



**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

Financial Statements and
Required Supplementary Information

June 30, 2017 and 2016

(With Independent Auditors' Report Thereon)

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

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Independent Auditors' Report

The Board of Water and Power Commissioners
City of Los Angeles
Department of Water and Power:

Report on the Financial Statements

We have audited the accompanying financial statements of the City of Los Angeles Department of Water and Power Power Revenue Fund (Power System), an enterprise fund of the City of Los Angeles, California, as of and for the years ended June 30, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the Power System's basic financial statements for the years then ended 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 U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free 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 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 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the City of Los Angeles Department of Water and Power Power Revenue Fund as of June 30, 2017 and 2016, and the changes in its financial position and its cash flows for the years then ended, in accordance with U.S. generally accepted accounting principles.



Emphasis of Matter

As discussed in note 1a to the financial statements, the financial statements present only the Power System and do not purport to, and do not, present fairly the financial position of the City of Los Angeles, California as of June 30, 2017 and 2016 the changes in its financial position, or where applicable, its cash flows for the years then ended in accordance with U.S. generally accepted accounting principles. Our opinion is not modified with respect to this matter.

Other Matter

Required Supplementary Information

U.S. generally accepted accounting principles require that the Management’s Discussion and Analysis on pages 3–17 and the other required supplementary information on pages 87–89 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 December 13, 2017, on our consideration of the Power System’s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on 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 Power System’s internal control over financial reporting and compliance.

KPMG LLP

Los Angeles, California
December 13, 2017

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Management's Discussion and Analysis

(Unaudited)

June 30, 2017 and 2016

The following discussion and analysis of the financial performance of the City of Los Angeles Department of Water and Power's Power Revenue Fund (the Power System) provides an overview of the financial activities for the fiscal years ended June 30, 2017 and 2016. Descriptions and other details pertaining to the Power System are included in the notes to the financial statements. This discussion and analysis should be read in conjunction with the Power System's financial statements, which begin on page 18.

Using this Financial Report

This annual financial report consists of the Power System's financial statements and required supplementary information and reflects the self-supporting activities of the Power System that are funded primarily through the sale of energy, transmission, and distribution services to the public it serves.

Statements of Net Position; Statements of Revenues, Expenses, and Changes in Net Position; and Statements of Cash Flows

The financial statements provide an indication of the Power System's financial health. The statements of net position include all of the Power System's assets, deferred outflows, liabilities, deferred inflows, and net position using the accrual basis of accounting, as well as an indication about which assets can be utilized for general purposes and which assets are restricted as a result of bond covenants and other commitments as of June 30, 2017 and 2016. The statements of revenues, expenses, and changes in net position report all of the revenues and expenses during the fiscal years ended June 30, 2017 and 2016. The statements of cash flows report the cash provided by and used in operating activities, noncapital financing activities, capital and related financing activities, and investing activities during the fiscal years ended June 30, 2017 and 2016.

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The following table summarizes the financial condition and changes in net position of the Power System as of and for the fiscal years ended June 30, 2017, 2016, and 2015:

**Table 1 – Condensed Schedule of Assets, Deferred Outflows, Liabilities,
Deferred inflows, and Net Position**

(Amounts in millions)

Assets and Deferred Outflows	June 30		
	2017	2016	2015
Utility plant, net	\$ 10,773	10,322	9,926
Restricted investments	593	595	642
Other noncurrent assets	3,045	2,947	3,232
Current assets	2,449	2,484	2,292
Deferred outflows	1,098	514	619
	<u>\$ 17,958</u>	<u>16,862</u>	<u>16,711</u>
 Net Position, Liabilities and Deferred Inflows			
Net position:			
Net investment in capital assets	\$ 1,433	1,342	1,235
Restricted	1,484	1,396	1,582
Unrestricted	2,851	2,853	2,599
Total net position	<u>5,768</u>	<u>5,591</u>	<u>5,416</u>
Long-term debt, net of current portion	9,276	8,943	8,568
Other long-term liabilities	1,575	858	962
Current liabilities	980	864	898
Deferred inflows	359	606	867
	<u>12,190</u>	<u>11,271</u>	<u>11,295</u>
	<u>\$ 17,958</u>	<u>16,862</u>	<u>16,711</u>

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Table 2 – Condensed Schedule of Revenues, Expenses, and Changes in Net Position

(Amounts in millions)

	Year ended June 30		
	2017	2016	2015
Operating revenues:			
Residential	\$ 1,180	1,127	1,034
Commercial and industrial	2,331	2,308	2,201
Sales for resale	88	73	94
Other	99	9	8
Total operating revenues	<u>3,698</u>	<u>3,517</u>	<u>3,337</u>
Operating expenses:			
Fuel for generation and purchased power	(1,458)	(1,356)	(1,400)
Maintenance and other operating expenses	(1,107)	(1,096)	(1,045)
Depreciation and amortization	(521)	(540)	(496)
Total operating expenses	<u>(3,086)</u>	<u>(2,992)</u>	<u>(2,941)</u>
Operating income	<u>612</u>	<u>525</u>	<u>396</u>
Nonoperating revenues (expenses):			
Investment income	22	65	50
Federal bond subsidies	33	33	33
Other nonoperating revenue, net	59	20	17
Debt expense, net	(317)	(267)	(260)
Total nonoperating revenues (expenses), net	<u>(203)</u>	<u>(149)</u>	<u>(160)</u>
Income before capital contributions and transfers	409	376	236
Capital contributions	32	66	67
Transfers to the reserve fund of the City of Los Angeles	(264)	(267)	(266)
Increase in net position	177	175	37
Beginning balance of net position	<u>5,591</u>	<u>5,416</u>	<u>5,379</u>
Ending balance of net position	<u>\$ 5,768</u>	<u>5,591</u>	<u>5,416</u>

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Assets

Utility Plant

During fiscal years 2017 and 2016, the Power System's net utility plant increased \$450 million and \$396 million, respectively. Net utility plant consists of significant investments in generation, transmission, distribution, and general plant infrastructure and fuel resources less accumulated depreciation.

During fiscal year 2017, utility plant additions totaled \$930 million. Approximately \$343 million of the \$930 million in additions were construction work in progress (CWIP) expenditures and the remaining \$587 million were direct additions to utility plant categories. Major CWIP additions/expenditures during the year included \$18 million for 138 KV underground transmission cable, \$22 million for Scattergood-Olympic cable, \$22 million Castaic Power Plant minor additions and betterments, \$20 million for Substation Automation Systems, and \$16 million to replace Sylmar Converter Station AC filters. About \$550 million in CWIP projects were transferred from CWIP to plant accounts. Transfers from CWIP included \$243 million for the Barren Ridge to Haskell Canyon 230 KV transmission line, \$69 million for infrastructure for smart grid project, \$46 million for refurbishment of Unit 7 at Castaic Power Plant, \$37 million for construction of new 138 KV rack positions at Receiving Station Q, \$36 million for Harbor to Gramercy lines 1 & 2, and \$27 million for transformer bank replacements at various receiving stations. The completion of these large projects along with current year CWIP additions caused the balance in the CWIP account to decrease to \$207 million.

Direct additions are mostly related to improvements in distribution infrastructure as part of the Power System's Power Reliability Program (PRP). Many of the Department's assets were installed between 1920 and 1970. The PRP is a program that evaluates and prioritizes which assets should be replaced first to reduce the frequency of electric service disruptions and the duration of each disruption. Approximately, \$454 million and \$47 million were direct additions to distribution and transmission plant accounts, respectively.

The accumulated depreciation balance decreased by a net of \$485 million in fiscal year 2017, which included retirements of \$936 million offset by annual depreciation of \$451 million. Retirements were identified during the 2016 Depreciation Study. With the adoption of the 2016 Depreciation Study on July 1, 2016, the Power System now uses the straight-line depreciation method for all assets.

For fiscal year 2016, utility plant additions were \$966 million. Approximately \$421 million of the \$966 million in additions were CWIP expenditures and the remaining \$545 million were direct additions to utility plant categories. Direct additions are mostly related to improvements in distribution infrastructure as part of the Power System's PRP.

Additions from CWIP were mostly for additional generating station and transmission system assets. During fiscal year 2016, approximately \$1,275 million was transferred from CWIP to plant accounts. As part of the Power System's plan to discontinue using ocean water for cooling purposes (Once Through Cooling Program), Scattergood Unit 3 was placed into service December 2015, which cost approximately \$888 million to construct. The Power System also upgraded five main generating units for the modernization of Castaic Power Plant. Transmission structures and improvements included constructing 65 miles of overhead transmission from Barren Ridge to Haskell Switching Station, constructing a new Haskell Canyon Switching

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Station, and constructing 11 miles of underground cables between Scattergood Generating Station and Receiving Station K. With the completion of these large projects, the balance in the CWIP account decreased \$854 million.

In fiscal year 2016, accumulated depreciation increased \$537 million. The Power System used the straight-line depreciation method for assets completed after July 1, 1973, and the 5.0% sinking fund method for assets prior to 1973 based on estimated service lives. The increase in accumulated depreciation was mostly due to depreciation recognized on generation and distribution plant assets, and the write-down of the Navajo Generation Station. As discussed above, the Power System changed its depreciation method effective July 1, 2016.

Additional information regarding the Power System's utility plant assets can be found in note 3 to the financial statements.

The Department is a vertically integrated utility, meaning it owns its own energy-generating assets, transmission system, and distribution system. The Department has diverse power resources with net dependable capacity at 120% of peak demand. The tables that follow summarize the generating resources available to the Department as of June 30, 2017. These resources include those owned by the Department (either solely or jointly with other utilities), as well as resources available through long-term purchase agreements. Generating station capacity is measured in megawatts (MWs).

Department-Owned Facilities

<u>Type of fuel</u>	<u>Number of facilities</u>	<u>Number of units</u>	<u>Net maximum capacity (MWs)</u>	<u>Net dependable capacity (MWs)</u>
Natural gas	4 ⁽¹⁾	29	3,420 ⁽⁴⁾	3,319 ⁽⁴⁾
Large hydro	1 ⁽²⁾	7	1,265	1,265
Renewables	39	209 ⁽³⁾	462 ⁽⁴⁾	285 ⁽⁴⁾
Subtotal	44	245	5,147	4,869
Less payable to the California Department of Water Resources	—	—	(120) ⁽⁵⁾	(53) ⁽⁵⁾
Total	<u>44</u>	<u>245</u>	<u>5,027</u>	<u>4,816</u>

⁽¹⁾ Consists of the four Los Angeles Basin Stations (Haynes, Valley, Harbor, and Scattergood)

⁽²⁾ The Castaic Plant is undergoing modernization work scheduled to be completed by 2019.

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- (3) Includes 21 of the hydro units at the Los Angeles Aqueduct, Owens Valley, and Owens Gorge hydro units that are certified as renewable resources by the California Energy Commission. Also included are microturbine units at the Lopez Canyon Landfill, Department-built photovoltaic solar installations, the Pine Tree Wind Project, the Linden Wind Energy Project, and a local small hydro plant. Not included are the units that were upgraded at the Castaic Plant or the two Scattergood Generating Station gas-fueled units that partially burn digester gas.
- (4) Included as renewables and excluded from natural gas are the 16 MWs of renewable energy generated at the Scattergood Generating Station by the burning of digester gas from the Hyperion Sewage Treatment Plant.
- (5) Energy payable to the California Department of Water Resources for energy generated at the Castaic Plant This amount varies weekly up to a maximum of 120 MWs.

Jointly Owned Facilities

Type	Number of facilities ⁽⁵⁾	Department's net maximum capacity entitlement (MWs)	Department's net dependable capacity entitlement (MWs)
Coal	1	1,202 ⁽¹⁾	1,202
Natural gas	1	532	480
Large hydro	1	496 ⁽²⁾	304
Nuclear	1	387 ⁽³⁾	380
Renewables/distributed generation (DG)	27,705 ⁽⁴⁾	2,065	605
Total	<u>27,709</u>	<u>4,682</u>	<u>2,971</u>

- (1) The Department's Intermountain Power Project (IPP) entitlement is 48.6% of the maximum net plant capacity of 1,800 MWs. An additional 18.2% portion of the IPP entitlement is subject to variable recall. The IPP is owned by the Intermountain Power Agency, a subdivision of the State of Utah.
- (2) The Department's Hoover Power Plant contract entitlement is 496 MWs, 23.9% of the Hoover total contingent capacity. Hoover Power Plant (Hoover) output constantly varies due to lower water levels at Lake Mead resulting from the drought conditions. The increased snowpack during early 2017 calendar year has been beneficial. The Power System's estimated average net dependable plant capacity based on the U.S. Department of the Interior for FY2016–2017 is 304 MWs.
- (3) The Department's Palo Verde Nuclear Generating Station entitlement is 9.7% of the maximum net plant capacity of 4,003 MWs.

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- (4) The Department's contract renewable resources in service include landfill gas units at certain landfills in the Los Angeles area; biogas fuel purchases out of state; hydro unit locally; and wind farms in Oregon.
- (5) The Department is a member of the Southern California Public Power Authority (SCPPA), which is a California Joint Powers Agency that finances the construction or acquisition of generation, transmission, and renewable energy projects. The Department records its transactions with SCPPA as purchased power expense as the assets purchased by SCPPA are on SCPPA's financial statements.

Other Noncurrent Assets and Deferred Outflows

During fiscal year 2017, other noncurrent assets had a net increase of \$98 million primarily due to the reclassification of \$100 million from current unrestricted cash to fund the Rate Stabilization Fund and an increase of \$108 million to regulatory assets primarily for costs related to energy efficiency programs, offset by a decrease in notes receivable of \$55.2 million, a decrease in regulatory assets associated with pension of \$55.6 million, and decreases in underrecovered costs of \$30 million.

Deferred outflows increased approximately \$585 million due primarily to a \$576 million increase in deferred outflows related to pension, which represents the current year's recognition of deferred outflows due to changes in assumptions and net excess of projected earnings on plan investments over actual earnings, a \$21 million increase in the year-over-year pension contributions made after the measurement date, offset by a \$9 million decrease in gas derivative instruments due to the maturity of natural hedges, and a \$4 million decrease in deferred outflows on debt refunding due to amortization of gains and losses on bond refinancing.

During fiscal year 2016, other noncurrent assets decreased \$336 million primarily due to a net decrease of \$268 million in the regulatory asset for pension due to amortization, which is calculated as the difference between the Power System's contributions to the retirement plan and the pension expense for the year; \$75 million decrease in restricted cash and cash equivalents for construction purposes due to replenishing current cash for construction related costs; \$19 million decrease in long-term notes and other receivables due to maturities; and a \$30 million decrease in underrecovered costs due to the allowable recovery of legacy unrecovered energy and power reliability costs. These decreases were offset by a \$97 million net increase in certain regulatory assets due to greater customer participation in the Departments' Solar Incentive and Energy Efficiency programs and costs incurred to remediate issues related to Customer Care and Billing system. Other increases related to an increase of \$5 million in the postemployment asset due to higher funding than actuarially required contributions and a \$10 million increase in the self-insurance cash fund. Deferred outflows decreased approximately \$106 million due primarily to the maturity of natural gas derivative instruments of \$20 million and a \$70 million decrease in deferred outflows related to pension, which represents the current year's amortization.

Current Assets

During fiscal year 2017, current assets decreased \$35 million, or 1.4%. The majority of the decrease was due to a \$214 million increase in the current portion of underrecovered costs due to less consumption than forecasted causing pass-through revenue to decrease and not be adequate to cover forecasted costs; a \$41 million increase in net accounts receivable due to a \$75 million year-over-year increase in the accounts

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receivable gross balance, net of a \$34 million increase in the Power System's allowance based on management's analysis of aged accounts; and a \$27 million increase in the current portion of long-term notes receivable due to higher scheduled note maturities. Cash and cash equivalents, unrestricted decreased \$340 million due to higher expenditures; debt service costs, and the reclassification of approximately \$140 million from unrestricted to restricted cash and cash equivalents. Cash and cash equivalents, restricted increased \$88 million due to higher principal and interest payments and \$40 million from the sales of emission credits for which the proceeds must be used for carbon-reducing activities.

During fiscal year 2016, current assets increased \$197 million, or 8.6%. The majority of the increase was due to cash and cash equivalents, unrestricted, which increased \$225 million due to reimbursements from the construction fund for capital expenditures and a \$44 million decrease in net accounts receivable due to an increase of \$34 million to the Department's allowance based on management's analysis of aged accounts; an increase in materials and fuel of \$53 million; an increase in cash collateral received from securities lending transactions of \$20 million; and an increase of \$25 million in accrued unbilled revenue due to higher estimated consumption; offset by a \$65 million decrease in the current portion of long-term notes receivable due to lower scheduled note maturities; and a \$20 million decrease in cash and cash equivalents, restricted due to lower principal and interest payments.

Liabilities and Net Position

Long-Term Debt

As of June 30, 2017, the Power System's total outstanding long-term debt balance, including the current portion was approximately \$9.5 billion. The increase of \$365 million over the prior year's balance resulted from the sale of \$845.4 million in the Power System's revenue bonds issued plus \$143.4 million in issue premiums, offset by scheduled maturities of \$94.6 million, defeasance of \$455.0 million in the Power System's revenue bonds, of which \$395.6 million was defeased with new debt and the remaining defeased with operating cash, and \$74.5 million in net amortized premiums and discounts.

As of June 30, 2016, the Power System's total outstanding long-term debt balance including the current portion, was approximately \$9.2 billion. The increase of \$356 million over the prior year's balance resulted from the sale of \$768.6 million in the Power System's revenue bonds issued plus \$141.5 million in issue premiums, offset by scheduled maturities of \$113.5 million, defeasance of \$380.5 million in the Power System's revenue bonds, and \$60 million in net amortized premiums and discounts.

Outstanding principal, plus scheduled interest as of June 30, 2017, is scheduled to mature as shown in the chart below:

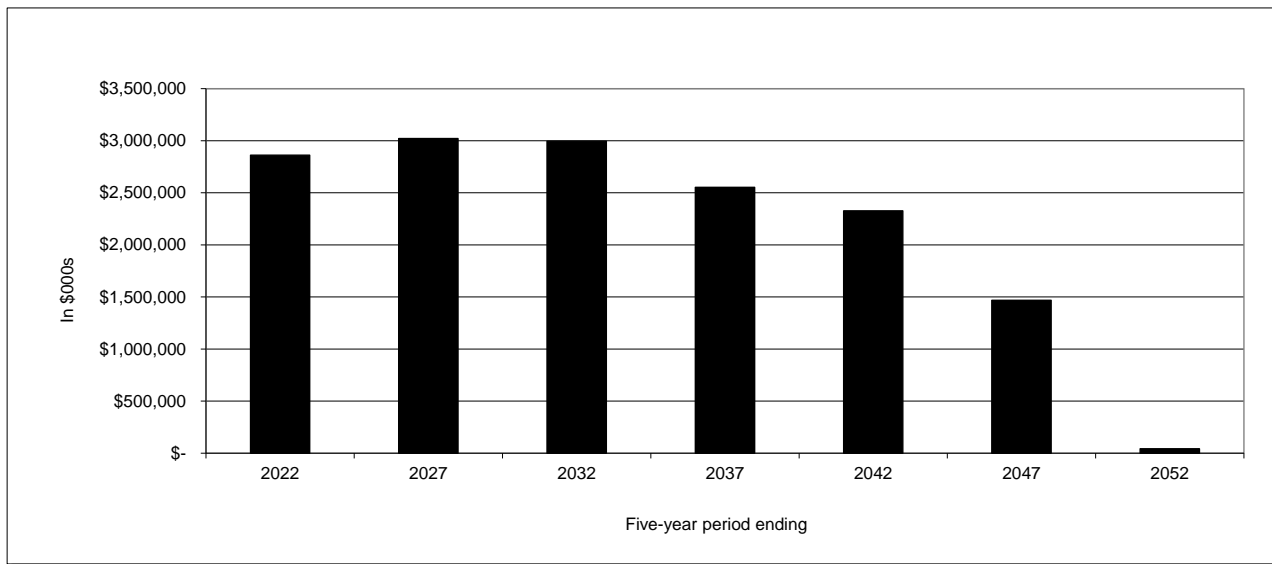
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Chart: Debt Service Requirements



In addition, the Power System had \$456.5 million and \$453.9 million in restricted investments available for the use of debt reduction as of June 30, 2017 and 2016, respectively.

In June 2017, S&P Global Ratings, Moody's Investors Service, and Fitch Ratings affirmed the Power System's bond rating of AA-, Aa2, and AA-, respectively, due to the Power System's broad revenue stream and a competitive power supply portfolio that has historically provided competitive retail electricity rates and evident strategic focus on positioning the utility to improve system reliability while meeting state mandated greenhouse emission rules and renewable energy standards.

The Master Bond Resolution allows for parity debt to be issued as long as the Department maintains debt service coverage of 1.25. The Power System debt service coverage for fiscal year 2016–2017 was 2.39.

Additional information regarding the Power System's long-term debt can be found in note 9 to the financial statements.

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Pensions

The Power System's pension liability increased \$721 million from fiscal year 2016 to 2017 and decreased \$90 million from 2015 to 2016 due to the pension activity below:

<u>Description</u>	<u>Fiscal year ended</u>		
	<u>2017</u>	<u>2016</u>	<u>2015</u>
Beginning net pension liability	\$ 771,122	860,748	1,207,513
Pension expense	214,407	(24,633)	62,173
Employer contributions	(248,620)	(256,288)	(260,077)
New net deferred inflows/outflows	661,546	75,365	(209,038)
Recognition of prior deferred inflows/outflows	94,053	115,930	60,177
Ending net pension liability	<u>\$ 1,492,508</u>	<u>771,122</u>	<u>860,748</u>

The net pension liability increased due to earning less than 1% on the market value of assets and changes in actuarial assumptions. Assuming actuarial projections are in the line with actual results, the pension liability increases with pension expense and decreases with employer contributions. Differences between expected and actual experience with economic and demographic factors; the effects of changes in assumptions about future economic and demographic factors; differences between actual and projected earnings and plan investments; differences between proportionate share of collective contributions and employer's actual contributions; and the effects of changes in proportion of the collective pension amounts are recorded as deferred outflows and deferred inflows and are amortized over periods ranging from 5 to 6 years in fiscal years 2017 and 2016.

Current Liabilities

During fiscal year 2017 current liabilities increased \$115 million, or 13%, of which \$80.1 million was related to increased accounts payable and accrued expenses, \$31.9 million was an increase in the current portion of long-term debt, \$12.8 million was an increase in accrued interest, and \$9.7 million was an increase in accrued employee expenses, offset by a reduction in securities lending obligations of \$19.7 million.

During fiscal year 2016 current liabilities decreased \$34 million, or 4%, of which \$31.3 million was related to a reduction in overrecovered costs. Reductions of \$19 million in the current portion of long-term debt were offset by an increase in securities lending obligations of \$20.4 million.

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Changes in Net Position

Operating Revenue

The Power System's rates are established by rate ordinances set by the Board of Water and Power Commissioners (the Board) based on the Board's powers and duties established in Section 676 of the City Charter. The Power System recognizes energy costs in the period incurred and accrues for estimated energy sold but not yet billed. Through a set of rate ordinances, the Power System bills its revenue through fixed and pass-through factors. As of April 15, 2016, the effective date of the 2016 Incremental Electric Rate Ordinance, all pass-through billing factors charged as part of the 2016 rates are uncapped, and a base rate revenue target was established for fiscal year 2016 through fiscal year 2020 to ensure sufficient revenue to meet fixed costs while implementing an aggressive energy efficiency program. The base rate revenue target is a decoupling mechanism that separates cost recovery from the energy usage underlying the calculated overall rate. This allows the Department to meet its financial obligations while still promoting energy conservation.

The operating revenue of the Power System is generated from wholesale and retail customers. There are four major customer categories of retail revenue. These categories include residential, commercial, industrial, and other, which includes public street lighting. Table 5 summarizes the percentage contribution of retail revenues from each customer segment in fiscal years 2017, 2016, and 2015:

Table 5 – Revenue and Percentage of Revenue by Customer Class

(Amounts in thousands)

	<u>Fiscal year 2017</u>		<u>Fiscal year 2016</u>		<u>Fiscal year 2015</u>	
	<u>Revenue</u>	<u>Percentage</u>	<u>Revenue</u>	<u>Percentage</u>	<u>Revenue</u>	<u>Percentage</u>
Type of retail customer:						
Residential	\$ 1,179,514	33 %	\$ 1,126,690	33 %	\$ 1,034,127	32 %
Commercial	2,060,490	57	2,041,906	59	1,939,870	60
Industrial	271,109	8	266,288	8	261,254	8
Other, net	98,712	2	9,220	—	7,845	—
	<u>3,609,825</u>	<u>100 %</u>	<u>3,444,104</u>	<u>100 %</u>	<u>3,243,096</u>	<u>100 %</u>
Sales for resale	<u>88,099</u>		<u>72,936</u>		<u>93,867</u>	
Total revenue	<u>\$ 3,697,924</u>		<u>\$ 3,517,040</u>		<u>\$ 3,336,963</u>	

While commercial customers consume the most electricity, residential customers represent the largest customer class. As of June 30, 2017, 2016, and 2015, the Power System had approximately 1.5 million

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customers. As shown in table 6, 1.4 million, or 91%, of total customers were in the residential customer class in fiscal years 2017, 2016, and 2015, respectively.

Table 6 – Number of Customers and Percentage of Customers by Customer Class

(Amounts in thousands)

	<u>Fiscal year 2017</u>		<u>Fiscal year 2016</u>		<u>Fiscal year 2015</u>	
	<u>Number</u>	<u>Percentage</u>	<u>Number</u>	<u>Percentage</u>	<u>Number</u>	<u>Percentage</u>
Type of retail customer:						
Residential	\$ 1,378	91 %	\$ 1,370	91 %	\$ 1,363	91 %
Commercial	113	8	113	8	113	8
Industrial	10	1	10	1	10	1
Other	7	—	7	—	7	—
	<u>\$ 1,508</u>	<u>100 %</u>	<u>\$ 1,500</u>	<u>100 %</u>	<u>\$ 1,493</u>	<u>100 %</u>

Fiscal Year 2017

Retail revenue increased \$166 million due to a \$77 million increase in base rate revenue from the Base Rate Revenue Target Adjustment (BRRTA), which sets a minimum amount of revenue to be recovered from fiscal years 2016 through 2020. Additionally, \$74 million in revenue was recognized from the incremental rate stabilization account as other operating income. Underrecovered costs of \$213.9 million were recognized as revenue and will be billed during fiscal year 2018.

Fiscal Year 2016

Retail revenue increased \$200 million in fiscal year 2016 primarily due to a \$156 million increase in base rate revenue from the BRRTA, which sets a minimum amount of revenue to be recovered from fiscal years 2016 through 2020 and higher consumption. Consumption for retail sales of electricity increased approximately 369 million kilowatt-hours year over year. The \$156 million was recognized in fiscal year 2016 as sales and underrecovered costs and will be billed over the next 24 months.

Operating Expenses

Fuel for generation and purchased power are some of the largest single operating expenses that the Power System incurs each fiscal year. Fuel for generation expense includes the cost of fuel that is used to generate energy. The majority of fuel costs include the cost of natural gas, coal, and nuclear fuel.

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

Management's Discussion and Analysis

(Unaudited)

June 30, 2017 and 2016

The table below summarizes the Power System's operating expenses during fiscal years 2017, 2016, and 2015:

Table 7 – Operating Expenses and Percentage of Expense by Type of Expense

(Amounts in thousands)

	Fiscal year 2017		Fiscal year 2016		Fiscal year 2015	
	Expense	Percentage	Expense	Percentage	Expense	Percentage
Type of expense:						
Fuel for generation	\$ 292,557	9 %	\$ 318,749	11 %	\$ 377,343	13 %
Purchased power	1,165,303	38	1,037,471	35	1,022,271	35
Other operating expenses	829,347	27	787,729	26	720,066	24
Maintenance	277,771	9	307,985	10	325,378	11
Depreciation and amortization	521,220	17	540,478	18	496,188	17
	<u>\$ 3,086,198</u>	<u>100 %</u>	<u>\$ 2,992,412</u>	<u>100 %</u>	<u>\$ 2,941,246</u>	<u>100 %</u>

Fiscal Year 2017

Fiscal year 2017 operating expenses were \$94 million higher as compared to fiscal year 2016, driven primarily by a \$128 million increase in purchased power costs, a \$42 million increase in other operating expenses, offset by \$26 million decrease in fuel for generation costs, a \$30 million decrease in maintenance expenses, and a \$19 million decrease in depreciation and amortization expense.

The \$128 million increase in purchased power costs can be primarily attributed to energy purchased from two new SCCPA renewable energy projects, Springbok 1 and Springbok 2, higher market purchases, and an increase in Feed-in-Tariff (a solar incentive program) program costs. The \$26 million decrease in fuel for generation costs is due to lower gas prices. The \$42 million increase in other operating expenses is due to higher transmission expense (\$9 million) due primarily to an increase in transmission costs at the Sylmar converter station, higher customer accounting (\$6 million) due to the customer billing system, higher administrative and general expenses (\$21 million) due to increased injuries and damages costs, higher distribution expenses (\$5 million) due primarily to an increase in services on customer premises, higher production expense (\$3 million), and higher marketing expenses (\$1 million), offset by lower customer service and information expense (\$3 million).

The \$30 million net decrease in maintenance expense for utility plant assets is the result of ongoing replacements and retrofits, which required less maintenance.

The \$19 million decrease in depreciation and amortization expense is the result of the 2016 Depreciation Study. The Power System now uses all straight-line depreciation method for assets as opposed to using the 5% sinking fund method based on estimated service lives.

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

Management's Discussion and Analysis

(Unaudited)

June 30, 2017 and 2016

Fiscal Year 2016

Fiscal year 2016 operating expenses were \$51 million higher as compared to fiscal year 2015, driven primarily by a \$15 million increase in purchased power costs, a \$68 million increase in other operating expenses, and a \$44 million increase in depreciation and amortization expense, and offset by \$59 million decrease in fuel for generation costs, and \$17 million decrease in maintenance expenses.

The \$15 million increase in purchased power costs can be primarily attributed to lower energy swap transaction revenue of \$14.1 million, which is used to offset or reduce purchased power costs. The \$59 million decrease in fuel for generation costs is due to lower gas prices. The \$68 million net increase in other operating expenses is due to higher administrative and general costs due to increased costs for insurance of \$3.2 million; outside services employed of \$5.4 million; injuries and damages of \$17.5 million; and a \$41.4 million impairment loss related to Navajo Generating Station.

The \$17 million decrease in maintenance of utility plant assets related to distribution plant infrastructure being replaced which required less maintenance.

Depreciation expense was computed using the straight-line method based on service lives for all projects completed after July 1, 1973, and for all office and shop structures, related furniture and equipment, and transportation and construction equipment. Depreciation for facilities completed prior to July 1, 1973 was computed using the 5% sinking fund method based on estimated service lives. The Department uses the composite method of depreciation and, therefore, groups assets into composite groups for purposes of calculating depreciation expense. Estimated service lives range from 5 to 75 years. Amortization expense for computer software is computed using the straight-line method over 5 to 15 years.

Nonoperating Revenues and Expenses

Fiscal Year 2017

The major nonoperating activities of the Power System for fiscal year 2017 included the transfer of \$264 million to City of Los Angeles (the City) General Fund, interest income earned on investments of \$21 million, \$33 million in federal bond subsidies, \$61 million in other nonoperating revenue, and \$317 million in debt expenses.

The \$44 million decrease in investment income is due mainly to changes in market values of investments and the restructuring of Intermountain Power Agreement's long-term notes.

The \$39 million increase in other nonoperating income is due mainly to the net sale of CO2 emission allowances, which were recorded to other nonoperating income in the net amount.

The \$49 million increase in debt expenses is mainly due to the interest expense on new bonds issued during the fiscal year net of a decrease in capitalized interest of \$23 million on the year.

The \$34 million decrease in capital contributions is mainly due to lower grants received from the state and federal government as compared to the prior year.

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
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Management's Discussion and Analysis

(Unaudited)

June 30, 2017 and 2016

Fiscal Year 2016

The major nonoperating activities of the Power System for fiscal year 2016 included the transfer of \$267 million to the City's general fund, interest income earned on investments of \$65 million, \$33 million in federal bond subsidies, and \$267 million in debt expenses.

The \$15 million increase in investment income is due mainly to changes in market values of investments.

The \$7 million increase in debt expenses is mainly due to the interest expense for new money bonds issued during the fiscal year offset by lower capitalized interest. Allowance for funds used during construction (AFUDC) decreased \$6 million year over year due to fewer CWIP projects.

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

Statements of Net Position

June 30, 2017 and 2016

(Amounts in thousands)

Assets and Deferred Outflows	2017	2016
Noncurrent assets:		
Utility plant:		
Generation	\$ 5,793,242	6,584,145
Transmission	1,658,924	1,300,427
Distribution	8,467,796	7,861,812
General	<u>1,757,767</u>	<u>1,745,403</u>
Total	17,677,729	17,491,787
Accumulated depreciation	<u>(7,803,778)</u>	<u>(8,289,312)</u>
Total utility plant, net	9,873,951	9,202,475
Construction work in progress	658,992	866,434
Nuclear fuel, at amortized cost	41,465	39,948
Natural gas field, net	<u>198,145</u>	<u>213,691</u>
Total	10,772,553	10,322,548
Restricted investments	592,887	594,698
Cash and cash equivalents – restricted	312,267	168,785
Long-term notes and other receivables, net of current portion	546,160	601,409
Underrecovered costs	155,628	185,607
Regulatory assets – other	755,303	646,674
Regulatory assets – pension	614,850	670,425
Net postemployment asset	<u>661,229</u>	<u>674,488</u>
Total noncurrent assets	<u>14,410,877</u>	<u>13,864,634</u>
Current assets:		
Cash and cash equivalents – unrestricted	991,182	1,331,543
Cash and cash equivalents – restricted	350,256	262,430
Cash collateral received from securities lending transactions	11,397	31,101
Customer and other accounts receivable, net of \$182,500 and \$148,303 allowance for losses for 2017 and 2016, respectively	349,112	307,990
Current portion of long-term notes receivable	48,512	21,747
Current portion of underrecovered costs	213,912	—
Due from Water System	8,602	7,918
Accrued unbilled revenue	194,833	196,532
Materials and fuel	170,065	218,554
Prepayments and other current assets	<u>110,731</u>	<u>106,444</u>
Total current assets	<u>2,448,602</u>	<u>2,484,259</u>
Total assets	<u>16,859,479</u>	<u>16,348,893</u>
Deferred outflows on derivative instruments	14,640	23,379
Deferred outflows on debt refunding	23,728	27,674
Deferred outflows – pension	793,045	217,131
Deferred outflows – pension contributions made after measurement date	<u>266,824</u>	<u>245,462</u>
Total deferred outflows	<u>1,098,237</u>	<u>513,646</u>
Total assets and deferred outflows	<u>\$ 17,957,716</u>	<u>16,862,539</u>

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

Statements of Net Position

June 30, 2017 and 2016

(Amounts in thousands)

Net Position, Liabilities, and Deferred Inflows	2017	2016
Net position:		
Net investment in capital assets	\$ 1,432,808	1,341,588
Restricted:		
Debt service	600,623	550,975
Other postemployment benefits	661,230	674,488
Other purposes	222,220	171,222
Unrestricted	<u>2,851,065</u>	<u>2,852,807</u>
Total net position	<u>5,767,946</u>	<u>5,591,080</u>
Long-term debt, net of current portion	<u>9,276,230</u>	<u>8,943,376</u>
Other noncurrent liabilities:		
Accrued liabilities	—	1,887
Accrued workers' compensation claims	67,410	61,945
Derivative instrument liabilities	14,640	23,379
Net pension liability	<u>1,492,508</u>	<u>771,122</u>
Total other noncurrent liabilities	<u>1,574,558</u>	<u>858,333</u>
Current liabilities:		
Current portion of long-term debt	243,049	211,133
Accounts payable and accrued expenses	412,963	332,211
Accrued interest	182,192	169,358
Accrued employee expenses	130,063	120,371
Overrecovered energy cost	—	44
Obligations under securities lending transactions	<u>11,397</u>	<u>31,101</u>
Total current liabilities	<u>979,664</u>	<u>864,218</u>
Total liabilities	<u>11,830,452</u>	<u>10,665,927</u>
Deferred inflows on debt refunding	14,144	7,075
Deferred inflow – pension	241,547	421,232
Deferred inflows from regulated business activities	<u>103,627</u>	<u>177,225</u>
Total deferred inflows	<u>359,318</u>	<u>605,532</u>
Total net position, liabilities, and deferred inflows	<u>\$ 17,957,716</u>	<u>16,862,539</u>

See accompanying notes to financial statements.

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
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Statements of Revenues, Expenses, and Changes in Net Position

Years ended June 30, 2017 and 2016

(Amounts in thousands)

	<u>2017</u>	<u>2016</u>
Operating revenues:		
Residential	\$ 1,179,514	1,126,690
Commercial and industrial	2,331,599	2,308,194
Sales for resale	88,099	72,936
Other	133,559	45,586
Uncollectible accounts	(34,847)	(36,366)
Total operating revenues	<u>3,697,924</u>	<u>3,517,040</u>
Operating expenses:		
Fuel for generation	292,557	318,749
Purchased power	1,165,303	1,037,471
Maintenance and other operating expenses	1,107,118	1,095,714
Depreciation and amortization	521,220	540,478
Total operating expenses	<u>3,086,198</u>	<u>2,992,412</u>
Operating income	<u>611,726</u>	<u>524,628</u>
Nonoperating revenues:		
Investment income	21,848	65,475
Federal bond subsidies	33,472	33,508
Other nonoperating income	60,955	23,025
Total nonoperating revenues	<u>116,275</u>	<u>122,008</u>
Other nonoperating expenses	<u>(2,235)</u>	<u>(2,742)</u>
Total nonoperating revenues, net	<u>114,040</u>	<u>119,266</u>
Debt expenses:		
Interest on debt	326,023	299,728
Allowance for funds used during construction	(9,373)	(32,200)
Total debt expenses	<u>316,650</u>	<u>267,528</u>
Income before capital contributions and transfers	409,116	376,366
Capital contributions	32,177	65,896
Transfers to the reserve fund of the City of Los Angeles	(264,427)	(266,957)
Increase in net position	<u>176,866</u>	<u>175,305</u>
Net position:		
Beginning of year	<u>5,591,080</u>	<u>5,415,775</u>
End of year	<u>\$ 5,767,946</u>	<u>5,591,080</u>

See accompanying notes to financial statements.

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

Statements of Cash Flows

Years ended June 30, 2017 and 2016

(Amounts in thousands)

	2017	2016
Cash flows from operating activities:		
Cash receipts:		
Cash receipts from customers	\$ 3,684,977	3,717,797
Cash receipts from customers for other agency services	648,050	677,838
Cash receipts from interfund services provided	621,693	629,369
Other cash receipts	18,458	—
Cash disbursements:		
Cash payments to employees	(555,045)	(599,620)
Cash payments to suppliers	(2,005,772)	(1,917,907)
Cash payments for interfund services used	(807,059)	(792,298)
Cash payments to other agencies for fees collected	(648,238)	(672,221)
Other operating cash payments	—	(70,536)
Net cash provided by operating activities	<u>957,064</u>	<u>972,422</u>
Cash flows from noncapital financing activities:		
Payments to the reserve fund of the City of Los Angeles	(264,427)	(266,957)
Interest paid on noncapital revenue bonds	(4,697)	(406)
Net cash used in noncapital financing activities	<u>(269,124)</u>	<u>(267,363)</u>
Cash flows from capital and related financing activities:		
Additions to plant and equipment, net	(980,433)	(929,706)
Capital contributions	36,888	68,254
Principal payments and maturities on long-term debt	(153,915)	(113,526)
Proceeds from issuance of bonds and revenue certificates	588,322	524,063
Debt interest payments	(374,183)	(354,857)
Federal bond subsidies	33,472	33,508
Net cash used in capital and related financing activities	<u>(849,849)</u>	<u>(772,264)</u>
Cash flows from investing activities:		
Purchases of investment securities	(885,835)	(1,096,021)
Sales and maturities of investment securities	884,926	1,145,543
Proceeds from notes receivable	21,747	84,212
Investment income	32,018	62,624
Net cash provided by investing activities	<u>52,856</u>	<u>196,358</u>
Net (decrease) increase in cash and cash equivalents	<u>(109,053)</u>	<u>129,153</u>
Cash and cash equivalents:		
Cash and cash equivalents at beginning of year	<u>1,762,758</u>	<u>1,633,605</u>
Cash and cash equivalents at end of year	<u>\$ 1,653,705</u>	<u>1,762,758</u>

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

Statements of Cash Flows

Years ended June 30, 2017 and 2016

(Amounts in thousands)

	2017	2016
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	\$ 611,726	524,628
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	521,220	540,480
Depletion expense	15,617	15,131
Amortization of nuclear fuel	13,610	14,181
Provision for losses on customer and other accounts receivables	34,847	36,366
Changes in assets and liabilities:		
Customer and other accounts receivable	(81,393)	5,414
Accrued unbilled revenue	1,699	(25,290)
Underrecovered costs	29,979	29,979
Current portion underrecovered costs	(213,912)	—
Materials and fuel	48,489	(52,990)
Regulatory assets	(53,052)	170,209
Due from Water System	(684)	(4,018)
Deferred outflows – related to pensions	(597,275)	83,609
Accounts payable and accrued expenses	70,102	(12,322)
Overrecovered energy cost	(44)	(31,299)
Net pension liability	721,387	(89,627)
Deferred inflows – related to pensions	(179,686)	(261,762)
Net other postemployment benefit asset	13,259	(4,596)
Prepayments and other	1,175	34,329
Net cash provided by operating activities	\$ 957,064	972,422
Supplemental disclosures of noncash capital and relating financing activities:		
During the year ended June 30, 2017, the Power System issued capital bonds to refund previously issued debt. The \$399.7 million of proceeds were deposited immediately into an irrevocable trust for the defeasance of \$395.6 million of debt. The net gain on refunding, after the write-off of previously recorded unamortized premiums, resulted in \$7.61 million, which will be amortized over the debt repayment period and recorded as a deferred inflow.		
During the year ended June 30, 2016, the Power System issued capital bonds to refund previously issued debt. The \$384.46 million of proceeds were deposited immediately into an irrevocable trust for the defeasance of \$380.57 million of debt. The net gain on refunding, after the write-off of previously recorded unamortized premiums, resulted in \$1.35 million, which will be amortized over the debt repayment period and recorded as a deferred inflow.		
Accounts payable related to capital expenditures	\$ 10,652	4,532

See accompanying notes to financial statements.

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

Notes to Financial Statements

June 30, 2017 and 2016

(In thousands)

(1) Summary of Significant Accounting Policies

The Department of Water and Power (the Department) exists as a separate department of the City of Los Angeles (the City) under and by virtue of the City Charter enacted in 1925, and as revised effective July 2000. The Department's Power Revenue Fund (the Power System) is responsible for the generation, transmission, and distribution of electric power for sale in the City. The Power System is operated as an enterprise fund of the City.

(a) Method of Accounting

The accounting records of the Power System are maintained in accordance with U.S. generally accepted accounting principles (GAAP) for state and local governmental entities. The financial statements have been prepared using the economic resources measurement focus and the accrual basis of accounting. The Power System is accounted for as an enterprise fund and applies all applicable Governmental Accounting Standards Board (GASB) pronouncements in its accounting and reporting.

The financial statements of the Power System are intended to present the net position, and the changes in net position and cash flows, of only that portion of the business-type activities and each major fund of the City that is attributable to the transactions of the Power System. They do not purport to, and do not, present fairly the financial position of the City as of June 30, 2017 and 2016, the changes in its financial position, or, where applicable, its cash flows for the years then ended, in conformity with GAAP.

The Department's rates are determined by the Board of Water and Power Commissioners and are subject to review and approval by the Los Angeles City Council. As a regulated enterprise, the Department follows the regulatory accounting criteria set forth in Governmental Accounting Standards Board (GASB) Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, which requires that the effects of the rate-making process be recorded in the financial statements. Such effects primarily concern the time at which various items enter into the determination of changes in net position. Accordingly, the Power System records various regulatory assets and liabilities to reflect the Board's actions and by deferring expenses and revenues that are recoverable or payable from rates provided in the electric rate ordinances. Regulatory liabilities comprise overrecovered costs, and deferred inflows and regulatory assets comprise regulatory assets and underrecovered costs in the statement of net position. Management believes that the Power System meets the criteria for continued application of GASB Statement No. 62, but will continue to evaluate its applicability based on changes in the regulatory and competitive environment. See note 6.

(b) Use of Estimates

The preparation of financial statements in conformity with GAAP 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.

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
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Notes to Financial Statements

June 30, 2017 and 2016

(In thousands)

(c) Utility Plant

The costs of additions to utility plant and replacements of retired units of property are capitalized. Costs include labor, materials, an allowance for funds used during construction, and allocated indirect charges, such as engineering, supervision, transportation and construction equipment, retirement plan contributions, healthcare costs, and certain administrative and general expenses. The costs of maintenance, repairs, and minor replacements are charged to the appropriate operations and maintenance expense accounts.

(d) Intangibles

The Department follows GASB Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, which requires that an intangible asset be recognized in the statement of net position only if it is considered identifiable. Additionally, it establishes a specified-conditions approach to recognize intangible assets that are internally generated. Effectively, outlays associated with the development of such assets are not capitalized until certain criteria are met. Outlays incurred prior to meeting these criteria are expensed as incurred. Intangible assets consist of land easements, water rights, and computer software and are included in general utility plant on the statements of net position.

(e) Impairment of Long-Lived Assets

The Department follows GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*. Governments are required to evaluate prominent events or changes in circumstances affecting capital assets to determine whether impairment of a capital asset has occurred. A capital asset is considered impaired when its service utility has declined significantly and unexpectedly. Under GASB Statement No. 42, impaired capital assets that will no longer be used by the government should be reported at the lower of carrying value or fair value. Impairment losses on capital assets that will continue to be used by the government should be measured using the method that best reflects the cause of the diminished service utility of the capital asset. During fiscal year 2016, the Department recognized an impairment loss of \$41.4 million due to the sale of the Navajo Generating Station effective July 1, 2016.

(f) Depreciation and Amortization

Beginning in fiscal year 2017, depreciation expense is computed using the straight-line method for all assets. Depreciation rates are per the 2016 Depreciation Study. For fiscal year 2016 and prior, depreciation expense was computed using the straight-line method based on service lives for all projects completed after July 1, 1973, and for all office and shop structures, related furniture and equipment, and transportation and construction equipment. Depreciation for facilities completed prior to July 1, 1973 was computed using the 5.0% sinking fund method based on estimated service lives.

The Department uses the composite method of depreciation and, therefore, groups assets into composite groups for purposes of calculating depreciation expense. Estimated service lives range from 5 to 75 years. Amortization expense for computer software is computed using the straight-line method over 5 to 15 years. Depreciation and amortization expense as a percentage of average depreciable utility plant in service was 2.8% and 3.1% for fiscal years ended 2017 and 2016, respectively.

**CITY OF LOS ANGELES
DEPARTMENT OF WATER AND POWER
POWER SYSTEM**

Notes to Financial Statements

June 30, 2017 and 2016

(In thousands)

(g) Nuclear Decommissioning

The Department owns a 5.70% direct ownership interest in the Palo Verde Nuclear Generating Station (PVNGS). In addition, through its participation in the Southern California Public Power Authority (SCPPA), the Department is party to a contract for an additional 3.95% of the output of PVNGS. Nuclear decommissioning costs associated with the Power System's output entitlement are included in purchased power expense. See note 5.

Decommissioning of PVNGS is expected to commence subsequent to the year 2044, since the Nuclear Regulatory Commission (the NRC) approved a request for a 30-year license extension in April 2011. As of April 28, 2014, all of the owners of PVNGS have executed the amendment to the participation agreement to extend the term of the agreement to cover the license extension of PVNGS. The decommissioning estimate is based on an updated site-specific study prepared by an independent consultant in 2013, escalated to year 2016 dollars. As of June 30, 2017 and 2016, the Power System has recorded \$153 million to accumulated depreciation – generation to provide for the decommissioning liability. See note 3.

Prior to December 1999, the Power System reserved \$70 million in accordance with the PVNGS participation agreement and the NRC requirements. During fiscal year 2000, the Department suspended contributing additional amounts to the reserve funds, as management believes that contributions made, combined with reinvested earnings, will be sufficient to fully fund the Department's share of decommissioning costs. The Department will continue to reinvest its investment income into the decommissioning reserves. The balance in the decommissioning funds increased in fiscal year 2017 by \$0.4 million, after increasing by \$4.0 million in fiscal year 2016. The fair value of the decommissioning funds, which are included in restricted investments, totaled \$133.8 million and \$133.4 million as of June 30, 2017 and 2016, respectively. The Department's current accounting policy recognizes any realized and unrealized investment earnings from nuclear decommissioning reserves as addition to accumulated depreciation. See note 7.

(h) Nuclear Fuel

Nuclear fuel is amortized and charged to fuel for generation on the basis of actual thermal energy produced relative to total thermal energy expected to be produced over the life of the fuel. Under the provisions of the Nuclear Waste Policy Act of 1982, the federal government assesses each utility with nuclear operations, including the Power System, \$1 per megawatt hour of nuclear generation. The Power System includes this charge as a current year expense in fuel for generation.

(i) Natural Gas Field

In July 2005, the Power System acquired approximately a 74.5% ownership interest in gas properties located in Pinedale, Wyoming. The Power System uses the successful-efforts method of accounting for its investment in gas-producing properties. Costs to acquire the mineral interest in gas-producing properties, to drill and equip exploratory wells that find proven reserves, and to drill and equip development wells are capitalized. Costs to drill exploratory wells that do not find proven reserves are expensed. Capitalized costs of gas-producing properties are depleted by the unit-of-production method based on the estimated future production of the proven wells.

**CITY OF LOS ANGELES
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POWER SYSTEM**

Notes to Financial Statements

June 30, 2017 and 2016

(In thousands)

Depletion expense related to the gas field is recorded as a component of fuel for generation expense. During fiscal years 2017 and 2016, the Power System recorded \$16 million and \$15 million of depletion expense, respectively.

(j) Cash and Cash Equivalents

As provided for by the State of California Government Code, the Power System's cash is deposited with the City Treasurer in the City's general investment pool for the purpose of maximizing interest earnings through pooled investment activities. Cash and cash equivalents in the City's general investment pool are reported at fair value on a recurring basis and changes in unrealized gains and losses are recorded in the statements of revenues, expenses, and changes in net position. Interest earned on such pooled investments is allocated to the participating funds based on each fund's average daily cash balance during the allocation period. The City Treasurer invests available funds of the City and its independent operating departments on a combined basis. The Power System classifies all cash and cash equivalents that are restricted either by creditors, the Board, or by law as restricted cash and cash equivalents in the statements of net position. The Power System considers its portion of pooled investments in the City's pool to be unrestricted cash and cash equivalents and the unspent construction funds as long-term restricted cash and cash equivalents.

At June 30, 2017 and 2016, restricted cash and cash equivalents include the following (amounts in thousands):

	June 30	
	2017	2016
Bond redemption and interest funds	\$ 311,209	262,430
Other restricted funds	39,047	—
Cash and cash equivalents – current portion	350,256	262,430
Self-insurance funds	180,575	163,779
Rate Stabilization fund	100,000	—
Bond redemption funds	15,123	5,000
Construction funds	16,569	6
Cash and cash equivalents – long term	312,267	168,785
Total restricted cash and cash equivalents	\$ 662,523	431,215

(k) Customer and Other Accounts Receivable

The Power Systems' accounts receivables consist of customer and other receivables. The receivables are reported net of allowance for losses. Customer account receivables result from the sale of energy to city residents and include related city taxes. Other receivables consist of billings to customers,

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federal, state, and local governments for work performed to improve or enhance energy distribution, energy sales to other utilities, and other miscellaneous receivables.

The Power System recognizes an allowance for losses on accounts receivable in an amount equal to the estimated probable losses, net of recoveries. The allowance is based upon factors, such as historical written-off amounts, current receivables aging, and assessment of customer collectibility. The expense associated with the allowance for losses is charged against revenue in the period recognized.

At June 30, 2017 and 2016, customer and other accounts receivable include the following (amounts in thousands):

	June 30	
	2017	2016
Customer accounts receivable	\$ 424,639	363,481
Allowance for losses	(175,000)	(145,006)
Customer accounts receivable	249,639	218,475
Customer accounts receivable, other	106,973	92,812
Allowance for losses, other	(7,500)	(3,297)
Customer accounts receivable other	99,473	89,515
Total customer accounts receivable	\$ 349,112	307,990

(l) Materials and Fuel

Materials and supplies are recorded at average cost. Fuel is recorded at lower of cost or market, on an average-cost basis.

(m) Accrued Unbilled Revenue

Accrued unbilled revenue is the receivable for estimated energy sales during the period for which service has been provided but the customer has not yet been billed.

(n) Investments

The Department follows GASB Statement No. 72, *Fair Value Measurement and Application*, which addresses accounting and fair value reporting issues related to fair value measurements by clarifying the definition of fair value, establishing general principles for measuring fair value, providing additional fair value application guidance, and enhancing disclosures about fair value measurements. This statement established a three-level hierarchy of inputs to valuation techniques used to measure fair value. Restricted investments include primarily commercial paper, U.S. government and governmental agency securities, and corporate bonds. Investments are reported at fair value on a recurring basis, and changes in unrealized gains and losses are recorded in the statements of revenues, expenses,

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and changes in net position. The stated fair value of investments is generally based on published market prices or quotations from major investment dealers.

(o) Accrued Employee Expenses

Accrued employee expenses include accrued payroll and an estimated liability for vacation leave, sick leave, and compensatory time, which are accrued when employees earn the rights to the benefits. Below is a schedule of accrued employee expenses as of June 30, 2017 and 2016 (amounts in thousands):

	June 30	
	2017	2016
Type of expenses:		
Accrued payroll	\$ 48,563	43,397
Accrued vacation	50,001	47,918
Accrued sick leave	12,848	11,914
Compensatory time	18,651	17,142
Total	\$ 130,063	120,371

(p) Debt Expenses

Debt premiums and discounts are capitalized and amortized to interest expense using the effective-interest method over the lives of the related debt issues. Gains and losses on refundings related to bonds redeemed by proceeds from the issuance of new bonds are amortized to interest expense using the effective-interest method over the shorter of the life of the new bonds or the remaining term of the bonds refunded.

(q) Accrued Workers' Compensation Claims

Liabilities for unpaid workers' compensation claims are recorded at their net present value. See note 12.

(r) Customer Deposits

Customer deposits represent deposits collected from customers upon opening of new accounts. These deposits are obtained when the customer does not have a previously established credit history with the Department. Original deposits plus interest are paid to the customer once a satisfactory payment history is maintained, generally after one to three years.

The Department's Water Revenue Fund (the Water System) is responsible for collection, maintenance, and refunding of these deposits for all the Department's customers, including those of the Power System. As such, the Water System's statements of net position include a deposit liability of \$189 million and \$162 million as of June 30, 2017 and 2016, respectively, for all customer deposits collected. In the event that the Water System defaults on refunds of such deposits, the Power System would be required to pay amounts it owes its customers.

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(s) Capital Contributions

Capital contributions and other grants received by the Department for constructing utility plant and other activities are recognized when all applicable eligibility requirements, including time requirements, are met.

(t) Allowance for Funds Used during Construction (AFUDC)

An AFUDC charge represents the cost of borrowed funds used for the construction of utility plant. Capitalized AFUDC is included as part of the cost of utility plant and as a reduction of interest expenses. As of June 30, 2017 and 2016, the average AFUDC rates were 3.5% and 3.3%, respectively.

(u) Use of Restricted and Unrestrictive Resources

The Power System's policy is to use unrestricted resources prior to restricted resources to meet expenses to the extent that it is prudent from an operational perspective. Once it is not prudent, restricted resources will be utilized to meet intended obligations.

(v) Pensions

Eligible employees of the Power System are members of the Water and Power Employees' Retirement Plan (the Plan), which is a single-employer defined-benefit pension plan. The Power System's policy is to fund all the required actuarially determined contributions; such costs to be funded are determined annually as of July 1 by an actuary utilized by the Plan. The assets of the Plan are accumulated and reported at fair value in a special trust fund of the City and, therefore, are not reported in the accompanying financial statements.

The Power System recognizes a net pension liability, which represents the Power System's proportionate share of the excess of the total pension liability over the fiduciary net position of the pension plan as reflected in the financial statements of the Plan. The net pension liability is measured as of the Power System's prior fiscal year-end. Changes in the net pension liability are recorded, in the period incurred, as pension expense or as deferred inflows of resources or deferred outflows of resources depending on the nature of the change. The changes in net pension liability that are recorded as deferred inflows of resources or deferred outflows of resources (that arise from changes in actuarial assumptions or other inputs and differences between expected or actual experience) are amortized over the weighted average remaining service life of all participants in the respective pension plan and are recorded as a component of pension expense beginning with the period in which they are incurred. Projected earnings on pension investments are recognized as a component of pension expense. Differences between projected and actual investment earnings are reported as deferred inflows of resources or deferred outflows of resources and amortized as a component of pension expense on a closed basis over a five-year period beginning with the period in which the difference occurred. Each subsequent year will incorporate an additional closed basis five-year period of recognition. Contributions made after the measurement date are recorded as deferred outflows and a reduction to the pension regulatory asset.

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For purposes of measuring the net pension liability and deferred outflows/inflows or resources relating to pensions and pension expense, information about the fiduciary net position of the Power System's pension plan and additions to/deductions from the plan's fiduciary net position has been determined on the same basis as they are reported by the Plan. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit's terms.

(w) Other Retirement Plan Benefits

Eligible employees of the Power System are members of the Water and Power Employees' Retirement Plan, which comprises a single-employer defined-benefit plan and a system of benefits. In addition to pension benefits, retirees can also receive healthcare and death benefits. The level of benefits is determined based on their years of civil service, age, and which pension tier they belong to. Active employees who qualify for disability can receive permanent disability benefits in accordance with the plan provisions up until retirement and temporary disability for up to 24 months.

(x) Reclassifications

Certain reclassifications have been made to 2016 amounts to conform to the 2017 financial statement presentation. There was no impact on the previously reported change in net position of the Power System.

(2) Recent Accounting Pronouncements

(a) GASB Statement No. 75

In June 2015, the GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. This statement replaces the requirements of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expenses/expenditures. This statement is effective for the Power System next fiscal year. The Power System is currently evaluating the effects the adoption of this statement will have on the financial statements.

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(b) GASB Statement No. 82

In March 2016, the GASB issued Statement No. 82, *Pension Issues—an amendment of GASB Statements No. 67, No. 68, and No. 73 (GASB Statement No. 82)*. The objective of this statement is to address certain issues that have been raised with respect to Statement No. 67, *Financial Reporting for Pension Plans*; and Statement No. 73, *Accounting and Financial Reporting for Pensions and Related Assets That Are Not within the Scope of GASB Statement 68, and Amendments to Certain Provisions of GASB Statements 67 and 68*. Specifically, this statement addresses issues regarding (1) the presentation of payroll-related measures in required supplementary information, (2) the selection of assumptions and the treatment of deviations from the guidance in an actuarial standard of practice for financial reporting purposes, and (3) the classification of payments by employers to satisfy employee (plan member) contribution requirements. This statement is effective for the Power System next fiscal year. The Power System is currently evaluating the effects this statement will have on the financial statements.

(c) GASB Statement No. 83

In November 2016, the GASB issued Statement No. 83, *Accounting and Financial Reporting for Certain Asset Retirement Obligations*. This statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance of this statement. This statement is effective for the Power System next fiscal year. The Power System is currently evaluating the effect this statement will have on the financial statements.

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(3) Utility Plant

The Power System had the following activities in utility plant during fiscal year 2017 (amounts in thousands):

	<u>Balance, June 30, 2016</u>	<u>Additions</u>	<u>Retirements and disposals</u>	<u>Transfers</u>	<u>Balance, June 30, 2017</u>
Nondepreciable utility plant:					
Land and land rights	\$ 196,953	4,951	—	—	201,904
Construction work in progress	866,434	342,606	—	(550,048)	658,992
Nuclear fuel	39,948	15,127	(13,610)	—	41,465
Natural gas field	213,691	71	(15,617)	—	198,145
	<u>1,317,026</u>	<u>362,755</u>	<u>(29,227)</u>	<u>(550,048)</u>	<u>1,100,506</u>
Total nondepreciable utility plant					
Depreciable utility plant:					
Generation	6,515,789	40,319	(892,402)	58,180	5,721,886
Transmission	1,220,320	46,704	(2,291)	312,132	1,576,865
Distribution	7,819,097	453,633	(7)	152,357	8,425,080
General	1,739,629	26,425	(41,439)	27,379	1,751,994
	<u>17,294,835</u>	<u>567,081</u>	<u>(936,139)</u>	<u>550,048</u>	<u>17,475,825</u>
Total depreciable utility plant					
Accumulated depreciation:					
Generation	(3,197,811)	(151,787)	892,402	—	(2,457,196)
Transmission	(502,987)	(27,967)	2,291	—	(528,663)
Distribution	(3,636,511)	(218,005)	7	—	(3,854,509)
General	(952,003)	(52,846)	41,439	—	(963,410)
	<u>(8,289,312)</u>	<u>(450,605)</u>	<u>936,139</u>	<u>—</u>	<u>(7,803,778)</u>
Total accumulated depreciation					
Total utility plant, net	<u>\$ 10,322,549</u>	<u>479,231</u>	<u>(29,227)</u>	<u>—</u>	<u>10,772,553</u>

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The Power System had the following activities in utility plant during fiscal year 2016 (amounts in thousands):

	<u>Balance, June 30, 2015</u>	<u>Additions</u>	<u>Retirements and disposals</u>	<u>Transfers</u>	<u>Balance, June 30, 2016</u>
Nondepreciable utility plant:					
Land and land rights	\$ 196,985	—	(32)	—	196,953
Construction work in progress	1,720,823	420,826	—	(1,275,215)	866,434
Nuclear fuel	39,469	14,660	(14,181)	—	39,948
Natural gas field	228,797	25	(15,131)	—	213,691
	<u>2,186,074</u>	<u>435,511</u>	<u>(29,344)</u>	<u>(1,275,215)</u>	<u>1,317,026</u>
Total nondepreciable utility plant					
Depreciable utility plant:					
Generation	5,427,597	118,067	(1,880)	972,005	6,515,789
Transmission	1,055,064	—	(3,159)	168,415	1,220,320
Distribution	7,373,709	379,241	(7)	66,154	7,819,097
General	1,643,814	32,833	(5,660)	68,641	1,739,628
	<u>15,500,184</u>	<u>530,141</u>	<u>(10,706)</u>	<u>1,275,215</u>	<u>17,294,834</u>
Total depreciable utility plant					
Accumulated depreciation:					
Generation	(2,998,944)	(200,747)	1,880	—	(3,197,811)
Transmission	(472,476)	(33,670)	3,159	—	(502,987)
Distribution	(3,378,802)	(257,716)	7	—	(3,636,511)
General	(910,135)	(47,528)	5,660	—	(952,003)
	<u>(7,760,357)</u>	<u>(539,661)</u>	<u>10,706</u>	<u>—</u>	<u>(8,289,312)</u>
Total accumulated depreciation					
Total utility plant, net	<u>\$ 9,925,901</u>	<u>425,991</u>	<u>(29,344)</u>	<u>—</u>	<u>10,322,548</u>

Depreciation and amortization expense during fiscal years 2017 and 2016 was \$521.2 million and \$540.5 million, respectively. Depreciation and amortization expense on the statements of cash flows includes amortization expense on software and regulatory assets, which is not included in additions to accumulated depreciation above. Additions to accumulated depreciation above also include increases in fair value related to the PVNGS decommissioning fund, which are not included in depreciation and amortization expense on the statements of cash flows. See note 1 (g).

Land and land rights are included in the balance sheet as utility plant assets in their functional category.

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(4) Jointly Owned Utility Plant

The Power System has undivided direct interests in several electric generating stations and transmission systems that are jointly owned with other utilities, as defined in GASB Statement No. 14, *The Reporting Entity*. As of June 30, 2017 and 2016, utility plant includes the following amounts related to the Power System's ownership interest in each jointly owned utility plant (amounts in thousands, except as indicated):

	Ownership interest	Share of capacity (MWs)	Utility plant in service June 30, 2017		Utility plant in service June 30, 2016	
			Cost	Accumulated depreciation	Cost	Accumulated depreciation
Palo Verde Nuclear Generating Station	5.7%	224	\$ 592,194	404,669	608,084	398,414
Navajo Generating Station	—	—	—	—	358,712	358,712
Mohave Generating Station	10.0	—	3,408	229	65,547	57,852
Pacific Intertie DC Transmission Line	40.0	1,240	189,549	76,667	188,318	72,333
Other transmission systems	—	Various	109,885	65,464	108,557	64,486
			<u>\$ 895,036</u>	<u>547,029</u>	<u>1,329,218</u>	<u>951,797</u>

The Power System will incur certain minimal operating costs related to the jointly owned facilities, regardless of the amount or its ability to take delivery of its share of energy generated. The Power System's proportionate share of the operating costs of the joint plants is included in the corresponding categories of operating expenses.

As of June 30, 2016, the Department recognized an impairment loss associated with its ownership interest in the Navajo Generating Station in the amount of \$41.4 million. On July 1, 2016, the Department sold its interest in the Navajo Generating Station. As such, the carrying value of the asset is \$0 at June 30, 2016.

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(5) Purchased Power Commitments

As of June 30, 2017, the Power System has entered into a number of energy and transmission service contracts that, regardless of the energy they take they are obligated to pay the following minimum costs (dollar amounts in thousands):

	Agency	Agency share	The Power System's interest in agency's share		
			Interest	Capacity (MWs)	Outstanding commitment**
Intermountain Power Project	IPA	100.0%	64.5%	1,161	\$ 542,498
Palo Verde Nuclear Generating Station	SCPPA	5.9	67.0	151	8,315
Mead-Adelanto Transmission Project	SCPPA	68.0	48.9	539	53,515
Mead-Phoenix Transmission Project	SCPPA	17.8–22.4	50.4	647	28,111
Southern Transmission System	SCPPA	100.0	59.5	1,429	321,728
Milford Wind I	SCPPA	100.0	92.5	188	173,160
Windy Point	SCPPA	100.0	100.0	262*	407,240
Linden Wind Energy Project	SCPPA	100.0	100.0	50*	118,010
Milford Wind II	SCPPA	100.0	100.0	102*	131,570
Apex Power Project	SCPPA	100.0	100.0	495	300,150
					\$ 2,084,297

* Power System will receive 100% of the energy, unless City of Glendale exercises its option to repurchase any of its contract output entitlement share.

** Portion of purchased power commitment based upon related agency's bond principal not including interest requirements. These long-term commitments extend through 2044.

IPA – The Intermountain Power Agency (IPA) is an agency of the State of Utah established to own, acquire, construct, operate, maintain, and repair the Intermountain Power Project (IPP). The Power System serves as the project manager and operating agent of IPP.

SCPPA – The Southern California Public Power Authority (SCPPA) is a California joint powers agency that finances the construction or acquisition of generation, transmission, and renewable energy projects. The Department is a member of SCPPA.

Unlike joint utility plant disclosed in note 4, the Power System does not have ownership of any assets related to these service contracts. As costs are paid each year, they are recorded as purchase power expense in the statement of revenue, expenses, and changes in net position.

In addition to commitments noted above for debt service, the Power System is required to pay an average annual fixed charge of approximately \$283 million during each of the next five years for operating and maintenance costs related to actual deliveries of energy under these agreements (averaging approximately \$755 million annually during each of the next five years). The Power System made total payments under these agreements of approximately \$894 million and \$868 million in fiscal years 2017

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and 2016, respectively, and they are recorded as purchased power expense in the statements of revenues, expenses, and changes in net position. These agreements are scheduled to expire from 2027 to 2044.

The Power System is reimbursed for services provided to IPP under the IPP project manager and operating agent agreements totaling \$30 million and \$27 million in fiscal years 2017 and 2016, respectively. These fees are recorded as a reduction to maintenance and other expense on the accompanying statements of revenues, expenses and net position.

(a) Long-Term Notes Receivable

Under the terms of its purchase power agreement with IPA, the Department is charged for its output entitlements based on its share of IPA's costs, including debt service. During fiscal year 2000, the Department restructured a portion of this obligation by transferring \$1 billion to IPA in exchange for long-term notes receivable. The funds transferred were obtained from the debt reduction funds and through the issuance of new variable rate debentures. See note 7. IPA used the proceeds from these transactions to defease and tender bonds with par values of approximately \$618 million and \$611 million, respectively.

On September 7, 2000, the Department paid \$187 million to IPA in exchange for additional long-term notes receivable. IPA used the proceeds to defease bonds with a face value of \$198 million.

On July 20, 2005, the Department paid \$97 million to IPA in exchange for additional long-term notes receivable. IPA used the proceeds to defease bonds with a face value of \$92 million.

The IPA notes are subordinate to all of IPA's publicly held debt obligations. The Power System's future payments to IPA will be partially offset by interest payments and principal maturities from the subordinated notes receivable. The net IPA notes receivable balance totaled \$595 million and \$623 million as of June 30, 2017 and 2016, respectively.

The IPA notes pay interest and principal monthly and mature on July 1, 2023. The interest rates range from 3.97% to 10.67%, subject to adjustments related to IPA bond refundings.

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Scheduled annual principal maturities are as follows:

Year	Amount
2018	\$ 48,512
2019	123,545
2020	159,309
2021	155,920
2022	68,365
2023	74,425
2024	6,303
	636,379
Unamortized discount	(41,707)
	594,672
Less current portion	(48,512)
Noncurrent portion	\$ 546,160

(b) Energy Entitlement

The Department has a contract through September 2067 with the U.S. Department of Energy for the purchase of available energy generated at the Hoover Powerplant. The Department's contractual share of contingent capacity at Hoover is 491 MW (maximum rated capability). The cost of power (approximately 455 MW of capacity and 599,000 MWH of energy) purchased under this contract, including the Lower Colorado River Basin Development Fund Contribution Charge, was approximately \$15 million and \$14 million as of June 30, 2017 and 2016, respectively. On December 20, 2011, President Barack Obama signed H.R. 470, the Hoover Power Allocation Act of 2011, into law. The legislation reallocated, for 50 more years, power from the Hoover Powerplant to existing contractors while creating an additional pool of 5% power for new entrants.

The Department has entered into contracts with SCPPA to purchase available renewable energy generated at various renewable energy project sites.

Unlike service contracts noted earlier in Note 5, the Power System only pays costs related to these contracts if energy is delivered. As of June 30, 2017, the Power System energy entitlement contracts

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with SCPPA allowed for additional capacity with the associated cost as follows (dollar amounts in millions):

	Agency	Agency share	The Power System's interest in agency's share		
			Interest	Capacity (MWs)	Cost of power purchased
Pebble Springs Wind Project	SCPPA	100.0	69.6	68.7	9.1
Don A Campbell I	SCPPA	100.0	84.6	13.7	14.0
Don A Campbell II	SCPPA	100.0	100.0	16.2	13.7
Copper Mountain Solar 3	SCPPA	100.0	84.0	210.0	48.6
Heber 1 Geothermal	SCPPA	100.0	66.7	41.7	16.6
Springbok 1 Wind Farm	SCPPA	100.0	100.0	105.0	30.1
Springbok 2 Wind Farm	SCPPA	100.0	100.0	155.0	22.6
Total energy costs under entitlement agreements					154.7

(c) Electricity Swap and Forward Contracts

In order to obtain the highest market value on energy that is sold into the wholesale market, the Department monitors the sales price of energy, which varies based on which hub the energy is to be delivered. There are three primary hubs within the Department's transmission region: Palo Verde, California – Oregon Border, and Mead. The Department enters into various locational swap transactions with other electric utilities in order to effectively utilize its transmission capacity and achieve the most economical exchange of energy purchased and sold.

The Department procures renewable energy resources located remotely. These resources provide intermittent and limited source of energy, and some of these resources are not directly connected to the Department's transmission system. In order to receive firm renewable energy, the Department entered into a green-for-green energy exchange with the same or different renewable energy credit source.

The Department enters into power and natural gas forward contracts in order to meet the electricity requirements to serve its customers. To assist the Department in achieving its Renewable Portfolio Standards goal of 25%, some of the forward purchases made are renewable energy and biomethane gas.

The Department does not enter into swap and forward transactions for trading purposes. All of these transactions are intended to be used in the Department's normal course of operations. The Department is exposed to risk of nonperformance if the counterparties default or if the swap agreements are terminated.

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As of June 30, 2017 and 2016, the Power System had the following forward contracts, which are not recorded in the Power System's financial statements based on the scope exclusion criteria in GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments* (amounts in thousands):

<u>Description</u>	<u>Notional amount (total contract quantities)</u>	<u>Contract price range dollar per unit</u>	<u>First effective date</u>	<u>Last termination date</u>	<u>Fair value</u>	<u>Cash paid at inception</u>
Forward contracts:						
Electricity	329,004 Mwh	\$ 19.06–52.80	07/01/17	12/31/17	\$ 776	—
Natural gas	10,296,000 MMBtu	10.85	07/01/17	10/31/21	(82,849)	—

<u>Description</u>	<u>Notional amount (total contract quantities)</u>	<u>Contract price range dollar per unit</u>	<u>First effective date</u>	<u>Last termination date</u>	<u>Fair value</u>	<u>Cash received at inception</u>
Forward contracts:						
Electricity	756,816 Mwh	\$ 23.56–80.00	07/01/16	12/31/16	\$ 287	—
Natural gas	22,708,500 MMBtu	2.11–10.85	07/01/16	10/31/21	(93,193)	—

(6) Regulatory Assets and Liabilities

Regulatory assets and liabilities are created by the actions of the Board of Water and Power Commissioners by deferring certain expenses and revenue that are recoverable or payable by future rate charges in accordance with the current-rate ordinances so as to more evenly match the recognition of revenue and expenses with the electric rates charged to retail customers.

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Below is a summary of the Power System's regulatory assets and liabilities:

Description	July 1, 2016	Additions	Reductions	June 30, 2017
Assets:				
(a) Under recovered costs – long term	\$ 185,607	—	(29,978)	155,629
(b) Regulatory assets – legal settlements	128,000		(16,000)	112,000
(c) Regulatory assets – solar incentive program	200,121	17,292	(12,099)	205,314
(d) Regulatory assets – energy efficiency program	282,239	133,489	(41,041)	374,687
(e) Regulatory assets – customer care and billing system	36,314	29,761	(2,773)	63,302
Regulatory assets – other	646,674	180,542	(71,913)	755,303
(f) Regulatory assets – pension	670,425	—	(55,575)	614,850
Total regulatory assets – noncurrent	1,502,706	180,542	(157,466)	1,525,782
(g) Under recovered costs – current	—	213,912	—	213,912
Total regulatory assets	<u>\$ 1,502,706</u>	<u>394,454</u>	<u>(157,466)</u>	<u>1,739,694</u>
Liabilities:				
(g) Overrecovered costs – current	\$ 44	—	(44)	—
(h) Deferred inflows from business activities	177,225	402	(74,000)	103,627
Total regulatory liabilities	<u>\$ 177,269</u>	<u>402</u>	<u>(74,044)</u>	<u>103,627</u>
Description	July 1, 2015	Additions	Reductions	June 30, 2016
Assets:				
(a) Under recovered costs	\$ 215,585	—	(29,978)	185,607
(b) Regulatory assets – legal settlements	144,000	—	(16,000)	128,000
(c) Regulatory assets – solar incentive program	165,400	44,893	(10,172)	200,121
(d) Regulatory assets – energy efficiency program	239,705	72,637	(30,103)	282,239
(e) Regulatory assets – customer care and billing system	—	42,846	(6,532)	36,314
Total regulatory assets – other	549,105	160,376	(62,807)	646,674
(f) Regulatory assets – pension	\$ 938,205	—	(267,780)	670,425
Total regulatory assets	<u>\$ 1,702,895</u>	<u>160,376</u>	<u>(360,565)</u>	<u>1,502,706</u>
Liabilities:				
(g) Overrecovered costs – current	31,343	—	(31,299)	44
(h) Deferred Inflows from business activities	176,557	668	—	177,225
Total regulatory liabilities	<u>207,900</u>	<u>668</u>	<u>(31,299)</u>	<u>177,269</u>

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(a) Under Recovered Costs – Long Term

These represent future receivables from customers related to costs incurred for renewable energy projects and the investments made in power reliability. The 2012 and 2016 Electric Rate Ordinances allow for these costs to be recovered through current rates. The costs are amortized over a 10-year period and are expected to be fully recovered by 2022 and thus the Power system has classified them as noncurrent. The balance of the long-term underrecovered costs at June 30, 2017 and 2016 is \$155,629 and \$185,607, respectively, net of annual amortization of \$29,978.

(b) Regulatory Assets – Legal Settlement

In June 2007, the Power System reached an agreement from the courts related to the inclusion of capital components in the rates charged to other governmental organizations. The agreement required the payment of \$160,000 to the governmental organizations. The payment settlement included an immediate payout of \$127,800, bill credits of \$17,200 to be issued over a 10-year period, and \$15,000 in payments to be paid over a 3-year period, the last of which is to be paid no later than December 2010.

As provided in the Power System's rate structure, beginning in July 2014, customers' bills include a charge for this legal settlement to be collected over a 10-year period. As rates are established at a level sufficient to recover all such costs, the Power System recorded a regulatory asset. The balance of this legal settlement at June 30, 2017 and 2016 is \$112,000 and \$128,000, respectively, net of annual amortization of \$16,000.

(c) Regulatory Assets – Solar Incentive Programs

As part of the California Solar Incentive Program, initiated by 2006 Senate Bill 1 (SB1), the Power System implemented a multiyear program to provide customers with solar incentives for installing solar panels and necessary equipment to generate energy. The program, per SB1, concluded at the end of calendar year 2016. Some payments for these incentives were processed in 2017.

As provided in the Power System's rate structure, beginning April 2011, customers' bills include a charge for these solar incentive programs to be collected over a 15-year period. As rates are established at a level sufficient to recover all such costs, the Power System recorded a regulatory asset. The balance of solar incentive programs at June 30, 2017 and 2016 is \$205,314 and \$200,121 respectively, net of annual amortization of \$12,099 and \$10,172, respectively.

(d) Regulatory Assets – Energy Efficiency Programs

As part of the Power System's ongoing efforts to reduce energy consumption and improve the environment, the Power System implemented numerous multiyear programs. The program began in June 2012 and is expected to continue through 2020. At June 30, 2017 and 2016, the Power System has 26 energy efficiency programs.

As provided in the Power System's rate structure, beginning July 2011, customers' bills include a charge for these energy efficiency programs to be collected over a 5-to 15-year period, depending on the program. As rates are established at a level sufficient to recover all such costs, the Power System

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recorded a regulatory asset. The balance of energy efficiency programs at June 30, 2017 and 2016 is \$374,687 and \$282,239, respectively, net of annual amortization of \$41,041 and \$30,103, respectively.

(e) Regulatory Assets – Customer Care and Billing System

In 2013, the Power System implemented the customer care and billing system (CC&B). The implementation of the system required significant investment in training of the Power System's employees.

As provided in the Power System's rate structure, beginning January 2014, customers' bills include a charge related to training for the CC&B to be collected over a 10-year period. As rates are established at a level sufficient to recover all such costs, the Power System recorded a regulatory asset. The balance of CC&B costs at June 30, 2017 and 2016 is \$63,302 and \$36,314, net of annual amortization of \$2,773, and \$6,532, respectively.

(f) Regulatory Assets – Pension

In connection with the recognition of the net pension liability under GASB Statement No. 68, the Power System established a regulatory asset in the amount of \$1,563,012, equal to the net pension liability reported at July 1, 2013. The pension regulatory asset is expected to be amortized over a period not to exceed 15 years. Amortization of the regulatory asset is the difference between amounts paid toward actuarial determined contributions and actual pension expense and totaled \$55,575 and \$267,780 for the years ended June 30, 2017 and 2016, respectively.

(g) Underrecovered Costs – Current

As provided in the electric rate ordinances, the Department is required to maintain balancing accounts to record differences between specific costs incurred and amounts billed through rates to recover those costs. The Power System plans to adjust rates to recover the accumulated balance in underrecovered costs in the next 12 months and thus, overrecovered costs are shown as a current liability and underrecovered costs are shown as a current asset and represent the balance in the balancing accounts when the amount billed through rates is higher or lower than the costs the Power System has incurred. The Power System had \$213,912 in under recovered costs for the year then ended June 30, 2017 due to less consumption than planned in the current year due to energy conservation efforts resulting in less pass through revenue. The Power System had \$44 million in over recovered costs for the year ended June 30, 2016.

(h) Deferred Inflows from Regulated Business Activities

These amounts represent revenue collected from customers where funds are deferred for future stabilization or deferred because the earnings process is not complete. For the year ended June 30, 2017, the Power System recognized \$74 million of these revenue. For the year ended June 30, 2016, the Power System did not recognize any of these revenue.

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(7) Cash, Cash Equivalents, and Investments

(a) Restricted and Other Investments

A summary of the Power System's restricted investments is as follows (amounts in thousands):

	June 30	
	2017	2016
Restricted and other investments:		
Restricted investments:		
Debt reduction funds	\$ 456,482	453,883
Nuclear decommissioning funds	133,805	133,372
Natural gas fund	350	215
Hazardous waste treatment fund	2,250	2,241
SCPPA Palo Verde investment	—	4,987
Total restricted investments	\$ 592,887	594,698

The Power System also has \$11 million and \$31 million of cash collateral received from securities lending transactions in the City's securities lending program as of June 30, 2017 and 2016, respectively.

All restricted investments are to be used for a specific purpose as follows:

(i) Debt Reduction Funds

The debt reduction funds were established during fiscal year 1997 to provide for the payment of principal and interest on long-term debt obligations and purchased power obligations arising from the Department's participation in IPP and SCPPA (note 5). The Department has transferred funds from purchased power precollections into these funds. Funds from operations may also be transferred by management as funds become available.

(ii) Nuclear Decommissioning Funds

Nuclear decommissioning funds will be used to pay the Department's share of decommissioning PVNGS at the end of its useful life. See note 1(g).

(iii) Natural Gas Fund

The natural gas fund was established to serve as a depository to pay for costs and post margin or collateral in connection with contracts for the purchase and delivery of financial transactions for natural gas. These transactions are entered into to stabilize the natural gas portion of the Department's fuel for generation costs.

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(iv) *Hazardous Waste Treatment Storage and Disposal Fund*

The hazardous waste treatment storage and disposal fund was established to provide financial assurance for closure of the Main Street treatment and disposal facility.

(v) *SCPPA Palo Verde Investment*

The SCPPA Palo Verde investment was a fixed-rate investment held by SCPPA and drawn down over the last two years to pay for purchased power obligations arising from the Department's participation in the SCPPA Palo Verde project. The fixed interest rate is 4.97%, and the maturity date was June 25, 2017.

As of June 30, 2017 and 2016, the Power System's restricted investments and their maturities are as follows (amounts in thousands):

2017 investment type	Fair value	Investment maturities				
		1 to 30 days	31 to 60 days	61 to 365 days	366 days to 5 years	Over 5 years
U.S. government securities	\$ 34,930	—	—	19,967	14,963	—
U.S. agencies	267,949	9,342	9,991	98,199	125,259	25,158
Supranationals	10,997	5,999	—	4,998	—	—
Medium-term corporate notes	134,573	5,066	1,000	76,785	51,722	—
Commercial paper	26,923	16,961	—	9,962	—	—
Certificates of deposit	43,014	8,000	5,002	30,012	—	—
California local agency bonds	28,551	—	8,153	7,011	13,387	—
California state bonds	10,080	—	—	1,005	9,075	—
Other state bonds	35,508	13,998	1,000	6,333	14,177	—
Money market funds	362	362	—	—	—	—
	<u>\$ 592,887</u>	<u>59,728</u>	<u>25,146</u>	<u>254,272</u>	<u>228,583</u>	<u>25,158</u>

2016 investment type	Fair value	Investment maturities				
		1 to 30 days	31 to 60 days	61 to 365 days	366 days to 5 years	Over 5 years
U.S. government securities	\$ 25,090	—	—	10,006	15,084	—
U.S. agencies	256,779	19,998	24,992	65,090	126,565	20,134
Supranationals	9,014	—	—	9,014	—	—
Medium-term corporate notes	122,144	8,077	5,005	36,330	72,732	—
Commercial paper	16,844	5,997	1,098	9,749	—	—
Certificates of deposit	62,026	11,002	3,001	48,023	—	—
California local agency bonds	36,486	5,000	6,503	8,027	16,956	—
California state bonds	14,166	—	—	8,953	5,213	—
Other state bonds	39,923	5,000	6,501	9,121	19,301	—
Money market funds	7,239	7,239	—	—	—	—
SCPPA Palo Verde investment	4,987	—	—	4,987	—	—
	<u>\$ 594,698</u>	<u>62,313</u>	<u>47,100</u>	<u>209,300</u>	<u>255,851</u>	<u>20,134</u>

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(i) *Interest Rate Risk*

The Department's investment policy limits the maturity of its investments to a maximum of 30 years for U.S. government and U.S. government agency securities; 5 years for medium-term corporate notes, California local agency obligations, California state obligations, and other state obligations; 270 days for commercial paper; 397 days for certificates of deposit; and 180 days for bankers' acceptances.

(ii) *Credit Risk*

Under its investment policy and the Government Code, the Department is subject to the prudent investor standard of care in managing all aspects of its portfolios. The prudent investor standard requires that the Department "shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to, the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and in familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency."

The U.S. government agency securities in the portfolio consist of securities issued by government-sponsored enterprises, which are not explicitly guaranteed by the U.S. government. Of the U.S. government agency securities in the portfolio as of June 30, 2017, \$263,629,940 (98%) was rated with either the highest or second highest possible credit ratings by the Nationally Recognized Statistical Rating Organizations (NRSROs) that rated them and \$4,319,051 (2%) was not rated. Of the U.S. government agency securities in the portfolio as of June 30, 2016, \$252,351,411 (98%) was rated with either the highest or second highest possible credit ratings by the NRSRO that rated them and \$4,427,249 (2%) was not rated.

The Department's investment policy specifies that medium-term corporate notes must be rated in a rating category of A or its equivalent or better by a NRSRO. Of the Power System's investments in corporate notes as of June 30, 2017, \$9,579,905 (7%) was rated in the category of AAA, \$71,083,223 (53%) was rated in the category of AA, and \$53,843,279 (40%) was rated in the category of A by at least one NRSRO. The remaining \$65,779 (less than 1%) of investments in corporate notes was not rated. Of the Power System's investments in corporate notes as of June 30, 2016, \$4,052,297 (3%) was rated in the category of AAA, \$58,192,071 (48%) was rated in the category of AA, and \$59,825,246 (49%) was rated in the category of A by at least one NRSRO. The remaining \$74,730 (less than 1%) of investments in corporate notes was not rated.

The Department's investment policy specifies that commercial paper must be of the highest ranking or of the highest letter and number rating as provided for by at least two NRSROs. As of June 30, 2017 and 2016, all of the Power System's investments in commercial paper were rated with at least the highest letter and number rating as provided by at least two NRSROs.

The Department's investment policy provides that negotiable certificates of deposit must be of the highest ranking or letter and number rating as provided for by at least two NRSROs and that for nonnegotiable certificates of deposit, the full amount of principal and interest is insured by the Federal Deposit Insurance Corporation (FDIC) or National Credit Union Administration. As of

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June 30, 2017, the Power System's investments in certificates of deposits included \$42,014,082 of negotiable certificates of deposit with at least the highest letter and number rating as provided by at least two NRSROs and \$1,000,000 of nonnegotiable certificates of deposit fully insured by the FDIC. As of June 30, 2016, the Power System's investments in certificates of deposits included \$61,025,451 of negotiable certificates of deposit with at least the highest letter and number rating as provided by at least two NRSROs and \$1,000,000 of nonnegotiable certificates of deposit fully insured by the FDIC.

The Department's investment policy specifies that California local agency obligations must be rated in a rating category of A or its equivalent or better by a NRSRO. As of June 30, 2017, all of Power System's investments in California local agency bonds were rated in the category of AA. Of the Power System's investments in California local agency bonds as of June 30, 2016, \$34,480,318 (95%) was rated in the category of AA and \$2,005,120 (5%) was rated in the category of A.

The Department's investment policy specifies that State of California obligations must be rated in a rating category of A or its equivalent or better by a NRSRO. As of June 30, 2017, all of the Power System's investments in State of California obligations were rated in the category of AA by at least one NRSRO. Of the Power System's investments in State of California obligations as of June 30, 2016, \$1,231,784 (9%) was rated in the category of AAA and \$12,934,431 (91%) was rated in the category of AA by at least one NRSRO.

The Department's investment policy specifies that obligations of other states in addition to California must be rated in a rating category of A or its equivalent or better by a NRSRO. Of the Power System's investments in other state obligations as of June 30, 2017, \$15,352,490 (43%) was rated in the category of AAA, \$13,163,374 (37%) was rated in the category of AA, \$1,993,680 (6%) was rated in the category of A, and \$4,998,104 (14%) was rated with the highest short-term rating by at least one NRSRO. Of the Power System's investments in other state obligations as of June 30, 2016, \$7,223,320 (18%) was rated in the category of AAA and \$32,699,881 (82%) was rated in the category of AA by at least one NRSRO.

The Department's investment policy specifies that money market funds may be purchased as allowed under the Government Code, which requires that the fund must have either (1) attained the highest ranking or highest letter and numerical rating provided by not less than two NRSROs or (2) retained an investment adviser registered or exempt from registration with the Securities and Exchange Commission (SEC) with not less than five years' experience in managing money market mutual funds with assets under management in excess of \$500 million. As of June 30, 2017 and 2016, each of the money market funds in the portfolio had the highest possible ratings by at least two NRSROs.

(iii) Concentration of Credit Risk

The Department's investment policy specifies that there is no percentage limitation on the amount that can be invested in U.S. government agency securities, except that a maximum of 30% of the

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cost value of the portfolio may be invested in the securities of any single U.S. government agency issuer.

Of the Power System's total investments as of June 30, 2017, \$102,726,035 (17%) was invested in securities issued by the Federal Home Loan Bank, \$88,814,829 (15%) was invested in securities issued by the Federal Home Loan Mortgage Corporation, and \$46,504,874 (8%) was invested in securities issued by the Federal National Mortgage Association.

Of the Power System's total investments as of June 30, 2016, \$115,351,927 (19%) was invested in securities issued by the Federal Home Loan Bank, \$72,599,346 (12%) was invested in securities issued by the Federal Home Loan Mortgage Corporation, and \$49,303,772 (8%) was invested in securities issued by the Federal National Mortgage Association.

(iv) Custodial Risk

All investments are held in the Department's name, and therefore, they do not have custodial risk.

(v) Fair Value Measurements

The Department holds investments and derivative instruments that are measured at fair value on a recurring basis. Because investing is not a core part of the Department's mission, the Department determines that the disclosures related to these investments only need to be disaggregated by major type. The Department chooses a tabular format for disclosing the levels within the fair value hierarchy. The Department categorizes its fair value measurements within the fair value hierarchy established by U.S. GAAP.

The hierarchy is based on the valuation inputs used to measure the fair value of the asset, as follows:

Level 1 inputs are quoted prices for identical assets or liabilities in an active market

Level 2 inputs are quoted prices of similar assets or liabilities in active or not active markets

Level 3 inputs are unobservable inputs using the best information available to management.

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	Fair value using				Not Classified
	June 30, 2017	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2) (In thousands)	Significant unobservable inputs (Level 3)	
Investments by fair value level:					
Debt securities:					
U.S. government securities	\$ 34,930	34,930	—	—	—
U.S. agencies	267,949	—	267,949	—	—
Supranationals	10,997	—	10,997	—	—
Medium-term corporate notes	134,572	—	134,572	—	—
California local agency bonds	28,550	—	28,550	—	—
California state bonds	10,081	—	10,081	—	—
Other state bonds	35,508	—	35,508	—	—
Total debt securities	<u>522,587</u>	<u>34,930</u>	<u>487,657</u>	<u>—</u>	<u>—</u>
Other:					
Commercial paper	\$ 26,924	—	26,924	—	—
Certificates of deposit	43,014	—	43,014	—	—
Money market funds	362	—	—	—	362
Total other	<u>70,300</u>	<u>—</u>	<u>69,938</u>	<u>—</u>	<u>362</u>
Total investments by fair value level	<u>\$ 592,887</u>	<u>34,930</u>	<u>557,595</u>	<u>—</u>	<u>362</u>
Derivative instruments:					
Financial natural gas hedges	\$ (14,640)	—	(14,640)	—	—

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	Fair value using				Not Classified
	June 30, 2016	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2) (In thousands)	Significant unobservable inputs (Level 3)	
Investments by fair value level:					
Debt securities:					
U.S. government securities	\$ 25,090	25,090	—	—	—
U.S. agencies	256,779	—	256,779	—	—
Supranationals	9,014	—	9,014	—	—
Medium-term corporate notes	122,144	—	122,144	—	—
California local agency bonds	36,486	—	36,486	—	—
California state bonds	14,166	—	14,166	—	—
Other state bonds	39,923	—	39,923	—	—
Total debt securities	<u>503,602</u>	<u>25,090</u>	<u>478,512</u>	<u>—</u>	<u>—</u>
Other:					
Commercial paper	16,844	—	16,844	—	—
Certificates of deposit	62,026	—	62,026	—	—
Money market funds	7,239	—	—	—	7,239
SCPPA Palo Verde investment	4,987	—	—	—	4,987
Total other	<u>91,096</u>	<u>—</u>	<u>78,870</u>	<u>—</u>	<u>12,226</u>
Total investments by fair value level	<u>\$ 594,698</u>	<u>25,090</u>	<u>557,382</u>	<u>—</u>	<u>12,226</u>
Derivative instruments:					
Financial natural gas hedges	\$ (23,379)	—	(23,379)	—	—

Debt and other securities classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those securities. Debt securities classified in Level 2 of the fair value hierarchy are valued using a multidimensional relationship model or matrix pricing model utilizing market data, including, but not limited to, benchmark yields, reported trades, and broker-dealer quotes. Natural gas hedges are valued using forward market prices available from broker quotes and exchanges. The SCPPA Palo Verde Guaranteed Investment Contract is recorded at contract value and, thus, is not required to be classified in the fair value hierarchy. Money market funds have maturities of less than one year and thus are recorded at amortized cost and not required to be classified.

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(b) Pooled Cash

The Power System's cash, cash equivalents, and its collateral value of the City's securities lending program are included within the City Treasury's general and special investment pool. As of June 30, 2017 and 2016, the Power System's share of the City's general and special investment pool was \$1,665,102 and \$1,793,859, which represents approximately 16.2% and 18.0% of the Pool, respectively. Amounts pooled in the City Treasury's general and special investment pool are not required to be classified in the fair value hierarchy per GASB Statement No. 72 since they are part of an internal investment pool.

Pooled cash is recorded as follows on the statement of position (in thousands):

	June 30	
	2017	2016
Cash and cash equivalents – unrestricted	\$ 991,182	1,331,543
Cash and cash equivalents – restricted noncurrent	312,267	168,785
Cash and cash equivalents – restricted current	350,256	262,430
Subtotal cash and cash equivalents per cash flow	1,653,705	1,762,758
Cash – securities lending transactions	11,397	31,101
	\$ 1,665,102	1,793,859

The cash balances of substantially all funds on deposit in the City Treasury are pooled and invested by the City Treasurer for the purpose of maximizing interest earnings through pooled investment activities, but safety and liquidity still take precedence over return. Special pool participants include the City, airports, the Department of Water and Power, harbor, sanitation, and the Municipal Improvement Corporation of Los Angeles. Interest earned on pooled investments is allocated to and recorded in certain participating funds, as authorized by the Council and permitted by the City Charter and the Code, based on each fund's average daily deposit balance. Unless allocation provisions are specifically stipulated in City ordinance, Council action, or funding source, interest earned on certain funds are allocated to and recorded in the general fund. The City measures and categorizes its investments using fair value measurement guidelines established by GAAP and GASB Statement No. 72.

Pursuant to California Government Code Section 53607 and the Council File No. 94-2160, the City Treasury shall render to the Council a statement of investment policy (the Policy) annually. Council File No. 11-1740 was adopted on December 12, 2016 as the City's investment policy. This Policy shall remain in effect until the Council and the mayor approve a subsequent revision. The Policy governs the City's pooled investment practices. The Policy addresses soundness of financial institutions in which the city treasurer will deposit funds and types of investment instruments permitted by California Government Code Sections 53600-53638, 16340, and 16429.1. The city treasury further reports that the current policy allows for the purchase of investments with maturities up to 30 years.

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At June 30, 2017, the investments held in the City Treasury's general and special investment pool programs and their maturities are as follows (in thousands):

Type of investments	Amount	Investment maturities			
		1 to 30 Days	31 to 60 Days	61 to 365 Days	366 Days to 5 years
U.S. Treasury notes	\$ 4,784,091	—	—	2,812	4,761,266
U.S. Agencies securities	1,468,181	182,345	220,935	560,889	469,324
Medium-term notes	1,440,354	—	—	190,051	1,250,303
Mutual fund	7,251	7,251	—	—	—
Commercial paper	1,418,930	732,478	238,464	447,989	—
Municipal bonds	79,684	—	—	—	79,683
Asset backed securities	70,100	—	—	—	70,100
Supranational obligations	650,957	454,777	15,000	31,755	149,425
Short-term investment funds	284,148	284,148	—	—	—
Securities lending short-term repurchase agreement	67,115	67,115	—	—	—
Total general and special pools	\$ 10,270,811	1,728,114	474,399	1,233,496	6,780,101

Interest Rate Risk. The Policy limits the maturity of its investments to 5 years for the U.S. Treasury and U.S. Agencies obligations, medium-term notes, CD placement service, negotiable certificates of deposit, collateralized bank deposits, mortgage pass-through securities, supranational obligations, and bank/time deposits; 1 year for repurchase agreements; 270 days for commercial paper; 180 days for bankers' acceptances; 92 days for reverse repurchase agreements; and no maturity for mutual funds. The Policy also allows City funds with longer-term investments horizons to be invested in securities that, at the time of the investment have a term remaining to maturity in excess of 5 years but with a maximum final maturity of 30 years.

Credit Risk. The Policy establishes minimum credit rating requirements for investments. There are no credit quality requirements for local agency bonds, U.S. Treasury obligations, State of California obligations, California local agency obligations, and U.S. Agencies (U.S. government-sponsored enterprises) securities. The City's \$1.5 billion investments in U.S. government sponsored enterprises consist of securities issued by the Federal Home Loan Bank – \$758.2 million, Federal National Mortgage Association (Fannie Mae) – \$354.5 million, Federal Home Loan Mortgage Corporation (Freddie Mac) – \$240.1 million, Federal Agriculture Mortgage Corporation (Farmer Mac) – \$95.2 million, and Tennessee Valley Authority – \$20.1 million. Of the City's \$1.5 billion investments in U.S. Agencies securities, \$499.1 million were rated AA+ by S&P and Aaa by Moody's; \$969.0 million were not rated individually by S&P nor Moody's.

Medium-term notes must be issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States. Medium-term notes must have at least an A rating at the time of purchase. The City's

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\$1.4 billion investments in medium-term notes consist of securities issued by banks and corporations that comply with these requirements and were rated A or better by S&P and A3 or better by Moody's. Subsequent to purchase, two issuers of \$62.6 million medium-term notes were downgraded to BBB+ by S&P and A3 by Moody's, and one issuer of \$20.0 million medium-term notes was downgraded to A by S&P and Baa1 by Moody's.

Commercial paper issues must have the highest letter and number rating by an NRSRO. The issuing corporation must be organized and operating within the United States and have assets in excess of \$500.0 million. The City's \$1.4 billion investments in commercial paper were rated A-1+/A-1 by S&P and P-1 by Moody's.

Mutual funds must receive the highest ranking by at least two NRSRO. The City's \$7.3 million investment in mutual fund were rated AAAm by S&P and not rated by Moody's.

Municipal bonds have no minimum rating requirement. The City's \$79.7 million investments in municipal bonds were rated AA- by S&P and Aa3 by Moody's.

Investments in supranational coupons must have a minimum of AA rating. The City's investments in supranational coupons of \$149.4 million were rated AAA by S&P and Aaa by Moody's; \$501.5 million were not rated individually by S&P nor Moody's.

Concentration of credit risk. The Policy does not allow more than 40% of its investment portfolio to be invested in commercial paper or bankers' acceptances, 30% in certificates of deposit or medium-term notes, 20% in mutual funds, money market mutual funds, or mortgage pass-through securities. The Policy further provides for a maximum concentration limit of 10% in any one issuer, including its related entities. There is no percentage limitation on the amounts that can be invested in U.S. Treasury and U.S. Agencies obligations. The City's pooled investments comply with these requirements. GAAP requires disclosure of certain investments in any one issuer that represent 5% or more of total investments. Of the City's total pooled investments as of June 30, 2017, \$693.8 million (6.8%) were invested in securities issued by Federal Home Loan Bank.

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At June 30, 2016, the investments held in the City Treasury's General and Special Investment Pool Programs and their maturities are as follows (in thousands):

Type of investments	Amount	Investment maturities				
		1 to 30 Days	31 to 60 Days	61 to 365 Days	366 Days to 5 years	Over 5 years
U.S. Treasury bills	\$ 206,762	144,991	34,991	26,780	—	—
U.S. Treasury notes	4,695,497	—	—	36,463	4,631,290	27,744
U.S. Agencies securities	1,362,106	335,597	130,941	430,867	445,957	18,744
Medium-term notes	1,321,557	20,008	—	115,563	1,185,986	—
Mutual fund	126,632	126,632	—	—	—	—
Negotiable certificates of deposit	10,000	10,000	—	—	—	—
Commercial paper	1,617,998	1,166,671	391,383	59,944	—	—
Municipal bonds	60,885	—	—	—	60,885	—
Supranational obligations	242,182	13,971	16,190	70,068	141,953	—
Short-term investment funds	170,261	170,261	—	—	—	—
Securities lending short-term repurchase agreement	166,278	166,278	—	—	—	—
Total general and special pools	\$ 9,980,158	2,154,409	573,505	739,685	6,466,071	46,488

Interest rate risk. The Policy limits the maturity of its investments to 5 years for the U.S. Treasury and government agency securities, medium-term notes, CD placement service, negotiable certificates of deposit, collateralized bank deposits, mortgage pass-through securities, supranational obligations, and bank/time deposits; 1 year for repurchase agreements; 270 days for commercial paper; 180 days for bankers' acceptances; 92 days for reverse repurchase agreements; and no maturity for mutual funds. The Policy also allows City funds with longer-term investments horizons to be invested in securities that, at the time of the investment, have a term remaining to maturity in excess of 5 years but with a maximum final maturity of 30 years.

Credit risk. The Policy establishes minimum credit rating requirements for investments. There are no credit quality requirements for local agency bonds, U.S. Treasury obligations, State of California Obligations, California Local Agency obligations, and U.S. Agencies (U.S. government-sponsored enterprises) securities. The City's \$1 billion investments in U.S. government in between sponsored enterprises consist of securities issued by the Federal Home Loan Bank – \$633 million, Federal National Mortgage Association (Fannie Mae) – \$428 million, Federal Home Loan Mortgage Corporation (Freddie Mac) – \$225 million, Federal Farm Credit Bank – \$25 million, Federal Agriculture Mortgage Corporation (Farmer Mac) – \$30 million, and Tennessee Valley Authority – \$20 million. Of the City's \$1 billion investments in U.S. Agencies securities, \$545 million were rated AA+ by S&P and Aaa by Moody's; \$817 million were not rated individually by S&P nor Moody's (issuers of these securities are rated AA+/A-1+ by S&P and Aaa/P-1 by Moody's).

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Medium-term notes must be issued by corporations organized and operating within the United States or by depository institutions licensed by the United States or any state and operating within the United States. Medium-term notes must have at least an A rating at the time of purchase. The City's \$1 billion investments in medium-term notes consist of securities issued by banks and corporations that comply with these requirements and were rated A or better by S&P and A3 or better by Moody's. Subsequent to purchase, one issuer of \$5 million medium-term notes was downgraded to A- by S&P and Baa2 by Moody's, one issuer of \$5 million medium-term notes was downgraded to BBB+ by S&P and Baa1 by Moody's, two issuers of \$63 million medium-term notes were downgraded to BBB+ by S&P and A3 by Moody's, and one issuer of \$20 million medium-term notes was downgraded to A by S&P and Baa1 by Moody's.

Commercial paper issues must have a minimum of A-1 or equivalent rating. If the issuer has issued long-term debt, it must be rated A without regard to modifiers. The issuing corporation must be organized and operating within the United States and have assets in excess of \$500 million. The City's \$1 billion investments in commercial paper were rated A-1+/A-1 by S&P and P-1 by Moody's.

Mutual fund must receive the highest ranking by at least two nationally recognized rating agencies. The City's \$127 million investment, in mutual funds were rated AAAm by S&P and not rated by Moody's.

Negotiable certificates of deposit have no minimum rating requirement. The City's \$10 million investments in negotiable certificates of deposit were rated A-1+/A- by S&P but P-1 by Moody's.

Municipal bonds have no minimum rating requirement. The City's \$61 million investments in municipal bonds were rated AA/AA- by S&P and Aa2/Aa3 by Moody's.

Investments in supranational coupons must have a minimum of AA rating. The City's investments in supranational coupons of \$142 million were rated AAA by S&P and Aaa by Moody's; \$100 million were not rated individually by S&P nor Moody's. These short-term securities are backed by the full faith of the issuing entities, which are rated AAA/Aaa.

Concentration of Credit Risk. The Policy does not allow more than 40% of its investment portfolio to be invested in commercial paper or bankers' acceptances, 30% in certificates of deposit or medium-term notes, and 20% in mutual funds, money market mutual funds, or mortgage pass-through securities. The Policy further provides for a maximum concentration limit of 10% in any one issuer, including its related entities. There is no percentage limitation on the amounts that can be invested in U.S. Treasury and government agencies. The City's pooled investments comply with these requirements. GAAP requires disclosure of certain investments in any one issuer that represent 5% or more of total investments. Of the City's total pooled investments as of June 30, 2016, \$633 million (6%) were invested in securities issued by Federal Home Loan Bank.

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The following table identifies the investment types that are authorized by the Policy as of June 30, 2017 and 2016:

- * Represents where the City's investment policy is more restrictive than the California Government Code. The sources used are Sections 16340, 16429.1, 53601, 53601.8, 53635, 53635.2, and 53638. Municipal Utilities Districts have the authority under the Public Utilities Code Section 12871 to invest in certain securities not addressed here.

Other restrictions on investments are summarized as follows:

Section 53601 provides that the maximum term of any investment authorized under this section, unless otherwise stated, is five years. However, the legislative body may grant express authority to make investments either specifically or as a part of an investment program approved by the legislative body that exceeds this five-year maturity limit. Such approval must be issued no less than three months prior to the purchase of any security exceeding the five-year maturity limit.

Percentages apply to all portfolio investments, regardless of source of funds. For instance, cash from a reverse repurchase agreement would be subject to the restrictions.

No more than 30% of the agency's money may be in bankers' acceptances of any one commercial bank.

"Select Agencies" are defined as a "city, a district, or other local agency that does not pool money in deposits or investment with other local agencies, other than local agencies that have the same governing body."

Local Agencies, other than counties or a city and county, may purchase no more than 10% of outstanding commercial paper of any single issuer.

Issuing Corporation must be organized and operating within the United States and have assets in excess of \$500.0 million.

"Other Agencies" are counties, a city and county, or other local agency "that pools money in deposits or investments with other local agencies, including local agencies that have the same governing body." Local agencies that pool exclusively with other local agencies that have the same governing body must adhere to the limits set for "Select Agencies" above.

No more than 30% of the agency's money may be invested in deposits, including CDs, through a placement service. No more than 30% of the agency's money may be invested in CDs through a placement service and negotiable CDs based on Sections 53601.8, 53635.8 and 53601(i). Excluding purchases of certificates of deposit pursuant to Sections 53601.8 and 53635.8, no more than 10% of the agency's money may be invested with any one private sector entity that assists in the placement of deposits.

Reverse repurchase agreements or securities lending agreements may exceed the 92-day term if the agreement includes a written codicil guaranteeing a minimum earning or spread for the entire period

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between the sale of a security using a reverse repurchase agreement or securities lending agreement and the final maturity dates of the same security.

Reverse repurchase agreements must be made with primary dealers of the Federal Reserve Bank of New York or with a nationally chartered or state-chartered bank that has a significant relationship with the local agency. The local agency must have held the securities used for the agreements for at least 30 days.

“Medium-term notes” are defined in Section 53601 as “all corporate and depository institution debt securities with a maximum remaining maturity of five years or less, issued by corporations organized and operating within the U.S. or by depository institutions licensed by the U.S. or any state and operating within the U.S.”

No more than 10% invested in any one mutual fund.

A mutual fund must receive the highest ranking by not less than two nationally recognized rating agencies or the fund must retain an investment advisor who is registered with the SEC (or exempt from registration), has assets under management in excess of \$500.0 million, and has at least five years’ experience investing in instruments authorized by Sections 53601 and 53635.

A money market mutual fund must receive the highest ranking by not less than two nationally recognized statistical rating organizations or retain an investment advisor registered with the SEC or exempt from registration and who has not less than five years’ experience investing in money market instruments with assets under management in excess of \$500.0 million.

Issuer must be rated in the category “AA”, or its equivalent or better as provided by a nationally recognized rating agency.

A joint powers authority pool must retain an investment advisor who is registered with the SEC (or exempt from registration), has assets under management in excess of \$500.0 million, and has at least five years’ experience investing in instruments authorized by Section 53601, subdivisions (a) to (o).

Local entities can deposit between \$200.0 million and \$10.0 billion into the Voluntary Investment Program Fund, upon approval by their governing bodies. Deposits in the fund will be invested in the Pooled Money Investment Account.

These are only those obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, International Finance Corporation, and Inter-American Development Bank.

General Investment Pool Securities Lending Program.

Securities lending is permitted and limited under provisions of California Government Code Section 53601. The Council approved the Securities Lending Program (SLP) on October 22, 1991 under Council File No. 91-1860, which complies with the California Government Code. The objectives of the SLP in priority order are safety of loaned securities and prudent investment of cash collateral to

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enhance revenue from the investment program. The SLP is governed by a separate policy and guidelines.

The City's custodial bank acts as the securities lending agent. In the event a counterparty defaults by reason of an act of insolvency, the bank shall take all actions, which it deems necessary or appropriate to liquidate permitted investment and collateral in connection with such transaction, and shall make a reasonable effort for two business days (the Replacement Period) to apply the proceeds thereof to the purchase of securities identical to the loaned securities not returned. If during the Replacement Period the collateral liquidation proceeds are insufficient to replace any of the loaned securities not returned, the bank shall, subject to payment by the City of the amount of any losses on any permitted investments, pay such additional amounts, as necessary, to make such replacement.

Under the provisions of the SLP, and in accordance with the California Government Code, no more than 20% of the market value of the General Investment Pool is available for lending. The City loans out U.S. Treasury notes and U.S. Agencies securities (e.g., Fannie Mae, Freddie Mac, Federal Home Loan Bank, Federal Agricultural Mortgage Corporation, Federal Farm Credit Bank, and Tennessee Valley Authority), medium-term notes, and Supranational coupons. The City receives cash as collateral on the loaned securities, which is reinvested in securities permitted under the Policy. In addition, the City receives securities as collateral on loaned securities, which the City has no ability to pledge or sell without borrower default. In accordance with the California Government Code, the securities lending agent marks to market the value of both the collateral and the reinvestments daily. Except for open loans where either party can terminate a lending contract on demand, term loans have a maximum life of 60 days. Earnings from securities lending accrue to the Pool and are allocated on a pro rata basis to all Pool participants.

During the fiscal year 2017, collateralizations on all loaned securities were compliant with the required 102% of the market value. The City can sell collateral securities only in the event of borrower default. The lending agent provides indemnification for borrower default. There were no violations of legal or contractual provisions and no borrower or lending agent default losses during the fiscal year. There was no credit risk exposure to the City, because the amounts owed to the borrowers exceeded the amounts borrowed. Loaned securities are held by the City's agents in the City's name and are not subject to custodial credit risk.

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The following table provides information on securities lent and collateral received as of June 30 (in thousands):

	<u>2017</u>	<u>2016</u>
Type of investment lent:		
For cash collateral:		
U.S. Agencies securities	\$ 40,648	10,258
U.S. Treasury notes	1,012	142,280
Supranational coupons	24,014	8,054
Medium-term notes	—	2,339
Total lent for cash collateral	<u>65,674</u>	<u>162,931</u>
For noncash collateral:		
U.S. Treasury notes	981,789	415,604
U.S. Agencies securities	31,397	161,334
Medium-term notes	—	1,364
Total lent for noncash collateral	<u>1,013,186</u>	<u>578,302</u>
Total securities lent	<u>\$ 1,078,860</u>	<u>741,233</u>
Type of collateral received		
Cash collateral*	\$ 67,115	166,278
Noncash collateral**		
For lent U.S. Treasury notes, U.S. Agencies securities, medium-term notes, and Supranational Coupons	<u>1,037,782</u>	<u>589,880</u>
Total collateral received	<u>\$ 1,104,897</u>	<u>\$ 756,158</u>

* Amount represents cash collateral received and reinvested in repurchase agreements that have the mark-to-market value of the cash collateral pool at 102% for the liquidity of the portfolio and 100% for the duration portfolio for fiscal years 2016 and 2017.

** The City has no ability to pledge or sell collateral securities without borrower default.

Fair Value Measurements

The City measures and categorizes its investments using fair value measurement guidelines established by GAAP. The hierarchy is based on the valuation inputs used to measure the fair value of the asset or liability. The levels of valuation inputs are as follows:

Level 1 – Quoted prices for identical assets or liabilities in an active market

Level 2 – Observable inputs other than quoted market prices

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Level 3 – Unobservable inputs.

At June 30, 2017 and 2016, the City's summary of the fair value hierarchy of investments is as follows (in thousands):

<u>Investments</u>	<u>Amount</u>	<u>June 30, 2017</u>	
		<u>Fair value measurements using</u>	<u>Quoted prices</u>
		<u>in active</u>	<u>Significant</u>
		<u>markets for</u>	<u>other</u>
		<u>identical</u>	<u>observable</u>
		<u>Assets (Level 1)</u>	<u>inputs</u>
		<u>Assets (Level 1)</u>	<u>Assets (Level 2)</u>
Investment Subject to fair value hierarchy:			
U.S. Treasury notes	\$ 4,784,091	601,390	4,182,701
U.S. Agencies securities	514,127	35,348	478,779
Medium-term notes	1,440,354	—	1,440,354
Municipal bonds	79,684	—	79,684
Asset-backed securities	70,100	—	70,100
Supranational obligations	149,425	—	149,425
Total investments subject to fair value	<u>7,037,781</u>	<u>636,738</u>	<u>6,401,043</u>
Investment not subject to fair value hierarchy:			
Mutual fund*	7,251		
Short-term investment funds*	284,148		
U.S. Agencies securities*	954,054		
Commercial paper*	1,418,930		
Supranational obligations*	501,532		
Securities lending short-term repurchase agreement **	67,115		
Total investments not subject to fair value	<u>3,233,030</u>		
Total Investments	<u>\$ 10,270,811</u>		

* These investments are recorded at amortized cost that have remaining maturities of one year or less at the time of purchase.

** These investments are recorded based on the cash collateral received and reinvested in repurchase agreement.

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<u>Investments</u>	<u>Amount</u>	<u>June 30, 2016</u>	
		<u>Fair value</u>	
		<u>measurements using</u>	
		<u>Quoted prices</u>	<u>Significant</u>
		<u>in active</u>	<u>other</u>
		<u>markets for</u>	<u>observable</u>
		<u>identical</u>	<u>inputs</u>
		<u>Assets (Level 1)</u>	<u>Assets (Level 2)</u>
Investment subject to fair value hierarchy:			
U.S. Treasury notes	\$ 4,695,497	212,916	4,482,581
U.S. Agencies securities	570,442	—	570,442
Medium-term notes	1,321,557	—	1,321,557
Municipal bonds	60,885	—	60,885
Supranational obligations	141,953	—	141,953
Total Investments subject to fair value	<u>6,790,334</u>	<u>212,916</u>	<u>\$ 6,577,418</u>
Investment not subject to fair value hierarchy:			
Mutual fund *	126,632		
Short-term investment funds*	170,261		
U.S. Treasury bills*	206,762		
U.S. Agencies securities*	791,664		
Negotiable certificates of deposit*	10,000		
Commercial paper*	1,617,998		
Supranational obligations*	100,229		
Securities lending short-term repurchase agreement**	<u>166,278</u>		
Total investments not subject to fair value	<u>3,189,824</u>		
Total investments	<u>\$ 9,980,158</u>		

* These investments are recorded at amortized cost that have remaining maturities of one year or less at the time of purchase.

** These investments are recorded based on the cash collateral received and reinvested in repurchase agreement.

Investments classified in Level 1 of the fair value hierarchy of \$636.7 million and \$212.9 million at June 30, 2017 and 2016, respectively, are valued using observable unadjusted quoted prices in an active market.

Investments in the Level 2 classification totaling \$6.4 billion and \$6.6 billion at June 30, 2017 and 2016, respectively, are valued using matrix pricing obtained from various pricing sources by the City's custodian bank. At the time of purchase, securities are automatically assigned a primary pricing source, which is used in the portfolio valuation report and evaluated based on market inputs such as

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benchmark yields, reported trades, broker-dealer quotes, issuer spreads, two-sided markets, benchmark securities, bids, offers, and reference data.

(8) Derivative Instruments

The Power System follows GASB Statement No. 53, which specifically requires governments to measure and report most derivative instruments at fair value in their financial statements, which are prepared using the economic resources measurement focus and the accrual basis of accounting. The requirement of reporting the derivative instruments at fair value on the face of the basic financial statements gives the users of those statements a clearer look into the risks their governments are sometimes exposed to when they enter into these transactions and how those risks are managed. The statement also addresses hedge accounting requirements and improve disclosures, providing a summary of the government's derivative instrument activity, its objectives for entering into derivative instruments, and its significant terms and risks.

In accordance with GASB Statement No. 53, the Power System records the fair value of its financial natural gas hedges on the statements of net position. As of June 30, 2017 and 2016, the fair values of the financial natural gas hedges were approximately \$(14.6) million and approximately \$(23.4) million, respectively.

(a) Financial Natural Gas Hedges

The Department enters into natural gas hedging contracts in order to stabilize the cost of gas needed to produce electricity to serve its customers. It is designed to cap gas prices over a portion of the forecasted gas requirements.

The Department does not speculate when entering into financial transactions. Financial hedges are variable to fixed-rate swaps and are layered by volumetric averaging. The Department is exposed to financial settlement risk if the counterparties default and/or the agreements are terminated. The Department did not receive any payments at the inception of any swap transaction.

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As of June 30, 2017 and 2016, the Power System's financial natural gas hedges by fiscal year are the following (amounts in thousands):

2017	Notional amount (Total contract quantities*)	Contract price range dollar per unit	First effective date	Last termination date	Fair value
Derivative description					
Financial natural gas:					
FY 2017–2018	18,432,500	\$ 2.72–7.14	07/01/17	06/30/18	\$ (12,493)
FY 2018–2019	10,950,000	2.51–2.78	07/01/18	06/30/19	(1,411)
FY 2019–2020	5,490,000	2.48–2.83	07/01/19	06/30/20	(704)
FY 2020–2021	<u>365,000</u>	2.61	07/01/20	06/30/21	<u>(32)</u>
Total	<u>35,237,500</u>	\$	07/01/17	06/30/21	<u>\$ (14,640)</u>

2016	Notional amount (Total contract quantities*)	Contract price range dollar per unit	First effective date	Last termination date	Fair value
Derivative description					
Financial natural gas:					
FY 2016–2017	3,197,500	\$ 6.61–9.83	07/01/16	06/30/17	\$ (14,656)
FY 2017–2018	<u>2,190,000</u>	6.76–7.14	07/01/17	06/30/18	<u>(8,723)</u>
Total	<u>5,387,500</u>	\$ 6.61–9.83	07/01/16	06/30/18	<u>\$ (23,379)</u>

* Contract quantities in million British thermal units

The fair value of the natural gas hedges decreased by \$8.74 million during the year ended June 30, 2017, is reported as a liability, and is offset by a deferred outflow on the statements of net position. All fair values were estimated using forward market prices available from broker quotes and exchanges.

(b) Credit Risk

The Power System is exposed to credit risk related to nonperformance by its wholesale counterparties under the terms of contractual agreements. In order to limit the risk of counterparty default, the Department has implemented a Wholesale Marketing Counterparty Evaluation Policy, which was renamed the Counterparty Evaluation Credit Policy (the Counterparty Policy) in 2008, and was updated and approved by the Board on November 28, 2017. Under the updated policy, the scope has been expanded beyond physical power transmission, physical natural gas, and financial natural gas,

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to include environmental credits and renewable energy credits. It also provided the use of new analytic tools and more stringent credit enhancement requirements.

The Policy provides a credit limit structure with two categories, namely: short-term and long-term. The short-term structure is applicable to transactions with terms of up to 18 months and the long-term structure cover transactions beyond 18 months. The Policy includes provisions to limit risk including the use of long-term credit ratings of all Department's counterparties; expected default frequency equivalent credit rating for short term transactions; the requirement for credit enhancements (including advance payments, irrevocable letters of credit, escrow trust accounts, and parent company guarantees) for counterparties that do not meet an acceptable level of risk; and the use of standardized agreements, which allow for the netting of positive and negative exposures associated with a single counterparty.

As of June 30, 2017, the 9 financial natural gas hedge counterparties were rated by Moody's as follows: one at Aa2, two at A3, one at A2, three at A1, one Baa1, and one WR. The counterparties were rated by S&P as follows: two at AA-, one at A+, one at A, two at A-, and three at BBB+. As of June 30, 2016, the 10 financial natural gas hedge counterparties were rated by Moody's as follows: two at Aa3, one at Aa2, two at A3, two at A2, two at A1, and one WR. The counterparties were rated by S&P as follows: two at AA-, one at A+, three at A, two at A-1, and two at BBB+.

Based on the International Swap Dealers Association agreements, the Department or the counterparty may be required to post collateral to support the financial natural gas hedges subject to credit risk in the form of cash, negotiable debt instruments (other than interest-only and principal-only securities), or eligible letters of credit. Collateral posted is held by a custodian. As of June 30, 2017 and 2016, the fair values of the financial natural gas hedges are within the credit limits, and collateral posting was not required.

(c) Basis Risk

Power System is exposed to basis risk between the financial natural gas hedges, which are settled monthly at NW Rocky Mountains Index, and the hedged gas deliveries, which are daily spot purchases at Kern River, Opal prices. However, these pricing points are in the same region and are highly correlated.

(d) Termination Risk

The Power System or its counterparties may terminate the contractual agreements if the other party fails to perform under the terms of the contract. No termination events have occurred, and there are no out-of-the-ordinary termination events contained in contractual documents.

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(9) Long-Term Debt

Long-term debt outstanding as of June 30, 2017 and 2016 consists of revenue bonds and refunding revenue bonds due serially in varying annual amounts as follows (amounts in thousands):

Bond issues	Date of issue	Effective interest rate %	Fiscal year of last scheduled maturity	Principal outstanding	
				2017	2016
Issue of 2001, Series B	06/05/01	Variable	2035	\$ 579,200	580,800
Issue of 2001, Series C1	11/15/01	4.788	2017	—	1,950
Issue of 2002, Series A	08/22/02	Variable	2036	334,700	388,500
Issue of 2002, Series C2	11/22/02	4.375	2018	5,119	5,220
Issue of 2004, Series C3	04/07/04	4.298	2020	4,231	4,384
Issue of 2006, Series C4	03/01/06	4.040	2017	3,204	4,913
Issue of 2007, Series A1	10/18/07	4.659	2040	12,215	237,325
Issue of 2007, Series A2	10/18/07	4.638	2033	—	182,120
Issue of 2008, Series A1	11/25/08	5.583	2039	200,000	200,000
Issue of 2008, Series A2	11/25/08	5.039	2033	252,240	315,605
Issue of 2009, Series A	02/19/09	4.773	2040	111,980	114,570
Issue of 2009, Series B	06/02/09	4.563	2025	171,590	172,125
Issue of 2010, Series A	06/02/10	3.898	2041	616,000	616,000
Issue of 2010, Series B	06/02/10	3.015	2023	28,470	28,485
Issue of 2010, Series C	08/25/10	2.188	2028	139,775	139,775
Issue of 2010, Series D	12/02/10	4.342	2046	760,200	760,200
Issue of 2011, Series A	06/30/11	2.715	2023	448,895	456,355
Issue of 2012, Series A	10/25/12	2.936	2036	100,355	100,355
Issue of 2012, Series B	10/25/12	4.164	2044	350,000	350,000
Issue of 2013, Series A	04/02/13	2.504	2032	498,200	507,205
Issue of 2013, Series B	06/04/13	3.347	2033	452,145	452,145
Issue of 2013, Series C	06/04/13	4.441	2038	27,855	27,855
Issue of 2014, Series A	05/06/14	Variable	2039	200,000	200,000
Issue of 2014, Series B	06/10/14	4.008	2044	322,000	322,000
Issue of 2014, Series C	08/05/14	2.912	2030	198,750	198,750
Issue of 2014, Series D	10/23/14	3.785	2045	450,000	450,000
Issue of 2014, Series E	01/08/15	3.833	2045	229,000	229,000
Issue of 2015, Series A	04/16/15	3.636	2041	520,280	520,280
Issue of 2015, Series B	10/01/15	1.179	2019	268,590	268,590
Issue of 2016, Series A	05/19/16	3.265	2047	275,000	275,000
Issue of 2016, Series B	06/23/16	3.259	2047	225,000	225,000
Issue of 2017, Series A	02/09/17	3.782	2048	500,000	—
Issue of 2017, Series B	04/04/17	3.666	2040	345,410	—
Total principal amount				<u>8,630,404</u>	<u>8,334,507</u>
Unamortized premiums and discounts				688,874	620,002
Revenue bonds, net				<u>9,319,278</u>	<u>8,954,509</u>
Revenue certificates				200,000	200,000
Bonds and revenue certificates due within one year (including current portion of variable rate debt)				<u>(243,049)</u>	<u>(211,133)</u>
				<u>\$ 9,276,229</u>	<u>8,943,376</u>

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Revenue bonds generally are callable 10 years after issuance. The Department has agreed to certain covenants with respect to bonded indebtedness. Significant covenants include the requirement that the Power Systems' net income, as defined, will be sufficient to pay certain amounts of future annual bond interest and of future annual aggregate bond interest and principal maturities. Revenue bonds and refunding bonds are collateralized by the future revenue of the Power System.

(a) Long-Term Debt Activity

The Power System had the following activity in long-term debt for the fiscal years ended June 30, 2017 and 2016 (amounts in thousands):

	<u>Balance, July 1, 2016</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance, June 30, 2017</u>	<u>Current portion</u>
Long-term debt:					
Bonds	\$ 8,954,509	988,764	(623,995)	9,319,278	223,049
Revenue certificates	200,000	—	—	200,000	20,000
Total	<u>\$ 9,154,509</u>	<u>988,764</u>	<u>(623,995)</u>	<u>9,519,278</u>	<u>243,049</u>
	<u>Balance, July 1, 2015</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance, June 30, 2016</u>	<u>Current portion</u>
Long-term debt:					
Bonds	\$ 8,598,446	910,108	(554,045)	8,954,509	191,133
Revenue certificates	200,000	—	—	200,000	20,000
Total	<u>\$ 8,798,446</u>	<u>910,108</u>	<u>(554,045)</u>	<u>9,154,509</u>	<u>211,133</u>

(b) New Issuances

Fiscal Year 2017

In February 2017, the Power System issued \$500 million of Power System Revenue Bonds, 2017 Series A. The net proceeds of \$587.2 million, including an \$87.2 million issue premium net of underwriter's discount, were deposited into the construction fund to be used for capital improvements.

In April 2017, the Power System issued \$345.4 million of Power System Revenue Bonds, 2017 Series B. The net proceeds of \$399.7 million, including a \$54.3 million issue premium net of underwriter's discount, were used to refund a portion of the outstanding Power System Revenue Bonds, 2007 Series A, Subseries A-1, amounting to \$213.5 million, and all of the \$182.1 million outstanding Power System Revenue Bonds, 2007 Series A, Subseries A-2. The transaction resulted in a net present value savings of \$60.1 million and a net gain for accounting purposes of \$7.6 million, which was capitalized as deferred outflows on debt refunding and is being amortized over the life of the refunded bonds.

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Fiscal Year 2016

In October 2015, the Power System issued \$268.6 million of Power System Revenue Bonds, 2015 Series B. The net proceeds of \$300 million, including a \$31.4 million issue premium net of underwriter's discount, were used to refund all of the outstanding Power System Revenue Bonds, 2012 Series C, amounting to \$300 million. The transaction resulted in a net gain for accounting purposes of \$2.79 million, which was capitalized as deferred outflows on debt refunding and is being amortized over the life of the refunded bonds.

In May 2016, the Power System issued \$275 million of Power System Revenue Bonds, 2016 Series A. The net proceeds of \$332.5 million, including a \$57 million issue premium net of underwriter's discount, were used to pay for budgeted capital improvements and refund a portion of the Power System Revenue Bonds, 2007 Series A, Subseries A-1, amounting to \$71.6 million and Subseries A-2, amounting to \$9.1 million. The transaction resulted in a net present value savings of \$10.5 million and a net loss for accounting purposes of \$1.44 million, which was capitalized and is being amortized as deferred inflows on debt refunding over the life of the refunded bonds.

In June 2016, the Power System issued \$225 million of Power System Revenue Bonds, 2016 Series B. The net proceeds of \$276.1 million, including a \$51.1 million issue premium net of underwriter's discount, were deposited into the construction fund to be used for capital improvements.

(c) Outstanding Debt Defeased

The Power System defeased certain revenue bonds in the current and prior years by placing cash or the proceeds of new revenue bonds in irrevocable trusts to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the Power System's financial statements.

At June 30, 2017, the following revenue bonds outstanding are considered defeased (amounts in thousands):

Bond issues	Principal outstanding
Second issue of 1993	\$ 5,865
Refunding issue of 1994	3,465
Issue of 1994	3,910
Issue of 2007 Series A, Subseries A-1	285,035
Issue of 2007 Series A, Subseries A-2	191,125
Issue of 2009 Series B	535
Issue of 2010 Series B	15
Issue of 2011 Series A	1,285
Issue of 2013 Series A	2,125
	\$ 493,360

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(10) Variable Rate Bonds

In May 2017, the Power System entered into a First Amendment to Continuing Covenant Agreement (Amended CCA) with Wells Fargo Bank to extend the expiration date of the current Continuing Covenant Agreement (CCA) to May 4, 2020. In May 2014, the \$200 million Power System Revenue Bonds, 2014 Series A (Power 2014A Bonds) were sold under the CCA in an index floating rate mode under a Direct Purchase structure. Under the Amended CCA, the Power 2014A Bonds will pay interest at a fixed spread of 23 basis points (0.23%) above the Securities Industry and Financial Markets Association Index for the three-year term. At the end of the three-year term, the Power System would have the option to either renegotiate and renew a new index floating rate term with Wells Fargo or another bank or convert the bonds to another mode, such as a fixed-rate mode or a traditional variable-rate mode, that utilizes a standby agreement.

As of June 30, 2017 and 2016, the Power System had \$1.1 billion in variable rate bonds. The variable rate bonds currently bear interest at weekly and daily rates ranging from 0.50% to 0.91% as of June 30, 2017 and 0.19% to 0.44% as of June 30, 2016. The Power System can elect to change the interest rate period of the bonds with certain limitations. The bondholders have the right to tender the bonds to the tender agent on any business day with seven days' prior notice. The Power System has entered into standby and line-of-credit agreements with a syndicate of commercial banks in an initial amount of \$579 million and \$335 million to provide liquidity for the variable rate bonds. The extended standby agreements expire in February 2018 for the \$268 million, February 2019 for the \$206 million, and January 2020 for the \$106 million, for a total of \$579 million, and in May 2020 for the \$335 million.

Under the agreements, the \$579 million variable-rate bonds will bear interest that is payable monthly at the greatest of (a) the prime rate plus 1.00%; (b) the federal funds rate plus 2.00%; (c) LIBOR quoted rate plus 3.00%; (d) 7.00%; and (e) 7.50%, while the \$335 million variable rate bonds will bear interest that is payable monthly at the greatest of (a) the prime rate plus 1.00%; (b) the federal funds rate plus 2.00%; and (c) 7.00%. The unpaid principal of each liquidity advance made by the liquidity provider is payable in 10 equal semiannual installments 90 days immediately following the related liquidity advance. At its discretion, the Power System has the ability to convert the outstanding bonds to fixed-rate obligations, which cannot be tendered by the bondholders.

The variable-rate bonds have been classified as long term in the statements of net position, as the liquidity facilities give the Power System the ability to refinance on a long-term basis and the Power System intends to either renew the facility or exercise its right to tender the debt as a long-term financing. The portion that would be due in the next fiscal year in the event that the outstanding variable rate bonds were tendered and purchased by the commercial banks under the standby agreements has been included in the current portion of long-term debt and was \$91 million and \$96 million at June 30, 2017 and 2016, respectively.

(11) Revenue Certificates

As of June 30, 2017 and 2016, the Power System has outstanding \$200 million of commercial paper bearing interest at an average rate of 0.95%. The commercial paper matures not more than 270 days from the date of issuance.

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The Department entered into a letter-of-credit and reimbursement agreement with a commercial bank in the amount of \$200 million to provide liquidity and credit support for the Department's commercial paper program. The agreement secures the payment when due of the principal and interest on commercial paper issued on or after July 1, 2016. Drawings on the agreement will represent advances to the Department and will bear interest that is payable monthly at the highest of (a) the prime rate plus 1.00%; (b) federal funds rate plus 2.00%; and (c) 7.50%. The unpaid principal of each advance is payable in 10 equal semiannual installments, commencing on the date six months after the advance. The Agreement terminates on June 28, 2019.

The revenue certificates have been classified as long-term debt in the statements of net position, as the Agreement gives the Power System the ability to refinance on a long-term basis, and the Power System intends to either renew the Agreement or exercise its option to draw on the Agreement. The portion that would be due in the next fiscal year in the event that the outstanding revenue certificates were advanced by the commercial bank under the Agreement has been included in the current portion of long-term debt and was \$20 million at both June 30, 2017 and 2016.

(12) Scheduled Annual Principal Maturities and Interest

Scheduled annual principal maturities and interest are as follows (amounts in thousands):

	<u>Principal</u>	<u>Interest and amortization</u>
Fiscal year(s) ending June 30:		
2018	\$ 131,658	336,321
2019	163,434	340,227
2020	193,675	341,727
2021	210,335	336,701
2022	225,918	330,697
2023–2027	1,331,446	1,512,268
2028–2032	1,671,113	1,203,599
2033–2037	1,569,290	907,985
2038–2042	1,733,160	549,482
2043–2047	1,342,520	114,232
2048–2052	42,855	—
Total requirements	<u>\$ 8,615,404</u>	<u>5,973,239</u>

Interest and amortization are net of \$679 million of unamortized discount/premium and gain/loss due to issuances of new and refunding bonds.

The maturity schedule presented above reflects the scheduled debt service requirements for all of the Power System's long-term debt, except for the portion of Power System Revenue Bonds 2010 Series C, of which a sinking fund is established in the amount of \$15 million as of June 30, 2017. The schedule is presented assuming that the tender options on the variable rate bonds, as discussed on the previous page, will not be exercised and that the full amount of the revenue certificates will be renewed. Should the

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bondholders exercise the tender options and the Power System convert all of the revenue certificates under the line of credit, the Power System would be required to redeem the \$1,314 million in variable-rate bonds and revenue certificates outstanding over the next six years as follows: \$111 million in fiscal year 2018, \$223 million in each of the fiscal years 2019 through 2020, \$263 million in each of the fiscal years 2021 through 2022, \$151 million in fiscal year 2023, and \$40 million in each of the fiscal years 2024 through 2025. Accordingly, the statements of net position recognize the possibility of the exercise of the tender options and reflect the \$111 million that could be due in fiscal year 2018 as a current portion of long-term debt payable. Interest and amortization include interest requirements for variable-rate bonds. Variable debt interest rate in effect at June 30, 2017 averages 0.908%.

(13) Retirement Plan

(a) Plan Description

The Department has a funded contributory retirement plan covering substantially all of its employees. The Water and Power Employees' Retirement Fund (the Plan) operates as a single-employer defined-benefit plan to provide pension benefits to eligible department employees. The Retirement Fund's assets are held in a special trust fund of the City. Plan benefits are generally based on years of service, age at retirement, and the employee's highest 12 consecutive months of salary before retirement. Active participants who joined the Plan on or after June 1, 1984 are required to contribute 6% of their annual covered payroll. Participants who joined the Plan prior to June 1, 1984 contribute an amount based upon an entry-age percentage rate. A new Tier 2 was added to the Plan and applies to members hired on or after January 1, 2014. Tier 2 plan participants are required to contribute 10% of their salary, and plan benefits are based on a three-year final average salary period.

Under the provisions of the City Charter, the Retirement Board of Administration (the Retirement Board) has the responsibility and authority to administer the Plan and to invest its assets. The Retirement Board members serve as trustees and must act in the exclusive interest of the Plan's members and beneficiaries. The Retirement Board has seven members: one member of the Retirement Board of Water and Power Commissioners, the general manager, the chief accounting employee, three employee members who are elected for three-year terms by active members of the Plan, and one retiree who is appointed by the Board of Water and Power Commissioners for a three-year term.

Plan amendments must be approved by both the Retirement Board and the Board. The Plan issues separately available financial statements on an annual basis. Such financial statements can be obtained from the Department of Water and Power Retirement Office, 111 North Hope, Room 357, Los Angeles, CA 90012.

(b) Benefits Provided

The Plan provides retirement benefits to eligible employees. Most employees of the Los Angeles Department of Water and Power become members of the Plan effective on the first day of biweekly payroll following employment or immediately following transfer from another city department. Members employed prior to January 1, 2014 are designated as Tier 1, and those hired on or after

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January 1, 2014 are designated as Tier 2 (unless a specific exemption applies to employee providing a right to Tier 1 status).

Tier 1 members are eligible to retire once they attain the age of 60 with 5 or more years of service or at age 55 with 10 or more years of service credit acquired in the last 12 years prior to retirement. A Tier 1 member with 30 years of service is eligible to retire regardless of age. Tier 2 members are eligible to retire once they attain the age of 60 with 10 or more years of service or at any age with 30 years of service. For both tiers, combined years of service between the Plan and the Los Angeles City Employees' Retirement System is used to determine retirement eligibility, and at least five years must be actual employment at the Department or City (not purchased). For both tiers, members receiving Permanent Total Disability benefits may retire regardless of age. For Tier 1, to be eligible for a Formula Pension, the employee must have worked or been paid disability four of the last five years immediately preceding eligibility to retire or while eligible to retire.

The Formula Pension benefit the member will receive is based upon the age at retirement, monthly average salary base, and years of retirement service credit. The Tier 1 Formula Pension is equal to 2.1% times years of service credit times monthly average salary base. In addition, members retiring after attaining age 55 with 30 years of service credit receive an increase in the benefit factor from 2.1% to 2.3%. A reduced early-retirement benefit is paid for those members attaining age 55 with 10 years of service or any age (under 55) with 30 years of service. The reduction is 1.5% for each year of retirement age between 60 and 55 and 3.0% for each year of retirement before age 55.

Under Tier 2, there are various benefit factors that apply, as shown below:

- 2.0% at age 55 with 30 years of service credit
- 1.5% at age 60 with 10 years of service credit
- 2.0% at age 63 with 10 years of service credit
- 2.1% at age 63 with 30 years of service credit.

Reduced early-retirement benefits are still available at any age (under 55) with 30 years of service, and the reduction factors are the same as Tier 1. Note that these reduction factors continue to include the reduction from age 60 to 55 and from 55 to age at retirement.

For Tier 1 members, the maximum monthly retirement allowance is 100% of monthly average salary base. For Tier 2 members, the maximum monthly retirement allowance is 80% of monthly average salary base. Under Tier 1, pension benefits are calculated based on the highest average salary earned during a 12-month period. Under Tier 2, pension benefits are calculated based on the average salary earned during a 36-month period.

The member may elect the full allowance or choose an optional retirement allowance. The full allowance provides the highest monthly benefit and up to a 50% continuance to an eligible surviving spouse or domestic partner. There are five optional retirement allowances the member may choose from. Each of the optional retirement allowances requires a reduction in the full allowance in order to

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allow the member the ability to provide various benefits to a surviving spouse, domestic partner, or named beneficiary.

(c) Plan Membership

At June 30, 2016 and 2015, pension plan membership, which consisted of Water and Power System members, consisted of the following:

	2016	2015
Retired members or beneficiaries currently receiving benefits	9,265	8,843
Vested terminated members entitled to, but not yet receiving, benefits	1,612	1,528
Active members	9,348	9,205
Total	20,225	19,576

(d) Contributions

The Department contributes \$1.10 for each \$1 contributed by participants plus an actuarially determined annual required contribution as determined by the Plan's independent actuary. The required contributions are allocated between the Power System and the Water System based on the current-year labor costs.

Employer contribution rates are adopted annually based upon recommendations received from the Plan's actuary after the completion of the annual actuarial valuation. The average employer contribution rates for fiscal years 2017, 2016, and 2015 (based on the July 1, 2016, 2015, and 2014 valuations) were 45.25%, 42.77%, and 46.17% of compensation, respectively. The average member contribution rate for fiscal years 2017, 2016, and 2015 (based on the July 1, 2016, 2015, and 2014 valuations) was 6.80% of compensation. Most Tier 1 members contribute at 6% of compensation and all Tier 2 members contribute at 10% of compensation. Employer contributions in fiscal years 2017, 2016, and 2015 amounted to \$267 million, \$245 million, and \$259 million, respectively. These contributions represented 98%, 97% and 99% of the annual required contributions in fiscal years 2017, 2016 and 2015, respectively.

(e) Net Pension Liability

At June 30, 2017 and 2016, the Power System reported a liability of \$1,493 million and \$771 million for its proportionate share of the net pension liability, respectively. The net pension liability was measured as of June 30, 2016 and 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of the same dates. The Power System's proportion of the net pension liability was based on the Power System's projected compensation for the year following the measurement date, relative to the projected compensation for the same period for both the Water System and the Power System. At June 30, 2017, the Power System's proportion was 68.1% compared to 67.4% and 67.7 as of June 30, 2016 and 2015, respectively.

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(f) Actuarial Assumptions

The Department's net pension liability as of June 30, 2017 and 2016, was determined by actuarial valuations as of July 1, 2016 and 2015, respectively. The actuarial assumptions used in the July 1, 2016 valuation were based on the results of an experience study for the period from July 1, 2012 through June 30, 2015. The actuarial assumptions used in the July 1, 2015 valuation were based on the results of an experience study for the period from July 1, 2009 through June 30, 2012. The following assumptions were applied to all periods included in the measurement for the July 1, 2016 and 2015 actuarial valuations:

<u>Actuarial assumptions</u>	<u>2016</u>	<u>2015</u>
Inflation	3.00%	3.25%
Salary increases	4.50%–10.00%	4.75%–10.00%
Investment rate of return	7.25%	7.50%
Cost-of-living adjustments	3.00% (Actual increases are contingent upon CPI increases, with a 3.00% maximum for Tier 1 and 2.00% maximum for Tier 2.)	3.00% (Actual increases are contingent upon CPI increases, with a 3.00% maximum for Tier 1 and 2.00% maximum for Tier 2.)
Mortality	Healthy: RP-2014 Combined Mortality Table set back one year with MP-2015 projection scale	Healthy: RP-2000 Combined Mortality Table set back one year projected to 2030 with Scale AA

(g) Discount Rate

The discount rate used to measure the pension liability was 7.25% and 7.50% as of June 30, 2017 and 2016, respectively. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rate and that employer contributions will be made at rates equal to the actuarially determined contribution rates. For this purpose, only employee and employer contributions that are intended to fund benefits for current plan members and their beneficiaries are included. Projected employer contributions that are intended to fund the service costs for future plan members and their beneficiaries, as well as projected contributions from future plan members, are not included. Based on those assumptions, the Plan's fiduciary net position was projected to be available to make all projected future benefit payments for current and inactive plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments, which is estimated to be 104 years, to determine the total pension liability at June 30, 2017 and 2016.

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The long-term expected rate of return on pension plan investments was determined using a building-block method in which the best estimate ranges of expected future real rates of return (expected returns, net of inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset proportionate share, adding expected inflation and subtracting expected investment expenses. The target allocation and projected best estimates of arithmetic real rates of return for each major asset class, after deducting inflation but before deducting investment expenses, used in the derivation of the long-term expected investment rate of return assumption are summarized in the following table:

<u>Asset class</u>	<u>June 30, 2016</u>	
	<u>Target allocation</u>	<u>Long-term expected real rate of return</u>
Domestic equity	29%	5.76%
Developed international equity	19	7.25
Fixed income	25	1.74
Real estate	8	4.37
Real return	5	2.39
Private equity	8	7.75
Covered calls	5	3.50
Cash and cash equivalents	1	(0.46)
Total	<u>100%</u>	

<u>Asset class</u>	<u>June 30, 2015</u>	
	<u>Target allocation</u>	<u>Long-term expected real rate of return</u>
Domestic equity	33%	0.06%
Developed international equity	21	7.00
Fixed income	24	0.77
Real estate	5	4.90
Real return	6	2.85
Private equity	5	9.00
Covered calls	5	4.88
Cash and cash equivalents	1	—
Total	<u>100%</u>	

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(h) Sensitivity of the Net Pension Liability to Changes in the Discount Rate

The following presents the net pension liability of the Department as of June 30, 2017 and 2016, calculated using the discount rate of 7.25% and 7.50%, respectively, as well as what the Department's pension liability would be if it were calculated using a discount rate that is one percentage point lower (6.25%) or one percentage point higher (8.25%) than the current rate (amounts in thousands):

<u>Net pension liability</u>	<u>1% decrease (6.25%)</u>	<u>Current discount rate (7.25%)</u>	<u>1% increase (8.25%)</u>
June 30, 2017	\$ 2,632,821	1,492,508	550,428

<u>Net pension liability</u>	<u>1% decrease (6.50%)</u>	<u>Current discount rate (7.50%)</u>	<u>1% increase (8.50%)</u>
June 30, 2016	\$ 1,733,853	771,121	(37,634)

(i) Pension Plan Fiduciary Net Position

The pension plan's fiduciary net position is determined based on the accrual basis of accounting, which is on the same basis of accounting as the Plan. Pension Plan investments are recorded at fair value except for short-term investments, which are recorded at amortized cost. Benefit payments include costs as designated by the Plan document, refunds of employee contributions due to terminations and member deaths, and administrative expenses.

(j) Pension Expense, Deferred Outflow of Resources, and Deferred Inflow of Resources

The Power System recognized pension expense of \$214,407 and \$(24,633) for the years ended June 30, 2017 and 2016 respectively. Pension expense is recorded as operation and maintenance expense or construction work in progress, depending on where the related payroll is charged. At June 30, 2017 and 2016, the Power System reported \$793,045 and \$217,131, respectively, for deferred outflows of resources and deferred inflows of resources of \$241,547 and \$421,232, respectively.

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The below tables summarize the deferred inflows of resources and deferred outflows of resources at June 30, 2017 and 2016 (amounts in thousands):

<u>Deferred outflows of resources</u>	<u>June 30</u>	
	<u>2017</u>	<u>2016</u>
Changes in proportion and differences between entity contributions and proportionate share of contributions	\$ 7,322	1,061
Net excess of projected over actual earnings on investments	231,908	—
Changes of assumptions and other inputs	<u>553,815</u>	<u>216,070</u>
Total deferred outflow of resources	<u>\$ 793,045</u>	<u>217,131</u>

<u>Deferred inflows of resources</u>	<u>June 30</u>	
	<u>2017</u>	<u>2016</u>
Changes in proportion and differences between entity contributions and proportionate share of contributions	\$ 5,538	7,989
Net difference between projected and actual earnings on pension plan investments	—	231,847
Difference between expected and actual experience in the total pension liability	<u>236,009</u>	<u>181,396</u>
Total deferred inflow of resources	<u>\$ 241,547</u>	<u>421,232</u>

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In addition to the deferred outflows noted above, there are also \$266,824 and \$245,462 of deferred outflows related to pension contributions made after the measurement date as of June 30, 2017 and 2016, respectively. These deferred outflows of resources are recognized as a reduction of the net pension liability in the subsequent fiscal year.

The net amount of deferred outflows of resources and deferred inflows of resources related to pensions that will be recognized in pension expense during the next five years and thereafter is as follows:

Year	June 30	
	2017	2016
2017	—	(93,094)
2018	61,173	(93,094)
2019	119,192	(35,669)
2020	183,245	27,716
2021	145,166	(9,960)
2022	42,722	—
Total	<u>551,498</u>	<u>(204,101)</u>

(14) Other Postemployment Benefit (Healthcare) Plan

(a) Plan Description

The Department provides certain other postemployment benefits, such as medical and dental plans, to active and retired employees and their dependents. The healthcare plan is administered by the Department. The Retirement Board and the Board have the authority to approve provisions and obligations. Eligibility for benefits for retired employees is dependent on a combination of age and service of the participants pursuant to a predetermined formula. Any changes to these provisions must be approved by the Retirement Board and the Board. The total number of active and retired Department participants entitled to receive benefits was approximately 17,844 and 17,244 for the fiscal years ended June 30, 2017 and 2016, respectively.

The health plan is a single-employer defined-benefit plan. During fiscal year 2007, the Retiree Health Benefits Fund was created to fund the postemployment benefits of the Department. The Fund is administered as a trust and has its own financial statements. Such financial statements can be obtained from the Department of Water and Power Retirement Office, 111 North Hope, Room 357, Los Angeles, CA 90012.

(b) Funding Policy

The Department pays a monthly maximum subsidy of \$1,943 for medical and dental premiums depending on the employee's work location and benefits earned. Participants choosing plans with a cost in excess of the subsidy they are entitled to are required to pay the difference.

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Although no formal funding policy has been established for the future benefits to be provided under this plan, the Department has made significant contributions into the Fund during previous years. In fiscal year 2017, the Department paid \$85.7 million in retiree medical premiums. In fiscal year 2016, the Department paid \$73 million in retiree medical premiums. The Power System's portion of retiree medical premium payments was \$58 million and \$46 million for 2017 and 2016, respectively. The remaining portion was paid by the Water System.

(c) Annual OPEB Cost and Net OPEB Obligation

The annual OPEB cost (expense) is calculated based on the employer Annual Required Contribution, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost under each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years.

The following table shows the components of the Department's Power and Water funds' combined annual OPEB cost for the year, the amount actually contributed to the Plan, and changes in the net OPEB asset (amounts in thousands):

	Year ended June 30	
	2017	2016
Annual required contribution	\$ 97,265	64,253
Interest on net OPEB asset	(76,059)	(77,024)
Adjustment to annual required contribution	80,048	74,238
Annual OPEB costs	101,254	61,467
Department contributions made	(85,736)	(72,994)
Change in net OPEB asset	15,518	(11,527)
Net OPEB asset at beginning of year	(994,951)	(983,424)
Net OPEB asset at end of year	\$ (979,433)	(994,951)

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The following table shows the components of the Power System's share in annual OPEB cost for the year, the amount actually contributed to the Plan, and changes in the net OPEB asset (amounts in thousands):

	Year ended June 30	
	2017	2016
Annual required contribution	\$ 68,086	43,692
Interest on net OPEB asset	(53,241)	(52,376)
Adjustment to annual required contribution	56,033	50,482
Annual OPEB costs	70,878	41,798
Department contributions made	(57,619)	(46,394)
Change in net OPEB asset	13,259	(4,596)
Net OPEB asset at beginning of year	(674,488)	(669,892)
Net OPEB asset at end of year	\$ (661,229)	(674,488)

The Department's Power and Water funds' combined annual OPEB cost, the percentage of ARC contributed to the Plan, and the net postemployment asset for fiscal years 2017, 2016, and 2015 were as follows (amounts in thousands):

	2017	2016	2015
Annual OPEB cost	\$ 101,254	61,467	68,150
Percentage of OPEB costs contributed	85%	119%	108%
Net postemployment asset at end of year	\$ 979,433	994,951	983,424

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The Power System's share in the annual OPEB cost, the percentage of ARC contributed to the Plan, and the net retirement asset for fiscal years 2017, 2016, and 2015 were as follows (amounts in thousands):

	<u>2017</u>	<u>2016</u>	<u>2015</u>
Annual OPEB cost	\$ 70,878	41,798	46,342
Percentage of OPEB costs contributed	81%	111%	103%
Net postemployment asset at end of year	\$ 661,229	674,488	669,892

(d) Funded Status and Funding Progress Based on Latest Actuarial Study

On October 3, 2017, the latest actuarial study as of July 1, 2017 was completed for fiscal year 2018. As of July 1, 2017, the Department's actuarial value of assets was \$1.9 billion, and its actuarial accrued liability (AAL) for benefits was \$2.35 billion, resulting in an unfunded actuarial accrued liability (UAAL) of \$0.45 billion, which represents 81% funding status. The covered payroll (annual payroll of active employees covered by the Plan) was \$992 million, and the ratio of the UAAL to the covered payroll was 45%.

On December 8, 2016, the actuarial study as of July 1, 2016 was completed for fiscal year 2017. As of July 1, 2016, the Department's actuarial value of assets was \$1.7 billion, and its AAL for benefits was \$2.33 billion, resulting in a UAAL of \$0.58 billion, which represents 75% funding status. The covered payroll (annual payroll of active employees covered by the Plan) was \$929 million, and the ratio of the UAAL to the covered payroll was 63%.

On October 30, 2015, the actuarial study as of July 1, 2015 was completed for fiscal year 2016. As of July 1, 2015, the Department's actuarial value of assets was \$1.64 billion, and its AAL for benefits was \$2 billion, resulting in an unfunded UAAL of \$.32 billion, which represents 84% funding status. The covered payroll (annual payroll of active employees covered by the Plan) was \$920 million, and the ratio of the UAAL to the covered payroll was 35%.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the Plan and ARCs of the Department are subject to continual revision, as actual results are compared with past expectations, and new estimates are made for the future. The schedule of funding progress, presented as required supplementary information, presents information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the AAL for benefits.

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(e) Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan understood by the Department and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the Department and the plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in AAL and the actuarial value of assets, consistent with the long-term perspective of the calculations. Benefits are a function of civil service credits and the retiree's age.

In the July 1, 2016 actuarial valuation, the entry age normal cost method was used. The actuarial assumptions include 7.25% discount rate, which represents the expected long-term return on plan assets and an annual healthcare cost trend rate of 6.50% initially, reduced by decrements to an ultimate rate of 5.00% over 6 years. Both rates include a 3.00% inflation assumption. The actuarial value of assets was determined using techniques that spread UAAL being amortized as a level percentage of projected payroll over a closed 30-year period, with 19 years remaining.

In the July 1, 2015 actuarial valuation, the entry age normal cost method was used. The actuarial assumptions include a 7.50% discount rate, which represents the expected long-term return on plan assets, and an annual healthcare cost trend rate of 6.75% initially, reduced by decrements to an ultimate rate of 5.00% over 7 years. Both rates include a 3.25% inflation assumption. The actuarial value of assets was determined using techniques that spread UAAL being amortized as a level percentage of projected payroll over a closed 30-year period, with 20 years remaining.

The required schedule of funding progress presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time.

(f) Healthcare Reform Legislation

The Patient Protection and Affordable Care Act (PPACA) was signed into law on March 23, 2010. One key provision of the PPACA is the assessment of the excise tax on high-cost plans beginning in 2018. Under this act, a 40% excise tax applies to plans with costs exceeding certain annual thresholds for non-Medicare retirees aged 55–64 (\$11,850 for single coverage; \$30,950 for family coverage). For all other retirees, the thresholds in 2018 are \$10,200 for single coverage and \$27,500 for family coverage. Significant uncertainties exist regarding the impact of the excise tax on high-cost plans without further regulatory guidance. Management estimated the potential impact of this tax on the liability is based on unadjusted thresholds and assuming the tax is shared between the Department and its participants in the same way that the current costs are shared. The estimated impact of the 40% excise tax provision on high-cost plans beginning in 2018, under the healthcare reform, is reflected in all actuarial valuation reports after July 1, 2010.

(g) Death and Disability Benefits

The Power System's allocated share of death and disability benefit plan costs and administrative expenses totaled \$22 million and \$20 million for fiscal years 2017 and 2016, respectively. Death and disability benefits are administered as part of the Retirement Plan, and funds are maintained in

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separate restricted funds to pay for each benefit. Disability benefits are paid to active employees only who qualify under the Plan provisions and terminate with the employee's retirement.

(15) Other Long-Term Liabilities and Deferred Inflows

(a) Other Long-Term Liabilities and Deferred Inflows

The Power System has the following other long-term liabilities and deferred inflows (amounts in thousands):

	<u>Balance, June 30, 2016</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance, June 30, 2017</u>
Accrued liabilities	\$ 1,887	—	(1,887)	—
Deferred inflows from regulated business activities:				
Rate stabilization	174,001	—	(74,001)	100,000
Green Power Program	3,224	403	—	3,627
	<u>\$ 177,225</u>	<u>403</u>	<u>(74,001)</u>	<u>103,627</u>
Accrued workers' compensation claims	\$ 61,945	5,465	—	67,410
Derivative instrument liabilities	23,379	—	(8,739)	14,640
	<u>Balance, July 1, 2015</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance, June 30, 2016</u>
Accrued liabilities	\$ 3,607	—	(1,720)	1,887
Deferred inflows from regulated business activities:				
Rate stabilization	174,001	—	—	174,001
Green Power Program	2,556	668	—	3,224
	<u>\$ 176,557</u>	<u>668</u>	<u>—</u>	<u>177,225</u>
Accrued workers' compensation claims	\$ 54,508	7,437	—	61,945
Derivative instrument liabilities	43,244	—	(19,865)	23,379

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(b) *Deferred Inflows from Regulated Business Activities*

The Power System has deferred inflows that are related to revenues collected from customers but have not been earned. These funds are deferred and recognized, as costs related to these deferrals are incurred.

(i) Rate Stabilization Account

In April 2008, the City Council approved an amendment to the electric rate ordinance, which required the balance of the Rate Stabilization Account to be maintained separately from the Energy Cost Adjustment Account. The ordinance also directed that the deferred amount within the Energy Cost Adjustment Account be the beginning balance of the Rate Stabilization Account.

In August 2017, the Board passed resolutions setting the rate stabilization target at \$100 million as of June 30, 2017, recognizing the amount above the \$100 million in the Rate Stabilization Account as other operating income, and creating a Rate Stabilization fund to match the \$100 million in the Rate Stabilization Account. As of June 30, 2017 and 2016, the balance in the Rate Stabilization Account was \$100 million and \$174 million, respectively.

(c) *Accrued Workers' Compensation Claims*

Liabilities for unpaid workers' compensation claims are recorded at their net present value when they are probable of occurrence and the amount can be reasonably estimated. The liability is actuarially determined based on an estimate of the present value of the claims outstanding and an amount for claim events incurred but not reported based upon the Department's loss experience, less the amount of claims and settlements paid to date. The discount rate used to calculate this liability at its present value was 2.0% at June 30, 2017 and 2.1% as of June 30, 2016. The Department has third-party insurance coverage for workers' compensation claims over \$1 million.

Overall indicated reserves for workers' compensation claims, for both the Water System and the Power System, undiscounted, have increased from \$104 million as of June 30, 2016 to \$115 million as of June 30, 2017. This increase is mainly attributable to the number of open cases filed at the Department. Workers' compensation claims typically take longer than one year to settle and close out. The entire discounted liability is shown as long term on the statements of net position as of June 30, 2017 and 2016.

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Changes in the Department's undiscounted liability since June 30, 2015 are summarized as follows (amounts in thousands):

	June 30		
	2017	2016	2015
Balance at beginning of year	\$ 103,699	95,379	99,519
Current year claims and changes in estimates	37,501	35,268	26,727
Payments applied	(26,096)	(26,948)	(30,867)
Balance at end of year	<u>\$ 115,104</u>	<u>103,699</u>	<u>95,379</u>

The Power System's portion of the discounted reserves as of June 30, 2017 and 2016 is \$67 million and \$62 million, respectively.

(16) Related Parties

(a) City of Los Angeles

Under the provisions of the City Charter, the Power System transfers funds at its discretion to the reserve fund of the City. Pursuant to covenants contained in the bond indentures, the transfers may not be in excess of the increase in net position before transfers to the reserve fund of the City of the prior fiscal year. Management believes such payments are not in lieu of taxes and are recorded as a transfer in the statements of revenues, expenses, and changes in net position. The Power System also reimburses the City for administrative costs incurred on behalf of the Power System. During fiscal year 2017, the Power System transferred \$264 million in transfers and \$24 million in administrative reimbursements. See note 8(a).

(b) Southern California Public Power Authority

SCPPA is a California Joint Powers Agency that finances the construction or acquisition of generation, transmission, and renewable energy projects. The Department is a member of SCPPA and records its transactions as purchased power expense. See note 5 of the financial statements for a description of the purchased power commitments the Power System has with SCPPA.

(c) Intermountain Power Agency

IPA – The Intermountain Power Agency is an agency of the State of Utah established to own, acquire, construct, operate, maintain, and repair the Intermountain Power Project. The Power System serves as the project manager and operating agent of IPP. See note 5 for of the financial statements for a description of the financial activities of IPA.

(d) La Kretz Innovative Campus (LKIC)

The Power System has entered into a 50-year prepaid lease agreement for \$12 million to lease an office building to the La Kretz Innovative Campus/(LKIC), a 501(c)3 nonprofit organization. LKIC prepaid the lease in fiscal year 2015, and the \$12 million is amortized to other nonoperating income

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starting February 2016. LKIC, in turn, leases some of the work spaces in the building to assist energy innovation companies with the resources needed to validate energy-efficient technology. The Power System does have energy efficiency staff also located at the building to work with inventors and determine if there are new energy efficiency programs to launch.

(17) Commitments and Contingencies

(a) Transfers to the Reserve Fund of the City of Los Angeles

Under the provisions of the City Charter, the Power System transfers funds at its discretion to the reserve fund of the City. Pursuant to covenants contained in the bond indentures, the transfers may not be in excess of the increase in fund net assets before transfers to the reserve fund of the City of the prior fiscal year. Such payments are not in lieu of taxes and are recorded as a transfer in the statements of revenues, expenses, and changes in fund net assets.

On September 14, 2017, the Los Angeles County Superior Court preliminarily approved a settlement of a class action lawsuit under which revenue collected under the 2016 Incremental Electric Rate Ordinance (the 2016 Ordinance) is precluded from being transferred to the reserve fund of the City. As of June 30, 2017, the Department has billed approximately \$52 million under the 2016 Ordinance that under the settlement agreement needs to be returned to customers net of attorneys' fees and other administrative costs. Accordingly, for the fiscal year ended June 30, 2017, the Department reduced retail revenue by the same \$52 million and increased current accrued expenses accordingly. In October 2017, \$52 million was placed in an escrow account for return to customers. Upon proof of such return, the Department can request funds from the escrow account accordingly. Going forward, the 2016 Ordinance rates will be reduced through the Variable Energy Cost Adjustment so that no revenue for transfers is billed under the 2016 Ordinance.

During fiscal year 2017, the 2008 Electric Rate Ordinance (the 2008 Ordinance) and the 2016 Ordinance were in effect. Revenue from each ordinance is listed below, as well as revenue from other sources, including contracts for wholesale energy and transmission revenue. The 12.628 cents under the 2008 Ordinance is determined based on the fiscal year's revenue billed and kilowatt-hour (kWh) usage as of November 3, 2010. The 2008 Ordinance was the only ordinance in effect at that time.

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The following table relates to revenue billed to customers for the year ended June 30, 2017:

Revenue type	Basis of revenue	kWh	Rate per kWh under the 2008 ordinance	Revenue (in dollars)
Retail sales	2008 Ordinance	22,490,122,681	\$ 0.12628	\$ 2,840,052,692
Retail sales	2016 Ordinance	22,490,122,681		577,330,575
Wholesale sales	Contract			40,869,669
Transmission sales	Contract			47,229,066
Rent from electric property	Contract			1,414,146
Other service charges	Fee schedule			19,536,672
Rate stabilization fund	Board action			74,000,000
Unbilled sales	Estimated			132,336,787
Bad debt expense	Estimated			(34,846,841)
Total operating revenue				<u>\$ 3,697,922,766</u>

The Department authorized total transfers of \$264 million and \$267 million in fiscal years 2017 and 2016, respectively, from the Power System to the reserve fund of the City.

(b) Asset Retirement Obligations

In accordance with federal guidelines, the Power System has \$134 million and \$133 million in investments as of June 30, 2017 and 2016, respectively, to fund its portion of the decommissioning of PVNGS. As funds were collected through rates to finance this reserve, a decommissioning liability of \$153 million as of June 30, 2017 and 2016 has been recorded as an increase in accumulated depreciation. The difference between investments and the liability for the decommissioning liability represent accumulated increases in fair value. Additional decommissioning funds may be needed in the future to decommission the Navajo Generating Station and other utility plant assets.

The Department's current practice of recording asset retirement obligations as part of accumulated depreciation is consistent with industry practice. Next fiscal year, the Department will adopt GASB Statement No. 83. This statement addresses accounting and financial reporting for certain AROs. An ARO is a legally enforceable liability associated with the retirement of a tangible asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance of this statement.

(c) Environmental Matters

Numerous environmental laws and regulations affect the Power System's facilities and operations. The Department monitors its compliance with laws and regulations and reviews its remediation obligations on an ongoing basis. The Department follows GASB Statement No. 49, *Accounting and Financial Reporting for Pollution and Remediation Obligations*. This statement addresses accounting and financial reporting standards for pollution (including contamination) remediation obligations, which

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are obligations to address the current or potential detrimental effects of existing pollution by participating in pollution remediation activities such as site assessments and cleanups. The scope of the statement excludes pollution prevention or control obligations with respect to current operations and future pollution remediation activities that are required upon retirement of an asset, such as landfill closure and postclosure care and nuclear power plant decommissioning. The Power System's obligations are included in accrued expenses on the statements of net position and were approximately \$38 million and \$29 million as of June 30, 2017 and 2016, respectively.

(d) Litigation

A number of claims and suits are pending against the Department for alleged damages to persons and property and for other alleged liabilities arising out of its operations. In the opinion of management, any ultimate liability, which may arise from these actions, is not expected to materially impact the Power System's financial position, results of operations, or cash flows as of June 30, 2017.

(e) Risk Management

The Power System is subject to certain business risks common to the utility industry. The majority of these risks are mitigated by external insurance coverage obtained by the Power System. For other significant business risks, however, the Power System has elected to self-insure. Management believes that exposure to loss arising out of self-insured business risks will not materially impact the Power System's financial position, results of operations, or cash flows as of June 30, 2017.

(f) Credit Risk

Financial instruments, which potentially expose the Power System to concentrations of credit risk, consist primarily of retail and wholesale receivables. The Power System's retail customer base is concentrated on commercial, industrial, residential, and governmental customers located within the City. Although the Power System is directly affected by the City's economy, management does not believe significant credit risk exists as of June 30, 2017, except as provided in the allowance for losses. The Power System manages its credit exposure by requiring credit enhancements from certain customers and through procedures designed to identify and monitor credit.

(18) Subsequent Events

(a) Bond Sale

In July 2017, the Power System issued \$375 million of Power System Revenue Bonds, 2017 Series C. The net proceeds of \$444.3 million, including a \$69.3 million issue premium net of underwriter's discount, were deposited into the construction fund to be used for capital improvements.

(b) Approval of Transfer to the Reserve Fund of the City of Los Angeles

On November 28, 2017, the Board of Water and Power Commissioners approved a resolution agreeing to the adoption of an ordinance to transfer \$241.8 million from the Power Revenue Fund to the reserve fund of the City of Los Angeles during fiscal year 2017-2018.

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Required Supplementary Information

June 30, 2017 and 2016
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Schedule of the Power System's Proportionate Share of the Net Pension Liability

Last 10 fiscal years*

(Amounts in thousands other than percentages)

	<u>2017</u>	<u>2016</u>	<u>2015</u>	<u>2014</u>
Power System's proportion of the collective net pension liability	68.108%	67.397%	67.656%	67.427%
Power System's proportionate share of the collective net pension liability	\$ 1,492,508	771,121	860,748	1,207,513
Power System's covered-employee payroll	586,967	565,605	554,731	551,159
Power System's proportionate share of the collective net pension liability as a percentage of covered payroll	254.27%	136.34%	155.16%	219.08%
Pension plan's fiduciary net position as a percentage of total pension liability	82.17%	89.80%	88.41%	82.30%

*The Power System implemented GASB Statement No. 68 effective July 1, 2013; therefore, no information is available for the measurement periods prior to June 30, 2013.

See accompanying independent auditors' report.

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Schedule of the Power System's Contributions

Last 10 fiscal years

(Amounts in thousands other than percentages)

Reporting date for Power System June 30 ⁽¹⁾	Actuarially determined contributions ⁽²⁾	Contributions in relation to the actuarially required contributions ⁽³⁾	Contributions deficiency (excess)	Power System's covered- employee payroll	Contributions as a percentage of covered employee payroll
2017	\$ 251,046	246,796	4,250	586,968	42.05%
2016	263,471	256,288	7,183	565,606	45.31
2015	262,485	260,077	2,408	554,732	46.88
2014	256,518	250,905	5,613	551,159	45.52
2013	228,830	218,515	10,315	545,461	40.06
2012	206,792	194,747	12,046	537,821	36.21
2011	136,248	136,558	(310)	521,622	26.18
2010	95,976	99,134	(3,158)	473,252	20.95
2009	91,465	96,363	(4,898)	423,646	22.75
2008	91,365	87,732	3,633	410,631	21.37

(1) The measurement date under GASB 68 is on a one-year lag.

(2) All actuarially determined contributions through June 30, 2014 were determined as the annual requirement under GASB Statement No. 25 and No. 27.

(3) Contributions do not include administrative expenses paid to the Plan.

See accompanying independent auditors' report.

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Postemployment Healthcare Plan – Schedule of Funding Progress

The following schedule provides information about the Department’s overall progress made in accumulating sufficient assets to pay benefits when due, prior to allocations to the Water System and the Power System (amounts in thousands):

Actuarial valuation date July 1	Actuarial value of assets	Actuarial accrued liability (AAL)	Unfunded AAL (UAAL)	Funded ratio	Covered payroll	UAAL as a percentage of covered payroll
2017	\$ 1,898,137	2,347,484	449,347	81%	\$ 991,815	45%
2016	1,752,195	2,334,043	581,848	75	928,889	63
2015	1,637,578	1,956,230	318,652	84	920,781	35

See accompanying independent auditors’ report.