Department of Water Resources
Electric Power Fund
Financial Statements

For the year ended June 30, 2018
(with comparative amounts for 2017)

Department of Water Resources Electric Power Fund
Table of Contents

Page

VAVRINEK, TRINE, DAY & CO., LLP
Certified Public Accountants

INDEPENDENT AUDITORS' REPORT

To the Director of the State of California Department of Water Resources
Department of Water Resources Electric Power Fund
Sacramento, California

Report on the Financial Statements

We have audited the accompanying financial statements of the State Water Resources Electric Power Fund (Fund), an enterprise fund of the State of California, as of and for the year ended June 30, 2018, 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 audit. We conducted our audit 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 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 auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Fund as of June 30, 2018, and the changes in financial position, and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

2151 River Plaza Dr., Suite 308, Sacramento, CA 95833 P 916.570.1880 F 916.570.1875 W vtdcpa.com

Emphasis of Matters

Reporting Entity

As disclosed in Note 1, the financial statements present only the Fund and do not purport to, and do not, present fairly the financial position of the State of California as of June 30, 2018, and the changes in its financial positions and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Change in Accounting Principles

As disclosed in Note 9 to the financial statements, the Fund implemented GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, effective July 1, 2017. Our opinion is not modified with respect to this matter.

Other Matters

Report on Summarized Comparative Information

Other auditors have previously audited the Fund's 2017 financial statements, and they expressed an unmodified audit opinion on those audited financial statements in their report dated December 1, 2017.

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, schedule of the Fund's proportionate share of the net pension liability, schedule of the Fund's Pension contributions, schedule of the Fund's proportionate share of the net other-post employment benefits (OPEB) liability, and schedule of the Fund's OPEB contributions, as listed in the table of contents, 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.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 26, 2019, on our consideration of the Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Fund's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Fund's internal control over financial reporting and compliance.

Vavrinek, Trine, Day & Co. LLP

Sacramento, California
March 26, 2019

USING THIS REPORT

This discussion and analysis is designed to assist the reader in focusing on significant financial issues and activities and to identify any significant changes in financial position of the Department of Water Resources Electric Power Fund (the Fund), which is administered by the California Department of Water Resources (DWR). Readers are encouraged to consider the information presented in the *Management's Discussion and Analysis* in conjunction with the financial statements that follow. This discussion and analysis and the financial statements do not relate to DWR's other governmental and proprietary funds.

The financial statements include three required statements, which provide different views of the Fund. The three required statements are:

- The Statement of Net Position: include all assets, liabilities and deferred outflows and inflows of resources as of the period ending date.
- The Statement of Revenues, Expenses and Changes in Net Position: present all of the current year's revenues, expenses, and changes in net position.
- The Statement of Cash Flows: report cash receipts, disbursements and the net change in cash resulting from four principal types of activities: operating, capital financing, non-capital financing and investing.

These statements provide current and long-term information about the Fund and its activities. These financial statements report information using accounting methods similar (although not identical) to those used by private sector companies. In order for the financial statements to be complete, they must be accompanied by a complete set of notes. The notes to financial statements provide disclosures which are required to conform to generally accepted accounting principles. The Fund is required to follow accounting standards promulgated by the Governmental Accounting Standards Board.

PURPOSE OF FUND

The Fund was established in January 2001 through legislation to assist in mitigation of the effects of a statewide energy supply emergency.

The Fund has the authority to secure and retain title to power for resale to end use customers in the State's investor owned utilities (IOUs) service areas under power supply contracts entered into prior to January 1, 2003. The scheduling, dispatch, and certain other administrative functions for the long-term contracts were performed by the IOUs as agents for the Fund. However, the Fund retained the legal and financial responsibility for each contract for the life of the contract or until such time as there was a complete assignment of the contract to an IOU and release of the Fund. The last remaining contract terminated during the 2015 fiscal year, releasing the Fund from substantially all future power supply obligations. The Fund does not have any significant legal or financial responsibility for any power supply contracts entered into pursuant to the legislation establishing its authority.

The Fund is entitled to recover revenue requirements for authorized activities, including but not limited to debt service, the costs of power purchases, administrative expenses and reserves. Revenue requirements are determined at least annually and transmitted to the California Public Utilities Commission (CPUC) for implementation. Under the terms of the rate agreement between the CPUC and the Fund, the CPUC is required to allocate the Department's costs on customers in the IOU service areas such that the Fund will always have monies to meet its revenue requirements. This includes "departing load" (such as direct access and Community Choice Aggregation) Electric Service Providers (ESPs).

CONDENSED STATEMENT OF NET POSITION

The Fund's assets, liabilities and net position as of June 30 are summarized as follows (in millions):

	2018	2017	2016
Long-term restricted cash, equivalents and investments	$ 884	$ 884	$ 911
Recoverable costs	1,631	2,467	3,245
Restricted cash and equivalents:			
Administrative cost account	12	11	8
Operating account	38	24	38
Bond charge collection and bond charge payment accounts	608	555	535
Recoverable costs receivable	109	106	72
Interest receivable	8	6	4
Total assets	3,290	4,053	4,813
Deferred outflows of resources related to pensions	2	2	2
Deferred outlfows of resources related to OPEB	9		
Deferral of loss on defeasance	88	117	116
Total deferred outflows of resources	99	119	118
Total assets and deferred outflows of resources	$ 3,389	$ 4,172	$ 4,931
Long-term debt, including current portion	$ 3,348	$ 4,128	$ 4,880
Net pension liability	5	6	5
Net OPEB liaiblity	8		
Net OPEB obligation	-	7	7
Interfund Loan	1		
Other current liabilities	25	31	39
Total liabilities	3,387	4,172	4,931
Deferred inflows of resources related to pensions	1	-	-
Deferred inflows of resources related to OPEB	1		
Total liabilities and deferred inflow of resources	$ 3,389	$ 4,172	$ 4,931

Long-Term Restricted Cash, Equivalents and Investments

The Debt Service Reserve Account remained unchanged at $884 million during the fiscal year ended June 30, 2018. The amount was determined in accordance with the Trust Indenture among the State of California, Department of Water Resources, Treasurer of the State of California, as Trustee and U.S. Bank, N.A, as Co-Trustee (Trust Indenture) and is based on the maximum annual debt service over the remaining life of the Fund's bonds.

The Debt Service Reserve Account decreased $27 million during the fiscal year ended June 30, 2017. The decrease in the Debt Service Reserve Account resulted from the release of funds to the escrow account related to Series P refunding on September 28, 2016. The refunding decreased the Debt Service Reserve Account to $884 million.

Recoverable Costs

Recoverable costs consist of costs that are recoverable through future billings. The $836 million decrease during fiscal year 2018 is due to the recovery of operating costs of $18 million; bond charges plus interest income exceeding interest and investment expense by $814 million and adjustment to the beginning balance of net OPEB (Other Postemployment Benefits) liability as a result of the implementation of GASB 75 for 4 million. The surplus of Bond Charge Collections over interest costs is primarily a result of the Fund's rate design which includes funding for annual debt service, including principal payments.

The $778 million decrease in recoverable costs during fiscal year 2017 was due to the recovery of operating costs of $26 million; and bond charges plus interest income exceeding interest and investment expense by $804 million. The surplus of Bond Charge Collections over interest costs is primarily a result of the Fund's rate design which includes funding for annual debt service, including principal payments.

Restricted Cash and Equivalents

The Administrative Cost Account increased $1 million in 2018 due to lower expenses as the Electric Power Fund operation continues to decline.

The Operating Accounts increased by $14 million in 2018 as a result of energy settlements received during the year.

The Bond Charge Collection and Bond Charge Payment Accounts increased by $53 million in 2018 and increased by $20 million in 2017 in accordance with required amounts specified in the Trust Indenture.

Recoverable Costs Receivable

Recoverable costs receivable reflects power and bond charges to customer in the IOU service areas that have not yet been collected and amounts receivable. The $109 million of recoverable costs receivable at June 30, 2018 is $3 million higher than at June 30, 2017. The increase was primarily due to expected litigation settlement money which is expected to be received in September 2018.

The $106 million of recoverable costs receivable at June 30, 2017 was $34 million higher than at June 30, 2016. The increase was due to higher bond charge rates during fiscal year 2017.

Deferred Outflows of Resources

Deferred outflows of resources related to pensions remained unchanged at $2 million for June 30, 2018 and 2017.

Deferred outflows of resources related to OPEB was $9 million at June 30, 2018 consisted of recognizing the difference between the current year actual and expected contribution of $4 million and recording deferred outflows of resources for contributions after the measurement date of $5 million.

Deferral of loss on defeasance decreased by $30 million, during the fiscal year ending June 30, 2018, due to the amortization of deferred loss on defeasance during the fiscal year.

Long-Term Debt

Long-term debt decreased to $3,348 million, as of June 30, 2018, from $4,128 million, as of June 30, 2017. Revenue bond principal payments were $719 million in fiscal year 2018. Net amortization of bond premium was $61 million in fiscal year 2018.

Long-term debt decreased to $4,128 million, during fiscal year ended June 30, 2017, from $4,880 million as of June 30, 2016.

Revenue bond principal payments were $690 million in fiscal year 2017. Net amortization of bond premium was $69 million in fiscal year 2017.

Net Pension Liability

The net pension liability decreased $1 million during fiscal year ended June 30, 2017 due to the reduction of discount rate from 7.65 percent to 7.15 percent.

The net pension liability as of June 30, 2017 was $6 million.

Other Postemployment Benefits

In addition to pension benefits, the State of California provides postemployment health care benefits to all employees who retire on or after attaining certain age and length of service requirements. The State of California is funding postemployment benefits on a pay-as-you-go basis. The Fund's net OPEB obligation decreased to $0 (zero) million due to implementing of GASB 75 and The Fund's net OPEB liability was $8 million as a result of the implementation of GASB 75 at June 30, 2018.

Other Current Liabilities

Other current liabilities consist of accounts payable and accrued interest payable. Accounts payable reflects one month's accrual for employee and consultants, as payments are normally made in the latter half of the month following purchase.

Accounts payable at June 30, 2018 and 2017 remained unchanged at $2 million from June 30, 2016.

Accrued interest payable at June 30, 2018 was $6 million lower than at June 30, 2017 due to fewer bonds outstanding resulting from the maturity of $719 million in bonds in fiscal year 2018.

Accrued interest payable at June 30, 2017 was $8 million lower than at June 30, 2016 due to fewer bonds outstanding resulting from the maturity of $690 million in bonds in fiscal year 2017 and lower total debt outstanding after Series P refunding.

Deferred Inflows of Resources

Deferred inflows of resources related to pension was $1 million for fiscal years ended June 30, 2018 as a result of recording the current year activity.

Deferred inflows of resources related to OPEB was $1 million as of June 30, 2018 as a result of the implementation of GASB 75 this fiscal year.

CONDENSED STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

The Fund's activities for the years ended June 30 are summarized as follows (in millions):

	2018	2017	2016
Revenues:			
Power charges, net of refunds	$ -	$ (29)	$ (182)
Bond charges	918	948	886
Interest income	34	26	24
Total revenues	952	945	728
Expenses:			
Power purchases	-	-	-
Energy and financial settlements	(26)	(16)	-
Interest expense	138	170	193
Administrative expenses	8	13	9
Recovery of recoverable costs	832	778	526
Total expenses	952	945	728
Changes in net position	-	-	-
Net position, beginning of year	-	-	-
Net position, end of year	$ -	$ -	$ -

Power Charges

The cost of providing energy was recoverable primarily through Power Charges to IOU customers and certain customers of ESPs. Charges are determined by applying a CPUC adopted rate for each IOU service area to the megawatt hours of power delivered by the Fund to customers in each IOU service area.

Power Charges were zero compared to negative $29 million for fiscal year ended June 30, 2017. The increase was primarily due to the Fund not returning any excess amounts of previously received remittances to ratepayers in fiscal year 2018.

Power Charges increased by $153 million during fiscal year 2017. The increase reflects the lower return of excess amounts and previously received remittances to ratepayers. The return of excess amounts and previously received remittances was an allocation of excess reserves, litigation settlements and prior year over-collection from ratepayers. The return is implemented through separate monthly payments to the ratepayers through the IOUs.

Bond Charges

Bond Charges provide revenue for the payment of debt service on the revenue bonds and are determined by applying a CPUC adopted rate to the total megawatt hours of power delivered to all bundled customers and certain ESP customers in the IOU service areas. Bond Charges for the years ended June 30, 2018, 2017 and 2016 were $918 million, $948 million and $886 million, respectively, and were adequate to meet all debt service requirements and maintain Trust Indenture required account balances in the Bond Charge Collection, Bond Charge Payment, and Debt Service Reserve Accounts. The $30 million decrease in 2018 was a result of fewer remittances collected due to lower energy consumption.

The $62 million increase in 2017 is due to a combination of higher Bond Charge rates and higher sales to IOU customers.

Interest Income

Interest income for 2018 is $8 million higher than in 2017 due to higher interest rates earned on investments in the State of California Surplus Money Investment Fund (SMIF) and Forward Purchase Agreement (FPA) and the unrealized gain from the FPA. The average yield earned on SMIF, for the year ended June 30, 2018, was 1.38% compared to 0.75% for the year ended June 30, 2017.

During fiscal year 2017 interest income was $2 million higher than in 2016 due to higher interest rates earned on investments in the State of California Surplus Money Investment Fund (SMIF) and Forward Purchase Agreement (FPA) and the unrealized gain from the FPA. The average yield earned on SMIF, for the year ended June 30, 2017, was 0.75% compared to 0.43% for the year ended June 30, 2016.

Energy and Financial Settlements

Energy settlements, including those related to complex regulatory proceedings before the Federal Energy Regulatory Commission (FERC), arising from events in California energy markets in 2001, are recorded as a decrease in operating expenses.

Additionally, the Fund has begun to be involved in litigation with various financial institutions to resolve alleged manipulation of financial market benchmark interest rates and their impact on the Fund's bond offerings and interest rate swap agreements.

The Fund received energy settlements of $15.8 million from Shell Energy North America (US), L.P (successor-in-interest to Coral Power, LLC). On June 1, 2018 the Fund submitted a claim for $9.8 million to the Deutsch Bank LIBOR AG Settlement. While expected to be received after June 30, 2018, this amount was considered an accrual for fiscal year 2018. Total energy and bond settlements were $25.6 million for fiscal year 2018.

During fiscal year 2017, $16 million in energy settlements was received. The Fund received $3.6 million from Allegheny Energy Supply Company, $3.5 million from Commerce Energy Inc and $9.1 million from Merrill Lynch Capital Services Inc.

Interest Expense

Interest expense was $32 million lower in 2018 when compared to 2017. The decrease was due to lower total interest paid on outstanding debt along with higher amortization of loss on defeasance offset by higher amortization of bond premium.

In 2017 interest expense was $23 million lower when compared to 2016. The decrease was due to lower total interest paid on outstanding debt along with higher amortization of loss on defeasance offset by higher amortization of bond premium.

Administrative Expenses

Administrative expenses decreased $5 million in 2018 from 2017 due to lower employee expenses as the Electric Power Fund operation continues to decline and the implementation of GASB 75 OPEB.

Administrative expenses increased $4 million in 2017 from 2016. The increase was related to fair share allocation of cost for service provided by central service agencies for the overall administration of state government and to support the implementation of statewide accounting system upgrades.

Recovery of Recoverable Costs

The individual components of the recovery of recoverable costs are as follows (in millions):

	2018		2017		2016	
Operations	$	18	$	(26)	$	(191)
Debt service and related costs		814		804		717
	$	832	$	778	$	526

Operations

The $18 million operations recovery, in the year ended June 30, 2018, is primarily due to energy settlements received and lower administrative expenses.

The negative $26 million operations recovery, in the year ended June 30, 2017, primarily reflected the return of excess amounts to ratepayers in the IOU service areas and no material power charge revenues received.

Debt Service and Related Costs

The recovery of debt service and related costs in all three years are a result of bond charges and interest income providing funds to pay interest expense and retire debt. The recoveries in 2018 and 2017 were higher due to lower interest expense and higher bond charges collected from IOU customers.

LIQUIDITY

Various provisions of the Trust Indenture provide resources for the Fund to meet its cash requirements. In addition to its determination of revenue requirements, prepared annually or more frequently if necessary, to meet both operating and bond related expenditures, the Fund has a Debt Service Reserve Fund in order to meet expenditures if bond charge revenue is impaired. The minimum balance in the Debt Service Reserve Fund is based on the Maximum Annual Debt Service.

With the termination of the last remaining power contract, reserves for operating the Fund's power purchase program are no longer necessary. As of January 2016, the remaining Operating Reserve Account funds were transferred to the Operating Account for return to customers in the IOU service areas.

Under the Section 80130 of the California Water Code, the Fund has a total debt issuance limit of $13.4 billion, which does not include refunding debt issued: (i) to obtain a lower interest rate, (ii) to convert variable rate debt to fixed rate debt or (iii) to replace debt for which the credit rating of the insurer or credit facility provider has been or will be downgraded or withdrawn.

On August 30, 2016, Moody's Investor Service raised the underlying rating on Power Supply Revenue Bonds from "Aa2" to "Aa1" with a stable rating outlook. On March 24, 2015, Standard & Poor's Ratings Services raised the underlying rating on the Power Supply Revenue Bonds from "AA-" to "AA" with a stable rating outlook. Also, on March 24, 2015, Fitch Ratings raised the underlying rating on the Power Supply Revenue Bonds from "AA" to "AA+" with a stable rating outlook. More information can be obtained from each credit rating agency's website: www.moodys.com, www.fitchratings.com, and www.standardandpoors.com

Requests for Information

This financial report is designed to provide a general overview of the Fund's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Chief, Enterprise Accounting Branch, 1416 Ninth Street Room 816, Sacramento, CA 95814.

Department of Water Resources Electric Power Fund
Statement of Net Position
June 30, 2018 (with comparative amounts for 2017)
(in millions)

	2018	2017
Assets		
Long-term assets:		
Restricted cash, equivalents and investments:		
Debt Service Reserve Account	$ 884	$ 884
Recoverable costs	1,631	2,467
Total long-term assets	2,515	3,351
Current assets:		
Restricted cash and equivalents:		
Administrative Cost Account	12	11
Operating Account	38	24
Bond Charge Collection and Bond Charge Payment Accounts	608	555
Recoverable costs receivable	109	106
Interest receivable	8	6
Total current assets	775	702
Total assets	3,290	4,053
Deferred outflows of resources		
Deferred outflows of resources related to pensions	2	2
Deferred outflows of resources related to OPEB	9	
Deferral of loss on defeasance	88	117
Total assets and deferred outflows of resources	$ 3,389	$ 4,172
Liabilities		
Non-Current liabilities:		
Long-term debt	$ 2,542	$ 3,349
Net pension liability	5	6
Net OPEB liability	8	
Net OPEB obligation	-	7
Interfund Payable	1	
Total non-current liabilities	2,556	3,362
Current liabilities:		
Current portion of long-term debt	806	779
Accounts payable	2	2
Accrued interest payable	23	29
Total current liabilities	831	810
Total liabilities	3,387	4,172
Deferred inflows of resources		
Deferred inflows of resources related to pension	1	-
Deferred inflows of resources related to OPEB	1	-
Total liabilities and deferred inflows of resources	$ 3,389	$ 4,172

See notes to financial statements

Department of Water Resources Electric Power Fund
Statement of Revenues, Expenses and Changes in Net Position
For the year ended June 30, 2018 (with comparative amounts for 2017)
(in millions)

	2018	2017
Operating revenues:		
Power charges, net of refunds	$ -	$ (29)
Operating expenses:		
Energy and financial settlements	(26)	(16)
Administrative expenses	8	13
Recovery of recoverable operating costs	18	(26)
Total operating expenses	-	(29)
Income from operations	-	-
Nonoperating revenues and expenses:		
Bond charges	918	948
Interest income	34	26
Interest expense	(138)	(170)
Recovery of recoverable debt service and related costs	(814)	(804)
Changes in net position	-	-
Net position, beginning of year	-	-
Net position, end of year	$ -	$ -

See notes to financial statements

Department of Water Resources Electric Power Fund
Statement of Cash Flows
For the year ended June 30, 2018 (with comparative amounts for 2017)
(in millions)

	2018	2017
Cash flows from operating activities:		
Receipts:		
Power charges, net of refunds	$ 8	$ (29)
Energy and financial settlements	23	16
Payments to employees for services	(14)	(2)
Payments for power purchases and other expenses	(4)	(10)
Net cash provided by (used for) in operating activities	13	(25)
Cash flows from non-capital financing activities:		
Receipt of bond charges	918	914
Bond payments	(719)	(690)
Interest payments	(176)	(215)
Proceeds from issuance of revenue bonds	-	1
Payment to advance refund escrow agent		(27)
Net cash provided by (used for) used in non-capital financing activities	23	(17)
Cash flows from investing activities:		
Interest received on investments	32	24
Changes in restricted cash and equivalents	68	(18)
Restricted cash and equivalents, beginning of period	1,172	1,190
Restricted cash and equivalents, end of period	$ 1,240	$ 1,172
Restricted cash and equivalents included in:		
Debt Service Reserve Account (a component of the total of $884 and $844 at June 30, 2018 and 2017, respectively)	582	582
Administrative Cost Account	12	11
Operating Account	38	24
Bond Charge Collection and Bond Charge Payment Accounts	608	555
Restricted cash and equivalents, end of year	$ 1,240	$ 1,172

See notes to financial statements

Department of Water Resources Electric Power Fund
Statement of Cash Flows (Continued)
For the year ended June 30, 2018 (with comparative amounts for 2017)
(in millions)

	2018	2017
Reconciliation of income from operations to net cash used in operating activities:		
Income from operations	$ -	$ -
Adjustments to reconcile income from operations to net cash used in operating activities:		
Recovery of recoverable operating costs	18	(26)
	18	(26)
Changes in net assets and liabilities to reconcile income from operations to net cash used in operations:		
Recoverable costs receivable	$ 1	$ -
Net OPEB liability and related deferred inflows/outflows	(7)	-
Net pension liability and related deferred inflows/outflows	-	1
Interloan payable	1	-
Net change in assets & liabilities:	(5)	1
Net cash provided by (used for) used in operating activities	$ 13	$ (25)
Noncash financing and investing activities:		
Amortization of revenue bond premiums	$ 61	$ 69
Amortization of deferral of loss on defeasance	30	31
Defeasance of premium on refunded revenue bonds	-	5
Bond proceeds paid directly to advance refund escrow agent	-	565
Unrealized gain on investment	-	1

See notes to financial statements

1. Reporting Entity

In January 2001, the Governor of California issued an emergency proclamation directing the Department of Water Resources (DWR) to enter into contracts and arrangements for the purchase and sale of electric power to assist in mitigating the effect of a statewide energy supply emergency.

The Department of Water Resources Electric Power Fund (the Fund), administered by DWR, was established in January 2001 through legislation adding Division 27 to the California Water Code (the Code).

The Fund purchases power from wholesale suppliers under contracts entered into prior to January 1, 2003 for resale to customers in the service areas of the State’s investor owned utilities (IOUs): Pacific Gas & Electric Company (PG&E), Southern California Edison Company (SCE), and San Diego Gas and Electric Company (SDG&E). The Code prohibits the Fund from entering into new power purchase agreements after December 31, 2002, but allowed the Fund to enter into gas purchase contracts to provide fuel for power generation.

The Fund’s power is delivered to customers through the transmission and distribution systems of the IOUs and payments from customers are collected for the Fund by the IOUs pursuant to servicing arrangements approved and/or ordered by the California Public Utilities Commission (CPUC).

Under the Code, the Fund has the authority to establish a revenue requirement to recover all Fund costs, including debt service. At least annually, Fund management establishes a determination of the revenue requirement, which then is submitted to the CPUC. Under the terms of a rate agreement between the Fund and the CPUC, the CPUC implements the Fund’s determination of its revenue requirements by establishing end use customer rates that meet the Fund’s revenue needs to assure the payment of debt service, power purchases, administrative expenses and maintenance of operating and debt service reserves.

2. Summary of Significant Accounting Policies

Basis of Presentation

The Fund is accounted for as an enterprise fund and is financed and operated in a manner similar to that of a private business enterprise. The Fund uses the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles, which considers the Fund a Regulated Operation under GASB Statement No. 62. The Fund is accounted for with a set of self-balancing accounts that comprise of assets, deferred outflows of resources, liabilities, deferred inflows of resources, net position, revenues and expenses.

The financial statements of the Fund are intended to present the financial position, and the changes in financial position and cash flow, of only that portion of the business-type activities and major funds of the State of California that is attributable to the transactions of the Fund. They do not purport to, and do not, present the financial position of the State of California and the changes in its financial position and its cash flows, in conformity with accounting principles generally accepted in the United States of America.

Comparative data for prior years have been presented for certain sections of the accompanying financial statements in order to provide an understanding of changes in the Fund's financial position and operations.

Current Year GASB Implementation

For the year ended June 30, 2018, the Fund implemented GASB Statement No. 75 (GASB 75), *Accounting and Financial Reporting for Postemployment Benefits other than Pensions.* This statement replaces the requirement of Statements No.45, *Accounting and Financial Reporting by Employers for Postemployment Benefits other than Pensions,* as amended, and No, 57, *OPEB Measurements* by *Agent Employers and Age Multiple-Employer Plans*.

The primary objective of this statement is to improve accounting and financial reporting by state and local governments for postemployment benefits other than pensions (other postemployment benefits or OPEB).

Restricted Cash, Equivalents and Investments

Under the terms of the Trust Indenture among the State of California, Department of Water Resources, Treasurer of the State of California, as Trustee and U.S. Bank, N.A, as Co-Trustee (Trust Indenture) separate restricted cash and investment accounts were established. The accounts and their purpose follow:

Administrative Account:

- Administrative Cost Account: Salaries, consultant fees and other administrative expenses were previously funded by Power Charges transferred from Operating Account. Since there are no longer power charge remittances, funds are now transferred from the Bond Charge Payment Account as of January 1, 2016.

Power Charge Account:

- Operating Account: Power Charges (see Revenues and Recoverable Costs) and miscellaneous revenue are deposited into the operating account. Monies are available for payment of residual contract obligations and return of excess amounts to ratepayers.

Bond Charge Accounts:

- Bond Charge Collection Account: Bond Charges (see Revenues and Recoverable Costs) are deposited into the Bond Charge Collection Account. Monthly, funds needed for debt service payments and administrative costs are transferred to the Bond Charge Payment Account.
- Bond Charge Payment Account: Monies in the Bond Charge Payment Account are used to pay debt service and related fees for the revenue bonds and administrative costs. After receipt of the monthly transfer from the Bond Charge Collection Account, the balance in the Bond Charge Payment Account must at least equal debt service and fees estimated to accrue or be payable for the next succeeding three months.
- Debt Service Reserve Account: The Debt Service Reserve Account was initially funded with proceeds of the Series 2002 Bonds. The Debt Service Reserve Account is to be funded at all times with the amount of maximum aggregate annual debt service on all outstanding debt. If the Debt Service Reserve Account needed to be replenished, the funds would be transferred from the Bond Charge Collection Account.

Restricted cash and equivalents, for purposes of the Statement of Cash Flows, include cash on hand and deposits in the Surplus Money Investment Fund (SMIF). The Debt Service Reserve Account (net of investments) is classified as long-term restricted cash due to requirements under the Trust Indenture to hold amounts in excess of anticipated current payments for bond related expenses. Amounts required to be held in reserve are determined annually by the Fund's revenue requirement

SMIF has an equity interest in the State of California Pooled Money Investment Account (PMIA). Generally, the investments in the PMIA are available for withdrawal on demand. The PMIA cash and investments are recorded at amortized cost, which approximates fair value. The PMIA funds are on deposit with the State's Centralized Treasury System and are managed in compliance with the California Government Code, described in Note 3.

Long-term investments are held solely in the Debt Service Reserve Account by the bond co-trustee and consist of guaranteed investment contracts (GICs) and a U.S. government backed agency security in accordance with a FPA. The GICs are carried at cost and the U.S. government backed agency security (FPA) is carried at fair value.

Net Position

The Fund does not record the difference between assets and liabilities as net position. The difference between assets and deferred outflows of resources and liabilities and deferred inflows of resources on the Statement of Net Position is presented as recoverable costs such that there is no net position. The Fund anticipates that amounts in the recoverable costs will be recovered in subsequent years prior to program expiration.

Revenues and Recoverable Costs

The Fund is required, at least annually, to establish a determination of the revenue requirement to be transmitted to the CPUC, which then sets end use customer remittance rates. The Fund's financial statements are prepared in accordance with GASB Statement No. 62, which requires that the effects of the revenue requirement process be recorded in the financial statements. Accordingly, all expenses and credits, normally reflected in the change in net position as incurred, are recognized as recoverable costs in the Statement of Net Position and are recovered from IOU customers. Costs that are recoverable through future billings are recorded as long-term assets.

Customer charges are separated into two primary components, power charges and bond charges. Power charge revenues recover the cost of power purchases, other expenses and operating reserves and are recognized when energy provided by the Fund is delivered to IOU customers. Bond charge revenues recover debt service, debt service reserves and other bond related costs and are recognized when energy provided by the IOU, or an ESP, is delivered to customers in the IOU service areas. Costs are recovered over the life of the bonds as determined by the Fund's revenue requirement process.

Pensions

For purposes of measuring the net pension liability and deferred outflows/inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Fund's portion of the California Public Employees' Retirement System (CalPERS) Miscellaneous Plan (Plan) and additions to/deductions from the Plan's fiduciary net position have been determined on the same basis as they are reported by CalPERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

OPEB

The State of California provides medical and prescription drug benefits to retired state employee and dependents through CalPERS under the Public Employee's Medical and Hospital Care Act, and dental benefits under the State Employees' Dental Care Act. The State, and certain bargaining units and judicial employees (valuation groups) have agreed to refund retiree healthcare benefits. Assets are held in separate accounts by valuation group within the California Employers' Retiree Benefit Trust (CERBT), an Agent Multiple-Employer Defined Benefit Other Postemployment Benefits Plan administered by CalPERS.

3. Restricted Cash and Investments

As of June 30, 2018, and 2017, the Fund had the following cash, equivalents and investments (in millions):

Investment	Maturity June 30, 2018	Maturity June 30, 2017	2018	2017
State of California Pooled Money Investment Account - Surplus Money Investment Fund	6.3 months avg.	6.4 months avg.	$ 1,237	$ 1,170
Cash			3	2
Total cash and equivalents			1,240	1,172
Guaranteed investment contracts	May 1, 2022	May 1, 2022	200	200
Forward purchase agreement	November 1, 2018	November 1, 2017	102	102
			$ 1,542	$ 1,474

	2018	2017
Reconciliation to Statements of Net Position:		
Debt Service Reserve Account	$ 884	$ 884
Administrative Cost Account	12	11
Operating Account	38	24
Bond Charge Collection and Bond Charge Payment Accounts	608	555
	$ 1,542	$ 1,474

Custodial Credit Risk: Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party. The State of California has a deposit policy for custodial credit risk that requires deposits held by financial institutions to be insured by federal depository insurance or secured by collateral held in the State's name. At June 30, 2018 and 2017, one of the guaranteed investment contracts in the amount of $100 million was uninsured and uncollateralized.

Interest Rate Risk: Interest rate risk is the risk that the value of fixed income securities will decline because of changing interest rates. The prices of fixed income securities with a longer time to maturity, measured by effective maturity, tend to be more sensitive to changes in interest rates and, therefore, more volatile than those with shorter maturities. The State Treasurers Investment Policy, Pooled Money Investment Account, provides for spreading investments over various maturities to minimize the risk of portfolio depreciation due to a rise in interest rates. The State Treasurers Investment Policy limits investments to the following maximum maturities: U.S. Treasury securities, 5 years; federal agency securities, 5 years; bankers acceptances – domestic and foreign, 180 days; certificates of deposits, 5 years; commercial paper, 180 days; corporate bonds and notes, 5 years; repurchase agreements and reverse repurchase agreements, 1 year.

Credit Risk: Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The PMIA funds are on deposit with the State's Centralized Treasury System and are managed in compliance with the California Government Code, according to a statement of investment policy which sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. These investments consist of U.S. government securities, securities of federally-sponsored agencies, U.S. corporate bonds, interest bearing time deposits in California banks, primerated commercial paper, bankers' acceptances, negotiable certificates of deposit, repurchase and reverse repurchase agreements. The PMIA policy limits the use of reverse repurchase agreements to limits of no more than 10% of the PMIA and commercial paper to limits not to exceed 30% of the PMIA. The PMIA does not invest in leveraged products or inverse floating rate securities. The PMIA is not rated.

Concentration of Credit Risk: The SMIF concentration of credit risk is limited by spreading the investment mix over different investment types and issuers to minimize the impact any one industry, investment class, or institution can have on the SMIF portfolio. At June 30, 2018 and 2017, the Fund's investments in the FPA and two GICs individually exceed 5.0% of total investments. The ratings of the investments and their relative percentages of total investments is shown in the following table:

	Amount	S&P Credit Rating	Percent of Total Investments 2018	Percent of Total Investments 2017
FPA Provider				
Merrill Lynch: Federal Home Loan Mortgage Corporation Discounted Notes	$ 102	Not Rated	6.59%	6.91%
GIC Providers				
FSA	$ 100	Not Rated	6.48%	6.78%
Royal Bank of Canada	100	Not Rated	6.48%	6.78%
	$ 200			

Interest on deposits in the SMIF varies with the rate of return of the underlying portfolio and approximated 1.5% and 0.9% at June 30, 2018 and 2017, respectively. For the years ended June 30, 2018 and 2017, interest earned on the deposit in the SMIF was $19 million and $10 million, respectively.

Interest on the GICs is paid semi-annually at interest rates ranging from 5.3% to 5.5%. Interest earned on the GICs was $11 million for the years ended June 30, 2018 and 2017.

The FPA allows the Fund to continuously reinvest funds in U.S. government or U.S. government agency securities through May 2022 to earn a minimum rate of return of 4.7%, as specified in the Reserve Fund FPA, dated May 1, 2004. The reinvested securities are to mature every six months. Interest earned on the FPA was $5 million for the years ended June 30, 2018 and 2017.

Fair Market Value Measurement: The Fund categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; level 2 inputs are significant other observable inputs; level 3 are significant unobservable inputs. Guaranteed Investment Contracts are reported as cost.

The Fund has the following recurring fair value measurements at June 30, 2018:

- The FPA of $102 million is valued using market approach (Level 2)

4. Long-Term Debt

The following activity occurred in the long-term debt accounts during the years ended June 30, 2018 and 2017 (in millions):

	Revenue Bonds	Unamortized Premium	Total
Balance, June 30, 2016	$ 4,609	$ 271	$ 4,880
Refunding			
Issuance of Debt	567	-	567
Defeasance of Debt	(555)	(5)	(560)
Payments	(690)	-	(690)
Amortization	-	(69)	(69)
Balance, June 30, 2017	3,931	197	4,128
Payments	(719)	-	(719)
Amortization	-	(61)	(61)
Balance, June 30, 2018	3,212	136	3,348
Less current portion	754	52	806
	$ 2,458	$ 84	$ 2,542

Long-term debt consists of the following at June 30, 2018 and 2017, respectively (in millions):

Series	Rates	Fiscal Year of Final maturity	Fiscal Year of First Call Date	Amount Outstanding 2018	Amount Outstanding 2017	2018 Current Portion
G	Fixed (4.38-5.00%)	2018	Non-callable		$ 75	
H	Fixed (4.70-5.00%)	2022	2018		25	
K	Fixed (4.00%)	2018	Non-callable		279	
L	Fixed (3.50-5.00%)	2022	2020	$ 1,062	1,258	$ 561
M	Fixed (3.00-5.00%)	2020	Non-callable	157	199	153
N	Fixed (3.00-5.00%)	2021	Non-callable	669	766	35
O	Fixed (2.00-5.00%)	2022	Non-callable	766	766	-
P	Fixed (1.71-2.00%)	2022	Non-callable	558	563	5
				3,212	3,931	754
Plus unamortized bond premium				136	197	52
				$ 3,348	$ 4,128	$ 806

Bond Debt Refunding Transaction

On September 28, 2016, the Fund issued $567 million of Series P refunding revenue bonds. Proceeds of $566 million from the refunding bonds, less $2 million for issuance expenses and $38 million released from the Debt Service Reserve and Bond Charge Payment accounts totaling $603 million, were used to purchase securities that were deposited in an irrevocable trust with an escrow agent that will provide resources sufficient to pay the future debt service on the advance refunded $555 million of outstanding Series F and Series H revenue bonds. As a result, the refunded bonds are considered defeased and have been removed from the Statement of Net Position. This loss on the bond refunding is reported as deferred outflows of resources on the Statement of Net Position and will be amortized over the life of the refunding bonds. As of June 30, 2018, the outstanding balance of refunded bonds is $294 million

Key Terms

Principal and interest payments are payable from bond charges. The Fund is subject to certain bond covenants, including establishing funding and expenditure requirements for several restricted cash and investment accounts. The bonds are limited special obligations of the Fund. Neither the principal nor any interest thereon constitutes a debt of the State of California.

The Series H and L are callable at a redemption rate of 100 percent in 2020. The Series G, K, M, N, O and P are non-callable.

Maturities

Future payment requirements on the revenue bonds are as follows at June 30, 2018 (in millions):

Fiscal Year	Principal	Interest	Total
2019	$ 754	$ 140	$ 894
2020	790	104	894
2021	803	67	870
2022	865	34	899
	$ 3,212	$ 345	$ 3,557

5. Commitments and Contingencies

Litigation and Regulatory Proceedings

Certain pending legal and administrative proceedings involving the Fund or affecting the Fund's power supply program are summarized below.

California Refund Proceedings: During 2001 and 2002, the Fund purchased power in bilateral transactions (both short-term and long-term), sold power to the California Independent System Operator (CAISO), paid for power purchased by the CAISO and purchased power from the CAISO for sale to customers of the IOUs. In July 2001, the Federal Energy Regulatory Commission (FERC) initiated an administrative proceeding to calculate refunds for inflated prices in the CAISO and California Power Exchange (PX) markets during 2000 and 2001. FERC ruled that the Fund would not be entitled in that proceeding to approximately $3,500 million in refunds associated with the Fund's approximately $5,000 million of short-term purchases because the Fund made those purchases bilaterally, not in the PX or CAISO markets. The Ninth Circuit Court of Appeals affirmed FERC, but left open the possibility of refunds on the Fund's bilateral purchases in other FERC proceedings. In contrast, FERC ruled that the Fund is entitled to refunds on purchases made by the CAISO where the Fund actually paid the bill.

Of the Fund's $5,000 million in short-term bilateral purchases, $2,900 million was imbalance energy which the Fund sold to the CAISO at the Fund's cost in order to meet the CAISO's emergency needs during 2001. The Fund is treated in the FERC refund proceeding as a seller of that energy to CAISO, and in May 2004, FERC issued an order requiring the Fund to pay refunds on the sales to the CAISO. In September 2005, the Ninth Circuit Court of Appeals held that FERC does not have authority to order refunds from governmental entities such as the Fund. In November 2008, FERC found that although FERC cannot order a governmental entity, such as the Fund, to pay refunds, it can enforce the terms of the CAISO's tariff, which requires that all purchases and sales in a given hourly settlement period are netted. But for the more than 50 refund settlements the Fund has entered into to date, this order would have resulted in a substantial reduction to the refunds payable to the Fund. Settlements executed to date with various sellers, however, have reduced to a de minimums amount, the amount by which refunds payable to the Fund will be reduced on account of the Fund's sales to the CAISO. Refund payable to the Fund will be offset to the extent that the Fund must pay refunds on its sales to the CAISO. Proceedings before FERC, including related appeals, are ongoing and could, together with the terms of any future settlements entered into by the Fund to resolve its remaining claims in the California Refund Proceedings, increase or decrease of refunds the Fund ultimately receives.

Direct Access Proceeding: On February 28, 2008, the CPUC approved a decision concluding that the suspension of direct access cannot be lifted at the present time because the Fund is still supplying power under the Act. However, the decision continued the proceeding to consider possible approaches to expediting the Fund's exit from its role of supplying power under the Act. On November 21, 2008, the CPUC adopted a plan with the goal of the early exit of the Fund from its role as supplier of power to retail electric customers. Under this plan, the Fund's power purchase contracts would be replaced by agreement between the IOUs and the Fund's power supplier counterparties that are not detrimental to ratepayers, through novation and/or negotiation.

Senate Bill 695: On October 11, 2009, Senate Bill (SB) 695 was signed into law as an urgency statute. SB 695 allows individual retail nonresidential end-use customers to acquire electric service from other providers in each IOU service area, up to a maximum allowable limit. Except for this express authorization for increased direct access transactions under SB 695, the previously enacted suspension of direct access remains in effect. On March 15, 2010, the CPUC issued Decision 10-03-022 which authorizes increases in the maximum direct access load for each IOU service area, as specified in SB 695. The maximum load of allowable direct access volume is established for each IOU as the maximum total kilowatt hour (kWh) supplied by all other providers to distribution customers of the IOU during any sequential 12-month period between April 1, 1998 and the effective date of the section of the Public Utilities code modified by SB 695, October 11, 2009.

Decision 10-03-033 phases in the additional load allowance over a four-year period beginning on April 11, 2010. The annual phase in of the limits combined with the concurrent expiration of several long-term contracts has not resulted in impacts to the Power Charges. Regardless of the level of direct access participation within the IOU service area, direct access customers will still be assessed Bond Charges and the Fund's revenue requirement will be recovered in the same manner as has been successfully implemented over the duration of the Power Supply Program.

Other Contingencies

The Fund is self-insured for most risks, including general liability and workers' compensation. Management believes the Fund's exposure to loss is immaterial and that any costs associated with such potential losses are recoverable from customers as part of the Fund's revenue requirement.

Commitments

The last remaining power purchase contract and natural gas transmission capacity contract were terminated during fiscal year 2015. The Fund is no longer exposed to future obligations related to power or natural gas purchases under any of the contracts which had been scheduled to require payments through 2018.

6. Energy and Financial Settlements

The Fund and other parties have entered into settlement agreements with various energy suppliers which resolve potential and alleged causes of action against suppliers for their part in alleged manipulation of natural gas and electricity commodity and transportation markets during the 2000 - 2001 California energy crisis, and also received settlements from other FERC actions.

Additionally, the Fund has begun to be involved in litigation with various financial institutions to resolve alleged manipulation of financial market benchmark interest rates and their impact on the Fund's bond offerings and interest rate swap agreements.

The Fund received energy settlements of $15.8 million from Shell Energy North America (US), L.P (successor-in-interest to Coral Power, LLC). On June 1, 2018 the Fund submitted a claim for $9.8 million to the Deutsch Bank LIBOR AG Settlement. While expected to be received after June 30, 2018, this amount was considered an accrual for fiscal year 2018. Total energy and bond settlements were $25.6 million for fiscal year 2018.

During fiscal year 2017 $16 million in energy settlements was received. The Fund received $3.6 million from Allegheny Energy Supply Company, $3.5 million from Commerce Energy Inc and $9.1 million from Merrill Lynch Capital Services Inc.

7. Retirement Plan

Plan Description

All of the employees of the Fund participate in the CalPERS Miscellaneous Defined Benefit Pension Plan (Plan), which is included in the State of California's (State) Comprehensive Annual Financial Report as a fiduciary component unit. CalPERS administers the Plan within the Public Employees' Retirement Fund (PERF-A). PERF-A is an agent multiple-employer defined benefit pension plan. Departments and agencies within the State, including the Fund, are in a cost-sharing arrangement in which all risks and costs are shared proportionately by participating State agencies. Since all State agencies and certain related organizations, including the Fund, are considered collectively to be a single employer for plan purposes, the actuarial present value of vested and non-vested accumulated plan benefits attributable to the Fund employees cannot be determined. The significant actuarial assumptions used to compute the actuarially determined State contribution requirements are the same as those used to compute the State pension benefit obligation as defined by CalPERS. CalPERS issues a publicly available financial report that includes financial statements and required supplementary information for this plan. This report is available online at www.calpers.ca.gov.

The California Legislature passed and the Governor signed the "Public Employees' Pension Reform Act of 2013" (PEPRA) on September 12, 2012. PEPRA contained a number of provisions intended to reduce future pension obligations. PEPRA primarily affects new pension plan members who are enrolled for the first time after December 2012. Benefit provisions and other requirements are established by State statute.

Benefits Provided

The benefits for the Plan are based on members' years of service, age, final compensation, and benefit formula. Benefits are provided for disability, death, and survivors of eligible members or beneficiaries. Members become fully vested in their retirement benefits earned to date after five or ten years of credited service.

The Plan's provisions and benefits in effect at June 30, 2018 and 2017, are summarized as follows:

First Tier:

Hire date	**Prior to January 15, 2011**	**January 15, 2011 to December 31, 2012**	**On or after January 1, 2013**
Benefit formula	2% @ 55	2% @ 60	2% @ 62
Benefit vesting schedule	5 years service	5 years service	5 years service
Benefit payments	monthly for life	monthly for life	monthly for life
Retirement age	50 to 67	50 to 67	52 to 67
Monthly benefits, as a % of eligible compensation	1.1 to 2.5%	1.092 to 2.418%	1.0 to 2.5%

Second Tier:

Hire date	**Prior to January 1, 2013**	**On or after January 1, 2013**
Benefit formula	1.25% @ 65	1.25% @ 67
Benefit vesting schedule	10 years service	10 years service
Benefit payments	monthly for life	monthly for life
Retirement age	50 to 67	52 to 67
Monthly benefits, as a % of eligible compensation	0.5 to 1.25%	0.65 to 1.25%

Contributions

Section 20814(c) of the California Public Employees Retirement Law (PERL) requires that the employer contribution rates for all public employers be determined on an annual basis by the actuary and shall be effective on the July 1 following notice of a change in the rate. The total plan contributions are determined through the CalPERS' annual actuarial valuation process. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The employer is required to contribute the difference between the actuarially determined rate and the contribution rate of employees. For the measurement periods ended June 30, 2017 and 2016 (the measurement dates) the employer's contribution rates are approximately 28.4% and 25.2. %, respectively, of annual payroll. Employer contribution rates may change if plan contracts are amended. It is the responsibility of the employer to make necessary accounting adjustments to reflect the impact due to any Employer-Paid Member Contributions or situations where members are paying a portion of the employer contribution. Contributions to the plan for the fiscal years ended June 30, 2018 and 2017, were $1.0 million and $0.5 million for each year.

Pension Liabilities, Pension Expense and Deferred Outflows/Inflows of Resources Related to Pensions

As of June 30, 2018, and 2017, the Fund reported a net pension liability for the proportionate share of the net pension liability of $5.4 million and $5.7 million, respectively.

The Fund's net pension liability for the Plan is measured as the proportionate share of the net pension liability. The net pension liability of the Plan is measured as of June 30, 2017, and the total pension liability for the Plan used to calculate the net pension liability was determined by an actuarial valuation as of June 30, 2016 rolled forward to June 30, 2017 using standard update procedures. The Funds' proportion of the net pension liability was based on the State Controller's Office (SCO) projection for the fund. The SCO identified a total of 29 entities that are reported in the State's CAFR which are proprietary funds (enterprise and internal service) and fiduciary funds (pension and other employee benefit trust funds), component units (discretely presented and fiduciary), and related organizations, that have State employees with pensionable compensation (covered payroll). The SCO calculated and provided these funds/organizations with their allocated pensionable compensation percentages by plan. The Fund's proportionate share of the net pension liability for the Plan measured as of June 30, 2017 was 0.01475%, and measured as of June 30, 2016 was 0.01741%.

For the years ended June 30, 2018 and 2017, the Fund recognized pension expense of $0.9 million and 0.9 million, respectively. At June 30, 2018 and 2017, the Fund reported deferred outflows of resources and inflows of resources related to pensions from the following sources (in millions):

	Deferred Outflows of Resources		Deferred Inflows of Resources	
	2018	2017	2018	2017
Contributions subsequent to the measurement date	$ 1.0	$ 0.5	$ -	$ -
Change in proportion	0.4	0.4	-	-
Differences between expected and actual experience	0.6	-	0.75	-
Net differences between projected and actual earnings on pension plan investments	0.2	0.7	-	-
Total	$ 2.2	$ 1.8	$ 0.75	$ -

The $1.0 million reported as deferred outflows of resources related to contributions subsequent to the measurement date at June 30, 2017 will be recognized as a reduction of the net pension liability in the year ending June 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized as pension expense as follows (in millions):

Year Ended June 30	
2019	$ 0.3
2020	0.1
2021	0.1
2022	(0.1)
Total	$ 0.4

Actuarial Assumptions

The June 30, 2016 and 2015 valuations were rolled forward to determine the June 30, 2017 and 2016, respectively, (measurement date) total pension liabilities, based on the following actuarial method and assumptions:

	2016	2015
Actuarial Cost Method	Entry-Age Normal	Entry-Age Normal
Actuarial Assumptions:		
Discount Rate	7.15%	7.65%
Inflation	2.75%	2.75%
Salary Increases	Varies (1)	Varies (1)
Investment Rate of Return	7.15% (2)	7.65% (2)
Mortality(3)	CalPERS' Membership Data	CalPERS' Membership Data
Post Retirement Benefit Increase	Up to 2.75%(4)	Up to 2.75%(4)

(1) Depending on age, service and type of employment
(2) Net of pension plan investment expenses, includes inflation
(3) The mortality table used was developed based on CalPERS specific data. The table includes 20 years of mortality improvements using Society of Actuaries Scale BB. For more details on this table, please refer to the 2014 experience study report.
(4) Contract COLA up to 2.75% until Purchasing Power Protection Allowance Floor on Purchasing Power applies

All other actuarial assumptions used in the June 30, 2016 valuation were based on the results of an actuarial experience study for the period from 1997 to 2011, including updates to salary increase, mortality and retirement rates. The Experience Study report can be obtained at CalPERS website under Forms and Publications.

Change of Assumptions

The discount rate used to measure the total pension liability was 7.15% for the Plan. In 2017, the discount rate reduced from 7.65% to 7.15%.

Discount Rate

To determine whether the municipal bond rate should be used in the calculation of a discount rate for each plan, CalPERS stress tested plans that would most likely result in a discount rate that would be different from the actuarially assumed discount rate. Based on the testing of the plans, the test revealed the assets would not run out. Therefore, the current 7.15% discount rate is appropriate, and the use of the municipal bond rate calculation is not deemed necessary. The long-term expected discount rate of 7.15% is applied to all plans in the Public Employees Retirement Fund. The stress test results are presented in a detailed report called "GASB Crossover" Testing Report" that can be obtained at CALPERS' website under the GASB 68 section.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rate of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class.

In determining the long-term expected rate of return, CALPERS took into account both short-term and long-term market return expectations as well as the expected pension fund cash flows. Such cash flows were developed assuming that both members and employers will make their required contributions on time and as scheduled in all future years. Using historical returns of all the funds' asset classes, expected compound (geometric) returns were calculated for each fund. The expected rate of return was set by calculating the single equivalent return that arrived at the same present value of benefits for cash flows as the one calculated using both short-term and long-term returns. The expected rate of return was then set equivalent to the single equivalent rate calculated above and rounded down to the nearest one quarter of one percent.

The following table reflects long-term expected real rate of return by asset class. The rate of return was calculated using the capital market assumptions applied to determine the discount rate and asset allocation. The target allocation shown was adopted by the CALPERS' Board of Administration effective of July 1, 2014.

Asset Class	New Strategic Allocation	Real Return Years 1 – 10 (a)	Real Return Years 11+ (b)
Global Equity	47.0%	4.90%	5.38%
Global Fixed Income	19.0%	0.80%	2.27%
Inflation Sensitive	6.0%	0.60%	1.39%
Private Equity	12.0%	6.60%	6.63%
Real Estate	11.0%	2.80%	5.21%
Infrastructure and Forestland	3.0%	3.90%	5.36%
Liquidity	2.0%	-0.40%	-0.90%
Total	100.0%		

(a) An expected inflation of 2.5% used for this period.
(b) An expected inflation of 3.0% used for this period.

Sensitivity of the Fund's Proportionate Share Net Pension Liability to Changes in the Discount Rate

The following table presents the Fund's proportionate share of Plan's net pension liability as of the measurement date, calculated using the discount rate of 7.15%, as well as what the net pension liability would be if it were calculated using a discount rate that is 1 percentage-point lower (6.15%) or 1 percentage-point higher (8.15%) than the current rate (amounts in thousands):

	Discount Rate -1% (6.15%)	Current Discount Rate(7.15%)	Discount Rate +1% (8.15%)
The Fund's Proportionate Share of Plan's Net Pension Liability	$ 7	$ 5	$ 4

8. Other Post-Employment Health Care Benefits (OPEB)

Plan Description - The State of California provides medical and prescription drug benefits to retired state employees and dependents through CalPERS, an agent multiple-employer public employee retirement system that acts as a common investment and administrative agent for participating public entities within the State of California under the Public Employees' Medical and Hospital Care Act. Dental benefits are provided under the State Employee' Dental Care Act. Departments and agencies within the State, including the Fund, are in a cost-sharing arrangement in which all risks and costs are shared proportionately by participating State agencies. Since all State agencies and certain related organizations, including the Fund, are considered collectively to be a single employer for plan purposes, the actuarial present value of vested and non-vested accumulated plan benefits attributable to the Fund employees cannot be determined.

Benefits Provided - A member is eligible to enroll in a CALPERS health plan if he or she retires within 120 days of separation from employment, was eligible for health benefits upon separation and receives a monthly retirement allowance. CALPERS provides healthcare benefits for retirees and their dependents through payment of insurance premiums up to the maximum State Contribution amount.

Contribution - The State and certain bargaining units and judicial employees (valuation groups) have agreed to prefund retiree healthcare benefits. Assets are held in separate accounts by valuation group within the California Employers' Retiree Benefit Trust (CERBT), an agent multiple-employer defined benefit other postemployment benefits plan administered by CALPERS. Assets within each valuation retirees and dependents associated with that valuation group. Contributions are based on a percentage compensation with the ultimate goal of contributions 100 percent of the actuarially determined normal cost shared equality between the State and employees. Pre-funding contributions and investment income are not available to pay plan benefits until the earlier of 2046 or the year that actuarial liabilities are fully funded. The State also makes pay-as-you-go contributions for benefits paid to current retirees and the portion of benefits paid to future retirees that are not prefunded for the fiscal year June 30, 2018, the Fund's total contributions was $4.8 million.

OPEB Liabilities, OPEB Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to OPEB

At June 30, 2018, the Fund reported a liability of $7.8 million for its proportionate share of the Net OPEB liability. The Net OPEB liability was measured as of June 30, 2017, and the Total OPEB liability used to calculate the net OPEB liability was determined by an actuarial valuation as of the same date. The Fund's proportion of the net OPEB liability was based on the State Controller's Office (SCO) projection for the Fund. The proportion is based off of the Fund's pensionable compensation relative to the pensionable compensation of all valuation groups which include the Fund's employee. The pensionable compensation amounts are used to calculate each state entity's proportionate share of OPEB amounts for each valuation group. At June 30, 2018, the Fund's total proportionate share of the net OPEB liability for all applicable valuation groups was 0.011%. At June 30, 2017, the Fund's total proportionate share of the net OPEB liability for all applicable valuation groups was 0.018%.

For the year ended June 30, 2018, the Fund recognized OPEB expense of $1.2 million. At June 30, 2018, the Fund reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

	Deferred Outflows of Resources 2018	Deferred Inflows of Resources 2018
Contributions subsequent to the measurement date	$ 5	$ -
Difference between actual and expected contributions	4	-
Change in assumptions	-	1
Total	$ 9	$ 1

$5 million reported as deferred outflows of resources related to OPEB resulting from amounts paid by the Fund subsequent to the measurement date will be recognized as a reduction of the Net OPEB liability in the year ended June 30, 2019. Other amounts reported as deferred outflows of resources and deferred outflows of resources related to OPEB will be recognized in OPEB expense as follows:

Year Ended June 30	
2019	$ 0.6
2020	0.6
2021	0.6
2022	0.6
2023	0.6
Thereafter	0.3
	$ 3.3

Actuarial Assumption - For the measurement period June 30, 2017 (the measurement date), the Net OPEB liability was determined using a June 30, 2017 valuation date. The June 30, 2016 beginning Net OPEB liability was determined by rolling back the June 30, 2017 Net OPEB liability. The June 30, 2017 Net OPEB liability was based on the following actuarial methods and assumptions.

Discount Rate:	Blended rate for each valuation group, consisting of 7.28% when assets are available to pay benefits, Otherwise 20-year Municipal G.O. Bond AA Index Rate of 3.56%
Inflation:	2.75%
Salary Increase:	Varies by entry age and service
Investment Rate of Return:	7.28%, net of OPEB plan investment expense
Healthcare Cost Trend Rates:	*Pre-Medicare coverage:* Actual rates for 2018, Increasing to 8.00% in 2019, decreasing 0.50% per year to an ultimate rate of 4.5% for 2027 and later years. *Post - Medicare coverage:* Actual rates for 2018, Increasing to 8.5% in 2019, decreasing 0.5% per year to an ultimate rate of 4.5% for 2027 and later years. *Dental coverage:* 0.00% in 2018 and 4.5% thereafter.
Mortality Rate Table:	Derived using CALPERS' membership data for all Member

The mortality table used was developed based on CALPERS' specific data. The table includes 20 years of mortality improvements using the Society of Actuaries Scale BB. Other demographic assumptions used in the June 30 ,2017 valuation were also based on the results of the Experience Study, including updates to termination, disability, mortality assumptions and retirement rates.

Healthcare related assumptions such as plan participation, aging factors, adjustments for disabled members, and adjustments for children of current retirees and survivors are based on the 2015 experience study performed by Gabriel, Roeder, Smith and Company (GRS) for the period 2007 to 2014. Other healthcare assumptions such as member healthcare plan selection, coverage and continuance, select and ultimate healthcare cost trend rates, and per capita claim costs and expense, are based on the most current information available.

Discount Rate - The discount rate used to measure the Net OPEB liability was based on a blended rate for each valuation group. The blended rate used to measure the June 30, 2016 Net OPEB liability consists of the 20-Bond G.O. Index rate of 2.85% as of June 30, 2016, as reported by Bond Buyer Index (general obligation, 20 years to maturity, mixed quality), when prefunding assets are not available to pay benefits, and 7.28% when prefunding assets are available to pay benefits. The blended rate used to measure the June 30, 2017 Net OPEB liability consists of the 20-year Municipal G.O. Bond AA Index rate of 3.56% as of June 30, 2017, as reported by Fidelity Index, when prefunding assets are not available to pay benefits, and 7.28% when prefunding assets are available to pay benefits. The cash flow projection used to calculate the blended discount rate were developed assuming that prefunding agreements in which actuarially determined normal costs are shared between employees and the State will continue and that the required contributions will be made on time and as scheduled in future years. The prefunding agreements are subject to collective bargaining and legislative approval.

The long-term expected rate of return on OPEB plan investments was determined by CALPERS using a building-block method in which expected future real rates of return (expected returns, net of OPEB plan investment expense and inflation) are developed for each major asset class. Expected compound (geometric returns were calculated over a closed period. Based on separate expected nominal returns for the short-term (first 10 years) and the long-term (11-60 years), a single expected nominal returns rate of 7.28% was calculated for year 1-60. If applied to expected cash flows during that period, the resulting present value of benefits is expected to be consistent with the present value of benefits that would be determined by applying the short and long-term expected rates to the same cash flows.

The following table reflects the long-term real rate of return by assets class:

Assets Class	Target Asset Allocation	Real Returns Years 1-20	Real Returns Year 11-20
	%	%	%
Global Equity	57.00	5.25	5.71
Global Fixed Income	27.00	1.79	2.40
Inflation Sensitive	5.00	1.00	2.25
Real Estate	8.00	3.25	7.88
Commodities	3.00	0.34	4.95

Real Return Years 1-10 used an expected inflation rate of 2.5% for this period. The Real Return Years 11-60 used an expected inflation rate of 3.00% for this period.

Sensitivity of the Fund's Proportionate Share of the Net OPEB liability to Changes in the Discount Rate – The following presents the Fund's proportionate share of the Net OPEB liability, as well as what the Fund's proportionate share of the Net OPEB liability would be if it were calculated using a discount rate that is 1- percentage-point lower or 1-percentage higher than the current discount rate:

	1% Decrease	Blended Discount Rate	1% Increase
Net OPEB Liability	$ 9	$ 8	$ 7

Sensitive of the Fund's Proportionate Share of the Net OPEB liability to Changes in the Healthcare Cost Trend Rates – The following presents the Fund's proportionate share of the Net OPEB liability, as well as what the Fund's proportionate share of the Net OPEB liability would be if it were calculated using healthcare cost trend rate that are 1-percentage-point lower or 1-percentage higher than the current healthcare cost trend rates:

	1% Decrease	Healthcare Cost Trend Rate	1% Increase
Net OPEB Liability	$ 7	$ 8	$ 9

9. Change in Accounting Principles

The Fund adopted Governmental Accounting Standards Board (GASB) Statements No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, effective July 1, 2017. Refer to Note 8 for further disclosures related to the Plan and related balances. As a result of the implementation, the Fund restated beginning recoverable costs as noted below:

Governmental Activities	June 30, 2017 Previously Presented	Restatement	July 1, 2017 Restated
Deferred Outflows of Resources Related to OPEB	$ -	$ 5.3	$ 5.3
Other Postemployment Benefit (OPEB) Liability		(8.2)	(8.2)
Other Postemployment Benefit (OPEB) Obligation	(7.0)	7.0	
Recoverable Costs - Beginning of Year	$ 3.0	$ 4.0	$ 7.0

REQUIRED SUPPLEMENTARY INFORMATION

DEPARTMENT OF WATER RESOURCES ELECTRIC POWER FUND
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF THE FUND'S PROPORTIONATE
SHARE OF THE NET PENSION LIABILITY
Last 10 Years*
(in millions)

	2018	2017	2016	2015
Measurement Period	2017	2016	2015	2014
The Fund's proportion of the net pension liability	0.01475%	0.01741%	0.01921%	0.01777%
The Fund's proportionate share of the net pension liability	$ 5	$ 6	$ 5	$ 5
The Fund's covered-employer payroll	$ 2	$ 2	$ 2	$ 2
The Fund's proportionate share of the net pension liability as a percentage of their covered-employee payroll	250.00%	300.00%	250.00%	250.00%
Plan fiduciary net position as a percentage of the total pension liability	66.42%	66.81%	70.68%	73.05%

Notes to Schedule:

Change of benefit terms: For all years presented, there were no changes to the benefit terms.

Change in assumptions: GASB 68 states that the long-term expected rate of return should be determined net of pension plan investment expenses, but without reduction for pension plan administrative expenses. The discount rate changed from 7.65% (net of adminitrative expenses in 2016) to 7.15% as of the June 30, 2017 measurement date to correct the adjustment, which previously reduced the discount rate for administrative expenses.

*Fiscal year 2015 was the 1st year of implementation, therefore only four years are shown.

DEPARTMENT OF WATER RESOURCES ELECTRIC POWER FUND
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF THE FUND'S CONTRIBUTIONS
Last 10 Years*
(in millions)

	2018	2017	2016	2015
Contractually required contribution	$ 1	$ 0.5	$ 0.5	$ 0.5
Contribution in relation to the contractually required contribution	1	0.5	0.5	0.5
Contribution deficiency (excess)	$ -	$ -	$ -	$ -
Fund's covered-employee payroll	$ 1.8	$ 1.9	$ 1.9	$ 2.0
Contributions as a percentage of covered-employee payroll	55.56%	26.32%	26.32%	25.00%

*Fiscal year 2015 was the 1st year of implementation, therefore only four years are shown.

DEPARTMENT OF WATER RESOURCES ELECTRIC POWER FUND
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF THE FUND'S PROPORTIONATE SHARE OF THE NET OPEB LIABILITY
Last 10 Years*
(in millions)

		2018
The funds proportion of the net OPEB liability		0.011%
The funds proportionate share of the net OPEB liability	$	8
The funds covered payroll	$	2
The funds proportionate share of the net OPEB liability as a percentage of its covered payroll		456.062%
Plan fiduciary net position as a percentage of the total OPEB liability		0.003%

*Fiscal year 2018 is the 1st year of implementation, therefore only one year are shown.

DEPARTMENT OF WATER RESOURCES ELECTRIC POWER FUND
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF THE FUND'S CONTRIBUTION
Last 10 Years*
(in millions)

	2018
Contractually required contribution	$ 5
Contribution in relation to the contractually required contribution	(5)
Contribution deficiency (excess)	$ -
Fund's covered payroll	$1,710,263.18
Contributions as a percentage of covered payroll	292.4%

*Fiscal year 2018 is the 1st year of implementation, therefore only one year are shown.

INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

To the Director of the State of California Department of Water Resources
Department of Water Resources Electric Power Fund
Sacramento, California

We have audited, in accordance with the 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, the financial statements of the State Water Resources Electric Power Fund (Fund), an enterprise fund of the State of California, as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements, and have issued our report thereon dated March 26, 2019. Our report contained an emphasis of matter paragraph regarding the Fund's adoption of Governmental Accounting Standards Board (GASB) Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions.* Our report also contained an emphasis of matter paragraph regarding that the financial statements present only the Fund and do not purport to and do not present fairly the financial position of the State of California as of June 30, 2018.

Internal Control over Financial Reporting

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

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

2151 River Plaza Dr., Suite 308, Sacramento, CA 95833 P 916.570.1880 F 916.570.1875 W vtdcpa.com

Compliance and Other Matters

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

Purpose of this Report

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

Vavrinek, Trine, Day & Co. LLP

Sacramento, California
March 26, 2019