEB asset at September 30, 2018 and 2017, respectively. See Note G for details.

NOTES TO THE FINANCIAL STATEMENTS

Note M – Other Post-Employment Benefits (continued)

The following schedule presents information about the OPEB-related deferred outflows of resources and deferred inflows of resources at September 30:

(Dollars in thousands)	2018	2017
Deferred outflows of resources		
Employer's contributions to the plan subsequent to the measurement of total OPEB liability	\$ 9,068	\$ 13,384
Differences between expected and actual experience	1,694	2,308
Net difference between projected and actual investment earnings	-	2,085
Total deferred outflows of resources	\$ 10,762	\$ 17,777
Deferred inflows of resources		
Differences between expected and actual experience	\$ 18,542	\$ 19,888
Changes in assumptions	3,719	2,511
Net difference between projected and actual investment earnings	3,545	-
Total deferred inflows of resources	\$ 25,806	\$ 22,399

The following schedule presents the future amortization of OPEB-related deferred outflows of resources and deferred inflows of resources, excluding the balance attributable to the employer's contribution to the plan in the current fiscal year and subsequent to the NOL measurement date. The difference between projected and actual earnings on plan investments is recorded in OPEB expense over a five-year period. Changes in assumptions and the difference between expected and actual experience in the measurement of TOL are recorded in OPEB expense over a period equal to the average of the expected remaining service lives of all participants in the plan.

Amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense for the years ended September 30:

(Dollars in thousands)	Net deferred outflows of resources
2019	\$ (5,173)
2020	(5,173)
2021	(6,854)
2022	(6,049)
2023	(863)
Thereafter	-
Total	\$ (24,112)

Note N – Hedging Activities

OUC manages the impacts of interest rate and fuel market fluctuations on its earnings, cash flows and market value of assets and liabilities through its hedging programs.

Interest rate hedges: Interest rate risk for variable rate debt, is managed through the execution of interest rate swap agreements (swaps). Swaps are executed in accordance with the Treasury policy, presented to the Finance Committee and approved by the Board. Swaps are initiated in conjunction with bond transactions and as such, have inception and termination dates that align with the underlying debt series. Early termination of a swap can be executed in accordance with the terms of the agreement.

The Treasury policy requires counterparty creditworthiness to achieve at least an "A" rating category from at least two of the three nationally recognized rating agencies, at the time of execution, maintaining a rating for qualified swap providers. In addition, two-way credit support agreements may be required with parental guarantees and/or letters of credit or collateral. In respect to the fair value of swaps, the value of these agreements takes into consideration the prevailing interest-rate environment and the specific terms and conditions of each contract. Fair value amounts are estimated using the zero-coupon discounting method, including utilizing option pricing models, which consider probabilities, volatilities, time, underlying prices and other variables.

NOTES TO THE FINANCIAL STATEMENTS

Note N – Hedging Activities (continued)

Fuel rate hedges: Oversight of the fuel hedge program is performed by the ERMOC. ERMOC's responsibilities include establishing volume and financial limits, as well as overall program compliance and counterparty creditworthiness. Counterparty creditworthiness is evaluated considering the market segment, financial ratios, agency and market implied ratings and other factors.

As a result of engaging in hedging activities, OUC is subject to the following key risks:

- **Credit risk:** This is the risk that results when counterparties are unable or unwilling to fulfill their present and future obligations. OUC addresses this risk through creditworthiness criteria included in its Treasury policy and responsibilities of the ERMOC. Interest rate counterparties must have minimum credit ratings of "A-", issued by Standard and Poor's or Fitch Ratings or "A3", issued by Moody's Investors Service at the time the agreement is executed.
- **Interest rate risk:** This is the risk that changes in interest rates may adversely affect the fair values of OUC's financial instruments or cash flows. OUC is exposed to this risk through its pay-fixed receive variable rate swaps and, as such, has managed this risk through active management. There is no exposure to this risk for fuel hedges.
- **Basis risk:** This is the risk that arises when variable rates or prices of swaps and fuel hedges are based on different reference rates. OUC is exposed to this risk on its interest rate swaps associated with the Series 2015B Bonds and Series 2011A Bonds, as the variable-rate index received by OUC differs from the rate paid on the swap. OUC is exposed to this risk for fuel hedges due to a difference in commodity value between different delivery points or between cash market prices and the pricing points used in the financial markets.
- **Termination risk:** This is the risk that a derivative instrument's unplanned end will affect OUC's asset and liability strategy or potentially require termination payments. This risk is mitigated through OUC's creditworthiness criteria. To date, no instances of this nature have occurred.
- **Rollover risk:** This is the risk that a derivative instrument associated with a hedged item does not extend to the maturity of the hedged item. OUC is not exposed to this risk as all derivative instruments are hedged to maturity.
- **Market access risk:** This is the risk that OUC will not be able to enter credit markets for both swaps and fuel hedges or that credit markets will become more costly. OUC maintains a strong credit rating; "AA" from Standard & Poor's and Fitch Ratings and "Aa2" from Moody's Investors Service and to date, has not encountered any market barriers or credit market challenges.

In accordance with GASB Statement No. 53, "*Accounting and Financial Reporting for Derivative Instruments*" (Statement No. 53), outstanding derivatives are evaluated and classified as either hedging derivative instruments (effective) or investment derivative instruments (ineffective), with the accumulated change in fair market value recognized as deferred inflows/outflows of resources or investment income/expense, respectively.

Interest rate derivatives: As of September 30, 2018 and 2017, OUC's interest rate swaps related to the Series 2015B Bonds and Series 2017A Bonds have been determined to be effective and, as such, changes in the fair value of these derivatives were included on the Statements of Net Position. In January 2017, the 2011A swap was determined to be ineffective, requiring the current market cost valuation to be recognized as expense in the Statements of Revenues, Expenses and Changes in Net Position in accordance with Statement No. 53. Proceeds from the newly issued Series 2017A Bonds were used to refund the Series 2011A Bonds and suspend cash payments on the forward interest rate contract. A regulatory asset was also established in accordance with Statement No. 62 in the amount of the outstanding swap liability, which is anticipated to be recovered through future market valuation changes.

NOTES TO THE FINANCIAL STATEMENTS

Note N – Hedging Activities (continued)

The following statement summarizes the interest rate derivative contracts outstanding for the years ended September 30:

(Dollars in thousands)	2017 Fair value	Change in fair value	Settlement / (termination) amount	2018 Fair value	Net settlement charges	Notional amount
Interest rate swap agreements						
2015B Bonds (1)	\$ 883	\$ 4,291	\$ -	\$ 5,174	\$ 1,121	\$ 115,090
Forward interest rate contracts						
2017A Bonds (1) (2)	(12,748)	2,750	-	(9,998)	-	100,000
	<u>\$ (11,865)</u>	<u>\$ 7,041</u>	<u>\$ -</u>	<u>\$ (4,824)</u>	<u>\$ 1,121</u>	

(Dollars in thousands)	2016 Fair value	Change in fair value	Settlement / (termination) amount	2017 Fair value	Net settlement charges	Notional amount
Interest rate swap agreements						
2007 Bonds (1)	\$ (224)	\$ -	\$ 224	\$ -	\$ -	\$ 13,400
2015B Bonds (1)	(3,745)	4,628	-	883	1,746	115,090
Forward interest rate contracts						
2017A Bonds (1) (2)	(29,178)	6,816	9,614	(12,748)	1,407	100,000
	<u>\$ (33,147)</u>	<u>\$ 11,444</u>	<u>\$ 9,838</u>	<u>\$ (11,865)</u>	<u>\$ 3,153</u>	

(1) See Note H for additional information.

(2) Upon the refunding of the Series 2011A *Windows* Bonds by the Series 2017A Bonds, the Series 2017A Bonds became the series of bonds related to the 2017A Sw ap.

Fuel derivatives: Fuel derivatives are settled in the period in which the option expires and are recognized as fuel expenses on the Statements of Revenues, Expenses and Changes in Net Position. Settlement gains and losses for the year ended September 30, 2018 and 2017 for fuel-related derivatives resulted in net losses of \$1.8 million and \$1.5 million, respectively. The outstanding fuel derivatives were determined to be effective, and as such, the changes in fair value have been recorded on the Statements of Net Position as either a deferred outflow of resources or deferred inflow of resources until such time as the contracts mature. The following is a summary of the fuel-related derivative transactions for the years ended September 30:

(Dollars in thousands)	2017 Fair value	Change in Fair value	2018 Fair value	2018 Notional amount	Volume ⁽¹⁾
Natural gas	\$ 577	\$ (549)	\$ 28	1,100	MMBTU
Heating Oil	72	245	317	11	BBL
Total current fuel hedge assets	<u>649</u>	<u>(304)</u>	<u>345</u>		
Natural gas	146	(146)	-	-	MMBTU
Heating Oil	35	(35)	-	-	BBL
Total non-current fuel hedge assets	<u>181</u>	<u>(181)</u>	<u>-</u>		
Accumulated increase in fair value hedging derivatives	<u>\$ 830</u>	<u>\$ (485)</u>	<u>\$ 345</u>		
Natural gas	\$ (1,333)	\$ 299	\$ (1,034)	7,700	MMBTU
Crude oil	(62)	62	-	-	MBBLS
Total current fuel hedge liabilities	<u>(1,395)</u>	<u>360</u>	<u>(1,034)</u>		
Natural gas	(703)	(799)	(1,502)	9,590	MMBTU
Total non-current fuel hedge liabilities	<u>(703)</u>	<u>(799)</u>	<u>(1,502)</u>		
Accumulated decrease in fair value hedging derivatives	<u>\$ (2,098)</u>	<u>\$ (439)</u>	<u>\$ (2,536)</u>		

⁽¹⁾ Million British Thermal Units (MMBTU), Thousand Barrels (MBBLS), Barrels (BBL)

NOTES TO THE FINANCIAL STATEMENTS

Note N – Hedging Activities (continued)

(Dollars in thousands)	2016 Fair value	Change in Fair value	2017 Fair value	2017 Notional amount	Volume ⁽¹⁾
Natural gas	\$ 2,040	\$ (1,463)	\$ 577	3,740	MMBTU
Heating Oil	-	72	72	9	BBL
Total current fuel hedge assets	2,040	(1,391)	649		
Natural gas	461	(315)	146	2,550	MMBTU
Heating Oil	80	(45)	35	12	BBL
Total non-current fuel hedge assets	541	(360)	181		
Accumulated increase in fair value hedging derivatives	\$ 2,581	\$ (1,751)	\$ 830		
Natural gas	\$ (2,490)	\$ 1,157	\$ (1,333)	2,830	MMBTU
Crude oil	(621)	559	(62)	8	MBBLS
Total current fuel hedge liabilities	(3,111)	1,716	(1,395)		
Natural gas	(2,876)	2,173	(703)	7,250	MMBTU
Crude oil	(10)	10	-	-	MBBLS
Total non-current fuel hedge liabilities	(2,886)	2,183	(703)		
Accumulated decrease in fair value hedging derivatives	\$ (5,997)	\$ 3,899	\$ (2,098)		

REQUIRED SUPPLEMENTARY INFORMATION

Pension Plan

Schedule of changes in net pension liability (NPL), total pension liability (TPL) and related ratios: The following schedules present multi-year trend information that demonstrate the components of change in the TPL and NPL from year to year, as well as trends in related statistical information. Information is presented related to all periods for which the required data is available. Amounts presented were determined as of the measurement date for September 30:

Qualified plan (Dollars in thousands)	2018	2017	2016	2015
Total pension liability				
Service cost	\$ 5,748	\$ 5,539	\$ 5,570	\$ 5,935
Interest on the total pension liability	33,535	32,767	32,104	29,891
Benefit changes	408	-	-	15,187
Difference between expected and actual experience	3,706	(106)	(2,501)	(2,546)
Assumption changes	-	171	29,125	(14,449)
Benefit payments, including refunds of plan member contributions	(28,663)	(27,324)	(25,773)	(23,095)
Net change in total pension liability	14,734	11,047	38,525	10,923
Total pension liability - beginning of year	471,131	460,084	421,559	410,636
Total pension liability - end of year	\$ 485,865	\$ 471,131	\$ 460,084	\$ 421,559
Plan fiduciary net position				
Contributions - employer	\$ 21,876	\$ 17,803	\$ 18,573	\$ 21,198
Contributions - plan members	660	748	821	882
Total investment income, net of investment expense	48,761	29,872	4,783	28,906
Benefit payments, including refunds of plan member contributions	(28,663)	(27,324)	(25,773)	(23,095)
Administrative expense	(115)	(36)	(122)	(85)
Net change in plan fiduciary net position	42,519	21,063	(1,718)	27,806
Plan fiduciary net position - beginning of year	348,336	327,273	328,991	301,185
Plan fiduciary net position - end of year	\$ 390,855	\$ 348,336	\$ 327,273	\$ 328,991
Net pension liability - beginning of year	\$ 122,795	\$ 132,811	\$ 92,568	\$ 109,451
Net pension liability - end of year	\$ 95,010	\$ 122,795	\$ 132,811	\$ 92,568
Plan fiduciary net position as a percentage of total pension liability	80.5%	73.9%	71.1%	78.0%
Covered payroll	\$ 78,314	\$ 75,405	\$ 72,479	\$ 70,147
Net pension liability as a percentage of covered payroll	121.3%	162.8%	183.2%	132.0%
Non-qualified plan (1) (Dollars in thousands)	2018	2017	2016	
Total pension liability				
Service cost	\$ 28	\$ 22	\$ 21	
Interest on the total pension liability	38	41	40	
Benefit changes	1,124	-	-	
Difference between expected and actual experience	373	47	-	
Assumption changes	(132)	97	-	
Benefit payments, including refunds of plan member contributions	(80)	(51)	(56)	
Net change in total pension liability	1,351	156	5	
Total pension liability - beginning of year	1,262	1,106	1,101	
Total pension liability - end of year	\$ 2,613	\$ 1,262	\$ 1,106	
Covered payroll	\$ 1,458	\$ 920	\$ 804	
Total pension liability as a percentage of covered payroll	179.2%	137.2%	137.6%	

(1) For the non-qualified plan, there were no assets accumulated in a trust that meets the criteria in GASB Statement No. 73, "Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68," to pay related benefits. As such, assets were reported in OUC's financial statements and were not netted against the total pension liability.

Notes to schedule

Benefit and assumption changes: There were no revisions in benefits since September 30, 2017, the date of the last actuarial valuation. In 2017, the Plan was amended to include a limited increase in the benefit multiplier, which resulted in a \$0.4 million impact to the TPL as of the September 30, 2017 measurement date. In August 2015, an assumption study and experience review for the six-year period ended September 30, 2014 was completed, and changes were implemented effective September 30, 2015 to the salary, retirement, termination, and mortality assumptions.

REQUIRED SUPPLEMENTARY INFORMATION

Pension Plan (continued)

The investment return rate was 7.25 percent as of the September 30, 2017 and 2016 valuation dates. As the plan fiduciary net position was projected to be available to make all projected benefit payments, the single discount rate was also 7.25 percent as of September 30, 2017 and 2016, respectively.

Schedule of employer contributions to the pension plan: The following schedule presents multi-year trend information regarding employer contributions to the plan for the years ended September 30:

(Dollars in thousands)	Actuarially determined contribution	Actual contribution	Contribution deficiency / (excess) (1)	Covered payroll (CP) (2)	Contributions as a percentage of CP
2018 (3)	\$ 22,614	\$ 22,614	\$ -	\$ 89,170	25.4%
2017	\$ 21,876	\$ 21,876	\$ -	\$ 78,314	27.9%
2016	\$ 18,322	\$ 17,803	\$ 519	\$ 75,405	23.6%
2015	\$ 20,500	\$ 18,573	\$ 1,927	\$ 72,479	25.6%
2014	\$ 21,184	\$ 21,198	\$ (14)	\$ 70,147	30.2%
2013	\$ 18,893	\$ 17,729	\$ 1,164	\$ 73,230	24.2%
2012	\$ 17,120	\$ 16,151	\$ 969	\$ 69,967	23.1%
2011	\$ 17,162	\$ 15,726	\$ 1,436	\$ 28,964	54.3%
2010	\$ 15,012	\$ 15,020	\$ (8)	\$ 30,479	49.3%
2009	\$ 9,970	\$ 10,249	\$ (279)	\$ 30,981	33.1%

(1) Funding requirements were adjusted to include approved ad hoc cost of living adjustments (COLA) benefits provided for the periods of 2001 to 2013 and paid outside the Plan on a pay-as-you-go basis through December 31, 2014. Effective January 1, 2015, the Plan was amended to begin paying these benefits through the Plan.

(2) In 2011, covered payroll increased due to the establishment of the hybrid plan cash balance pension offering in addition to the traditional defined benefit pension offering.

(3) The actuarially determined contribution rates were calculated as of October 1 of the year preceding the contribution year, using the following assumptions:

Actuarial cost method: Entry Age Normal

Amortization method and remaining amortization period: Level dollar, closed and 14 years

Asset valuation method: 20.0 percent of the difference between expected actuarial value (based on assumed return) and market value is recognized each year with 10.0 percent corridor around market value.

Inflation: 2.25 percent

Salary increases: 3.75 percent to 7.5 percent depending on years of service, including inflation

Investment rate of return: 7.25 percent

Retirement age: Experience-based table of rates, prior to most recent experience study

Mortality: RP-2000 Combined Healthy Participant Mortality Table for active members and the RP-2000 Mortality Table for Annuitants for non-disabled inactive members, with mortality improvements projected to all future years using Scale BB.

REQUIRED SUPPLEMENTARY INFORMATION

Other Post-Employment Benefits (OPEB)

Schedule of changes in net OPEB liability (NOL) and related ratios: The following schedule presents multi-year trend information that demonstrates the components of change in the NOL from year to year, as well as trends in related statistical information. Information is presented related to all periods for which the required data is available. Amounts presented were determined as of the measurement date of the NOL for September 30:

(Dollars in thousands)	2017	2016	2015
Total OPEB liability			
Service cost	\$ 1,331	\$ 1,346	\$ 1,480
Interest on the total OPEB liability	10,434	11,882	12,134
Difference between expected and actual experience	(3,285)	(23,970)	3,536
Assumption changes	(2,093)	(2,670)	(452)
Benefit payments, including refunds	(6,374)	(8,063)	(9,067)
Net change in total OPEB liability	13	(21,475)	7,631
Total OPEB liability - beginning of year	145,775	167,250	159,619
Total OPEB liability - end of year	\$ 145,788	\$ 145,775	\$ 167,250
Plan fiduciary net position			
Contributions - employer	\$ 13,384	\$ 12,628	\$ 14,117
Net investment income/(loss)	13,420	9,621	(1,195)
Benefit payments, including refunds	(6,374)	(8,062)	(9,067)
Administrative expense	(18)	(18)	(32)
Net increase in plan fiduciary net position	20,412	14,169	3,823
Plan fiduciary net position - beginning of year	100,230	86,061	82,238
Plan fiduciary net position - end of year	\$ 120,642	\$ 100,230	\$ 86,061
Net OPEB liability - beginning of year	\$ 45,545	\$ 81,189	\$ 77,381
Net OPEB liability - end of year	\$ 25,146	\$ 45,545	\$ 81,189
Plan fiduciary net position as a percentage of total OPEB liability	82.8%	68.8%	51.5%
Covered payroll	\$ 78,447	\$ 71,856	\$ 72,990
Net OPEB liability as a percentage of covered payroll	32.1%	63.4%	111.2%

Notes to schedule

Benefit and assumption changes: There were no revisions in benefits since September 30, 2017, the date of the last actuarial valuation. In August 2015, an assumption study and experience review for the six-year period ended September 30, 2014 was completed and changes were implemented effective September 30, 2015 to the salary, retirement, termination, and mortality assumptions.

The investment return rate was 7.25 percent as of the September 30, 2017, 2016 and 2015. Because the plan fiduciary net position was projected to be available to make all projected benefit payments, the single discount rate was also 7.25 percent as of September 30, 2017, 2016 and 2015.

REQUIRED SUPPLEMENTARY INFORMATION

Other Post-Employment Benefits (continued)

Schedule of employer contributions to the OPEB plan: The following schedule presents multi-year trend information regarding employer contributions to the plan for the years ended September 30:

(Dollars in thousands)	Actuarially determined contribution	Actual contribution	Contribution deficiency/ (excess)	Covered payroll (CP)	Actual contribution as a % of CP
2018 (1)	\$ 9,068	\$ 9,068	\$ -	\$ 86,892	10.4%
2017	\$ 13,384	\$ 13,384	\$ -	\$ 78,447	17.1%
2016	\$ 12,628	\$ 12,628	\$ -	\$ 71,856	17.6%
2015	\$ 14,117	\$ 14,117	\$ -	\$ 72,990	19.3%
2014	\$ 13,558	\$ 13,558	\$ -	\$ 72,990	18.6%
2013	\$ 14,358	\$ 14,325	\$ (33)	\$ 70,692	20.3%
2012	\$ 14,167	\$ 14,177	\$ 10	\$ 71,121	19.9%
2011	\$ 14,213	\$ 14,953	\$ 740	\$ 68,806	21.7%
2010	\$ 14,149	\$ 14,142	\$ (7)	\$ 67,873	20.8%
2009	\$ 13,683	\$ 14,509	\$ 826	\$ 66,679	21.8%

(1) The actuarially determined contribution rates are calculated as of October 1 of the year preceding the contribution year, using the following assumptions:

Actuarial cost method: Entry Age Normal

Amortization method: Level percentage of payroll, closed

Remaining amortization period: 7 years

Asset valuation method: 20.0 percent of the difference between expected actuarial value (based on assumed return) and market value is recognized each year with 10.0 percent corridor around market value

Inflation: 2.25 percent per year for the first 10 years and 2.5 percent per year thereafter

Salary increases: 3.75 percent to 7.5 percent depending on service, including inflation

Investment rate of return: 7.25 percent

Retirement age: Experience-based table of rates that are specific to the type of eligibility condition. Last updated for the 2015 valuation pursuant to an experience study completed in August 2015.

Mortality: RP-2000 Healthy Annuitant Mortality Table with mortality improvements projected to all future years using Scale BB.



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Report of Independent Auditors on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To Management and the Commissioners of Orlando Utilities Commission

We have audited, 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, the financial statements of Orlando Utilities Commission (OUC), which comprise the statement of net position as of September 30, 2018, and the related statements of revenues, expenses and changes in net position, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated December 3, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered OUC's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of OUC's internal control. Accordingly, we do not express an opinion on the effectiveness of OUC's internal control.

A deficiency in internal control 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 and correct misstatements on a timely basis. *A material weakness* is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.



Compliance and Other Matters

As part of obtaining reasonable assurance about whether OUC's 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*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads 'Ernst & Young LLP'.

December 3, 2018



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