Powering Our Community
with Excellence in Energy Solutions

CITY OF LAKELAND, FLORIDA
DEPARTMENT OF ELECTRIC UTILITIES

FINANCIAL STATEMENTS

September 30, 2011 and September 30, 2010

DEPARTMENT OF ELECTRIC UTILITIES
AN ENTERPRISE FUND OF THE
CITY OF LAKELAND, FLORIDA

SOLAR FARM - PHASE ONE
LAKELAND LINDER REGIONAL AIRPORT

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Vision

Powering our community with excellence in energy solutions

Mission

We are committed to provide safe, reliable, competitive and environmentally responsible energy solutions to enrich our customers' quality of life

Values

Accountability: Take responsibility for our actions with an appropriate sense of urgency

Appreciation: Recognize and celebrate our successes, learn from our mistakes, and value the opinion of others

Customer Focus: Strive for excellence in meeting internal and external customer needs

Diversity: Recognize and utilize our differences

Initiative: Encourage and value creativity, innovation, and sensible business risk

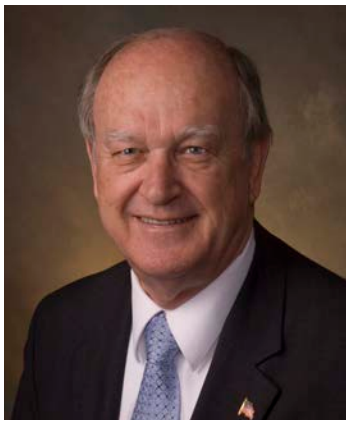
Integrity: Be sincere and honest in what we do

Open Communications: Speak from the heart and listen with respect

Safety: Prevent injury to our fellow employees and the general public

Teamwork: Share information and work together to achieve more

Lakeland Electric is well positioned for a strong performance over the next year and the next decade.



JIM STANFIELD
GENERAL MANAGER

Our employees continue their commitment to a high level of performance even amid continuing financial restraints and uncertainties which for several years have confronted the utility. Uncertainties regarding Federal regulations, pay and benefits as the economy changes, NERC compliance issues and the continuing difficulties of staffing. But, their dedication and commitment is evidenced by Lakeland Electric again meeting or exceeding its budget expectations in a year of economic downturn and lagging system sales. It is evidenced by substantially meeting or completing the majority of Key Success Indicators on the 2011 Strategic Plan. For example, we again significantly beat our target for uncollectable as a percentage of revenue which is a reduction of bad debt in a down economy. Working as a team the result of an on-site NERC compliance audit found no actionable violations of standards.

Again, we begin a new fiscal year maintaining a consistent message with the same five goals:

1. Be a customer focused organization
2. Manage assets and resources to optimize return
3. Attract, motivate, develop and retain talented employees
4. Efficiently integrate technology into business operations
5. Anticipate future system requirements through proactive planning

Lakeland Electric measures our progress against these goals and is using a prioritized budget system to assure we are addressing the right actions. We have been able to make relatively quick adjustments as conditions change; examples include a 25% co-firing of natural gas in our coal unit without derating the unit and accommodating a large high load factor customer by quickly preparing an appropriate tariff. Other factors that contribute to our success and favorable outlook: Our service territory is well defined and concentrated; we know who and where our customers are and what their needs are. Our prices are competitive and expected to remain so throughout 2012. We are part of a power pool which reduces our supply reliability risk. Our units, while some are old, are performing as well as any in the state. Recent repairs to our two base load units give us confidence that we will maintain a successful production cost profile; in fact our main gas combined cycle unit successfully completed a record 122 consecutive days of operation. By the end of 2012 Lakeland Electric will have a fully functional smart grid throughout the distribution system. Our growth rate is modest, but not regressing; it enables us to hold the line on capital. We have a well trained employee cadre' and divisional workforce plans in place to address shortfalls. We have a cross functional Risk Oversight Committee to properly vet technical and financial risks to the Utility. We have a strong, well involved governing Commission. Lakeland Electric is well positioned for the next decade.

LAKELAND ELECTRIC
Your Essential Link to a Quality Life

April 3, 2012

Honorable Mayor Gow Fields, Members of the Utility Committee and Customers of Lakeland Electric:

The annual financial report for the City of Lakeland, Florida's Department of Electric Utilities (Lakeland Electric, or "LE") for the fiscal year ended September 30, 2011, as prepared by the City's Finance Department, is hereby submitted. Responsibility for both the accuracy of the data, and the completeness and fairness of the presentation, including all disclosures, rests with management. I believe this report is accurate in all material respects and that the information displayed and disclosed is presented in a manner that presents fairly the Utility's financial condition. All disclosures necessary to enable the reader to gain an understanding of the Utility's activities have been included. The Finance Department is delighted to take this opportunity to provide you with an overview and summary of the Utility's finances, economic prospects, and achievements.

Management's discussion and analysis (MD&A) immediately follows the independent auditor's report and provides a narrative introduction, overview, and analysis of the basic financial statements. MD&A complements this letter of transmittal and should be read in conjunction with it.

PROFILE OF LAKELAND ELECTRIC

Lakeland Electric is an enterprise fund governed by the Lakeland City Commission, and is the largest department of the City of Lakeland. It has a budgeted staff of 601 full time employees including 310 employees who are members of the Utility Workers Union of America, Local 604. The Utility's service territory consists of approximately 246 square miles including the incorporated area of the City and a number of unincorporated communities lying within a 15-mile radius of the City. During Fiscal Year 2011, an average of 121,941 electric accounts were served. The Utility's territory is bordered on the north by the Withlacoochee Rural Electric Cooperative, Inc., on the south by the City of Bartow, and on the east and west by the Tampa Electric Company. Lakeland Electric is a vertically integrated utility with generation capacity of 984 MW and is also a member of the Florida Municipal Power Pool (FMPP) that includes Orlando Utilities Commission (OUC) and Florida Municipal Power Authority (FMPA).

MAJOR INITIATIVES AND FINANCIAL HIGHLIGHTS

Major Initiatives

North American Electric Reliability Corporation (NERC) Compliance - In response to the worst blackout in history that occurred in 2003, NERC Reliability Standards became mandatory and enforceable in the United States. Penalties for non-compliance ranged from $1,000 to $1,000,000, per day, per violation, per occurrence. As part of a three-year cycle, LE was audited in fiscal year 2011. LE had an extremely successful audit that resulted in no penalties or fines.

Environmental - Fiscal year 2011 featured a full year of operation of our selective catalytic reduction (SCR) system on the coal plant. Compared to 5 years ago, LE has reduced its emission of nitrogen oxides and sulfur dioxides in the air by 58% and 77% on a tons/year basis respectively from our base load units.

Smart Grid - Beginning in 2010, LE is scheduled to complete the Smart Grid project by the end of 2012. It will give LE more control over its utility grid, and also give the customer more information and control over their electricity usage than ever before. 42% of the project was funded by a grant from the Department of Energy.

Solar Program - Construction of 2.3 MW of solar photovoltaic (PV) energy plants began in fiscal year 2011 with commissioning of the facility in early 2012. This solar energy system will produce enough electricity over the next 20 years to offset 807 million pounds of carbon dioxide and sustain approximately 7,200 homes with clean energy. Another 3.2 Megawatt (MW) of solar development is scheduled for the future. It is one of the largest utility-sponsored solar programs in the United States and it was completed without any capital costs to the Utility.

Energy Efficiency and Conservation Block Grant (EECBG) - During fiscal year 2011, LE administered a revolving loan program, funded by the Department of Energy, allowing eligible customers to obtain zero interest loans up to $5,000 to install select energy efficiency and renewable energy measures in their homes. Due to the success of the program, additional funding was granted. LE also expanded the program to include replacement of old refrigerators with new Energy Star rated refrigerators.

Power Academy - In response to an aging workforce and a very competitive market for skilled labor, LE is now in its fourth year of the Power Academy which was developed to provide the utility with a pool of qualified candidates. To date, 35 students have graduated from the Academy with another 85 enrolled.

Rate Case - During fiscal year 2011, LE did engage in a base rate study. Due to a poor local economy, no base rates were increased. However, LE developed and implemented rates for Time of Use in association with Smart Grid, Electric Vehicle rates and rates for Large Demand Interruptible customers. LE ended the fiscal year in the lowest quartile for both base and total rates for all major customer classes in the state of Florida.

Financial Highlights

In fiscal year 2011, Lakeland Electric's service territory was in the middle of a very slow recovery from the Great Recession that resulted in flat customer growth and little expansion of commercial or industrial activity. 2011 was a more normal year for weather and featured much less weather driven demand as compared to 2010. Despite these challenges, LE was able to achieve strong financial performance through innovation and fiscal management. Highlights include:

- Change of net assets of $20.2 million which was a slight increase from a very successful 2010
- Debt service coverage well above the requirement from bond covenants.
- Capital spending above depreciation resulting in addition to book value of the Utility.
- No significant change in liquidity or reserves
- Maintained excellent credit rating
- Strong expense management discipline of controllable costs

AKNOWLEDGMENTS

The preparation of this report could not be accomplished without the efficient and dedicated service of the entire staff of the Electric Finance Department. I would like to express my appreciation to all members of the staff who assisted and contributed to its preparation, with special thanks to the City's Finance Director, Greg Finch and also to Mark Meeks, Manager of Utilities Finance and Accounting. We also appreciate the assistance and cooperation of Crowe Horwath LLP for their completion of the independent audit. I would like to thank you for your interest in the Utility's financial matters and support of this report.

Respectfully Submitted,

Don Eckert
Assistant General Manager - Fiscal Operations

CREATING A CULTURE OF COMPLIANCE

HISTORY OF COMPLIANCE

In late 2003, North America experienced its worst blackout ever, as 50 million people lost power in the Northeastern and Midwestern United States and Ontario, Canada. This blackout resulted in the United States government electing to make reliability standards mandatory and enforceable. In 2006, Federal Energy Regulatory Commission (FERC) certified North American Electric Reliability Corporation (NERC), a non-profit corporation, as the "electric reliability organization" for the United States. NERC delegated its authority to monitor and enforce compliance with NERC Reliability Standards in the United States to eight Regional Entities; Lakeland Electric's Regional Entity is the Florida Reliability Coordinating Council (FRCC).

On June 18, 2007, compliance with approved NERC Reliability Standards became mandatory and enforceable in the United States. The Compliance program was designed to ensure that the right practices are in place so that the likelihood and severity of future system disturbances are substantially reduced, while recognizing that no standards or enforcement process can fully prevent all such disturbances from occurring.

MANDATORY STANDARDS

To date there are one hundred and four 'Mandatory Standards Subject to Enforcement', eighty two of which are enforceable for Lakeland Electric. Each Standard has Requirements and Sub-Requirements which carry penalties directly related to the risk of the reliability to the Bulk Electric System for non-compliance. The penalty matrix for non-compliance ranges from one thousand dollars to one million dollars, per day, per violation, per occurrence.

AUDIT RESULTS

Lakeland Electric is audited on a three year cycle. During the week of October 25th, 2010, Lakeland Electric was audited on thirty eight Standards, by the Regional Entity. Lakeland Electric had an extremely successful audit outcome, all in part to the dedication of our skilled employees and the support of management.

MAINTAINING COMPLIANCE

The Compliance division maintains an Internal Compliance Program. This program was built around the idea of company-wide responsibility. This company-wide responsibility is guided by the Manager of Electric System Compliance, through interaction with all the divisions of Lakeland Electric. This interaction provides a companywide perspective, which facilitates buy-in from each area and reduces the potential of non-compliance with the program's initiatives, policies, and procedures.

Additionally, the Manager of Electric System Compliance sets a goal to self-audit all Reliability Standards applicable to Lakeland Electric annually. The Compliance staff evaluates documentation and evidence submitted by each division to validate compliance with Standards and Requirements.

ENVIRONMENTAL

Lakeland Electric has reduced emissions of pollutants to the environment considerably over the years. In the past five calendar years alone, 2005 through 2010, Lakeland Electric has reduced its emissions of nitrogen oxides and sulfur dioxide, two major pollutants regulated by EPA, by 58% and 77% on a tons/year basis respectively from our large electric generating units.

In 2009, Lakeland Electric began installation of a selective catalytic reduction (SCR) system on our sole coal unit. The purpose of the SCR is to reduce emissions of nitrogen oxides that are emitted from the unit into the atmosphere. Large emissions reductions are already being seen as the SCR system and low-NOx burners are in their first few years of operation.

LAKELAND ELECTRIC CUSTOMER ASSISTANCE

Lakeland Electric provides multiple services for customers to help them reduce their energy use, get help with their utility bill, and contribute to community assistance efforts.

ENERGY EFFICIENCY PROGRAMS

Over the past year we helped 6,626 customers reduce their energy footprint through the use of rebates, energy saving kits, and lighting changes. Our program provides rebates for insulation upgrades, HVAC maintenance, new heat pumps, and weatherization upgrades. At community events our employees provide customers with free energy saving kits and free compact fluorescent lights.

HOME ENERGY AUDITS

Nearly 2,500 customers received a free home energy audit from one of our certified auditors. Our auditors review heating and cooling efficiency, insulation levels, lighting efficiency, and tips on how to reduce customer's energy use.

CUSTOMER ADVOCATE TEAM

Lakeland Electric staffs a Customer Advocate Team that is charged with handling complex customer transactions that typically require additional research, as well as interaction with multiple, internal resources in order to complete a customer request. Over the past year the team resolved over 200 complex customer cases.

PAYMENT ASSISTANCE

Lakeland Electric offers 24/7 payment assistance through our web site, enabling over 2,000 customers last year to make arrangements that fit their circumstances without having to work through an agent. In addition our customer service agents helped one in four customers work through a payment assistance plan.

PROJECT CARE

Through contributions, drawings, and contests, Lakeland Electric employees contributed over $35,000 to the Project Care fund that provides assistance for customer bills.

SOCIAL SERVICE PROGRAMS

By working with local social service agencies we helped allocate $1,296,000 in utility bill payment assistance.

working TOGETHER for a brighter tomorrow.

»projectcare your small change can make a big difference.

SMART GRID

THE SMART GRID INITIATIVE

The Smart Grid initiative is the evolution of the nation's utility grid to make it more effective, efficient and responsive to the needs of the country, the utility industry and most of all-customers. Smart Grid will give Lakeland Electric more control over its utility grid, and also give the customer more information and control over their electricity usage than ever before.

Lakeland Electric has currently installed over 60,000 Smart Meters in its service area, which consists of approximately 120,000 customers. We are in the process of testing samples of Smart Meters on our retrieval system to compare with our meter readers. Once all the Smart Meters have been installed, and all of the tests on the system have been completed, we will be relocating our current meter readers to other positions across Lakeland Electric and the customer meters will be read from the Lakeland Electric offices.

UTILITY EFFICIENCY AND CONTROL:

Lakeland Electric will have the ability to monitor and control operations and actions within the distribution area through the use of our two-way communication system. Smart Meters will be read every hour, instead of once a month. Lakeland Electric will have more readily available information about the electric system, which will better equip us to supervise and prevent unauthorized use of electricity.

CUSTOMER CONTROLS:

Lakeland Electric customers will be able to log into a customer portal, available on our website, and view their electricity usage at any time. This will give our customers the ability to monitor their electricity consumption, and give them the opportunity to reduce their energy costs by changing to a different rate structure. Instead of the tradition rate structure, customer may change to a Time of Use rate structure.

TIME OF USE (TOU)

TOU allows our customers to take advantage of lower energy rates during the off-peak service times. With customers shifting some of their load from an on-peak time to an off-peak time they not only save themselves money, but they also allow us to reduce the amount of energy we generate. Reducing our generation permits our generators to be used more efficiently and delays the need for replacements.

COMMITMENT TO CLEAN, RENEWABLE ENERGY

Solar power represents a clean, renewable energy source that offers tremendous benefit to both the environment and the health of future generations. What's more, the development of solar photovoltaic "PV" energy plants creates good, local jobs for the new energy economy--more jobs per megawatt hour than any other energy type.

A leader in the development of solar PV systems, Lakeland Electric is committed to environmental sustainability and to providing innovative energy solutions to Floridians. Two years ago, Lakeland Electric laid out a long-term plan with solar developer SunEdison to integrate 24 megawatts of solar capacity into our energy mix by 2018. One of the largest utility-sponsored solar programs per metered customer in the United States, this system will produce enough zero-emission solar electricity over 20 years to offset nearly 807 million pounds of carbon dioxide and sustain approximately 7,200 homes with clean, environmentally-friendly energy.

During 2011 Lakeland Electric made a huge stride toward utility-scale solar generation with the installation of a 2.3 mega-watt PV system at Lakeland's municipal airport. By building this facility on the airport's Runway Protection Zone, Lakeland Electric has made use of land that would not have been developed for any other public activity, a win-win situation for both the utility and the airport. During construction this project created construction jobs for ninety-one local workers.

Plans call for another 3.2 megawatts of solar development at the airport, which will bring the total solar generation capacity up to 5.5 megawatts. This additional capacity is expected to be completed during the summer of 2012. Upon full build out the airport solar facility will generate 8,250,000 kWh of electricity annually.

REEnergize LAKELAND

The City of Lakeland was awarded an Energy Efficiency & Conservation Block Grant by the U.S. Department of Energy under the American Recovery & Reinvestment Act. The EECBG program is housed in the municipal electric utility, Lakeland Electric. The EECBG funds must be used to reduce the overall energy consumption and carbon footprint of the municipality. A portion of the funds were used to replace the antiquated HVAC system in City Hall, and the remainder was obligated to assist Lakeland Electric's residential customer class to reduce their electric consumption by improving the energy efficiency of their homes.

The primary program established is a revolving loan program, entitled REEnergize Lakeland Finance, whereby eligible customers can obtain a zero interest loan up to $5,000 to install select energy efficiency and renewable energy measure in their homes. Customers then repay the loan as a line-item on their electric bill. The initial funding for the program, in the amount of $250,000, was awarded in four months to fifty-four households, and will result in an annual electric reduction of 143 MWhs. Due to the success of the program, Lakeland Electric has obligated an additional $100,000 to increase the program scope, increasing the number of customers who will be able to take advantage of this innovative on-bill financing program.

In order to reduce peak electric consumption, Lakeland Electric also obligated $93,300 to be used as a rebate for customers to replace their old refrigerators with a new Energy Star rated refrigerator. The rebate is only available for refrigerators due to their high electric consumption and the fact that they run 24 hours/day, 7 days/week. Other high-consumption household appliances, such as clothes dryers and dishwashers, can be operated during off-peak hours as a result of slight modifications in customer behavior. To date, over 100 rebates have been provided of a planned total of 415.

Lakeland Electric is excited about these programs that will help our residential customers reduce their electric consumption and result on lower bills. The revolving loan program in particular will result in many years of savings due to its ability to recycle the funds as repayments are made.

THE POWER ACADEMY

Lakeland Electric, in partnership with the Polk County School Board, opened the Lakeland Electric Power Academy at Tenoroc High School in August, 2008, to support our workforce strategy to develop a pipeline of qualified applicants to fill vacant entry level positions in preparation for a projected increase in retirements. The academy curriculum focuses on an awareness of the various careers available in the industry and the competencies and skills required. The four-year academy is offered in a traditional high school setting where students receive their general education courses and are able to participate in extracurricular activities. A highlight of the program is the 15-week job shadowing experience available to seniors who successfully complete all other requirements. Students shadow Lakeland Electric employees in three job rotations of six hours a week for five weeks. In addition, upon successful completion of written tests and skill demonstration requirements, students earn the nationally recognized National Center for Construction Education and Research (NCCER) industry certifications in Electrical I and II. Thirty-five students have graduated from the Academy and 89 students are currently enrolled. Lakeland Electric has employed five Power Academy graduates--three in full-time positions, and two in Power Academy Intern positions. Lakeland Electric has received several awards for this successful industry/education partnership.

2011 Power Academy graduates receive recognition at a Lakeland Electric Utility Committee meeting.

Power Academy senior, Zoe Lauters, won first place in Florida's 2011 "Get Into Energy" week essay contest on the topic, "Energy Workers Make a World of Difference." (Pictured left to right, Ernest Joe, Jr., Tenoroc High School Principal, Jim Stanfield, General Manager of Lakeland Electric, Zoe Lauters, LE Power Academy senior, Betsy Levingston, LE Director of Training and Workforce Development, and Gary Kiger, Power Academy Instructor.

Lakeland Electric Power Academy

Get Into Energy!

PRICING & RATES

Lakeland Electric is cognizant of its commercial value in comparison to other Florida electric utilities. Figure X is a retail price comparison at year's end with other utilities (investor owned, municipals, and cooperatives) by customer group. Two competitive measures are followed. First is the relative value of the total bill paid by the customer, an indication of long-term competitiveness. The second metric is the customer bill net of any Fuel Charge which is indicative of business operating efficiency.

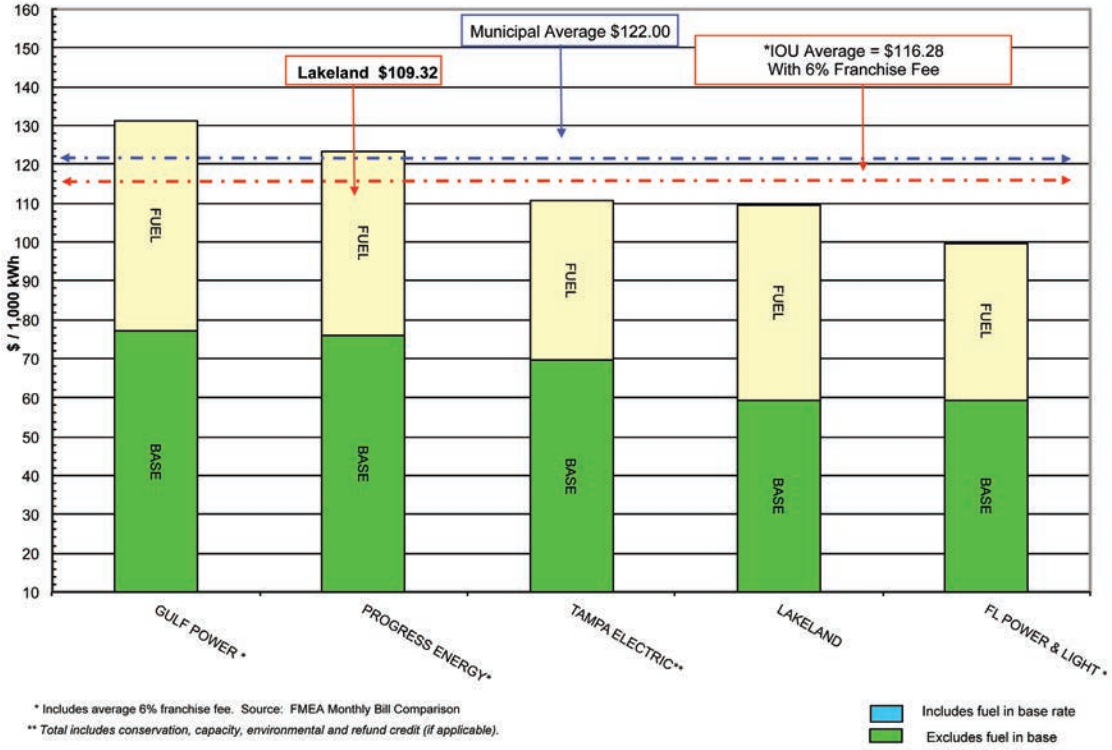


FIGURE X RESIDENTIAL BILL COMPARISON, SELECT MUNICIPALS, NOVEMBER 2011

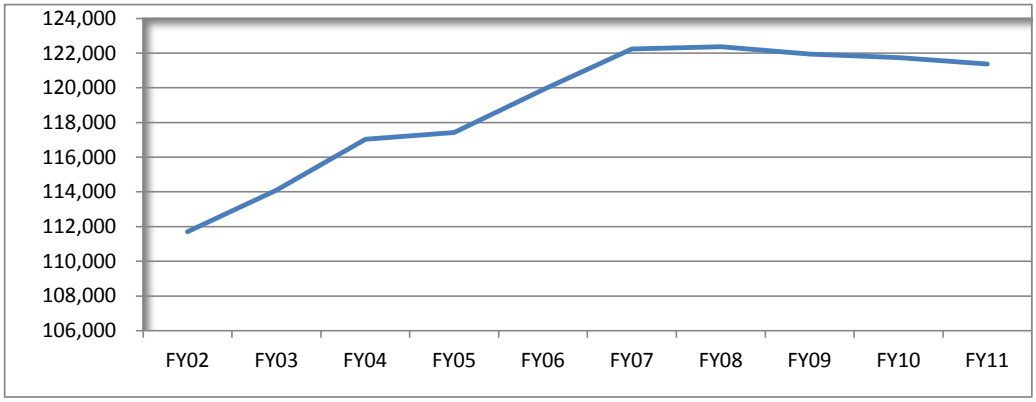
Fiscal 2011 included restarting the retail rate study deferred the previous year. A new cost of service analysis confirmed the perception that not all customers were sharing equally in the recovery of utility operating costs. Review also identified unfunded capital projects and unfunded operating costs associated with the union contract and non-union wages and benefits. Justification for increasing retail electric rates was presented to the Utility Committee/City Commission. Coincident with these discussions the fiscal year continued to accumulate unexpected Net Income After Transfers on its balance sheet. The final disposition to the rate study was to not increase any existing rates for a nominal two years. New services were approved for time-of-day trial rates, charging electric vehicles, and serving large demand interruptible customers at time-of-day prices. Lakeland Electric anticipates starting the next rate study within the next twelve months with an effective date for any rate increase no earlier than Fiscal Year 2014.

Lakeland Electric
Selected Statistical and Financial Data

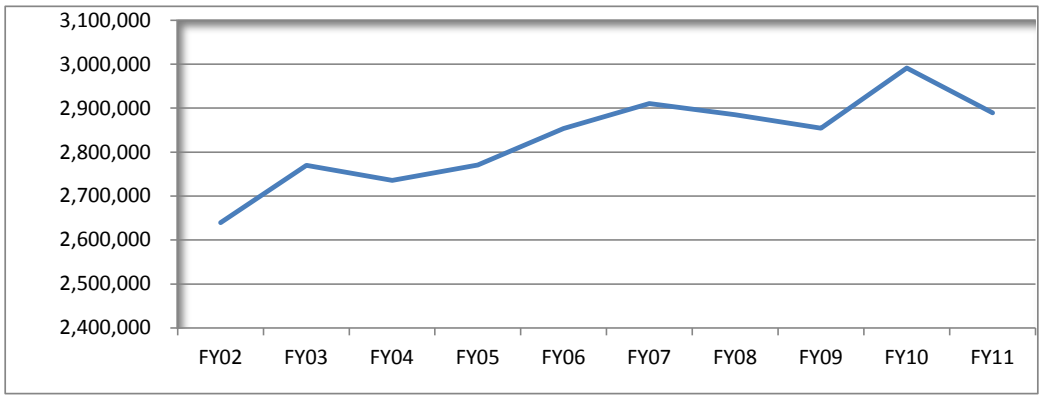
	FY2011	FY2010	Percent Incr/-Decr
Plants	3	3	0.0%
Nameplate Generation (MWH)	984	984	0.0%
Retail service territory (square miles)	246	246	0.0%
Substations	23	23	0.0%
Transmission lines (miles)			
69 KV	123.0	116.0	6.0%
230 KV	28.0	28.0	0.0%
Distribution lines:			
Overhead (miles)	1,276	1,279	-0.3%
Underground (miles)	626	624	0.3%
Retail electric customers:			
Residential	100,545	100,638	-0.1%
Commercial and Industrial	12,339	12,400	-0.5%
Roadway and private area lights	8,493	8,701	-2.4%
Number of employees (FTE's)	564	573	-1.6%
Retail sales (MWH)	2,889,577	2,991,123	-3.4%
Average Demand (MWH)	340	354	-4.0%
Summer Peak (MWH)	611	638	-4.2%
Winter Peak (MWH)	655	804	-18.5%

	(Dollars in thousands)		Percent
	FY2011	FY2010	Incr/-Decr
Retail sales, excluding fuel revenue	$ 170,618	$ 175,679	-2.9%
Operating expenses, excluding fuel and taxes	$ 72,048	$ 71,888	0.2%
Fuel and purchased power expenses	$ 161,967	$ 171,526	-5.6%
Depreciation expense	$ 35,704	$ 35,888	-0.5%
Operating income	$ 63,193	$ 66,467	-4.9%
Change in net assets	$ 20,172	$ 19,213	5.0%
Current assets	$ 131,310	$ 131,262	0.0%
Current liabilities	$ 20,976	$ 21,057	-0.4%
Current ratio	6.26	6.23	0.4%
Utility plant, net	$ 637,285	$ 631,078	1.0%
Long-term debt, net	$ 486,526	$ 484,410	0.4%
Debt service coverage (ordinance)	2.93	3.03	-3.3%

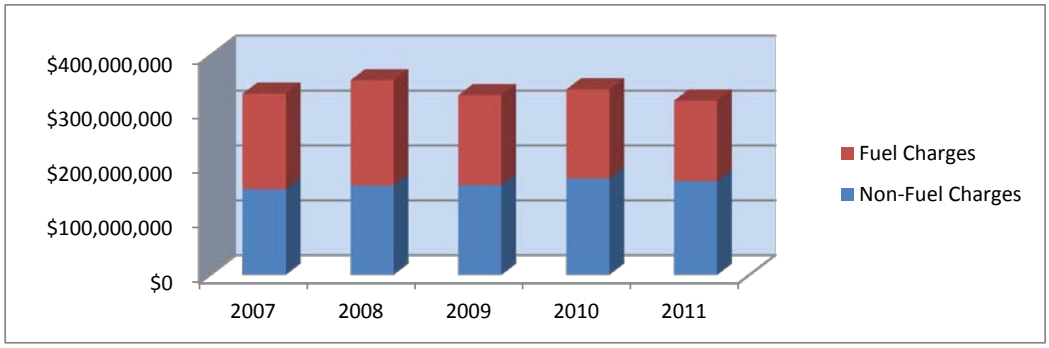
Retail customer count for FY2011 and previous nine years:



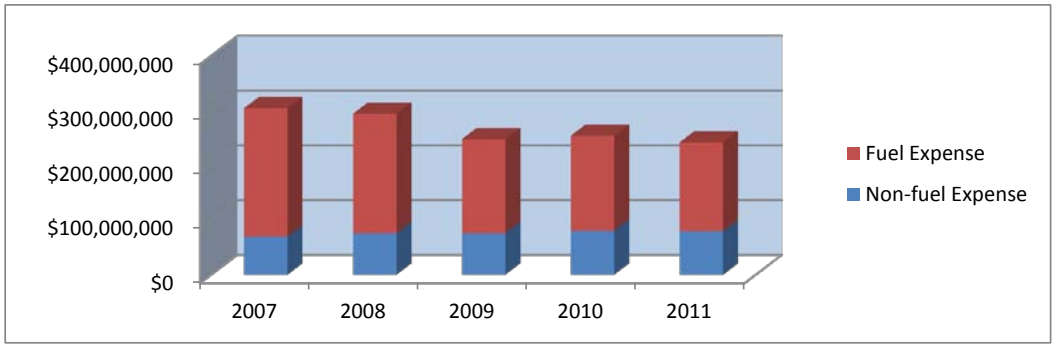
Net retail customer load for FY2011 and previous nine years (in megawatt hours)



Retail sales of electicity for FY2011 and previous four years:



Operating expenses for FY2011 and previous four years:

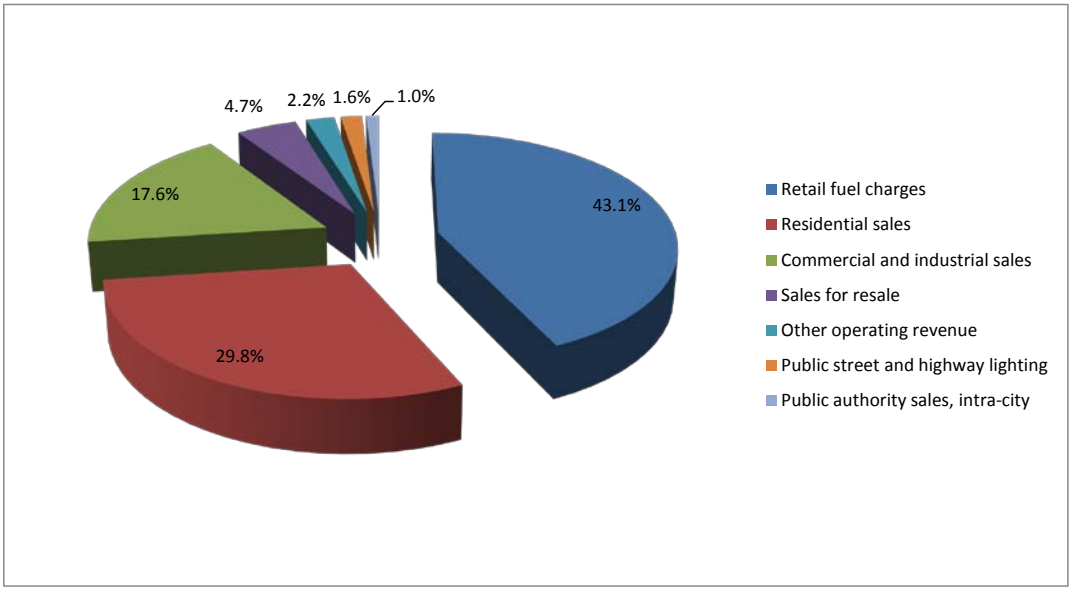


Lakeland Electric

Fiscal Year 2011

Operating Revenue

Retail fuel charges	$ 146,923,431
Residential sales	101,699,309
Commercial and industrial sales	60,081,729
Sales for resale	15,874,978
Other operating revenue	7,465,356
Public street and highway lighting	5,567,490
Public authority sales, intra-city	3,269,563
Total	$ 340,881,856

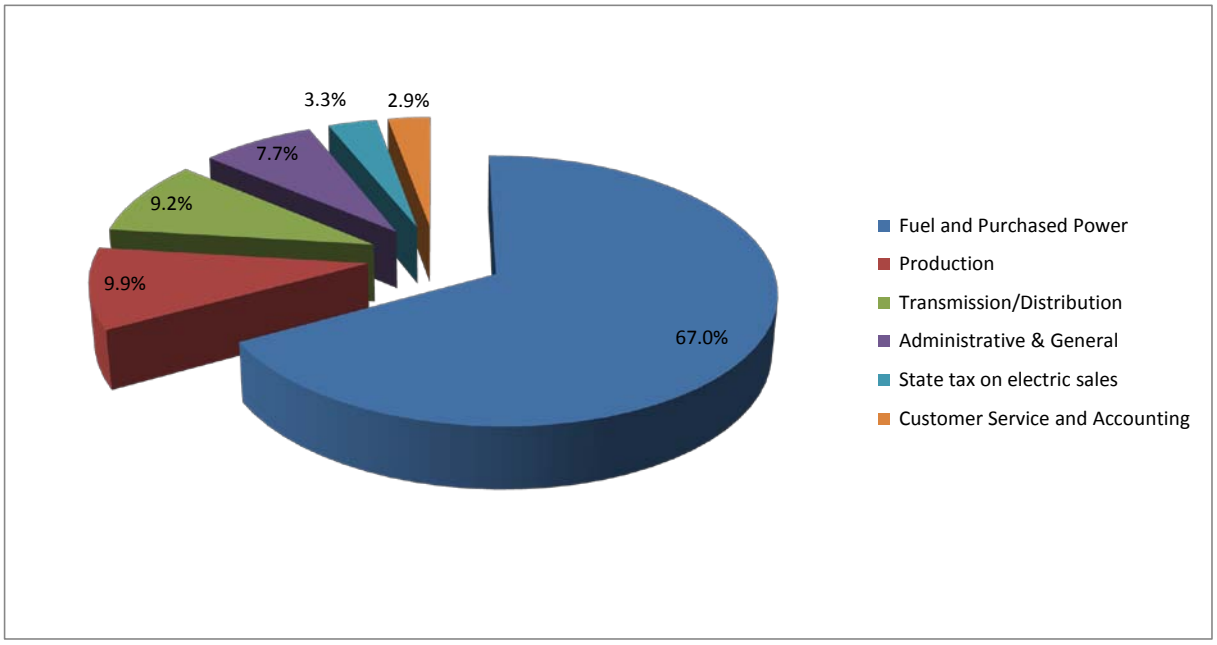


Lakeland Electric

Fiscal Year 2011

Operating Expenses

Fuel and Purchased Power	**$ 161,966,709**
Production	**23,924,605**
Transmission/Distribution	**22,264,926**
Administrative & General	**18,953,380**
State tax on electric sales	**7,971,034**
Customer Service and Accounting	**6,904,619**
Total	**$ 241,985,273**



LAKELAND ELECTRIC

AUDITED FINANCIAL STATEMENTS

FISCAL YEAR END 2011

C O N T E N T S

Crowe Horwath LLP
Independent Member Crowe Horwath International

REPORT OF INDEPENDENT AUDITORS

Honorable Mayor, City Commissioners
and City Manager
City of Lakeland, Florida

We have audited the accompanying financial statements business-type activities of the Department of Electric Utilities of the City of Lakeland, Florida, (the Department) as of and for the years then ended September 30, 2011 and 2010. These financial statements are the responsibility of the Department's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

As discussed in Note A, the financial statements present only the Department of Electric Utilities of the City of Lakeland, Florida, and do not purport to, and do not, present fairly the financial position of the City of Lakeland, Florida, as of September 30, 2011 and 2010, and the changes in its financial position and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of the Department of Electric Utilities of the City of Lakeland, Florida, as of September 30, 2011 and 2010, and the changes in financial position and cash flows thereof for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with Government Auditing Standards, we have also issued our report dated April 6, 2012, on our consideration of the Department of Electric Utilities of the City of Lakeland, Florida's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing results of our audit.

The *Management's Discussion and Analysis* on pages 2 through 6 is not a required part of the basic financial statements but is supplementary information required by the accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Crowe Horwath LLP

Crowe Horwath LLP

Lakeland, Florida
April 6, 2012

CITY OF LAKELAND, FLORIDA
DEPARTMENT OF ELECTRIC UTILITIES
Management's Discussion and Analysis

Management's Discussion and Analysis provides a narrative overview of the City of Lakeland's Department of Electric Utilities' (Lakeland Electric) financial activities for the fiscal year ending September 30, 2011. Lakeland Electric's operations consist of electric generation, transmission and distribution. Readers are encouraged to consider the information presented in this section in conjunction with additional information contained in the financial report. The following condensed Summary of Financial Position and Summary of Revenues, Expenses and Changes in Net Assets summarizes the financial condition and operations of Lakeland Electric for the year ended September 30, 2011 and the previous two fiscal years:

	(In Thousands)		
	September 30		
	2011	2010	2009
Assets			
Current assets	$ 131,310	$ 131,262	$ 127,601
Utility plant, net	637,285	631,078	619,187
Noncurrent assets	180,071	166,487	157,004
	$ 948,667	$ 928,827	$ 903,792
Liabilities and Net Assets			
Current liabilities	$ 20,839	$ 19,303	$ 22,465
Noncurrent liabilities	609,797	611,665	602,682
Net assets invested in capital assets, net of related debt	120,302	112,707	89,526
Unrestricted net assets	197,729	185,152	189,119
	$ 948,667	$ 928,827	$ 903,792
Revenues, Expenses and Changes in Net Assets			
OPERATING REVENUES			
Sales of energy - retail	$ 317,542	$ 337,890	$ 327,651
Sales of energy and capacity sales - wholesale	15,875	10,087	9,906
Other electric operating revene	7,465	6,239	5,810
	340,882	354,216	343,367
OPERATING EXPENSES			
Fuel and purchased power	161,967	171,526	171,901
Energy supply	23,924	22,985	21,849
Energy delivery	22,265	21,005	19,478
Customer service and accounting	6,905	7,118	7,539
Administrative and general	18,953	20,779	18,840
State tax on electric sales	7,971	8,448	7,768
Depreciation	35,704	35,888	35,433
	277,689	287,749	282,808
OPERATING INCOME	63,193	66,467	60,559
NON-OPERATING ACTIVITY			
Investment and other income	8,768	7,612	10,023
Interest and amortization	(26,827)	(28,418)	(28,124)
Transfers to/from other funds (net)	(24,962)	(25,398)	(23,630)
Loss on disposal of fixed assets	-	(1,049.69)	0
Plant costs recovered from capital contributions	(9,951)	(4,695)	(4,603)
Capital Contributions	9,951	4,695	4,603
	(43,021)	(47,254)	(41,731)
CHANGE IN NET ASSETS	$ 20,172	$ 19,213	$ 18,828

Financial Highlights

- Retail kilowatt hours (kWh) sales decreased by 3.5 percent in 2011 from the previous fiscal year. The decline in sales was primarily weather related, as the previous fiscal year featured record retail consumption. Growth in the customer base remained flat for the second consecutive year. Retail revenues, excluding fuel, averaged $59.05 per 1,000 kWh in FY 2011 compared to $58.73 in FY 2010. The minor increase resulted from the reclassification of some commercial and industrial customers during 2011. Lakeland Electric has not increased its base retail electric rates since 2007.

- Lakeland Electric's non-fuel operating expenses, excluding gross receipts tax and depreciation, were $72.0 million in fiscal year 2011, which was a slight increase from $71.9 million in 2010. The previous year included $1.4 million of additional payroll costs associated with a Utility Workers Union of America (UWUA) settlement. Total operating and maintenance costs (excluding fuel, gross receipts tax, and depreciation) averaged $24.93 per 1,000 retail kWh in 2011, which was a 4 percent increase from $24.03 in 2010.

- The profitability of retail operations increased by $1.0 million from the previous fiscal year in spite of a $3.8 million reduction in non-fuel retail revenues. Favorable variances occurred in total operating expenses ($0.5 million), operating transfers ($0.4 million), and non-operating income ($2.8 million). No impairment losses were recorded in 2011, while there was a $1.0 million impairment loss in the previous year. The profitability of wholesale operations was approximately the same.

- Fuel and purchased power expenses decreased by $9.6 million from the previous fiscal year as a result of the reduced customer load, as well as a reduction in fuel prices. The average fuel cost to generate 1,000 kWh of energy to serve the retail load fell from $54.59 in fiscal year 2010 to $51.39 in fiscal year 2011. The decrease resulted from a 9 percent drop in the average cost of natural gas (per mmbtu). Lakeland Electric recovers 100 percent of fuel costs from retail customers in the form of a fuel charge that is revised quarterly, as needed, based on a forecast of fuel costs for the following twelve months. As of September 30, 2011, the retail fuel charge was $50.65 per 1,000 kWh, compared to a rate of $53.15 which was in effect twelve months earlier. As of September 30, 2011, Lakeland Electric had an over-recovery of fuel charges in the amount of $1.4 million compared to $1.2 million at the end of the previous fiscal year. The over-recovery represents, on a cumulative basis, the difference between fuel costs incurred to serve retail load and fuel revenues realized. See Note F, Deferred Regulatory Accounts.

- In May 2010, the City of Lakeland was awarded a grant from the U.S. Department of Energy (DOE) for Smart Grid power distribution technology, which will ultimately result in improved reliability and efficiency as well as provide a variety other benefits to retail electric customers. The total project budget is $35.1 million, of which $14.9 million is funded by the grant. The implementation period for the Smart Grid runs through May 16, 2015. As of the September 30, 2011, a total of $21.7 million had been spent on the Smart Grid project, with a net cost of $12.5 million to Lakeland Electric.

- Capital spending for the 2011 fiscal year totaled $41.3 million compared to $41 million in fiscal year 2010 and $46.1 million in 2009. Capital outlay in 2011 included: $18.9 million for power production projects, $11.6 million for transmission and distribution projects, and $10.8 million for other capital projects, including $9.5 million for the City's share of the Smart Grid project. Capital projects completed during fiscal year 2011 included: $4.8 million for plant equipment related to the McIntosh Unit 5 long-term service agreement, $6 million for replacement equipment in Unit 5 during the major inspection outage, $5.3 million for McIntosh Unit 1 boiler refurbishment, and $8.2 million for Smart Grid assets that were placed in service.

- Depreciation expense in fiscal year 2011 was $35.7 million compared to 35.9 million in 2010. McIntosh Units 1 and 2 were fully depreciated in 2010. Depreciation expense is expected to rise in future years as a result of capital projects placed in service.

Financial Highlights (Continued)

- Lakeland Electric funds the cost of capital improvements through a combination of bond financing and cash generated from retail utility rates. The capital improvements plan prepared by Lakeland Electric projects future spending at an average of approximately $38 million over the next 4 years.

- Capital contributions (contributions in aid of construction) from outside the City were approximately $10 million during fiscal year 2011, including $7.1 million in grant recoveries from the DOE for Smart Grid. Comparably, contributions in aid of construction were $4.7 million in the previous fiscal year.

- Lakeland Electric provides a dividend to the General Fund each year in the form of a cash transfer. The total amount of the dividend in fiscal year 2011 was $24.2 million, compared to $25.2 million in 2010. The dividend rate for both years was $8.41 per 1,000 kWh of retail sales. The dividend in fiscal year 2011 was 7.1 percent of gross operating revenues of Lakeland Electric, which is consistent with the industry median as reported by the American Public Power Association. The dividend for fiscal year 2012 is budgeted at $24.5 million.

Capital Assets

The following table contains a summary of Lakeland Electric plant investment net of accumulated depreciation as of the September 30, 2011 and 2010:

	(In Thousands)	
	September 30	
	2011	2010
Land	$ 15,883	$ 15,883
Construction in process	21,246	29,301
Buildings	13,513	14,424
Machinery and equipment	9,580	10,808
Equipment under capital leases	420	531
Electric transmission and distribution	247,464	241,414
Electric plants in service	329,179	318,716
	$ 637,285	$ 631,077

The generating capacity of the production units owned by the City is 984 megawatts (MW). The most cost effective unit in the generating fleet, when natural gas prices are above $4/MMBTU, is the 365 MW McIntosh 3 coal fired unit, of which 60 percent or 218 MW is owned by Lakeland Electric. During the past ten years, Lakeland Electric has placed a 350 MW combined cycle natural gas unit, which is the most efficient unit in the fleet, and a 50 MW internal combustion peaking facility into service. Lakeland Electric has sufficient generation and transmission capacity to cover its projected load requirements for at least the next five years.

Debt

At September 30, 2011, Lakeland Electric had $511.2 million in net long-term debt outstanding compared to $520.4 million at the end of 2009 as shown in the following table. The Series 2010 energy system revenue and refunding bonds, issued October 19, 2010, defeased all of the Series 2001B bonds and a portion of the Series 1999A bonds.

	(In Thousands)	
	September 30	
	2011	2010
Electric System Revenue Bonds:		
Series 1999A	$ 21,907	$ 184,730
Series 1999B	15,310	15,310
Series 1999C	33,420	48,285
Series 2001B	-	30,000
Series 2006	42,030	42,850
Series 2009	199,225	199,225
Series 2010	199,300	-
	511,192	520,400
Less Current Portion	(23,633)	(21,992)
Less unamortized loss on refunding	(24,995)	(13,967)
Unamortized bond discount (net of premium)	23,961	(31)
	$ 486,525	$ 484,410

Economic Factors

As indicated in Note N, coverage on bonded debt of Lakeland Electric remains strong at 2.93 times the annual debt service requirement for the fiscal year ended 2011. Per the enabling bond ordinance, an amount equal to 20 percent of the fund balance of Lakeland Electric is included as a component of net revenues in preparing this calculation. Removing this aspect of the coverage calculation yields a coverage ratio of 2.11.

Significant natural gas and oil price fluctuations have occurred in recent years. Lakeland Electric has created a fuel hedging program that is intended to mitigate fuel price volatility over the near term. The program was modified in March 2010 to reduce costs based on a prolonged depressed natural gas market (see Note T).

During fiscal year 2011, the average demand for energy placed on the system from retail customers was approximately 340 MWH, with peak demand during winter of 665 MWH on January 13, 2011, and summer peak demand of 611 MWH on August 12, 2011. Lakeland Electric expects to see minimal change in the retail customer base during fiscal year 2012.

Using This Annual Report

This annual report includes the Statement of Net assets, Statement of Revenues, Expenses and Change in net assets, statement of cash flows and notes to the financial statements for Lakeland Electric, which is an enterprise fund of the City of Lakeland. Please refer to the annual report of the City of Lakeland for more information about the City of Lakeland as a whole.

Requests for Information

This financial report is designed to provide a general overview of Lakeland Electric's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to: Manager of Utilities Finance and Accounting, Lakeland Electric, 501 East Lemon Street, Lakeland, FL 33801. mark.meeks@lakelandgov.net.

CITY OF LAKELAND, FLORIDA
DEPARTMENT OF ELECTRIC UTILITIES
STATEMENTS OF NET ASSETS

	2011	2010
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	$ 55,245,416	$ 52,654,645
Accounts receivable	44,913,210	46,459,450
Less allowance for uncollectibles	(1,038,616)	(1,055,896)
Inventories	32,143,181	33,108,851
Other current assets	47,137	95,457
Total current assets	131,310,328	131,262,507
UTILITY PLANT		
Utility plant in service	1,130,475,426	1,088,040,852
Less accumulated depreciation	(514,436,291)	(486,264,240)
	616,039,135	601,776,612
Construction in progress	21,245,958	29,301,314
Total utility plant, net	637,285,093	631,077,926
OTHER ASSETS		
Asset apportionments		
Cash and equivalents	109,803,202	107,966,682
Accounts receivable	361,375	914,614
Due from other governments	-	307,799
Restricted assets		
Cash and equivalents	15,909,021	9,632,291
Accounts receivable	262,642	-
Due from other governments	1,627,677	1,897,251
Deferred hedge derivative outflows	44,837,448	37,920,271
Other noncurrent assets	7,269,732	7,847,161
Total other assets	180,071,097	166,486,069
Total Assets	948,666,518	928,826,502

See accompanying notes to financial statements

CITY OF LAKELAND, FLORIDA
DEPARTMENT OF ELECTRIC UTILITIES
STATEMENTS OF NET ASSETS (continued)

	September 30	
	2011	2010
LIABILITIES		
CURRENT LIABILITIES, payable from current assets		
Accounts payable	15,710,974	13,059,534
Accrued liabilities	2,544,980	5,523,479
Deferred revenue	477,984	477,984
Due to other funds	137,473	137,473
Deferred regulatory liabilities	1,857,074	1,754,047
Obligation under capital leases	109,985	104,412
Total current liabilities, payable from current assets	20,838,470	21,056,929
OTHER LIABILITIES		
Long-term debt, due beyond twelve months	486,525,655	484,410,056
Accrued liabilities, less current portion	25,945,688	34,553,923
Advances from other funds, less current portion	-	137,473
Obligation under capital leases, less current portion	333,678	443,662
Deferred revenue, less current portion	2,310,258	2,788,243
Deferred liabilities - hedge derivatives	42,734,673	33,648,208
Liabilities payable from apportioned assets		
Accrued liabilities	2,165,167	5,682,804
Current portion of bonds payable	23,632,510	21,992,218
Accrued interest payable	12,135,996	11,934,160
Liabilities payable from restricted assets		
Accounts payable	547,233	1,470,666
Accrued liabilities	26,209	46,809
Deferred revenue	250,000	-
Meter deposits payable	13,190,341	12,802,396
Total other liabilities	609,797,408	609,910,618
Total liabilities	630,635,878	630,967,547
NET ASSETS		
Invested in capital assets, net of related debt	120,301,454	112,706,815
Unrestricted	197,729,186	185,152,140
Total net assets	$ 318,030,640	$ 297,858,955

See accompanying notes to financial statements

CITY OF LAKELAND, FLORIDA
DEPARTMENT OF ELECTRIC UTILITIES
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

	Year ended September 30	
	2011	2010
OPERATING REVENUES		
Sales of energy - retail	$ 317,541,522	$ 337,890,451
Sales of energy and capacity sales - wholesale	15,874,978	10,086,724
Other electric operating revenue	7,465,356	6,238,521
Total operating revenues	340,881,856	354,215,696
OPERATING EXPENSES		
Fuel and purchased power	161,966,709	171,525,680
Energy supply	23,924,605	22,985,301
Energy delivery	22,264,926	21,005,230
Customer service	6,904,619	7,117,895
State tax on electric sales	7,971,034	8,447,732
Administrative and general	18,953,380	20,779,164
Total operating expenses	241,985,273	251,861,002
OPERATING INCOME BEFORE DEPRECIATION	98,896,583	102,354,694
Less depreciation	35,703,714	35,887,506
OPERATING INCOME	63,192,869	66,467,188
NONOPERATING REVENUES (EXPENSES)		
Investment revenue (less $278,153 and $305,115 capitalized in 2011 and 2010, respectively)	7,473,028	5,874,020
Net increase in the fair value of cash equivalents	696,777	936,476
Miscelleous revenue	598,281	801,453
Interest expense and fiscal charges (less $1,514,165 and $653,646 capitalized in 2011 and 2010, respectively)	(24,743,825)	(25,867,501)
Amortization expense	(2,083,151)	(2,550,344)
Plant cost recovered through capital contributions	(9,951,197)	(4,695,036)
Loss on impairment of fixed assets	-	(1,049,692)
TOTAL NONOPERATING REVENUES (EXPENSES)	(28,010,087)	(26,550,624)
INCOME BEFORE CAPITAL CONTRIBUTIONS AND TRANSFERS	35,182,782	39,916,564
CAPITAL CONTRIBUTIONS	9,951,197	4,695,036
TRANSFERS TO OTHER FUNDS	(24,962,294)	(25,398,285)
CHANGE IN NET ASSETS	20,171,685	19,213,315
NET ASSETS, beginning of year	297,858,955	278,645,640
NET ASSETS, end of year	$ 318,030,640	$ 297,858,955

See accompanying notes to financial statements

CITY OF LAKELAND, FLORIDA
DEPARTMENT OF ELECTRIC UTILITIES
STATEMENTS OF CASH FLOWS

	Year ended September 30	
	2011	2010
Cash flows from operating activities:		
Receipts from customers	$ 343,022,084	$ 353,561,403
Payments for interfund services	(10,083,554)	(9,816,220)
Payments to suppliers	(187,944,374)	(194,492,074)
Payments to employees	(39,052,635)	(36,240,147)
Net cash provided by operating activities	105,941,521	113,012,962
Cash flows used in noncapital financing activities:		
Interest paid on Customer Deposits	(652,134)	(704,241)
Operating transfers to other funds	(24,962,294)	(25,398,285)
Cash flows used in noncapital financing activities	(25,614,428)	(26,102,526)
Cash flows used in capital and related financing activities:		
Interest paid on long-term debt issued to finance capital assets	(28,325,670)	(29,570,127)
Proceeds from capital grant programs	7,691,741	609,991
Proceeds from repayment of interfund loans	-	14,470,000
Payments on interfund loans	(137,473)	(137,473)
Proceeds from issuance of long-term debt	16,496,379	197,820,000
Payments on and maturities of long-term debt	(22,096,628)	(226,099,834)
Purchase of capital assets	(51,421,226)	(43,536,105)
Cash flows used in capital and related financing activities:	(77,792,877)	(86,443,548)
Cash flows provided by investing activities:		
Investment revenue	7,473,028	5,874,021
Net increase in the fair value of cash equivalents	696,777	936,476
Cash flows provided by investing activities	8,169,805	6,810,497
Net increase in cash and cash equivalents	10,704,021	7,277,385
Cash and cash equivalents, beginning of year	170,253,618	162,976,233
Cash and cash equivalents, end of year	$ 180,957,639	$ 170,253,618
Adjustments to reconcile operating income to net cash provided by operating activities:		
Operating income	$ 63,192,869	$ 66,467,188
Depreciation	35,703,714	35,887,506
Miscellaneous revenue	598,281	801,453
Decrease (increase) in receivables, net	1,528,962	(1,926,862)
Decrease in inventory	965,670	8,670,100
Decrease in other current assets	48,320	7,275,259
Decrease (Increase) in net pension asset	153,415	(10,186)
(Increase) in deferred hedge outflows	(6,917,177)	(37,920,271)
Increase in deferred regulatory liabilities	103,025	445,881
Increase (decrease) in accounts payable	2,651,440	(3,423,650)
Increase in net other post employment benefit obligation	2,078,088	1,688,890
(Decrease) in deferred revenue	(477,985)	(477,984)
(Decrease) increase in accrued liabilities	(3,161,511)	1,384,200
Increase in deferred hedge inflows	9,086,465	33,648,208
Increase in deposits payable	387,945	503,230
Net cash provided by operating activities	$ 105,941,521	$ 113,012,962

See accompanying notes to financial statements

NOTE A -SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These financial statements present only the financial position, changes in net assets, and cash flows of the City of Lakeland, Department of Electric Utilities (Lakeland Electric) and not of the City as a whole. Lakeland Electric is an enterprise fund that accounts for the City's electric utility operations. These operations are accounted for in a manner similar to private business enterprises with the stated intent that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis are financed or recovered primarily through user charges.

Basis of Accounting:

Lakeland Electric uses the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America (GAAP) as required by the Governmental Accounting Standards Board (GASB). Lakeland Electric has adopted the uniform system of accounts (USOA) prescribed by the Federal Energy Regulatory Commission (FERC) for electric operations, and is substantially in conformity with accounting methods prescribed by the FERC. Lakeland Electric is required to follow the pronouncements of the Financial Accounting Standards Board (FASB) issued through November 30, 1989 that do not conflict with or contradict GASB pronouncements.

Lakeland Electric applies the accounting principles required with respects to “Accounting for the Effects of Certain Types of Regulation”. Lakeland Electric’s rates are designed to recover the cost of providing services, and Lakeland Electric is able to collect those rates from its customers. This guidance requires Lakeland Electric to defer certain expenses and revenues, and to record various regulatory assets and liabilities in accordance with rate actions of the Lakeland City Commission. See Note F.

Cash and Cash Equivalents:

Lakeland Electric has defined Cash and Cash Equivalents to include cash on hand, demand deposits, cash with paying agents, as well as Lakeland Electric’s equity in the city’s pooled cash (see Note C). Additionally, Lakeland Electric’s equity in the City’s internal investment pool (see Note C) is considered to be a cash equivalent since Lakeland Electric can deposit or effectively withdraw cash from the pool at any time without prior notice or penalty. Investments that are categorized as cash equivalents on the Statement of Net Assets are valued at fair value.

Receivables:

Lakeland Electric bills customers monthly on a cyclical basis. An estimate of uncollectible accounts is recognized based upon historical experience. Lakeland Electric has recognized in receivables an estimated amount for services rendered but not yet billed as of September 30, 2011 and 2010, respectively.

Inventories:

Inventories (see Note D) are valued at cost, not in excess of replacement cost, using the weighted average cost method.

Restricted and Apportioned Assets:

Revenue bond ordinances and certain other agreements with parties outside the City require the restriction of certain fund assets for specific purposes such as bond proceeds, which are restricted by revenue bond ordinance to finance certain capital improvements, and meter deposits held on behalf of utility customers. Apportionments do not represent legal restrictions imposed by parties external from the local government and may be rescinded at any time. See Notes G and H.

NOTE A -SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Due to/from Other Funds:

Amounts receivable from or payable to other funds in the City of Lakeland are reflected in the accounts of the fund until liquidated by payment or authorized inter-fund transactions. See Note L.

Operating/Non-operating Revenue:

Revenues that are earned as a result of the business operations of Lakeland Electric are recorded as operating revenues. Interest earnings and other miscellaneous revenues are recorded as non-operating revenues.

Deferred Revenue:

Lakeland Electric records revenue as earned. During August 2009, Lakeland Electric received a $3,823,875 termination fee in a natural gas discount settlement with Florida Gas Utility. Lakeland Electric is amortizing the lump sum settlement as fuel revenue over a period of eight years, which is approximately the length of time that the natural gas discount would have been otherwise maintained. The unamortized long-term portion of the deferred revenue was $2,310,258 as of September 30, 2011.

Contributions in Aid of Construction:

Non-refundable payments received from consumers and developers for extension of electric services, and funds received from developers and customers for assets owned and maintained by Lakeland Electric, are recorded as capital contributions in the period in which they have been received on the Statements of Revenues, Expenses and Changes in Net Assets. For financial reporting purposes, there is a corresponding expense for contributed plant costs in the Statements of Revenues, Expenses and Changes in Net Assets.

Utility Plant:

Lakeland Electric records the acquisition and disposition of assets essentially in accordance with the guidelines of FERC. Utility plant and equipment are recorded at cost. Electric plant does not include cost or other value that has been contributed. These funds are recorded as reductions to gross plant costs and amortized over the life of the related assets. Interest costs on funds used for the construction of utility plant are capitalized as part of the costs of these assets.

Impaired assets are recorded in accordance with GASB 42. No impairment losses occurred during the fiscal year ending September 30, 2011. During the year ending September 30, 2010, an impairment loss in the amount of $1,049,692 was recorded to remove prior years' capital costs associated with the partial implementation of a data warehouse software application.

Routine maintenance and repairs, including additions and improvements of less than $2,500 are charged to operating expense as incurred. Individual equipment items with a cost of $1,000 or more are capitalized. In accordance with accounting requirements of the Federal Energy Regulatory Commission, electric transformers and certain specialty plant replacement components which are critical in nature are classified as utility plant and are depreciated prior to being placed in service. Total depreciation expense as a percentage of depreciable assets was approximately 3.2 percent and 3.3% in 2011 and 2010, respectively. Depreciation is computed using the straight-line method over the estimated useful lives of the assets as follows:

Land improvements	40 years
Buildings	50 years
Utility Plant	25 - 35 years
Improvements, other than buildings	10 - 45 years
Machinery and equipment	5 - 40 years

NOTE A -SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Intangible assets:

In accordance with GASB 51, intangible assets are classified as Utility plant, and are depreciated according to Lakeland Electric's policy.

Amortization:

Bond issue costs and bond discount are amortized over the life of the issue using the straight-line method. Lakeland Electric considered the effective interest method of amortizing bond discounts and determined that no material difference results from the continued use of the straight-line method.

Transfers to/From Other Funds:

Lakeland Electric accounts for subsidy payments to other funds as transfers to other funds in the statement of revenues, expenses and changes in net assets. Lakeland Electric made annual transfers to the City of Lakeland as follows:

	September 30	
	2011	2010
Annual dividend to the City of Lakeland	$ 24,200,000	$ 25,155,347
Transfer to Fleet Management Fund for new vehicles	62,394	53,874
Transfers to other funds	699,900	189,064
	$ 24,962,294	$ 25,398,285

Accumulated Unpaid Vacation and Sick Pay:

The amounts of unpaid vacation and sick leave accumulated by Lakeland Electric employees are accrued as expenses when incurred. Total available sick leave hours are multiplied by the current pay rate to determine the accrued liability. The entire unpaid liability for sick leave is classified as a non-current liability based on Lakeland Electric's benefit accrual policies. Lakeland Electric has separated that portion of the liability for vacation time that is expected to be paid from current assets as a current liability. The amount is included in accrued liabilities (See Note M, Long-Term Debt – Accrued Liabilities).

Derivatives and Interest Rate Swap Agreements:

Derivative instruments are used by Lakeland Electric in conjunction with debt financing and fuel purchases. Changes in fair value of hedges are reported as either deferred inflows (asset) or deferred outflows (liability) in the statement of net assets. See Note T, Derivative and Hedging Activities.

Other Significant Accounting Policies:

Other significant accounting policies are set forth in the financial statements and the notes thereto.

NOTE B – NEW ACCOUNTING PRONOUNCEMENTS

In February 2009, the GASB issued Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definition*, which is effective for the City of Lakeland's fiscal year ending September 30, 2011. Statement No. 54 is not applicable to Lakeland Electric, because it is an enterprise fund of the City of Lakeland

In June 2009, GASB issued Statement No. 59, *Financial Instruments Omnibus*. The statement addresses financial reporting and disclosure requirements for certain financial instruments and external investment pools. The statement is effective for the City of Lakeland's fiscal year ending September 30, 2011. It has been determined that statement No. 59 has no material impact on Lakeland Electric.

NOTE C - CASH, CASH EQUIVALENTS AND INVESTMENTS

Deposits:

All of the City of Lakeland cash accounts have been pooled and all deposits are in a single financial institution and are carried at cost. The deposits are insured or collateralized. Florida Statutes, Chapter 280, sets forth the qualifications and requirements that a financial institution must meet in order to become a qualified public depository. The statute also defines the amount and type of collateral that must be pledged in order to remain qualified. The financial institution in which the City maintains its deposits is a qualified public depository. Refer to the City of Lakeland, Florida comprehensive annual financial report for additional disclosures.

The following is a summary of the key controls which the City of Lakeland utilizes to mitigate investment risk.

Interest rate risk exists when there is a possibility that changes in interest rates could adversely affect an investment's fair value. The City utilizes the "segmented time distribution" method as a measure of interest rate risk.

Credit risk is the risk of loss due to the failure of the security issuer or other counterparty.

Custodial credit risk is the risk that in the event of a bank failure, the City of Lakeland's deposits may not be returned. Florida Statutes require deposits by governmental units in a financial institution be collateralized. The City of Lakeland's policy, in accordance with the Florida Security for Public Deposits Act, requires deposits in a financial institution be collateralized and requires the use of only authorized dealers and institutions, qualified public depositories, who meet the standards as set forth by the State of Florida and the Securities and Exchange Commission's Rule 15c3-1. In the event of a failure of a qualified public depository, the remaining public depositories would be responsible for covering any resulting losses. Accordingly, all amounts reported as deposits are deemed as insured or collateralized with securities held by the entity or its agent in the entity's name. The carrying amount of Lakeland Electric's share of pooled demand and time deposits with financial institutions as of September 30, 2011 was $30,145,029. By comparison, the carrying amount of Lakeland Electric's pooled demand and time deposits in the previous fiscal year was $33,927,786.

The types of investments in which the City of Lakeland may directly invest are governed by several forms of legal and contractual provisions. The City of Lakeland may directly invest in obligations of, or obligations on which the principal of and interest are unconditionally guaranteed by the United States of America, obligations issued or guaranteed by any agency or instrumentality of the United States of America, interest bearing time deposits or repurchase agreements issued by banks, trust companies or national banking associations which are secured by obligations of or guaranteed by the United States of America or its agencies or instrumentalities. The City of Lakeland also may invest monies with the Florida State Board of Administration or other investments which at the time are legal investments under the laws of the State of Florida. Additionally, the various funds of the City have combined some of their resources into an internal investment pool in order to maximize investment earnings. The pool is comprised of money market funds, time deposits, notes, bonds, amounts invested with the Florida State Board of Administration, other securities, and accrued interest.

Lakeland Electric has an equity interest in the City's internal investment pool. There were no violations of legal or contractual provision for deposits and investments during the year. Information regarding credit risk categories for pooled investments is disclosed in the comprehensive annual financial report for the City. Credit risk is the risk of loss due to the failure of the security issuer or other counterparty. The City of Lakeland's investment policy minimizes credit risk by limiting investments in securities that have higher credit risks, pre-qualifying the financial institutions, brokers/dealers, intermediaries, and advisors with which the City will do business, and diversifying the investment portfolio so that potential losses on individual securities will be minimized.

NOTE C - CASH, CASH EQUIVALENTS AND INVESTMENTS (CONTINUED)

As of September 30, 2011, Lakeland Electric's share of the City's Investment Pool debt security investments had the following credit quality ratings:

S&P Rating:

	Cost	%	Market	%
AAA	$ 4,966,769	3.53%	$ 4,968,190	3.42%
AA+ to AA-	31,240,332	22.20%	33,021,863	22.74%
A+ to A-	25,784,808	18.32%	26,855,903	18.50%
BBB+ to BBB-	15,678,462	11.14%	15,567,594	10.72%
Below BB-	492,318	0.35%	471,452	0.32%
Below BB-	1,002,174	0.71%	894,516	0.62%
NR	61,555,281	43.74%	63,408,092	43.67%
	$ 140,720,144	100.00%	$ 145,187,610	100.00%

Moody's Rating:

Aaa	$ 10,493,584	7.46%	$ 10,586,014	7.29%
Aa1 to Aa3	16,479,571	11.71%	17,074,929	11.76%
A1 to A3	34,617,553	24.60%	36,924,756	25.43%
Baa1 to Baa3	21,499,869	15.28%	21,312,069	14.68%
Ba1 to Ba3	-	0.00%	-	0.00%
Below Ba3	1,002,174	0.71%	894,516	0.62%
NR	56,627,393	40.24%	58,395,326	40.22%
	$ 140,720,144	100.00%	$ 145,187,610	100.00%

Concentration of Credit Risk:

The City of Lakeland limits investments to avoid over concentration in securities from a specific issuer or business sector (excluding US Treasury securities) and continuously invests a portion of the portfolio in readily available funds such as local government investment pools, money market funds or overnight repurchase agreements.

The City of Lakeland's overall investment policy concentration limits and actual concentration limits in investment types as of September 30, 2011 are as follows:

Type of Security (Market)	Maximum % of Total	% of Total
US Government Obligations	100%	13.61%
Federal Agency & instrumentality Obligations	100%	33.76%
Local Government Investment Pools	100%	0.27%
Certificates of Deposits	25%	0.62%
Collateralized Repurchase Agreements	15%	0.99%
Other Investment Pools (rated "A" or better)	10%	2.00%
Mutual Funds	0%	0.00%
High Grade Corporate Debt	15%	14.04%
Investment Grade Obligations of State and Local Govts	15%	30.90%
Money Market Mutal Funds	N/A	3.81%
		100.00%

NOTE C - CASH, CASH EQUIVALENTS AND INVESTMENTS (CONTINUED)

As of September 30, 2011 and 2010 the fair value of the total investment pool and Lakeland Electric's share of the pool was as follows:

	Reported Amount Fair Value
As of September 30, 2011:	
Total Investment Pool	$ 392,193,649
Lakeland Electric's Share of the Investment Pool	$ 145,187,610
As of September 30, 2010:	
Total Investment Pool	$ 373,368,979
Lakeland Electric's Share of the Investment Pool	$ 136,324,306

Cash, cash equivalents and investments are included in the following captions in the accompanying Statement of Net Assets:

	September 30	
	2011	2010
Current assets:		
Cash and cash equivalents	$ 55,245,416	$ 52,654,645
Asset Apportionments:		
Cash and cash equivalents	109,803,202	107,966,682
Restricted assets:		
Cash and cash equivalents	15,909,021	9,632,291
	$ 180,957,639	$ 170,253,618

NOTE D - INVENTORIES

The major classes of inventory consist of the following:

	September 30	
	2011	2010
Fuel oil	$ 9,500,094	$ 9,972,389
Coal	5,982,718	6,520,242
Spare parts	16,660,369	16,616,220
	$ 32,143,181	$ 33,108,851

NOTE E - OTHER CURRENT ASSETS

Lakeland Electric's other current assets balance consists of prepaid expenses, representing payments made in advance for certain goods and services. Lakeland Electric prepaid expenses were $47,137 and $95,469 in 2011 and 2010, respectively.

NOTE F – DEFERRED REGULATORY ACCOUNTS

Accounting guidance for the effects of certain types of regulation requires the recognition of revenues provided, either before or after the costs are incurred, as assets or liabilities. Lakeland Electric's deferred regulatory assets/liabilities represents the amount due from (or payable to) retail customers for those costs which are not recovered through Lakeland Electric's base retail rate structure.

The following table summarizes the regulatory account balances as of September 30, 2011 and September 30, 2010:

	September 30	
	2011	2010
Under-recovery of fuel charges	$ 1,419,193	$ 1,152,512
Under-recovery of environmental compliance charges	42,086	308,910
Under-recovery of future energy conservation charges	395,795	292,625
Total net deferred regulatory liabilities	$ 1,857,074	$ 1,754,047

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NOTE G - RESTRICTED ASSETS

Bond ordinances and contractual agreements require the restriction of certain assets for specific purposes. Bond Proceeds from series 2010 revenue and refunding bonds, issued on October 19, 2010, have provided Lakeland Electric's share of the Smart Grid project, which is 42.33 percent funded by the Department of Energy (DOE). The customer deposits balance represents cash held from electric customers, which is completely offset by a liability payable from restricted assets. Guarantees from customers, other than cash, are not recorded as assets or liabilities on Lakeland Electric's Statements of Net Assets. Lakeland Electric is participating in a three-year energy efficiency revolving loan program, which was began in December 2009, and is funded by a DOE block grant.

Lakeland Electric's restricted assets and restricted liabilities due within twelve months, as of September 30, 2011 and 2010 consist of the following:

	Bond Proceeds	Customer Deposits	Block Grant	Total Restricted
September 30, 2011				
Cash and cash equivalents	$ 2,744,066	$ 13,214,241	$ (49,286)	$ 15,909,021
Accounts receivable	20,114	-	242,528	262,642
Due from other governments	1,567,981	-	59,696	1,627,677
Restricted assets	$ 4,332,161	$ 13,214,241	$ 252,938	$ 17,799,340
Accounts payable	$ 546,624	$ -	$ 609	$ 547,233
Accrued expenses	2,310	-	-	2,310
Accrued interest payable	-	23,899	-	23,899
Deferred revenue	-	-	250,000	250,000
Meter deposits payable	-	13,190,341	-	13,190,341
Restriced liabilities, due within twelve months	$ 548,934	$ 13,214,240	$ 250,609	$ 14,013,783

	Bond Proceeds	Customer Deposits	Grants	Total Restricted
September 30, 2010				
Cash and cash equivalents	$ -	$ 12,881,448	$ (3,249,157)	$ 9,632,291
Due from other governments	-	-	1,897,251	1,897,251
Restricted assets	$ -	$ 12,881,448	$ (1,351,906)	$ 11,529,542
Accounts payable	$ -	$ 44,220	$ 1,426,446	$ 1,470,666
Accrued expenses	-	-	11,977	11,977
Accrued interest payable	-	34,832	-	34,832
Meter deposits payable	-	12,802,396	-	12,802,396
Restriced liabilities, due within twelve months	$ -	$ 12,881,448	$ 1,438,423	$ 14,319,871

NOTE H – ASSET APPORTIONMENTS

The City of Lakeland and Lakeland Electric have established long range plans concerning the utility. As part of the plan to achieve its objectives, the City Commission has set aside certain assets that will be used to fund its plans for future expansion. Debt service funds are also set aside monthly and apportioned for the purpose of paying current principal and interest requirements.

Asset apportionments and related liabilities of Lakeland Electric as of September 30, 2011 and 2010 consist of the following:

September 30, 2011:	Debt Service Funds	Capital Expansion	Emergency Repair	Total Designated
Cash and cash equivalents	$ 28,682,865	$ 31,662,001	$ 13,689,832	$ 74,034,698
Cash with paying agent/trustee	35,768,504	-	-	35,768,504
Accounts receivable	-	361,375	-	361,375
Due from other governments	-	-	-	-
Asset apportionments	$ 64,451,369	$ 32,023,376	$ 13,689,832	$ 110,164,577
Current portion of revenue bonds payable	$ 23,632,510	$ -	$ -	$ 23,632,510
Accounts payable	1,418,765	558,568	-	1,977,333
Accrued expenses	-	187,834	-	187,834
Accrued interest payable	12,135,996	-	-	12,135,996
Liabilities payable from apportioned assets, due within twelve months	$ 37,187,271	$ 746,402	$ -	$ 37,933,673

September 30, 2010:	Debt Service Funds	Capital Expansion	Emergency Repair	Total Designated
Cash and cash equivalents	$ 29,334,883	$ 32,145,145	$ 12,560,252	$ 74,040,280
Cash with paying agent/trustee	33,926,402	-	-	33,926,402
Accounts receivable	-	914,614	-	914,614
Due from other governments	-	307,799	-	307,799
Asset apportionments	$ 63,261,285	$ 33,367,558	$ 12,560,252	$ 109,189,095
Current portion of revenue bonds payable	$ 21,992,218	$ -	$ -	$ 21,992,218
Accounts payable	1,423,949	3,501,333	-	4,925,282
Accrued expenses	-	757,522	-	757,522
Accrued interest payable	11,934,160	-	-	11,934,160
Liabilities payable from apportioned assets, due within twelve months	$ 35,350,327	$ 4,258,855	$ -	$ 39,609,182

NOTE I - OTHER NONCURRENT ASSETS

Other noncurrent assets of Lakeland Electric as of September 30, 2011 and 2010 consist of the following:

	September 30	
	2011	2010
Unamortized bond issue costs	$ 3,418,854	$ 3,842,868
Net pension obligation	3,850,878	4,004,293
	$ 7,269,732	$ 7,847,161

NOTE J - UTILITY PLANT

Utility plant in service consists of the following:

Fiscal year 2011:	September 30, 2010	Additions	Deletions	September 30, 2011
Non-depreciable assets:				
Land	$ 15,882,890	$ -	$ -	$ 15,882,890
Construction in process	29,301,314	38,064,712	46,120,068	21,245,958
	45,184,204	38,064,712	46,120,068	37,128,848
Depreciable assets:				
Buildings	24,067,151	-	-	24,067,151
Machinery and equipment	31,591,380	1,906,065	4,445,667	29,051,778
Equipment under capital leases	671,161	-	-	671,161
Electric plants in service:				
Electric delivery	368,225,494	17,957,756	6,284,433	379,898,817
Electric supply	647,602,776	37,248,409	3,947,556	680,903,629
Total plant assets	1,117,342,166	95,176,942	60,797,724	1,151,721,384
Less Accumulated Depreciation:				
Buildings	9,643,376	913,323	2,422	10,554,277
Machinery and equipment	20,783,053	1,733,225	3,044,513	19,471,765
Equipment under capital leases	139,829	111,862	-	251,691
Electric plants in service:				
Electric delivery	126,810,567	9,710,060	4,086,266	132,434,361
Electric supply	328,887,415	23,235,244	398,462	351,724,197
Total plant assets	486,264,240	35,703,714	7,531,663	514,436,291
Total Utility plant net of accumulated depreciation	$ 631,077,926	$ 59,473,228	$ 53,266,061	$ 637,285,093

NOTE J - UTILITY PLANT (CONTINUED)

Fiscal year 2010:	September 30, 2009	Additions	Deletions	September 30, 2010
Non-depreciable assets:				
Land	$ 15,630,708	$ 255,682	$ 3,500	$ 15,882,890
Construction in process	20,896,436	23,452,859	15,047,981	29,301,314
	36,527,144	23,708,541	15,051,481	45,184,204
Depreciable assets:				
Buildings	23,835,350	231,801	-	24,067,151
Machinery and equipment	38,331,719	2,049,868	8,790,207	31,591,380
Equipment under capital leases	671,161	-	-	671,161
Electric plants in service:				
Electric Delivery	356,773,471	15,262,508	3,810,485	368,225,494
Electric Supply	644,238,590	27,647,204	24,283,018	647,602,776
Total plant assets	1,100,377,435	68,899,922	51,935,191	1,117,342,166
Less Accumulated Depreciation:				
Buildings	9,069,508	603,454	29,586	9,643,376
Machinery and equipment	26,465,020	3,407,005	9,088,972	20,783,053
Equipment under capital leases	27,966	111,863	-	139,829
Electric plants in service:				
Electric Delivery	118,753,894	9,333,272	1,276,599	126,810,567
Electric Supply	326,873,837	22,431,912	20,418,334	328,887,415
Total plant assets	481,190,225	35,887,506	30,813,491	486,264,240
Total Utility plant net of accumulated depreciation	$ 619,187,210	$ 33,012,416	$ 21,121,700	$ 631,077,926

Allowance for Funds Used During Construction:

In accordance with GASB guidance regarding capitalized interest, Lakeland Electric has adopted the policy of capitalizing net interest costs on funds used for the construction of fixed assets. As required by the provisions of the related accounting pronouncements, interest charges on borrowed funds and interest earnings on borrowed funds have been capitalized as follows:

	September 30	
	2011	2010
Net capitalized interest		
Interest expense capitalized	$ 1,514,165	$ 653,646
Interest revenue capitalized on bond proceeds	(278,153)	(305,115)
	$ 1,236,012	$ 348,531
Interest cost was reduced by amounts capitalized as follows:		
Total interest paid	26,257,990	26,521,147
Less capitalized interest expense	(1,514,165)	(653,646)
	$ 24,743,825	$ 25,867,501

NOTE K - UTILITY PLANT PARTICIPATION AGREEMENT

On April 4, 1978, the City entered into a fifty-year participation agreement with the Orlando Utilities Commission (OUC). Under the terms of this agreement, the City of Lakeland has a 60 percent interest and OUC a 40 percent interest in McIntosh Unit #3, a 364-megawatt coal-fired steam generating unit. The Orlando Utilities Commission constructed, at its expense, a 230 KV transmission line to deliver its share of the output to its service area.

The City of Lakeland issued revenue bonds to cover a portion of its initial investment in the plant. OUC also issued revenue bonds to cover a portion of its investment in the plant and the cost of its 230 KV transmission line. Each participant is solely responsible for its debt issued.

The City has operational control of this project and accounts for its undivided ownership interest based on its pro- rata share of the project's construction costs and operating expenses. Capital costs related to McIntosh Unit #3 during fiscal year 2011, most of which were related to renewal and replacement projects, were $2,608,947 with an OUC share of $1,043,579. Shared operating expenses for the fiscal years ending September 30, 2011 and 2010, were as follows:

Fiscal year 2011:

	City Share	OUC Share	Total
McIntosh unit #3 fuel expense	$ 45,144,813	$ 30,096,542	$ 75,241,356
McIntosh unit #3 direct operating & maintenance expenses	9,278,793	6,185,862	15,464,654
Other shared operating and administrative expenses	3,128,550	2,085,700	5,214,250
	$ 57,552,156	$ 38,368,104	$ 95,920,260

Fiscal year 2010:

	City Share	OUC Share	Total
McIntosh unit #3 fuel expense	$ 38,749,972	$ 25,833,315	$ 64,583,287
McIntosh unit #3 direct operating & maintenance expenses	6,783,517	4,522,344	11,305,861
Other shared operating and administrative expenses	4,896,852	3,264,568	8,161,420
	$ 50,430,341	$ 33,620,227	$ 84,050,568

No separate financial statements are issued for the utility participation agreement.

NOTE L - DUE TO OTHER FUNDS

Lakeland Electric's liabilities include an advance from the Department of Information Technology (DOIT) for Lakeland Electric's share of the City of Lakeland's radio system. A $137,473 current portion is included on the Statement of Net Assets for both 2011 and 2010. A noncurrent portion of $137,473 is included in fiscal year 2010, but not in 2011, because the liability will be fully extinguished in 2012.

NOTE M - LONG-TERM DEBT

Accrued liabilities are classified on the Statement of Net Assets as follows:

	September 30		
	2011	2010	2009
Current:			
Accrued taxes payable	$ 758,722	$ 750,376	$ 792,170
Compensated absences	1,786,258	4,773,103	3,166,372
	$ 2,544,980	$ 5,523,479	$ 3,958,542
Accrued liabilities, less current portion:			
Compensated absences	$ 4,593,324	$ 4,776,335	$ 4,957,074
Other post employment benefits	7,974,773	6,285,883	4,596,993
Accrued capital appreciation interest payable	12,988,393	15,811,705	17,891,143
Advance bond refunding receipts	-	7,680,000	7,680,000
	$ 25,556,490	$ 34,553,923	$ 35,125,210

Long term debt, due beyond twelve months consists of the following:

	September 30		
	2011	2010	2009
Revenue bonds payable, less current portion	$ 487,559,961	$ 498,407,472	$ 518,994,690
Less unamortized loss on refunding	(24,995,034)	(13,966,587)	(14,089,581)
Plus (less) unamortized bond discount (net of premium)	23,960,728	(30,829)	(58,744)
	$ 486,525,655	$ 484,410,056	$ 504,846,365

NOTE N - REVENUE BONDS

Lakeland Electric revenue bonds payable as of September 30, 2011:

	Interest Rate %	Final Maturity	September 30, 2010	Additions	Deletions	September 30, 2011
Series 1999A	3.05% to 5.00%	10-01-2036	$ 184,729,689	$ -	$ 162,822,218	$ 21,907,471
Series 1999B	5.3% to 6.55%	10-01-2014	15,310,000	-	-	15,310,000
Series 1999C	5.3% to 6.55%	10-01-2012	48,285,000	-	14,865,000	33,420,000
Series 2001B	5.00% to 5.50%	10-01-2018	30,000,000	-	30,000,000	-
Series 2006	4.00% to 5.00%	10-01-2036	42,850,000	-	820,000	42,030,000
Series 2009	Variable	10-01-2037	199,225,000	-	-	199,225,000
Series 2010	4.00% to 5.25%	10-01-2036	-	199,300,000	-	199,300,000
			$ 520,399,689	$ 199,300,000	$ 208,507,218	$ 511,192,471
			(21,992,217)			(23,632,510)
			$ 498,407,472			$ 487,559,961

Series 2010 Energy System Revenue and Refunding Bonds were issued on October 19, 2010 refunding all of the the Series 2001B Bonds and a portion of the 1999A Bonds.

NOTE N - REVENUE BONDS (CONTINUED)

The following is a schedule of the debt service requirements, excluding the current portion for outstanding revenue bonds and excluding the impact of interest swaps on variable rate bonds as of September 30, 2011:

	Series 1999A Sr.		Series 1999B Sr.		Series 1999C Sr.	
Fiscal Year(s)	Principal	Interest	Principal	Interest	Principal	Interest
2012	$ 5,626,267	$ 4,988,732	$ -	$ 926,255	$ 17,240,000	$ 1,043,020
2013	5,308,195	5,311,805	6,815,000	926,255	-	-
2014	5,020,499	5,599,501	8,495,000	513,948	-	-
2015	-	-	-	-	-	-
2016	-	-	-	-	-	-
2017-2021	-	-	-	-	-	-
2022-2026	-	-	-	-	-	-
2027-2031	-	-	-	-	-	-
2032-2036	-	-	-	-	-	-
2037-2041	-	-	-	-	-	-
	$ 15,954,961	$ 15,900,038	$ 15,310,000	$ 2,366,458	$ 17,240,000	$ 1,043,020

	Series 2006 Sr.		Series 2009		Series 2010	
Fiscal Year(s)	Principal	Interest	Principal	Interest	Principal	Interest
2012	$ 885,000	$ 1,997,694	$ 8,360,000	$ 2,351,636	$ 705,000	$ 9,931,150
2013	930,000	1,953,444	2,475,000	2,279,501	7,260,000	9,902,950
2014	975,000	1,906,944	2,550,000	2,249,942	6,285,000	9,612,550
2015	1,020,000	1,867,944	2,635,000	2,219,487	15,510,000	9,298,300
2016	1,055,000	1,827,144	2,715,000	2,188,017	16,280,000	8,522,800
2017-2021	6,085,000	8,331,144	24,304,000	10,377,583	58,515,000	30,811,750
2022-2026	7,755,000	6,661,063	44,433,000	8,305,114	28,155,000	21,649,463
2027-2031	9,895,000	4,518,563	40,802,000	5,591,545	28,775,000	14,444,063
2032-2036	12,575,000	1,847,750	51,186,000	3,087,767	37,170,000	6,053,513
2037-2041	-	-	19,765,000	236,053	-	-
	$ 41,175,000	$ 30,911,688	$ 199,225,000	$ 38,886,647	$ 198,655,000	$ 120,226,538

	TOTAL		
Fiscal Year(s)	Principal	Interest	Total
2012	$ 32,816,267	$ 21,238,487	$ 54,054,754
2013	22,788,195	20,373,955	43,162,149
2014	23,325,499	19,882,884	43,208,383
2015	19,165,000	13,385,731	32,550,731
2016	20,050,000	12,537,961	32,587,961
2017-2021	88,904,000	49,520,477	138,424,477
2022-2026	80,343,000	36,615,639	116,958,639
2027-2031	79,472,000	24,554,170	104,026,170
2032-2036	100,931,000	10,989,030	111,920,030
2037-2041	19,765,000	236,053	20,001,053
	$ 487,559,961	$ 209,334,388	$ 696,894,348

NOTE N - REVENUE BONDS (CONTINUED)

The following is a schedule of combined senior and junior lien revenue bond coverage for fiscal year 2011 and the previous five years per the current senior lien ordinance:

Fiscal Year	Net Revenues Available	Debt Service Principal	Debt Service Interest	Total Debt Service	Operations from Operations	Bond Ordinance Coverage
2011	$ 108,053,867	$ 23,632,510	$ 27,423,459	$ 51,055,969	2.11	2.93
2010	109,966,644	21,992,217	27,974,283	49,966,500	2.20	3.03
2009	106,015,433	28,180,719	28,309,330	56,490,049	1.88	2.58
2008	95,251,355	18,760,000	25,661,622	44,421,622	2.14	2.96
2007	76,058,287	17,300,000	24,885,697	42,185,697	1.80	2.58
2006	68,237,133	575,000	23,093,002	23,668,002	2.88	4.01

Bond debt coverage for the year ended September 30, 2011 was calculated as follows:

Charges for services	$ 340,881,856	
Investment and other income	8,768,086	
Total revenue		$ 349,649,942
Less cost of operations		(241,985,273)
Net revenues from operations available for debt service		$ 107,664,669
Fund balance (as defined by bond ordinance):		
Cash and equivalents	$ 55,245,416	
Asset apportionments	110,164,577	
Accounts receivable (net of uncollectables)	43,874,594	
	$ 209,284,587	
20% of fund balance		41,856,917
Net available revenues plus 20% of fund balance		$ 149,521,586
Debt service requirement:		
Interest on bond debt		$ 25,579,280
Capital appreciation		1,844,179
Principal		23,632,510
Total		$ 51,055,969
Bond coverage		2.93
Bond coverage from operations		2.11

NOTE N - REVENUE BONDS (CONTINUED)

All of the outstanding revenue bonds are secured by a first lien on and pledge of the net revenues of the Electric system. As of September 30, 2011, the City is in compliance with all required covenants of the bond ordinances, including compliance with federal arbitrage regulations.

Electric Revenue Refunding Bonds, Series 1999 A, B, & C:

In April 1999, the City issued the Electric Revenue Refunding Bonds, Series 1999A in the amount of $195,635,409 to provide funds to refund all of the City's outstanding Electric & Water Revenue Bonds, Series 1989, the Electric & Water Revenue Bonds, Series 1996, and the Electric & Water Revenue Bonds, Series 1996B, and to pay certain costs and expenses related to the issuance of the Series 1999A Bonds. These bonds will mature on October 1, 2036. Principal payments are payable October 1 of each year and interest payments are payable October 1 and April 1 of each year. The majority of these bonds were refunded in October of 2010. The remaining principal and interest requirement on these bonds aggregate to $42,475,000.

In April 1999, the City issued the Electric Revenue Refunding Bonds, Series 1999B in the amount of $144,305,000 in exchange for the City's outstanding Electric & Water Revenue Bonds (Junior Subordinate Lien), Refunding Series 1996. The bonds will mature on October 1, 2014. Interest is payable October 1 and April 1 of each year. The remaining interest requirement for these bonds is $2,829,585.

In April 1999, the City issued the Energy System Refunding Revenue Bonds, Series 1999C in the amount of $64,525,000 in exchange for the City's outstanding Electric & Water Revenue Bonds (Junior Subordinate Lien), Refunding Series 1996B. The bonds will mature on October 1, 2012. Principal payments are payable October 1 of each year and interest payments are payable October 1 and April 1 of each year. The remaining interest requirement for these bonds is $2,053,975.

Energy System Revenue Bonds, Series 2001B:

In May 2001, the City issued the Energy System Revenue Bonds, Series 2001B in the amount of $30,000,000 to finance certain capital improvements for the City's electric power system and to pay certain costs and expenses related to the issuance of the Series 2001B Bonds. These bonds will mature on October 1, 2018. Interest is payable October 1 and April 1 of each year. All of these bonds were refunded in October of 2010

Energy System Revenue and Refunding Bonds, Series 2006:

In August 2006, the City issued the Energy System Revenue and Refunding Bonds, Series 2006 in the amount of $44,870,000 to finance certain capital improvements for the electric power system of the City, to refund, on a current basis, a portion of the City's outstanding Energy System Refunding Revenue Bonds, Series 1999B, and to pay certain costs and expenses related to the issuance of the Bonds. The bonds mature on October 1, 2036. Principal payments are payable October 1 of each year and interest payments are payable October 1 and April 1 of each year. The remaining interest requirement for these bonds is $31,927,634.

Variable Rate Energy System Refunding Bonds, Series 2009:

In October 2009, the City issued the Energy System Variable Rate Refunding Bonds, Series 2009 in the amount of $199,225,000 to refund on a current basis all of the City's outstanding Variable Rate Energy System Revenue and Refunding Bonds, Series 2008A and Variable Rate Energy System Revenue and Refunding Bonds, Series 2008B and to pay certain costs and expenses related to the issuance of the Bonds. The bonds mature on October 1, 2014. Principal payments are payable October 1 2012 and 2014 interest payments are payable October 1 and April 1 of each year. The remaining interest requirement for these bonds is $36,631,080, assuming that the bonds are refinanced based on amortization schedules associated with the interest rate swaps that convert these obligations to a synthetic fixed rate.

NOTE N - REVENUE BONDS (CONTINUED)

Energy System Refunding and Revenue Bonds, Series 2010:

In October 2010, the City issued the Energy System Revenue and Refunding Bonds, Series 2010 in the amount of $199,300,000 to (1) finance certain capital improvements to the electric power system of the City, (2) to refund on a current basis, a portion of the City's outstanding Electric and Water Refunding Revenue Bonds, Series 1999A and to refund on an advance basis, all of the City's outstanding Energy System Revenue Bonds, Series 2001B, (3) to pay costs associated with the termination of a conditional bond warrant agreement, and (4) to pay certain costs and expenses related to the issuance of the Bonds. The bonds mature on October 1, 2036. Principal payments are payable October 1 of each year and interest payments are payable October 1 and April 1 of each year. The remaining interest requirement for these bonds is $125,205,013.

Interest Rate Swaps:

As a means to partially hedge the variable rate risk exposure associated with the issuance of the $90,000,000 2001A Energy System Variable Rate Revenue Bonds in April of 2001, the City entered into a basis swap in May of 2001. Under the swap, the city pays CitiGroup Financial Products Inc. (the counterparty) a payment equal to $90,000,000 (the notional amount) times an interest rate equal to the SIFMA Municipal Bond Index. In return, the counterparty pays the City an amount equal the notional amount times 74.125% of the monthly USD-LIBOR-BBA rate. To the extent the relationship between SIFMA and LIBOR approximates a marginal tax rate of more than 25.9 percent; the net borrowing cost on the underlying 2001 debt issue will be reduced as a result of this swap. The notional amount remains unchanged over the term of the swap, which ends May 1, 2021. Settlement payments are made quarterly. As of September 30, 2011, the swap had a negative fair value of $2,885,506 developed using the Market Quotation method. The negative fair value may be countered by reductions in total net interest payments on the underlying debt resulting from the swap. As of September 30, 2011, the City was not exposed to credit risk because the swap had a negative fair value. The City is exposed to basis risk to the extent the relationship of SIFMA to LIBOR increases to greater than 74.1%. For the year ended September 30, 2011, the average ratio of SIFMA to LIBOR was 94.6% - which resulted in net settlement payments to the counterparty for the year in the aggregate amount of $41,764. This is the equivalent of less than 5 basis points in additional net interest cost on the notional amount of outstanding debt. Since inception of this swap in 2001, the City has been the recipient of $275,278 in net payments from the counterparty. The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay, bankruptcy, or a rating downgrade by Moody's or S&P issued to either the City or the counterparty.

In order to reduce borrowing costs when compared to the market rates paid by issuers of fixed–rate bonds, the City entered into an interest rate swap in connection with the issuance of the Energy System Variable Rate Refunding Revenue Bonds Series 2003, which were sold in January 2003. Under the swap, the City pays CitiGroup Financial Products Inc. (the counterparty) a payment equal to $47,860,000 (the notional amount) times a fixed interest rate of 3.74 percent. In return, the counterparty pays the City an amount equal the notional amount times 67 percent of the monthly USD-LIBOR-BBA. To the extent the relationship between SIFMA and LIBOR approximates a marginal tax rate of more than 33 percent; the synthetically fixed rate paid on underlying bonds is equal to 3.74 percent plus the cost of liquidity, remarketing fees, or any spread above SIFMA paid on the underlying variable rate issue. The notional amount of the swap will corresponds with the maturity schedule on the Series 2003 bonds. Settlement payments on this swap are made monthly. As of September 30, 2011, the swap had a negative fair value of $17,944,515 developed using the Market Quotation method. The negative fair value may be countered by reductions in total net interest payments on the underlying debt resulting from the swap. As of September 30, 2011, the City was not exposed to credit risk because the swap had a negative fair value. The City is exposed to basis risk to the extent the relationship of SIFMA to LIBOR increases to greater than 67 percent. For the year ended September 30, 2011, the average ratio of SIFMA to LIBOR was 94.6%, which resulted in a combination of net settlement payments to the counterparty for the year and interest payments on the underlying variable rate debt in the aggregate amount of $438,717 above the targeted rate of 3.74 percent. This is equivalent to 92 basis points in additional net interest cost on the notional amount of outstanding debt.

NOTE N - REVENUE BONDS (CONTINUED)

Interest Rate Swaps (continued):

The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. An additional termination event also occurs in the event of a rating downgrade by Moody's or S&P issued to either the City or the counterparty.

In order to reduce borrowing costs when compared to the market rates paid by issuers of fixed–rate bonds, the City entered into an interest rate swap in connection with the issuance of the Energy System Variable Rate Refunding Revenue Bonds Series 2006A, which were sold in August of 2006. Under the swap, the City pays the counterparty a payment equal to $90,000,000 (the notional amount) times a fixed interest rate of 4.283 percent (annualized). In return, the counterparty pays the City an amount equal the notional amount times the weighted average SIFMA Municipal Bond Index. This exchange of cash flows occurs quarterly. This swap transaction was split between two counterparties; Goldman Sachs in the amount of $60,000,000 and CitiGroup Financial Products Inc in the amount of $30,000,000.

The combined notional amount of the swaps decreases over time based on the bond maturity schedule associated with at portion of the million of Energy System Refunding Revenues Bonds Series 2006A allocated to refunding the Energy System Variable Rate Revenue Bonds, Series 2001A. As of September 30, 2011, the two swaps had a combined negative fair value of $26,170,021 developed using the Market Quotation method. The negative fair value may be countered by reductions in future net interest payments on the underlying debt resulting from the swap. As of September 30, 2011, the City was not exposed to credit risk because the swap had a negative fair value. The City was not exposed to basis risk, because the underlying variable rate debt payments are directly tied to the SIFMA index. The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. An additional termination event also occurs in the event of a rating downgrade by Moody's or S&P issued to either the City or the counterparty.

In order to reduce borrowing costs when compared to the market rates paid by issuers of fixed–rate bonds, the City entered into an interest rate swap in connection with the issuance of the Energy System Variable Rate Refunding Revenue Bonds Series 2008A and 2008B, which were sold in July of 2008. Under the swap, the City pays Goldman Sachs (the counterparty) a payment equal to $62,140,000 (the notional amount) times a fixed interest rate of 3.163 percent. In return, the counterparty pays the City an amount equal the notional amount times 67 percent of the monthly USD-LIBOR-BBA. To the extent the relationship between SIFMA and LIBOR approximates a marginal tax rate of more than 33 percent; the synthetically fixed rate paid on underlying bonds is equal to 3.163 percent plus the cost of liquidity and remarketing fees on the underlying variable rate issue.

The notional amount of the swap corresponds with the maturity schedule on the new money component of the Series 2008A bonds. Settlement payments on this swap are made monthly. As of September 30, 2011, the swap had a negative fair value of $8,879,299 developed using the Market Quotation method. The negative fair value may be countered by reductions in total net interest payments on the underlying debt resulting from the swap. As of September 30, 2011, the City was not exposed to credit risk because the swap had a negative fair value. The City is exposed to basis risk to the extent the relationship of SIFMA to LIBOR increases to greater than 67 percent. For the year ended September 30, 2010, the average ratio of SIFMA to LIBOR was 94.6% - - which resulted in a combination of net settlement payments to the counterparty for the year and interest payments on the underlying variable rate debt in the aggregate amount of $453,697 above the targeted rate of 3.163 percent. This is the equivalent of 73 basis points in additional net interest cost on the notional amount of outstanding debt. The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay and bankruptcy. An additional termination event also occurs in the event of a rating downgrade by Moody's or S&P issued to either the City or the counterparty.

NOTE N - REVENUE BONDS (CONTINUED)

Interest Rate Swaps (continued):

In August of 2006, the City retired the both the Energy System Variable Rate Revenue Bonds, Series 2001A and the System Variable Rate Refunding Revenue Bonds Series 2003. These two bond issue were retired by the Energy System Refunding Revenues Bonds Series 2006A, issued in August of 2006. The 2006A bonds were themselves retired from the proceeds of two repurchase agreements entered into between the City of Lakeland and Goldman Sachs in February of 2008. Those repurchase agreements were retired from a portion of the proceeds of the Variable Rate Energy System Revenue and Refunding Revenues Bonds Series 2008A and 2008B issued in August of 2008. The 2008A and 2008B bonds were retired by the Variable Rate Energy System Refunding Bonds, Series 2009. The replacement bonds take the form of Variable Rate Bonds which are reset weekly based on the published SIFMA rate plus a defined spread averaging 92.43 basis points. The defined spread effectively replaces the credit support and marketing fees associated with traditional variable rate date structures. The City elected to retain the financial risks and benefits of the aforementioned interest rate swaps dated May 2001 in the notional amount of $90,000,000; dated November 2002 in the notional amount of $47,860,000; dated March 2006 in the amount of $90,000,000; and dated July 2008 in the notional amount of $62,140,000 and integrate those swaps into the refunding bond issue. Accordingly, the annual maturity dates and maturity amounts for the refunding and refunded bonds are essentially identical.

As of September 30, 2011, future debt service requirements on the variable-rate debt and net swap payments based on the terms in each of the underlying swaps appear as follows. These calculations are based on an average SIFMA rate of 0.16 percent as of September 30, 2011; and effective LIBOR interest rate of 0.239 percent as of September 30, 2011. As rates vary, variable rate bond interest payments and net swap payments will vary.

Note that the Series 2009 variable rate bonds mature in two large tranches on October 1, 2012 and October 1, 2014. It is the City's intention to refinance those two bond maturities with replacement debt. For purposes of preparing the following schedule, it is assumed that the replacement bonds will retain the same maturity schedules that have been incorporated into the underlying swap transactions.

Fiscal Year Ending September 30,	Variable-Rate Bonds		Interest Rate Swaps, Net	Total
	Principal	Interest		
2012	2,320,000	2,172,255	7,152,721	11,644,976
2013	6,040,000	2,160,235	7,035,544	15,235,779
2014	2,475,000	2,160,235	6,962,506	11,597,741
2015	2,550,000	2,087,667	6,887,067	11,524,734
2016	2,635,000	2,000,813	6,809,225	11,445,038
2017-2021	19,044,000	9,525,181	32,694,540	61,263,721
2022-2026	42,842,000	7,772,585	26,989,693	77,604,278
2027-2031	43,224,000	5,310,974	18,608,388	67,143,362
2032-2036	48,605,000	3,066,937	10,436,532	62,108,469
2037-2038	29,490,000	374,199	1,234,922	31,099,121
	$ 199,225,000	$ 36,631,081	$ 124,811,138	$ 360,667,219

NOTE N - REVENUE BONDS (CONTINUED)

Interest Rate Swaps (continued):

As a means to reduce borrowing costs on a portion of the Electric and Water Refunding Revenue Bonds Series 1999A the City entered into an interest rate swap in June 2004. Under the swap, the City pays CitiGroup Financial Products Inc. (the counterparty) a payment equal to $159,000,000 million (the notional amount) times an interest rate equal to the SIFMA Municipal Bond index. In return, the counterparty pays the City an amount equal the notional amount times an interest rate equal to 67 percent of the three-month USD-LIBOR-BBA index, plus a spread of .046%. The notional amount of the swap was to be equal the amount of the outstanding amount of that component of the underlying issue consisting of term bonds which mature serially from October 2004 thru October 2036. Settlement payments are made semi-annually. As of September 30, 2011, the swap had a negative fair value of $1,494,590 developed using the Market Quotation method. The negative fair value may be countered by reductions in total net interest payments on the underlying debt resulting from the swap. As of September 30, 2011, the City was not exposed to credit risk because the swap had a negative fair value. The City is exposed to basis risk to the extent the relationship of SIFMA to LIBOR increases to greater than 67 percent plus the quoted spread of .046%. For the year ended September 30, 2011, the average ratio of SIFMA to LIBOR was 94.6% - which resulted in net settlement payments to the City for the year in the aggregate amount of $694,001. This is the equivalent of 44 basis points in lower net interest cost on the notional amount of outstanding debt. The derivative contract uses the International Swap Dealers Association Master Agreement, which includes standard termination events, such as failure to pay, bankruptcy, or a rating downgrade by Moody's or S&P issued to either the City or the counterparty.

In October of 2010, the City refunded the majority of the Electric and Water Refunding Revenue Bonds Series 1999A with the Energy System Revenue and Refunding Bonds, Series 2010. The City elected to retain the financial risks and benefits of the aforementioned interest rate swaps dated June 2004 in the notional amount of $156,515,000 and integrate that swaps into the refunding bond issue.

The underlying terms of these derivative contracts require that either party post collateral to secure the other parties risk that occur when the market valuation of the swaps exceeds certain thresh-holds. Because the market value of these swaps is significantly in the favor of the City's two counterparties, the City has posted collateral in the aggregate amount of $19,137,686 as of September 30, 2011. The collateral consists of a combination of treasury securities and approximately $6.5 million in cash. All investment income associated with the investments that comprise this collateral accrues back to the City.

The fair value of Lakeland Electric's interest rate swaps as of September 30, 2011 was $57,373,931. Also see Note T, Derivative and Hedging Activities.

Refunding Transactions:

In October of 2010, the City issued Energy System Revenue and Refunding Bonds, Series 2010 having a principal amount of $199,300,000. The proceeds were used to retire that portion of the Energy Electric and Water Refunding Revenue Bonds Series 1999A that mature from October 1, 2015 through 2036 and to advance refund all of the Energy System Revenue Bonds Series 2001B. The aggregate amount of the principal retired between these two issues was $186,515,000. In addition, the replacement bond issue included $15,900,000 to finance a portion of the cost of installing a smart metering system for use within the service territory of Lakeland Electric. The transaction resulted in a loss on refunding of $13,165,887 which is to be amortized over the life of the replacement bonds. All of that loss was the result of the early write-off of an equal amount of unamortized bond issue costs and unamortized loss on refunding from the series 1999A and 2001B bonds. The incremental cost of the transaction was approximately $2.1 million in issue costs associated with the replacement debt, which will be amortized over the lifetime of the replacement bonds.

NOTE O – CAPITAL LEASE

During July 2009 Lakeland Electric entered into a contract with Caterpillar Financial Services for the lease of a coal loader at McIntosh Unit 3 for a period of 72 months. Lakeland Electric's 60 percent share of the present value of the future minimum lease payments at the inception of the contract, using the implicit interest rate of 5.21 percent per the agreement, was $671,176. The following is a schedule of Lakeland Electric's portion of the obligation under capital lease, excluding the short-term portion, through the expiration of the contract in 2015:

Fiscal Year	Lease Obligation
2013	115,854
2014	122,039
2015	95,785
	$ 333,678

NOTE P - EMPLOYEE RETIREMENT SYSTEM

The City of Lakeland maintains and administers an Employee Pension and Retirement System Plan which is a single employer, defined benefit pension plan. It covers substantially all full-time, regular employees of the City. The Plan is funded from contributions provided by both the employer and employees. The plan is subject to periodic review by an independent actuary to determine the required funding level upon which the City bases the annual contributions.

Contributions:

Employee contributions are recorded in the period in which they are payroll deducted from plan participants. Contributions from the City are made and recorded at the same time. As of September 30, 2011 the contribution rates were 8.5 percent for the employee portion and 17.04 percent for the City portion. The contribution rates for the City's portion increase to 11 percent for employees and 19.54 percent effective February 15, 2012. Lakeland Electric's contributions to the City of Lakeland's pension fund totaled $5,813,905 and $5,873,637 during fiscal years 2011 and 2010, respectively.

Pension Benefits:

Plan participants as of September 30, 2003 may retire, without penalty, after attaining age 60 and contributing 10 or more years to this plan. The monthly benefit is determined by multiplying the average monthly salary by a service and benefit factor. The average monthly salary is computed using the average of the highest total earnings over a consecutive period of 36 months. The service factor is based on the length of continuous service determined as follows: 3 percent per year for the first 25 years of service plus 1 percent per year for all service above 25 years.

Plan participants who enter the plan on or after October 1, 2003 with 10 years or more of service may retire at normal retirement age of 62. The retirement income for an employee who retires on the normal retirement date will equal 2 percent of the highest total earnings over a consecutive period of 60 months multiplied times the number of years of credit service up to 10 years, 3 percent of the same average earnings for the next 20 years of credited service, and 1 percent per year of the same average for each year of service in excess of 30 years.

The Plan includes a provision for an annual across-the-board increase in the benefit paid to all retirees if certain conditions occur. The amount of the annual increase, if any, is a factor of the investment performance of the Plan for the preceding year considered in relation to the actuarially assumed rate of investment return.

NOTE P - EMPLOYEE RETIREMENT SYSTEM (CONTINUED)

Termination Benefits:

If a member employee is terminated, either voluntarily or involuntarily, the following benefits are payable: If the employee has less than 10 years of credited service, the employee shall be entitled to a refund of amounts contributed by the employee. If the employee has ten or more years credited service, the employee will be entitled to the accrued monthly retirement benefit to commence on normal retirement date, provided the employee's contributions are left in the fund. A terminated employee may also elect an early retirement benefit as described above. The authority for establishing or amending the benefit provisions and contribution provisions is contained in City ordinances.

For the following information, refer to the City of Lakeland, Florida, Employees' Pension and Retirement System stand-alone financial statements which can be obtained by contacting the City of Lakeland, Finance Department, City Hall, 228 S. Massachusetts Ave., Lakeland, FL 33801-5086:

Annual pension cost
Dollar amount of contributions
Date of Actuarial valuation
Identification of actuarial method and assumptions
Required supplemental information

NOTE Q - BUSINESS SEGMENT

Lakeland Electric is a department of the City of Lakeland, operating in only one business segment, that of providing electric service. The City of Lakeland has been generating power and providing electric service since 1904. Its service area is primarily the City of Lakeland and the immediate area surrounding the City.

NOTE R - POST-EMPLOYMENT BENEFITS

In addition to the pension benefits described in Note P, the City Commission has agreed to offer subsidized post-employment health care benefits to former employees who are receiving retirement benefits from the City.

On May 1, 1989, the City Commission agreed to subsidize 50 percent of the cost of Part A of Medicare insurance coverage purchased by any person receiving retirement benefits from the City of Lakeland. This agreement can be rescinded by the City at any time. To date, there have been no participants in this program.

On September 18, 1989, the City Commission agreed to subsidize the cost of health insurance coverage offered to any person receiving retirement benefits from the City of Lakeland. Effective September 22, 2002 the retirees' health insurance premium subsidy of 50 percent was reduced as follows: in fiscal year 2004 to 45 percent, in fiscal year 2005 to 40 percent, and in subsequent fiscal years to 35 percent. Effective October 1, 2002, the health insurance premium subsidy is based on years of service. Lakeland Electric's annual cost of this benefit was $515,609 and $506,986 during fiscal years 2011 and 2010, respectively, funded on a pay-as-you-go basis.

Effective January 1, 2004 any employee who wishes to have his/her spouse and dependents insured will be required to have them on the plan for one year prior to retirement. Should a participant at any time elect not to purchase coverage from the City-sponsored plan, all eligibility for future participation in that plan, including rights to the subsidy, are terminated. The subsidy program can be terminated by the City at any time. During the fiscal year ended September 30, 2009, there were more than 200 retired employees of Lakeland Electric participating in the program.

NOTE R - POST-EMPLOYMENT BENEFITS (CONTINUED)

In accordance with the GASB's prescribed accounting treatment for *Other Post Employment Benefits (OPEB*), the City has measured the long-term liability and associated required contributions necessary to finance the explicit subsidy provided to retired employees as a percentage of annual insurance premiums, and an implicit subsidy associated with the state mandate that health insurance premiums for retired employee equal the amount charged to active employees, without regard to the increased health insurance costs associated with retired employees based on claims experience. The City has elected to fund the explicit subsidy within a formal Trust established to accumulate and invest assets necessary to pay for the accumulated liability. The City has not established a trust to finance cost of the implicit subsidy.

The Net OPEB obligation represents the excess of the annual required contribution necessary to amortize both the explicit and implicit subsidies on an actuarially sound basis over the amount actually funded on a pay-as-you go basis for the City of Lakeland. The portion of the liability attributable to the operations of Lakeland Electric was $8,363,971 as of September 30, 2011, and $6,285,883 as of September 30, 2010.

NOTE S - DEFERRED COMPENSATION PROGRAM

The City has a Deferred Compensation Program pursuant to Chapter 75-295, as amended by Chapter 76-279, Florida Statutes. In accordance with the Deferred Compensation Program, the City may, by contract and/or collective bargaining agreement, agree with any City employee to defer up to 25 percent of an employee's gross salary (not to exceed $13,000 in one year).

Under the terms of the Deferred Compensation program, the City may purchase, at the direction of the employee, fixed or variable life insurance, annuity contracts or mutual fund shares for the purpose of "informally" funding the deferred compensation agreements of the employee. The investments will, at all times, remain solely the property of the employee, held in trust until the employee is eligible to draw the amounts contributed. The compensation deferred under the program is not included in employees' taxable income until such amounts are actually received by employees under the terms of the program.

NOTE T – DERIVATIVE AND HEDGING ACTIVITIES

Accounting for Derivatives and Hedging Activities:

The City follows GASB 53, Accounting and Financial Reporting for Derivative Instruments. Changes in fair value of hedges are reported as either deferred inflows (asset) or deferred outflows (liability) in the statement of net assets. For accounting purposes, in order to qualify as a hedge, the relationship between the derivative and the underlying asset must result in a hedge that is "effective" in mitigating risk. If the hedge transaction is considered "ineffective" the valuation of the instrument is considered investment income or loss on the Statements of Changes of Revenues, Expenses and in Net Assets. GASB 53 outlines five methods for evaluating hedge effectiveness:

- Critical Terms
- Synthetic Instrument
- Dollar Offset
- Regression Analysis
- Other Quantitative Methods

NOTE T – DERIVATIVE AND HEDGING ACTIVITIES (CONTINUED)

Accounting for Derivatives and Hedging Activities (continued):

For purposes of performing effectiveness testing, Lakeland Electric can use any or all of the evaluation methods and is not limited to using the same method from period to period. Therefore, if the result of any one prescribed evaluation method indicates the hedge is ineffective, Lakeland Electric may apply another method to verify effectiveness. In addition, the calculations for effectiveness may be based on either a life to date period or be limited to the immediately preceding annual accounting period.

Fuel Hedges:

To achieve its goals of minimizing volatility in both cash flow and fuel rates to the ratepayers, Lakeland Electric was hedged at various volumes for a rolling 30 month forward period with emphasis on upside protection thru the purchase of swaps. Due to a depressed natural gas market, the costs of the program became significant. To control the cost of the program, Lakeland Electric's Utility Committee implemented changes to the policy in March 2010. When a swap is placed, at or near the same time, a put option will be placed to provide opportunity to participate in a downward market. Swaps should be placed at no more than a $1/MMBtu above market and option premiums at $0.50/MMBTU resulting in a maximum cost of $1.50/MMBTU. Each quarter, when a fuel rate change is proposed, the next 12 months of forecasted volumes will be approximately 63 percent hedged as follows:

1st quarter will be 100% hedged
2nd quarter will be 75% hedged
3rd quarter will be 50% hedged
4th quarter will be 25% hedged

Fuel related derivative transactions are executed in accordance with the fuel hedging policies established by Lakeland Electric's Energy Risk Management Oversight Committee. The primary objective of these policies is to minimize exposure to natural gas price volatility for cash flow and fuel rate stabilization purposes. The Committee has a defined organizational structure and responsibilities, which include approving all brokerage relationships, counterparty credit worthiness, specific fuel volumes and financial limits in addition to overall policy compliance. Acquisition of these hedge transactions are managed by The Energy Authority (TEA) based on a contractual relationship created in March 2007. TEA performs the front and back office functions associated with such trades, in accordance with overall hedging policies developed jointly by TEA and the aforementioned oversight committee of Lakeland Electric.

The recording of fuel derivatives, when appropriate, is included on the Statement of Net Assets as either an asset or liability measured at fair value. Related gains and/or losses are deferred and recognized in the specific period in which the derivative is settled and included as part of Fuel and Purchased Power costs in the Statement of Revenues, Expenses and Changes in Net Assets. The premiums associated with the purchase of options are expensed upon expiration of the option. Premiums associated with unexpired options are embedded in the valuation table displayed later in this note. The valuation of market changes for contracts entered into within Lakeland Electric's Risk Management Program resulted in a net increase of $14,097,730 to the cost of fuel during the fiscal year ended September 30, 2011.

Lakeland Electric's natural gas swaps and put options have been evaluated using the regression method. According to this method, all of Lakeland Electric's derivatives were considered to be effective. Consequently, the R-Squared relationship between the derivative based on the NYMEX index as related to physical natural gas prices based on purchased gas from Florida Gas Transmission Zones 1, 2 and 3 was 0.8 or higher with a slope between -0.8 and -1.25. With GASB 53 compliance, the open swaps and options valuation of $12,672,870 includes mark to market of the swaps and both intrinsic and extrinsic mark to market of the options.

NOTE T – DERIVATIVE AND HEDGING ACTIVITIES (CONTINUED)

Derivate Instruments:

Lakeland Electric uses Over-the-Counter (OTC) swaps, put options, swing-swaps and fixed price firm physical purchases of natural gas as tools to stabilize the cost of natural gas that will be needed by the utility in the future. Any gain or loss of the value of these derivatives are ultimately rolled into the price of natural gas burned, offsetting the volatility in the price of that fuel. As of September 2011, Lakeland Electric had the following options, swaps and physical contracts outstanding in the following amounts, covered fiscal year 2011 and beyond:

Fiscal Year	Options	Swaps	Physicals	Market-to- Market Value at 9/30/11
2012	10,870,000	11,790,000	-	(8,951,470)
2013	1,490,000	2,410,000	-	(3,338,102)
2014		155,000	-	(383,298)
	12,360,000	14,355,000	-	$ (12,672,870)

Note N, Revenue Bonds, refers to the fair value of interest swap derivatives, which are evaluated for effectiveness using the same criteria required for fuel hedge derivatives under GASB 53. The fair value of all of Lakeland Electric's derivatives as of September 30, 2011 was as follows:

Deferred hedge assets:		Deferred hedge liabilities:	
Interest rate swaps	$ 57,373,931	Interest rate swaps	$ 57,373,931
Fuel hedges	(12,536,483)	Fuel hedges	(14,639,258)
	$ 44,837,448		$ 42,734,673

NOTE U - LITIGATION

Various suits and claims arising in the ordinary course of operations are pending against Lakeland Electric. While the ultimate effect of such litigation cannot be ascertained at this time, in the opinion of counsel for Lakeland Electric, the liabilities which may arise from such actions would not result in losses which would materially affect the financial position of Lakeland Electric or the results of their operations.

NOTE V - COMMITMENTS AND CONTINGENCIES

Self-Insurance Program:

The City of Lakeland has established a self-insurance fund for worker's compensation, general liability, public official's liability, airport liability, automobile liability, and health insurance. The purpose of this fund is to account for the cost of claims and management fees incurred in conjunction with self-insurance programs. The City makes contributions to the fund based on actuarially computed funding levels. The funding level for Lakeland Electric is determined actuarially based on Lakeland Electric's share of the total City budget, number of vehicles owned and rented, number of employees and payroll. Contributions in excess of these funding levels are accounted for as residual equity transfers in the paying fund. All claims pending at September 30, 2011, have been accrued in the financial statements of the Self-Insurance Fund. An estimated liability for incurred-but-not-reported claims also has been accrued in the financial statements of the Self-Insurance Fund. This program provides coverage up to a maximum of $400,000 per employee for worker's compensation claims. The City purchases commercial insurance for claims in excess of this amount up to $1,000,000 per employee. The program provides coverage of up to a maximum of $150,000 per employee for health insurance claims. The City purchases commercial insurance for claims in excess of this amount up to $1,000,000 per employee. Refer to the City of Lakeland, Florida comprehensive annual financial report for additional disclosures.

NOTE V - COMMITMENTS AND CONTINGENCIES (CONTINUED)

Contractual Commitments:

Lakeland Electric has contracts for the purchase and delivery of coal requiring the purchase of a minimum number of tons per year.

Lakeland Electric also has contracts for the supply and transportation of natural gas requiring the purchase and transportation of a minimum and a maximum number of cubic feet of natural gas per year.

Lakeland Electric has contracts for the purchase/sale and delivery of electric energy setting a maximum number of megawatts available for purchase.

Lakeland Electric has a long-term service agreement with Siemens/Westinghouse to provide labor, parts, and materials to cover all planned outages for McIntosh Unit 5, a 360 megawatt combined cycle gas turbine unit. In May 2010 Lakeland Electric reached a settlement with Siemens/Westinghouse regarding performance issues associated with McIntosh Unit 5. During fiscal year 2011, a milestone payment of $4,996,000 was made under the revised payment schedule, of which $4,656,000 was capitalized. The new agreement is scheduled to run until between 2019 and 2024, depending on future outages. Expected future payments, based on a twelve-month outage assumption, are as follows:

Fiscal Year	Operating	Capital	Total
2012	340,000	7,233,170	7,573,170
2013	340,000	7,443,050	7,783,050
2014	340,000	8,119,070	8,459,070
2015	340,000	8,341,190	8,681,190
2016-2019	1,360,000	54,724,371	56,084,371
	$ 2,720,000	$ 85,860,851	$ 88,580,851

Lakeland Electric had active construction projects as of September 30, 2011. Commitments for construction contracts and other capital outlay as of September 30, 2011 are as follows:

Smart grid project	$ 8,879,507
McInosth unit 3 renewal and replacement projects	1,637,405
Other energy supply projects	557,113
Energy delivery projects	1,917,451
Parker Street warehouse complex improvement	503,523
Miscellansous equipment and other capital outlay	180,531
	$ 13,675,530

Encumbrances:

In addition to the commitments for capital projects, Lakeland Electric had other outstanding purchase orders in the amount of $129,349,464 as of September 30, 2011, of which $123,658,934 represents contracts for the procurement and transportation of fuel and purchased power.

It is management's opinion that Lakeland Electric is in compliance with the requirements of all the aforementioned contractual commitments.

LAKELAND CITY COMMISSION

KEITH MERRITT
COMMISSIONER
NORTHEAST DISTRICT

JUSTIN TROLLER
COMMISSIONER
AT LARGE

DON SELVAGE
COMMISSIONER
SOUTHWEST DISTRICT

PHILLIP WALKER
COMMISSIONER
NORTHWEST DISTRICT

EDIE YATES
COMMISSIONER
SOUTHEAST DISTRICT

GOW FIELDS
MAYOR

HOWARD WIGGS
COMMISSIONER
AT LARGE

LAKELAND ELECTRIC EXECUTIVE TEAM

JIM STANFIELD

GENERAL MANAGER

FARZIE SHELTON

ASSISTANT GENERAL MANAGER
TECHNICAL SUPPORT

TONY CANDALES

ASSISTANT GENERAL MANAGER
PRODUCTION

DAVID KUS

ASSISTANT GENERAL MANAGER
CUSTOMER SERVICE

ALAN SHAFFER

ASSISTANT GENERAL MANAGER
DELIVERY

BETSY LIVINGSTON

DIRECTOR OF TRAINING AND
WORKFORCE DEVELOPMENT

LAKELAND ELECTRIC

www.lakelandelectric.com