



City of Hamilton, Ohio – Gas System

Financial Statements

Years Ended December 31, 2014 and 2013

With Independent Auditor's Report



Dave Yost • Auditor of State

Members of Council
City of Hamilton
345 High Street
Hamilton, Ohio 45011

We have reviewed the *Independent Auditors' Report* of the City of Hamilton – Gas System, Butler County, prepared by Clark, Schaefer, Hackett & Co., for the audit period January 1, 2014 through December 31, 2014. Based upon this review, we have accepted these reports in lieu of the audit required by Section 117.11, Revised Code. The Auditor of State did not audit the accompanying financial statements and, accordingly, we are unable to express, and do not express an opinion on them.

Our review was made in reference to the applicable sections of legislative criteria, as reflected by the Ohio Constitution, and the Revised Code, policies, procedures and guidelines of the Auditor of State, regulations and grant requirements. The City of Hamilton - Gas System is responsible for compliance with these laws and regulations.

A handwritten signature in black ink that reads "Dave Yost".

Dave Yost
Auditor of State

August 11, 2015

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INDEPENDENT AUDITORS' REPORT

To the Honorable Mayor and Members of Council
City of Hamilton, Ohio:

Report on the Financial Statements

We have audited the accompanying financial statements of the City of Hamilton, Ohio - Gas System, an enterprise fund of the City of Hamilton, Ohio (the Gas System), as of and for the years ended December 31, 2014 and 2013 and the related notes to the financial statements, as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

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Opinion

In our opinion, the financial statements referred to previously present fairly, in all material respects, the financial position of the City of Hamilton, Ohio - Gas System of as of December 31, 2014 and 2013, and the changes in financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As described in Note 1, the financial statements present only the Gas System and do not purport to, and do not present fairly the financial position of the City of Hamilton, Ohio as of December 31, 2014 and 2013, and the changes in its financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters*Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Clark, Schaefer, Hackett & Co.

Cincinnati, Ohio
June 15, 2015

City of Hamilton, Ohio

Gas System

Management's Discussion and Analysis
For the Years Ended December 31, 2014 and 2013
Unaudited

The discussion and analysis of the City of Hamilton, Ohio's Gas System's financial performance provide an overall review of that system's financial activities for the years ended December 31, 2014 and 2013. While the intent of this discussion and analysis is to look at the system's financial performance, readers should also review the Statements of Net Position, Revenues, Expenses and Changes in Net Position, and Cash Flows to enhance their understanding of the system's fiscal performance.

Financial Highlights

Key highlights for 2014 and 2013 are as follows:

- ❑ The assets and deferred outflow of resources of the Hamilton Gas System exceeded its liabilities at the close of 2014 and 2013, respectively, by \$38,065,271 and \$39,045,116 (net position). Of these amounts, \$3,685,381 and \$7,195,195 (unrestricted net position) in those years can be used to meet the system's ongoing obligations to customers and creditors.
- ❑ The system's total net position decreased by \$979,845 between 2014 and 2013, representing a 2.5% decrease.
- ❑ In 2014, the Gas System's total long-term debt, net of premiums and discounts, decreased by \$1,373,520.

Gas System Summary

The City has owned and operated a natural gas utility system since 1890. It is currently the largest municipal gas distribution operation in Ohio and serves approximately 23,460 customers located in the City and the immediate environs through approximately 275 miles of pipe. The City purchases natural gas from a supplier, then resells the gas to residential and general service (commercial and industrial) customers. The City also provides distribution delivery service to customers who have contracted with either the City or a natural gas supplier.

The Gas System provides full service (acquisition of gas supply, transportation of the gas supply to the City's interconnections and distribution of gas supply from the City's interconnections to the customer meter) and distribution delivery service (distribution delivery of the gas arranged for by, or on behalf of, the customer from the City's interconnections to the customer's meter.) Currently, the Gas System provides full service to residential and general service customers.

There are no franchise service territories for natural gas utilities in Ohio and the City is not prohibited from providing gas service in areas outside its corporate limits. Under the Ohio Constitution, however, the City's gas utility sales outside the corporate limits may not exceed 50% of the total service supplied within the City's corporate limits. Currently, less than 1% of the City's total gas sales are to customers located outside the City's corporate limits.

City of Hamilton, Ohio

Gas System

Management's Discussion and Analysis
For the Years Ended December 31, 2014 and 2013
Unaudited

The City is a participant, with other AMP communities in the AMP Fremont Energy Center (AFEC). The City is entitled to 34.5 MW of capacity from AFEC. Additionally, the City began utilizing its buying power through the Muni-Gas Program, in 2013, to serve as a gas supply intermediary for the City's allocation of gas at AFEC. The City passes along 50% of the savings from the Muni-Gas Discount to AFEC and retains the other 50% for Hamilton Gas (94.4%) and Electric (5.6%) Systems, creating an additional income stream for the Gas System, while providing a cost savings for the Electric System. In 2014, the Gas System sold 987,137 Dths to AFEC, via The Energy Authority, totaling \$4.675 million, or approximately \$4.74/Dth. These sales to AFEC netted approximately \$148,000 for the Gas System.

This annual report consists only of the Statement of Net Position, the Statement of Revenues, Expenses and Changes in Net Position, and the Statement of Cash Flows as well as Notes to the Financial Statements for the City of Hamilton, Ohio's Gas System for the years ended December 31, 2014 and 2013.

Reporting Hamilton's Gas System (Whole and Significant Fund)

The financial statements contained within this report include the City of Hamilton, Ohio's Gas System *only*. Readers desiring to view city-wide financial statements, as well as the impact that the Gas System has on the City's overall financial position and operating results, should refer to the City's Basic Financial Statements appearing in the Comprehensive Annual Financial Report for 2014 and 2013. The City of Hamilton's Gas System is reported as a business-type, enterprise fund and is considered a major fund for purposes of individual fund reporting. Payments made from the Gas Fund are restricted to Gas System purposes by municipal ordinance, Ohio Revised Code and indentures issued pursuant to long-term financing.

In the Statement of Net Position and the Statement of Revenues, Expenses and Changes in Net Position, the view of the system looks at all financial transactions of the Gas Fund and asks the question, "How did we do financially during 2014 and 2013?" These statements provide answers to that question. The statements include all assets, deferred outflow of resources, and liabilities of the System using the accrual basis of accounting similar to the accounting used by private sector companies. This basis of accounting considers all of the current year's revenues and expenses regardless of when the cash is received or paid. These two statements report the System's net position and the changes in the net positions. The change in net position is important because it tells the reader whether, for the System, the financial position of the City has improved or diminished. However, in evaluating this position, non-financial information including the condition of capital assets will also need to be evaluated. The Notes to the Gas System's Financial Statements provide additional information that is essential to a full understanding of the data provided.

The System provides services that have a charge based upon the amount of usage. The City's Gas System charges fees to recoup the cost of the entire operation of the Gas System as well as all capital expenses associated with these facilities.

City of Hamilton, Ohio

Gas System

Management's Discussion and Analysis
For the Years Ended December 31, 2014 and 2013
Unaudited

Financial Analysis

As noted earlier, net position may serve over time as a useful indicator of financial position. In the case of the Gas Fund, assets and deferred outflow of resources exceeded liabilities by \$38,065,271 as of December 31, 2014. By far the largest portion of the net position of the Gas System reflect its investment in capital assets (e.g. land, buildings, improvements, construction in progress, machinery and equipment) less any related debt used to acquire those assets that is still outstanding. The ratios of net investment in capital assets to total net position are as follows: 81.35% for 2014, 72.97% for 2013, and 67.85% for 2012. The System employs these assets in the delivery of natural gas to customers; consequently, these assets are not readily available for future spending. The System's investment in its capital assets is reported net of related debt and the resources needed to repay these debts must be provided from other sources, primarily the revenues of the System, since the capital assets themselves cannot be used to liquidate the liabilities.

Table 1 provides a summary of the Gas System's Statement of Net Position for the Years Ended December 31, 2014, 2013 and 2012:

	2014	2013	2012
Current and other assets	\$10,587,656	\$13,996,271	\$15,334,254
Capital assets	36,843,815	35,700,148	35,127,923
Total assets	47,431,471	49,696,419	50,462,177
Deferred outflow of resources	20,883	61,690	122,465
Long-term liabilities	4,673,075	6,140,167	7,447,904
Other liabilities	4,714,008	4,572,826	3,964,243
Total liabilities	9,387,083	10,712,993	11,412,147
Net investment in capital assets	30,969,361	28,492,981	26,577,513
Restricted	3,410,529	3,356,940	3,356,889
Unrestricted	3,685,381	7,195,195	9,238,093
Total net position	\$38,065,271	\$39,045,116	\$39,172,495

As of December 31, 2014 and 2013, the Gas System was able to report positive balances in net position of \$38,065,271 and \$39,045,116, respectively. In 2014, 2013 and 2012, the Gas System reported decreases in net position of \$979,845, \$127,379, and \$238,508, respectively. For the year ended December 31, 2014, there was an operating loss of \$1,446,791. For the years ended December 31, 2013 and 2012, there was operating income of \$266,817 and \$225,580, respectively. Net operating loss of \$1,446,791 decreased \$1,713,608 from 2014 to 2013. Unusually cold temperatures contributed to high demand, resulting in the increases in revenue as well as the costs for the purchase of gas. Net non-operating expenses of \$239,812 decreased by \$154,384, primarily due to a decrease in interest and fiscal charges, as the City continues to make its scheduled debt service payments, and an increase in investment earnings due to certificates of deposit, with a five-year term, maturing in 2014.

City of Hamilton, Ohio

Gas System

Management's Discussion and Analysis
For the Years Ended December 31, 2014 and 2013
Unaudited

Statements of Revenues, Expenses and Changes in Net Position

	2014	2013	2012
Operating revenues	\$29,369,479	\$24,742,117	\$16,574,138
Operating expenses:			
Purchased gas	22,756,500	16,943,459	8,898,738
Depreciation	1,915,763	1,878,725	1,913,431
Other operating expenses	6,144,007	5,653,116	5,536,389
Total operating expenses	<u>30,816,270</u>	<u>24,475,300</u>	<u>16,348,558</u>
Operating income (loss)	(1,446,791)	266,817	225,580
Non-Operating revenues (expenses)			
Interest and fiscal charges	(323,258)	(396,818)	(467,625)
Loss on disposal of capital assets	(36,027)	(1,326)	(34,106)
Other non-operating revenues	119,473	3,948	37,643
Total non-operating revenues (expenses)	<u>(239,812)</u>	<u>(394,196)</u>	<u>(464,088)</u>
Capital Contributions	706,758	-	-
Change in net position	(979,845)	(127,379)	(238,508)
Beginning net position	<u>39,045,116</u>	<u>39,172,495</u>	<u>39,411,003</u>
Ending net position	<u>\$38,065,271</u>	<u>\$39,045,116</u>	<u>\$39,172,495</u>

Capital Assets and Debt Administration

Capital Assets: The City's net investment in capital assets of the Gas System as of December 31, 2014, 2013 and 2012 amounted to \$31.0 million, \$28.5 million, and \$26.6 million, respectively, (net of accumulated depreciation and related debt). This investment in capital assets includes land, buildings, improvements, construction in progress, and machinery and equipment.

Note 5 (Capital Assets) provide Gas System capital asset activity during 2014 and 2013.

Debt Administration: At the end of 2014, the City had two outstanding long-term revenue bond issues, the 2003 Gas System Revenue Refunding Bonds totaling \$1,420,000 and the 2009 Gas System Revenue Bonds totaling \$4,500,000.

See Note 6 for a discussion of outstanding Gas System bonds and related activity.

City of Hamilton, Ohio

Gas System

Management's Discussion and Analysis
For the Years Ended December 31, 2014 and 2013
Unaudited

Economic Factors and Future Trends

The City's Gas System is continually monitoring the cost of natural gas and employs a structured hedging plan to mitigate price fluctuations to its customers. The cost of natural gas is highly volatile and the City is required by both ordinance and indentures to pass through these gas costs to its customers via the gas cost recovery charge (GCR). The GCR was \$0/MCF for January 2014, increased to \$1.5/MCF for February through October 2014 and decreased to \$1.0/MCF for November and December 2014. The overall number of customers has remained relatively steady while, like most gas systems, the usage per residential customer has continued to slowly decline as a result of improved efficiency of appliances.

In September 2011, City Council adopted an ordinance, creating the Natural Gas Residential Service Line Maintenance (RSLM) Program and Rider C for the Gas System. The RSLM and Rider C charges apply only to the City's residential gas accounts. The RSLM and funds collected through Rider C are earmarked for two separate and distinct activities: the replacement of Design A (field-assembled risers), in compliance with a Public Utilities Commission of Ohio (PUCO) Statewide order, and the assumption of the maintenance responsibility of gas service lines to residential customers by the City. The riser replacement portion of the RSLM is scheduled to be a five-year program, with a corresponding five-year collection period through Rider C. For 2014, the riser replacement portion of the RSLM resulted in a monthly charge to the City's residential customers of \$1.02 per month. The charge, through Rider C, for the residential gas service line normal maintenance and replacement portion of the RSLM, resulted in a monthly service charge of \$0.93 per residential customer. The total impact of the RSLM in 2014 was \$1.95 per month for all residential gas customers of the City.

Natural gas prices have stabilized recently due to extraction of shale gas and reduced demand from recessionary pressures. The City continues to monitor potential threats to supply and maintains its disciplined hedging program. The City's Gas System has continued its strong financial performance into 2014. The City maintains an A1 bond rating with a stable outlook for its Gas System and for both its 2003 Gas System Revenue Refunding Bonds and its 2009 Gas System Revenue Bonds.

Requests for Information

This financial report is designed to provide our citizens, customers, taxpayers, creditors, investors and elected officials with an overview of the City of Hamilton, Ohio's Gas System's finances and to show accountability for the money the system receives. If you have any questions about this report or need additional information, contact the City of Hamilton Finance Department, 345 High Street, Hamilton, Ohio 45011, (513) 785-7170, or visit the City website at www.hamilton-city.org.

**CITY OF HAMILTON, OHIO – GAS SYSTEM
STATEMENTS OF NET POSITION
DECEMBER 31, 2014 AND 2013**

	<u>2014</u>	<u>2013</u>
ASSETS		
Current assets:		
Cash and investments	\$ 2,722,092	6,769,125
Accounts receivable (less allowance for uncollectible accounts of \$2,468,663 and \$2,375,958, respectively)	4,154,387	3,579,387
Interest receivable	3,960	4,426
Inventory of supplies at cost	165,839	168,480
Prepaid expenses	<u>130,849</u>	<u>117,913</u>
Total current assets	<u>7,177,127</u>	<u>10,639,331</u>
Restricted assets:		
Cash and investments	<u>3,410,529</u>	<u>3,356,940</u>
Capital assets:		
Property, plant and equipment	72,151,642	69,646,648
Construction in progress	5,232,627	4,777,854
Accumulated depreciation	<u>(40,540,454)</u>	<u>(38,724,354)</u>
Total capital assets	<u>36,843,815</u>	<u>35,700,148</u>
Total assets	<u>47,431,471</u>	<u>49,696,419</u>
DEFERRED OUTFLOW OF RESOURCES		
Deferred charge on debt refunding	<u>20,883</u>	<u>61,690</u>
LIABILITIES		
Current liabilities:		
Accounts payable	2,264,661	2,242,068
Accrued wages and benefits	99,165	92,798
Intergovernmental payable	19,761	20,054
Accrued interest payable	53,552	67,319
Customer deposits payable	715,521	656,103
Compensated absences payable-current	141,348	139,484
Revenue bonds payable-current	<u>1,420,000</u>	<u>1,355,000</u>
Total current liabilities	<u>4,714,008</u>	<u>4,572,826</u>
Noncurrent liabilities:		
Compensated absences payable	197,738	226,310
Revenue bonds payable	<u>4,475,337</u>	<u>5,913,857</u>
Total noncurrent liabilities	<u>4,673,075</u>	<u>6,140,167</u>
Total liabilities	<u>9,387,083</u>	<u>10,712,993</u>
NET POSITION		
Net investment in capital assets	30,969,361	28,492,981
Restricted for debt service	910,529	856,940
Restricted for rate stabilization	2,500,000	2,500,000
Unrestricted	<u>3,685,381</u>	<u>7,195,195</u>
Total net position	<u>\$ 38,065,271</u>	<u>39,045,116</u>

See notes to financial statements.

CITY OF HAMILTON, OHIO - GAS SYSTEM
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
YEARS ENDED DECEMBER 31, 2014 AND 2013

	<u>2014</u>	<u>2013</u>
Operating revenues:		
Charges for services	\$ 29,366,601	24,734,744
Other operating revenues	<u>2,878</u>	<u>7,373</u>
Total operating revenues	<u>29,369,479</u>	<u>24,742,117</u>
Operating expenses:		
Personal services	1,809,364	1,892,381
Materials and supplies	486,951	440,581
Contractual services	1,207,783	1,495,153
Purchased gas	22,756,500	16,943,459
Depreciation	1,915,763	1,878,725
Other operating expenses	<u>2,639,909</u>	<u>1,825,001</u>
Total operating expenses	<u>30,816,270</u>	<u>24,475,300</u>
Operating income (loss)	(1,446,791)	266,817
Non-operating revenues (expenses):		
Investment earnings	119,473	3,948
Loss on disposal of capital assets	(36,027)	(1,326)
Interest and fiscal charges	<u>(323,258)</u>	<u>(396,818)</u>
Total non-operating revenues (expenses)	<u>(239,812)</u>	<u>(394,196)</u>
Income before contributions	(1,686,603)	(127,379)
Capital contributions	<u>706,758</u>	<u>-</u>
Change in net position	(979,845)	(127,379)
Net position - beginning of year	<u>39,045,116</u>	<u>39,172,495</u>
Net position - end of year	\$ <u>38,065,271</u>	<u>39,045,116</u>

See notes to financial statements.

CITY OF HAMILTON, OHIO - GAS SYSTEM
STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2014 AND 2013

	<u>2014</u>	<u>2013</u>
Cash flows from operating activities:		
Cash received from customers	\$ 28,853,897	23,816,257
Cash paid for employee services and benefits	(1,830,099)	(1,768,732)
Cash paid to suppliers for goods and services	<u>(27,024,216)</u>	<u>(20,073,925)</u>
Net cash provided (used) by operating activities	<u>(418)</u>	<u>1,973,600</u>
Cash flows from capital and related financing activities:		
Capital contributions	706,758	-
Payments for capital acquisition	(3,149,985)	(2,657,683)
Debt principal payments	(1,355,000)	(1,290,000)
Debt interest payments	<u>(314,738)</u>	<u>(379,238)</u>
Net cash used by capital and related financing activities	<u>(4,112,965)</u>	<u>(4,326,921)</u>
Cash flows from investing activities:		
Interest from investments	<u>119,939</u>	<u>454</u>
Net cash provided by investing activities	<u>119,939</u>	<u>454</u>
Net change in cash and investments	(3,993,444)	(2,352,867)
Cash and investments at beginning of year	<u>10,126,065</u>	<u>12,478,932</u>
Cash and investments at end of year	\$ <u><u>6,132,621</u></u>	<u><u>10,126,065</u></u>
Reconciliation of operating income (loss) to net cash provided (used) by operating activities:		
Operating income (loss)	\$ (1,446,791)	266,817
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:		
Depreciation	1,915,763	1,878,725
Changes in Assets and Liabilities:		
(Increase) decrease in receivables	(575,000)	(1,002,370)
(Increase) decrease in inventory	2,641	1,318
(Increase) decrease in prepaid items	(12,936)	(10,338)
Increase (decrease) in customer deposits payable	59,418	76,510
Increase (decrease) in payables	77,121	639,390
Increase (decrease) in accrued liabilities	(20,341)	127,612
Increase (decrease) in intergovernmental payables	<u>(293)</u>	<u>(4,064)</u>
Net cash provided by operating activities	\$ <u><u>(418)</u></u>	<u><u>1,973,600</u></u>
Schedule of noncash activities:		
Outstanding liabilities for purchase of certain capital assets	\$ 170,351	224,879
Change in fair value of investments	1,429	29,850

See notes to financial statements.

CITY OF HAMILTON, OHIO – GAS SYSTEM

Notes to Financial Statements Years Ended December 31, 2014 and 2013

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity – The City of Hamilton, Ohio – Gas System (Gas System) is a utility operating as a separate enterprise fund of the City of Hamilton, Ohio (City). The Gas System is controlled by and is dependent on the City’s executive and legislative branches. Control by or dependence on the City is determined on the basis of outstanding debt secured by revenues or general obligations of the City, obligation of the City to finance any deficits that may occur, or receipt of subsidies from the City.

Measurement Focus, Basis of Accounting and Basis of Presentation – The financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of cash flows.

Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the Gas System’s principal ongoing operations. The principal operating revenues are charges to customers for sales and services. Operating expenses include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting these definitions are reported as non-operating revenues and expenses.

Income Taxes – The Gas System, which is owned and operated by the City, is exempt from income taxes since it is a division of a municipality.

Cash and Investments – Certain Gas System cash and investments are held in the City Treasury and pooled for investment management purposes. The portion of these pooled funds owned by the Gas System is reported as cash and investments. The Gas System’s investments are stated at fair value. Interest earned on funds invested is distributed on the basis of the relationship of the average monthly balance of all funds, including the Gas System.

Inventories – Inventories are stated at the lower of cost or market based on a moving-average cost method.

Capital Assets – Expenditures that increase values or extend the useful life of the respective assets are capitalized while the costs of maintenance and repairs are charged to operating expenses. Interest costs related to the construction of property, plant and equipment are capitalized. Depreciation is calculated on a straight-line basis over the estimated useful life of the various classes of assets. The range of useful lives for computing depreciation is 3 to 75 years.

Bond Premiums and Discounts – Unamortized bond premiums and discounts are amortized on the interest method over the term of the related bonds. Amortization of bond premiums was \$26,903 and \$40,068 in 2014 and 2013, respectively. Amortization of bond discounts was \$8,383 and \$10,669 in 2014 and 2013, respectively.

Compensated Absences - The Gas System follows the provisions of GASB Statement No. 16, “Accounting for Compensated Absences”. Vacation and compensatory time benefits are accrued as a liability as the benefits are earned if the employees' rights to receive compensation are attributable to services already rendered and it is probable that the Gas System will compensate the employees for the benefits through paid time off or some other means. Sick leave termination benefits are accrued using the vesting method. The liability includes the employees who are currently eligible to receive termination benefits and those employees for whom it is probable that they will become eligible to receive payment in the future. The amount is based on accumulated sick leave and employees' wage rates at year-end.

Deferred Outflows of Resources – In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement reporting element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense) until then. The Gas System only has one item that qualifies for reporting in this category. It is the deferred charge on refunding reported in the statements of net position. A deferred charge on refunding results from the difference in the carrying value of refunded debt and its reacquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt.

Net Position – Net position represents the difference between assets, liabilities, and deferred outflows of resources. Net position invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction, or improvement of those assets. Net position is reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the City or through external restrictions imposed by creditors, grantors or laws or regulations of other governments. The Gas System applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position is available.

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

2. CASH AND INVESTMENTS

The Gas System follows the practice of pooling cash and investments with the City Treasurer except for the cash and investments of certain accounts maintained by trustees. Pooled cash and investments of the Gas System totaled \$5,222,092 and \$9,269,125 at December 31, 2014 and 2013, respectively and consisted of demand deposits, money market funds, U.S. government securities and STAR Ohio. Cash and investments held by trustees were \$910,529 and \$856,940 at December 31, 2014 and 2013, respectively.

Star Ohio is an investment pool managed by the State Treasurer’s Office, which allows governments within the State to pool their funds for investment purposes. STAR Ohio is not registered with the SEC as an investment company, but does operate in a manner consistent with Rule 2a7 of the Investment Company Act of 1940. Investments in STAR Ohio are valued at STAR Ohio’s share price, which is the price the investment could be sold for on December 31, 2014.

Deposits – Custodial credit risk is the risk that in the event of a bank failure, the City’s deposits may not be returned to it. The City does not have a custodial risk policy. As of December 31, 2014 and 2013, approximately 98% of the City’s deposits with financial institutions, including the amount of pooled deposits related to the Gas System, were exposed to custodial credit risk because they are considered uninsured and uncollateralized. However, the State of Ohio has established by statute a collateral pooling system for financial institutions acting as public depositories. Public depositories must pledge qualified securities with fair values greater than the total amount of all public deposits to be secured by the collateral pool. This pooled collateral covers the Gas System’s uninsured and uncollateralized deposits.

Investments – The State of Ohio statutes, Gas Revenue Bond indentures, and the City Charter authorize the City to invest in obligations of the U.S. Treasury, agencies, instrumentalities, and repurchase agreements. Custodial credit risk in regards to investments is the risk that, in the event of a failure of a counter party, the City will not be able to recover the value of its investments or collateral securities that are in possession of an outside party. The City employs the use of “safekeeping” accounts to hold and maintain custody of its investments as identified within this policy and as means of mitigating this risk.

Interest rate risk is the risk that the City will incur fair value losses arising from rising interest rates. Such risk is mitigated by the investment policy by limiting investments to certain maximum maturities. As a rule, unless specified otherwise within the policy, investments are to have a maximum maturity of five years unless the investment is matched to a specific expenditure. The context of a specific investment purchase must be weighed in proportion to the remainder of the existing investment portfolio and the “prudent investor” rule to attempt to limit such risk.

The City’s pooled investments, as well as the investments held by trustees specifically for the Gas System, are invested primarily in U.S. governmental agency securities with an AA+ credit rating and an average maximum maturity of 4.19 years and STAR Ohio which has a credit rating of AAAM.

3. ACCOUNTS RECEIVABLE

Receivables at December 31, 2014 and 2013 consist of the following:

	<u>2014</u>	<u>2013</u>
Earned and unbilled consumer accounts	\$ 2,479,675	2,077,627
Earned and billed consumer accounts	4,143,375	3,877,718
Less allowance for uncollectible accounts	<u>(2,468,663)</u>	<u>(2,375,958)</u>
Total	<u>\$ 4,154,387</u>	<u>3,579,387</u>

4. RESTRICTED ASSETS

Restricted assets consist of assets whose use has been restricted by bond indenture for debt service and rate stabilization. Restricted assets were \$3,410,529 and \$3,356,940 December 31, 2014 and 2013, respectively.

5. CAPITAL ASSETS

Capital asset activity for the years ended December 31, 2014 and 2013 was as follows:

	Balance 1/1/14	Increases	Decreases	Balance 12/31/14
<i>Capital assets not being depreciated:</i>				
Land	\$ 454,216	-	-	454,216
Construction in progress	4,777,854	2,725,810	(2,271,037)	5,232,627
Subtotal	<u>5,232,070</u>	<u>2,725,810</u>	<u>(2,271,037)</u>	<u>5,686,843</u>
<i>Capital assets being depreciated:</i>				
Buildings and improvements	516,419	760,005	-	1,276,424
Machinery and equipment	68,676,013	1,880,679	(135,690)	70,421,002
Subtotal	<u>69,192,432</u>	<u>2,640,684</u>	<u>(135,690)</u>	<u>71,697,426</u>
Totals at historical cost	<u>74,424,502</u>	<u>5,366,494</u>	<u>(2,406,727)</u>	<u>77,384,269</u>
Less accumulated depreciation:				
Buildings and improvements	536,939	51,208	-	588,147
Machinery and equipment	38,187,415	1,864,555	(99,663)	39,952,307
Total accumulated depreciation	<u>38,724,354</u>	<u>1,915,763</u>	<u>(99,663)</u>	<u>40,540,454</u>
Capital assets, net	\$ <u>35,700,148</u>	<u>3,450,731</u>	<u>(2,307,064)</u>	<u>36,843,815</u>

	Balance 1/1/13	Increases	Decreases	Balance 12/31/13
<i>Capital assets not being depreciated:</i>				
Land	\$ 454,216	-	-	454,216
Construction in progress	<u>3,082,305</u>	<u>1,932,316</u>	<u>(236,767)</u>	<u>4,777,854</u>
Subtotal	<u>3,536,521</u>	<u>1,932,316</u>	<u>(236,767)</u>	<u>5,232,070</u>
<i>Capital assets being depreciated:</i>				
Buildings and improvements	516,419	-	-	516,419
Machinery and equipment	<u>67,938,491</u>	<u>756,727</u>	<u>(19,205)</u>	<u>68,676,013</u>
Subtotal	<u>68,454,910</u>	<u>756,727</u>	<u>(19,205)</u>	<u>69,192,432</u>
Totals at historical cost	<u>71,991,431</u>	<u>2,689,043</u>	<u>(255,972)</u>	<u>74,424,502</u>
Less accumulated depreciation:				
Buildings and improvements	517,491	19,448	-	536,939
Machinery and equipment	<u>36,346,017</u>	<u>1,859,277</u>	<u>(17,879)</u>	<u>38,187,415</u>
Total accumulated depreciation	<u>36,863,508</u>	<u>1,878,725</u>	<u>(17,879)</u>	<u>38,724,354</u>
Capital assets, net	\$ <u>35,127,923</u>	<u>810,318</u>	<u>(238,093)</u>	<u>35,700,148</u>

6. LONG TERM DEBT

Dated May 1, 2003, the City issued \$14,540,000 in Gas System Revenue Refunding Bonds to refund the 1993 Gas System Revenue Bonds. The Gas System Revenue Refunding Bonds are due serially through 2015 with interest from 4.75% to 5.0% per annum.

On September 9, 2009, the City issued \$4,500,000 in Gas System Revenue Bonds to currently refund bond anticipation notes and provide funding for various Gas System distribution improvements. These bonds are due serially through 2029 with interest from 2.75% to 5.0% per annum, with the first payment due in 2016.

Activity for the year ended December 31, 2014 was as follows:

	Balance 1/1/14	Additions	Reductions	Balance 12/31/14	Due Within One Year
2003 Refunding Bonds	\$ 2,775,000	-	(1,355,000)	1,420,000	1,420,000
2009 Revenue Bonds	4,500,000	-	-	4,500,000	-
Less deferred amount for issuance premium	40,671	-	(26,903)	13,768	-
for issuance discounts	<u>(46,814)</u>	<u>-</u>	<u>8,383</u>	<u>(38,431)</u>	<u>-</u>
	\$ <u>7,268,857</u>	<u>-</u>	<u>(1,373,520)</u>	<u>5,895,337</u>	<u>1,420,000</u>

Activity for the year ended December 31, 2013 was as follows:

	Balance 1/1/13	Additions	Reductions	Balance 12/31/13	Within One Year
2003 Refunding Bonds	\$ 4,065,000	-	(1,290,000)	2,775,000	1,355,000
2009 Revenue Bonds	4,500,000	-	-	4,500,000	-
Less deferred amount for issuance premium	80,739	-	(40,068)	40,671	-
for issuance discounts	(57,483)	-	10,669	(46,814)	-
	<u>\$ 8,588,256</u>	<u>-</u>	<u>(1,319,399)</u>	<u>7,268,857</u>	<u>1,355,000</u>

Under the terms of the revenue bond indenture, the City has agreed to certain covenants including, among other things, maintaining revenue levels and providing for operating expenses and debt service. The revenue bonds are insured under municipal bond insurance policies. Under the terms of the policies, the payments of principal and interest are guaranteed by the insurer.

Annual debt service requirements to maturity for the refunding bonds are as follows:

	Principal	Interest	Total
2015	\$ 1,420,000	250,375	1,670,375
2016	250,000	182,925	432,925
2017	260,000	176,050	436,050
2018	270,000	168,250	438,250
2019	275,000	159,475	434,475
2020-2024	1,540,000	630,650	2,170,650
2025-2029	<u>1,905,000</u>	<u>275,525</u>	<u>2,180,525</u>
Total	<u>\$ 5,920,000</u>	<u>1,843,250</u>	<u>7,763,250</u>

7. DEFINED BENEFIT PENSION PLANS AND OTHER POSTEMPLOYMENT BENEFITS

The Gas System contributes to the Ohio Public Employees Retirement System, the City of Hamilton Metropolitan Pension Plan, and post-employment life insurance.

Ohio Public Employees Retirement System (OPERS)

The OPERS administers three separate pension plans:

- The Traditional Pension Plan – a cost-sharing multiple-employer defined benefit pension plan.
- The Member-Directed Plan – a defined contribution plan in which the member invests both member and employer contributions (employer contributions vest over five years at 20% per year). Under the Member-Directed Plan, members accumulate retirement assets equal to the value of member and vested employer contributions plus any investment earnings thereon.

- The Combined Plan – a cost sharing multiple-employer defined benefit pension plan. Under the Combined Plan, employer contributions are invested by the retirement system to provide a formula retirement benefit similar in nature to the Traditional Plan benefit. Member contributions, the investment of which is self-directed by the members, accumulate retirement assets in a manner similar to the Member-Directed Plan.

OPERS provides retirement, disability, survivor and death benefits, and annual cost of living adjustments to members and of the Traditional Plan and Combined Plan. Members of the Member-Directed Plan do not qualify for ancillary benefits. The authority to establish and amend benefits is provided by state statute per Chapter 145 of the Ohio Revised Code. OPERS issues a stand-alone financial report that may be obtained by writing to the OPERS, 277 East Town Street, Columbus, Ohio 43215-4642.

Plan members are required to contribute 10.0% of their annual covered salary. The City was required to contribute 14.0% of covered payroll for employees. The Gas System's required contributions to OPERS for the years ended December 31, 2014, 2013, and 2012 were approximately \$181,000, \$176,000, and \$186,000 respectively, equal to the required contributions for each year.

OPERS maintains a cost-sharing multiple employer defined benefit post-employment healthcare plan, which includes a medical plan, prescription drug program and Medicare Part B premium reimbursement, to qualifying members of both the Traditional Pension and the Combined Plans. Members of the Member-Directed Plan do not qualify for ancillary benefits, including post-employment health care coverage.

In order to qualify for post-employment health care coverage, age-and-service retirees under the Traditional Pension and Combined Plans must have 10 or more years of qualifying Ohio service credit. Health care coverage for disability benefit recipients and qualified survivor benefit recipients is available. The health care coverage provided by OPERS meets the definition of an Other Post Employment Benefit (OPEB) as described in GASB Statement 45.

The Ohio Revised Code permits, but does not mandate, OPERS to provide OPEB benefits to its eligible members and beneficiaries. Authority to establish and amend benefits is provided in Chapter 145 of the Ohio Revised Code.

The Ohio Revised Code provides the statutory authority requiring public employers to fund post retirement health care coverage through their contributions to OPERS. A portion of each employer's contribution to OPERS is set aside for the funding of post retirement health care benefits. Employer contribution rates are expressed as a percentage of the covered payroll of active members. In 2014, the City contributed 14.0% of covered payroll. The Ohio Revised Code currently limits the employer contribution to a rate not to exceed 14.0% of covered payroll. Active members do not make contributions to the OPEB Plan.

The OPERS' Post Employment Health Care plan was established under, and is administrated in accordance with, Internal Revenue Code 401(h). Each year, the OPERS Retirement Board determines the portion of the employer contribution rate that will be set aside for funding of postemployment health care benefits. The portion of employer contributions allocated to health care for members in the Traditional and Combined Plans was 2.0% during calendar year 2014. The OPERS Retirement Board is also authorized to establish rules for the retiree, or their surviving beneficiaries, to pay a portion of the health care benefits provided. Payments amounts vary depending on the number of covered dependents and the coverage selected. The portion of the Gas System's contributions that were used to fund post employment benefits was approximately \$26,000, \$13,000, and \$53,000 for 2014, 2013, and 2012, respectively.

Changes to the health care plan were adopted by the OPERS Retirement Board on September 19, 2012, with a transition plan commencing January 1, 2014. With the recent passage of pension legislation under SB 343 and the approved health care changes, OPERS expects to be able to consistently allocate 4% of the employer contributions toward the health care fund after the end of the transition period.

Metropolitan Pension Plan

Employees of the City who were not included under the Ohio Public Employees Retirement System (OPERS) prior to May 15, 1962 and who were included under a Group Annuity Contract of the Metropolitan Life Insurance Company participate in the City of Hamilton Metropolitan Pension Plan, a single-employer defined benefit pension plan.

Upon retirement, plan participants are entitled to a supplemental retirement benefit paid by the City, equal to the difference between OPERS benefits that would have been payable to such employee had the employee been covered by OPERS during the full period of employment and actual OPERS benefits received. Benefit provisions of the plan are established and may be amended by the City Council through ordinance. All current participants in the Metropolitan Pension Plan are retired from service with the City.

The Gas System's annual pension cost (APC) and net pension obligation (NPO) for the Metropolitan Pension Plan December 31, 2014, 2013, and 2012 are as follows:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Annual required contribution (ARC)	\$ 49,498	\$ 51,164	\$ 55,781
Interest on NPO	795	369	-
Adjustments to ARC	<u>(3,719)</u>	<u>(1,505)</u>	<u>-</u>
Annual pension cost (APC)	46,574	50,028	55,781
Contributions made	<u>36,227</u>	<u>39,361</u>	<u>46,568</u>
Increase in net pension obligation	10,347	10,667	9,213
Net pension obligation, beginning of year	<u>19,880</u>	<u>9,213</u>	<u>-</u>
Net pension obligation, end of year	<u>\$ 30,227</u>	<u>\$ 19,880</u>	<u>\$ 9,213</u>

The Gas System's APC, percentage of APC contributed, NPO, and unfunded actuarial accrued liabilities for years ended December 31, 2014, 2013, and 2012 are as follows:

Years Ended	Annual Pension Cost (APC)	Percentage of APC Contributed	Net Pension Obligation	Unfunded Actuarial Accrued Liability
2014	\$ 46,574	77.8%	\$ 30,227	\$ 248,264
2013	50,028	78.7%	19,880	264,613
2012	55,781	83.5%	9,213	313,174

The actuarial valuation date was December 31, 2014 and the accrued liability was calculated using the entry age normal cost method. The Metropolitan Pension Plan currently has no assets. The amortization method used was level dollar and the amortization period was 6 years.

Retiree Life Insurance

The City provides post-employment life insurance coverage through the Hartford Insurance Company. The insurance coverage provided is considered an other post-employment benefit (OPEB) as described in GASB Statement No. 45.

Eligible employees are grouped into two classes. Employees who retired prior to March 1, 1977 are eligible to receive \$2,000 in life insurance benefits. Employees who retired after March 1, 1977 are eligible to receive \$4,000 in life insurance benefits. Benefit provisions of the plan are established and may be amended by City Council through ordinance.

The Gas System's annual OPEB cost and net OPEB for the Retiree Life Insurance Plan for the years ended December 31, 2014, 2013, and 2012 are as follows:

	<u>2014</u>	<u>2013</u>	<u>2012</u>
Annual required contribution (ARC)	\$ 11,711	\$ 11,621	\$ 11,346
Interest on Net OPEB	125	65	-
Adjustments to ARC	<u>(182)</u>	<u>(87)</u>	<u>-</u>
Annual OPEB cost	11,654	11,599	11,346
Contributions made	<u>10,195</u>	<u>10,093</u>	<u>9,736</u>
Increase in Net OPEB	1,459	1,506	1,610
Net OPEB, beginning of year	<u>3,116</u>	<u>1,610</u>	<u>-</u>
Net OPEB, end of year	<u>\$ 4,575</u>	<u>\$ 3,116</u>	<u>\$ 1,610</u>

The Gas System’s annual OPEB cost, percentage of OPEB contributed, net OPEB, and unfunded actuarial accrued liabilities for years ended December 31, 2014, 2013, and 2012 are as follows:

<u>Years Ended</u>	<u>Annual OPEB Cost</u>	<u>Percentage of OPEB Contributed</u>	<u>Net OPEB Obligation</u>	<u>Unfunded Actuarial Accrued Liability</u>
2014	\$ 11,654	87.5%	\$ 4,575	\$ 250,418
2013	11,599	87.1%	3,116	164,032
2012	11,346	85.8%	1,610	164,697

The actuarial valuation date was December 31, 2014 and the accrued liability was calculated using the entry age normal cost method. The City’s post-employment life-insurance plan currently has no assets.

8. CONTINGENT LIABILITIES

Various claims and lawsuits are pending against the City involving the Gas System. The City believes that the ultimate disposition of such claims and lawsuits will not have a material adverse effect on the financial position of the Gas System.

9. RELATED PARTY TRANSACTIONS

The Gas System sells gas to the City’s Electric System for use in the generation of electricity. Revenues of approximately \$4,014,000 and \$1,587,000 from the Electric System to the Gas System are included in operating revenues in 2014 and 2013, respectively.

The City allocates the cost of certain administrative services. In addition, the City established internal service funds that provide services to various City departments. Charges to the Gas System for these services were approximately \$2,769,000 and \$2,246,000 in 2014 and 2013, respectively, and are included in other operating expenses.

10. RISK MANAGEMENT

The City is exposed to various risks of loss related to torts and liability, damage to and theft of or destruction of assets; errors and omissions; injuries to employees; and natural disasters. The City maintains comprehensive insurance coverage, for all City departments including the Gas System, with private carriers for real property, building contents, vehicle, property and general liability insurance, police professional liability, and public officials’ errors and omissions insurance. Vehicle policies include liability coverage for bodily injury and property damage. Claim payments have not exceeded coverage in the past three years. There was no decline in the level of coverage from the prior year.

11. CONTRACTUAL COMMITMENTS

At December 31, 2014, the Gas System had a contractual commitments related to property, plant and equipment improvements and additions, as well as various other contract and agreements to provide or receive services related to the operations of approximately \$445,000.

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Dave Yost • Auditor of State

CITY OF HAMILTON GAS SYSTEM

BUTLER COUNTY

CLERK'S CERTIFICATION

This is a true and correct copy of the report which is required to be filed in the Office of the Auditor of State pursuant to Section 117.26, Revised Code, and which is filed in Columbus, Ohio.

Susan Babbitt

CLERK OF THE BUREAU

**CERTIFIED
AUGUST 25, 2015**