Department of Water Resources
Electric Power Fund
Financial Statements

September 30, 2009

Index

USING THIS REPORT

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

The basic financial statements include three required statements, which provide different views of the Fund. They are: the statement of net assets, the statement of revenues, expenses and changes in net assets, and the statement of cash flows. These statements provide current and long-term information about the Fund and its activities. These financial statements report information using accounting methods similar (although not identical) to those used by private sector companies. The statement of net assets includes all assets and liabilities as of the year-end date. The statement of revenues, expenses and changes in net assets presents all of the current year's revenues, expenses, and changes in net assets. The statement of cash flows reports cash receipts, disbursements and the net change in cash resulting from three principal types of activities: operating, financing and investing. In order for the basic financial statements to be complete, they must be accompanied by a complete set of footnotes. The notes to the financial statements provide disclosures which are required to conform with generally accepted accounting principles. The Fund is required to follow accounting standards promulgated by the Governmental Accounting Standards Board.

PURPOSE OF FUND

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

DWR has the authority to secure and retain title to power for resale to end use customers of the State's investor owned utilities (IOUs) under power supply contracts entered into prior to January 1, 2003. The scheduling, dispatch, and certain other administrative functions for the long-term contracts are performed by the IOUs as agents for DWR. However, DWR retains the legal and financial responsibility for each contract for the life of the contract or until such time as there is complete assignment of the contract to an IOU and release of DWR. Most of the volume of power under contract expires by December 31, 2011 and the last of the contracts expires in 2015.

DWR is entitled to recover revenue requirements for authorized activities, including but not limited to debt service, the costs of power purchases, administrative expenses and reserves. Revenue requirements are determined at least annually and submitted to the California Public Utilities Commission (CPUC) for implementation. Under the terms of the rate agreement between the CPUC and DWR, the CPUC is required to set rates for the customers of the IOUs and "direct access" Electric Service Providers (ESPs) such that the Fund will always have monies to meet its revenue requirements.

This report should be read in conjunction with the Fund's June 30, 2009 audited financial statements. During the three month period ended September 30, 2009, DWR adopted the provisions of Governmental Accounting Standards Board Statement (GASB) No. 53, *Accounting and Financial Reporting for Derivative Instruments*. The effects of implementing GASB 53 are discussed in the Management Discussion and Analysis section along with a detailed description in Note 2, and further fair value detail in Note 5.

STATEMENTS OF NET ASSETS

The Fund's assets, liabilities and net assets as of September 30, 2009 and June 30, 2009 are summarized as follows (in millions):

	September 30, 2009	June 30, 2009
Long-term restricted cash, equivalents and investments	$ 1,493	$ 1,493
Recoverable costs, net of current portion	5,486	5,691
Restricted cash and investments:		
Operating and priority contract accounts	1,095	964
Bond charge collection and bond charge payment accounts	862	629
Recoverable costs, current portion	463	468
Interest receivable	13	13
Derivative financial instruments	223	233
Deferred charges	413	436
Other assets	30	72
Total assets	$ 10,078	$ 9,999
Net assets	$ -	$ -
Long-term debt, including current portion	8,998	9,001
Derivative financial instruments	413	436
Other deferred credits	54	43
Other current liabilities	613	519
Total capital and liabilities	$ 10,078	$ 9,999

ASSETS

Long-Term Restricted Cash and Investments

There is no change in the $543 million balance in the Operating Reserve Account at September 30, 2009 from June 30, 2009. The amount is determined in accordance with the bond indenture and is equal to the maximum one month priority contract cost amount under stress conditions for calendar year 2009 as forecast in the DWR 2009 revenue requirement determination. The balance of the Debt Service Reserve Account remains at $950 million, and was also determined in accordance with bond indenture requirements.

Recoverable Costs, Net of Current Portion

Long-term recoverable costs consist of costs that are recoverable through future billings. The $243 million net decrease in long-term recoverable costs during the three month period ended September 30, 2008 is the net of 1) operating revenues exceeding operating expenses by $94 million, as power costs were lower than expected due to the decline in the price for natural gas and 2) bond charge revenue exceeding interest expense by $149 million.

As a result of implementing GASB 53, $39 million of other assets were reclassified as derivative instruments at September 30, 2009. Additionally, in prior periods changes in the value of those other assets were recorded as a component of DWR's power costs; under GASB 53, changes in the value of these derivatives is deferred until the underlying contracts are settled. As a result, the impact of implementing GASB 53, had the effect of increasing long term recoverable costs by $39 million.

Restricted Cash and Investments

The Operating and Priority Contract Accounts increased by $131 million during the three month period ended September 30, 2009. Declining natural gas prices have resulted in lower than expected power costs than forecast as part of the 2009 revenue requirement, and have allowed DWR to collect higher amounts of remittances from ratepayers than necessary to recover its costs.

The Bond Charge Collection and Bond Charge Payment Accounts increased by $233 million in the period ended September 30, 2009 in anticipation of the semi-annual interest payment on fixed rate bonds due in November 1, 2009, and the next principal payment due May 1, 2010.

From the dates of issuance of the revenue bonds through September 30, 2009, the balances in each of the restricted cash and investments accounts met or exceeded balances required by the Bond Indenture.

Recoverable Costs, Current Portion

The current portion of recoverable costs reflects billings to IOU customers that have not yet been collected and amounts due for surplus sales of energy and gas. The current portion of recoverable costs of $463 million at September 30, 2009, is $5 million lower than at June 30, 2009. The slightly lower amounts are as a result of lower volumes of power sold in the summer months to end use customers. The lower sales are due to moderate temperatures and weaker economic conditions keeping DWR contract dispatch lower than seasonally expected.

Other Assets

DWR purchases natural gas as fuel for the production of power under the terms of certain power purchase contracts and maintains a brokerage account with a national brokerage firm in order to hedge natural gas costs. DWR invests funds to be used to meet realized losses as they occur, provide collateral for current positions, and enable future hedging activities that require margin or immediate payment. Assets in this account are classified as other assets on the Statements of Net Assets.

At September 30, 2009, other assets consisted of money market obligations, US Treasury bills, and government bonds valued at $30 million. DWR implemented GASB 53 during the three month period ended September 30, 2009. This resulted in $39 million of financial natural gas options that were included in as part of Other Assets at June 30, 2009 to be reclassified as derivative instruments, lowering the value of other assets on the Statement of Net Assets going forward. Retroactive application is required under the provisions of GASB 53 for all periods presented, however the impact of adjusting other assets at June 30, 2009 would not be material to DWR. Therefore the portion of other assets attributable to natural gas options was not reclassified as derivative financial instruments at June 30, 2009.

Derivative Financial Instruments

DWR implemented GASB 53 during the three month period ended September 30, 2009. GASB 53 requires governments to record derivative instruments on the statement of net assets as either assets or liabilities depending on the underlying fair value of the derivative.

The Fund is party to interest rate swap agreements and natural gas hedging positions that are considered to be derivatives under the provisions of GASB 53 and included on the statement of net assets for periods ended September 30, 2009 and June 30, 2009. The fair value of these derivatives has been recorded as assets if valued in DWR's favor or liabilities if not valued in DWR's favor. The derivatives have been classified on the statement of net assets as current for contracts with under 12 months remaining until expiration, or as non-current for contracts with over 12 months remaining until expiration. All of DWR's derivatives are considered hedging derivatives, with changes in fair value deferred on the statement of net assets.

Derivative financial instrument assets decreased $10 million, and totaled $223 million and $233 million at September 30, 2009 and June 30, 2009, respectively. The lower fair value of derivative financial instruments is primarily due to total notional amounts of natural gas hedges declining in the period along with slightly lower fair values of DWR's basis interest rate swaps, as detailed in Note 5.

Deferred Charges

As part of implementing GASB 53, changes in fair value of derivative liabilities considered effective hedges are recorded as deferred charges. The current portion of deferred charges is attributable to derivative instruments with less than twelve months remaining until expiration. The noncurrent portion of deferred charges is attributable to derivative instruments with more than twelve months remaining until expiration.

Deferred charges declined by $23 million to $413 million at September 30, 2009 from $436 million at June 30, 2009, as derivative financial instrument liabilities declined in value.

LIABILITIES

Long-Term Debt

The $4 million decrease in long-term debt for the three month period ended September 30, 2009 is attributable to the net amortization of bond premium and deferred loss on the advance bond refunding.

Derivative Financial Instruments

Derivative financial instrument liabilities decreased $23 million, and were valued at $413 million and $436 million at September 30, 2009 and June 30, 2009, respectively. While natural gas market prices were stable, the fair value declines in derivative financial instruments were due to total notional amounts of natural gas hedges declining in the period as detailed, offset by an increase in liability values for interest rate swaps highlighted in Note 5.

Deferred Credits and Other Current Liabilities

Accounts payable reflect one month's accrual for power and fuel purchases, as payments are normally made on the 20th of the month following purchase. At September 30, 2009 accounts payable are $34 million lower than at June 30, 2008 as a sharp decline in natural gas prices from levels in June offset higher seasonal contract volumes.

The $49 million increase in accrued interest payable is anticipated as the fixed rate bonds provide for semi-annual payments on May 1st and November 1st, while the variable rate bonds provide for more frequent payments.

As part of the implementation of GASB 53, deferred credits have been included on the statement of net assets, capturing the changes in fair value of effective derivative financial instrument assets.

The current portion of deferred credits have been included as part of other current liabilities. Current deferred credits declined by $31 in three month period ended September 30, 2009 to $169 million from $190 million at June 30, 2009, as current derivative instruments declined in value. The non-current portion of deferred credits is included as other deferred credits and increased by $11 million to $54 million at September 30, 2009 from $43 million at June 30, 2009.

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

The Fund's activities for the three months ended September 30, 2009 and 2008 are summarized as follows (in millions):

	2009	2008
Revenues:		
Power charges	$ 950	$ 962
Surplus sales	23	107
Bond charges	229	218
Interest income	10	26
Total revenues	1,212	1,313
Expenses:		
Power purchases	911	1,417
Energy settlements	(1)	(8)
Interest expense	90	99
Other expenses	7	5
(Deferral) recovery of recoverable costs	205	(200)
Total expenses	1,212	1,313
Net increase in net assets	-	-
Net assets, beginning of period	-	-
Net assets, end of period	$ -	$ -

REVENUES

Power Charges

The cost of providing energy is recoverable primarily through power charges to IOU customers and certain customers of ESPs. Charges are determined by applying a CPUC adopted rate for each IOU service area to the megawatt hours of power delivered by DWR to each IOU's customers.

Power charges decreased by $12 million in the three months ended September 30, 2009 compared to the same three month period in 2008. The small difference reflects a combination of slightly lower volume of power sales to end use customers and per unit remittance rates implemented in January 2009 with the 2009 revenue requirement that are substantially the same as rates that were in effect for 2008.

Surplus Sales

Surplus sales of energy and natural gas in the three month period ended September 30, 2009 were $84 million lower than in the same period in 2008. The primary factor was a sharp decline in volumes of surplus power sales occurring as a result of a change in remittance collection methodology adopted by DWR and its IOU limited agents as part of implementing operational changes to adapt to the California Independent System Operator's (CAISO) Market Redesign Technology Upgrade (MRTU) launched on March 31, 2009. DWR no longer receives a pro rata portion of surplus power sales to each IOU service area after the change. DWR has forecast this change in its 2009 revenue requirement and has implemented remittance rates that will maintain required minimum balances in excess of bond indenture requirements.

Lower gas sales volumes and lower prices received per unit of power and gas sold also contributed to the lower amounts during the 2009 period as commodity market prices declined sharply.

Bond Charges

Bond charges provide revenue for the payment of debt service on the revenue bonds and are determined by applying a CPUC adopted rate to the total megawatt hours of power delivered to all IOU customers and certain ESP customers.

Bond charges for the three months ended September 30, 2009 are $8 million higher than the same period in 2008, as higher rates offset slightly lower delivered volumes. The amount collected is adequate to meet all debt service requirements and maintain bond indenture required account balances in the Bond Charge Collection, Bond Charge Payment, and Debt Service Reserve Accounts.

Interest Income

Interest income of $10 million for the three months ended September 30, 2009 is lower than the interest income for the same period in 2008. A decline in interest earned on investments in the State of California Investment Pooled Money Investment Account-Surplus Investment Fund (SMIF) offset slightly higher cash balances outstanding.

EXPENSES

Power Purchases

Power costs are $406 million lower in the three months ended September 30, 2009 than in the same period in 2008. The decrease in costs is primarily due to the substantially lower price of natural gas in 2009 when compared to 2008 as commodities market prices continued to decline. In 2008 there were amounts expended to meet margin calls due to the rapid decline in natural gas costs in the three month period, while there were no funds transferred for margin calls in 2009.

DWR implemented GASB 53 during the three month period ended September 30, 2009. This resulted in an increase to power costs of $39 million, as financial natural gas options that were included in as part of Other Assets at June 30, 2009 were reclassified as derivative instruments. Prior to September 30, 2009, DWR included any change in fair value of its natural gas options as a component of power costs. Retroactive application is required under the provisions of GASB 53 for all periods presented, however the impact of adjusting power purchases for the three month period ended September 30, 2008 would not be material to DWR. Therefore power purchases were not adjusted for 2008.

Energy Settlements

Energy settlements in the three month period ended September 30, 2009 were $1 million as there were no large settlement actions. Future revenues under a number of settlements with larger suppliers including Mirant Corporation, Reliant Energy, Dynegy Inc, and Duke Energy Corporation, are subject to contingencies outlined in the underlying settlement and allocation agreements and will not be recognized until if and when the contingencies are resolved.

Interest Expense

Interest expense in the three months ended September 30, 2009 is $9 million lower than the amounts paid in the same period in 2008. The slight decrease was attributed to lower variable bond interest rate costs incurred resulting from the decline in interest rates as credit markets normalized and interest rates remain lower than experienced during the credit turmoil in 2008. The lower variable rates were partially offset by higher amounts of fixed rate debt outstanding after DWR remarketed $548 million of its variable rate bonds to fixed rate bonds in November 2008 and January 2009.

Other Expenses

Other expenses in the three months ended September 30, 2009 were $2 million higher than the same period in 2008, as a result of increased legal expenditures for contract renegotiations and ongoing litigation services regarding the 2000-2001 California energy crisis.

Recovery (Deferral) of Recoverable Costs

The individual components of the recovery (deferral) of recoverable costs are as follows for the three months ended September 30, 2009 and 2008 (in millions):

	2009	2008
Operations	$ 56	$ (345)
Debt service and related costs	149	145
	$ 205	$ (200)

Operations
There was a recovery of recoverable costs of $56 million for the three months ended September 30, 2009, compared to the $345 million deferral in the same period in 2008. The recovery in the three months ended September 30, 2009 reflects lower power costs than planned due to the sharp decrease in natural gas prices in 2009, while 2008 was affected by higher than planned gas prices causing the large deferral.

Debt Service and Related Costs
The recovery of debt service and bond related costs are $4 million higher for the three months ended September 30, 2009 compared to the same period in 2008. The recovery is comprised solely of the difference between bond charges and interest income less interest expense. The smaller recovery is primarily due to lower interest income due to the decline in cash balances and interest rates earned on those balances.

Department of Water Resources Electric Power Fund
Statements of Net Assets
September 30, 2009 and June 30, 2009 (in millions)

	September 30, 2009	June 30, 2009
Assets		
Long-term assets:		
Restricted cash, equivalents and investments:		
Operating Reserve Account	$ 543	$ 543
Debt Service Reserve Account	950	950
Derivative financial instruments, net of current portion	54	43
Other non-current assets	329	177
Recoverable costs, net of current portion	5,486	5,691
Total long-term assets	7,362	7,404
Current assets:		
Restricted cash and investments:		
Operating and Priority Contract Accounts	1,095	964
Bond Charge Collection and Bond Charge Payment Accounts	862	629
Recoverable costs, current portion	463	468
Interest receivable	13	13
Derivative financial instruments	169	190
Deferred charges	84	259
Other Assets	30	72
Total current assets	2,716	2,595
Total assets	$ 10,078	$ 9,999
Capitalization and Liabilities		
Capitalization:		
Net assets	$ -	$ -
Long-term debt:		
Revenue bonds	8,469	8,471
Total capitalization	8,469	8,471
Non-current liabilities		
Derivative financial instruments, net of current portion	329	177
Other deferred credits	54	43
	383	220
Current liabilities:		
Current portion of long-term debt	529	530
Derivative financial instruments	84	259
Accounts payable and other current liabilities	462	456
Accrued interest payable	151	63
Total current liabilities	1,226	1,308
Commitments and contingencies (Note 5)		
Total capitalization and liabilities	$ 10,078	$ 9,999

Department of Water Resources Electric Power Fund
Statements of Revenues, Expenses and Changes in Net Assets
For the three months ended September 30, 2009 and 2008 (in millions)

	2009	2008
Operating revenues:		
Power charges	$ 950	$ 962
Surplus sales	23	107
Total operating revenues	973	1,069
Operating expenses:		
Power purchases	911	1,417
Energy settlements	(1)	(8)
Other expenses	7	5
Deferral of recoverable operating costs	56	(345)
Total operating expenses	973	1,069
Income from operations	-	-
Bond charges	229	218
Interest income	10	26
Interest expense	(90)	(99)
Recovery of recoverable debt service and related costs	(149)	(145)
Net increase in net assets	-	-
Net assets, beginning of period	-	-
Net assets, end of period	$ -	$ -

Department of Water Resources Electric Power Fund
Statements of Cash Flows
For the three months ended September 30, 2009 and 2008 (in millions)

	2009	2008
Cash flows from operating activities:		
Receipts:		
Power charges	$ 948	$ 836
Surplus sales	26	174
Energy settlements	1	8
Payments for power purchases and other expenses	(849)	(1,301)
Net cash provided by (used in) operating activities	126	(283)
Cash flows from non-capital financing activities:		
Receipt of bond charges	234	242
Interest payments	(5)	(52)
Net cash provided by non-capital financing activities	229	190
Cash flows from investing activities:		
Interest received	10	24
Net cash provided by investing activities	10	24
Net increase (decrease) in cash and equivalents	364	(69)
Restricted cash and equivalents, beginning of period	2,786	2,861
Restricted cash and equivalents, end of period	$ 3,150	$ 2,792
Restricted cash and equivalents included in:		
Operating Reserve Account	$ 543	$ 548
Debt Service Reserve Account (a component of the total of $950 and $917 at September 30, 2009 and 2008, respectively)	650	467
Operating and Priority Contract Accounts	1,095	923
Bond Charge Collection and Bond Charge Payment Accounts	862	854
Restricted cash and equivalents, end of period	$ 3,150	$ 2,792
Reconciliation of operating income to net cash provided by (used in) operating activities:		
Income from operations	$ -	$ -
Adjustments to reconcile operating income to net cash provided by (used in) operating activities:		
Deferral of recoverable operating costs	56	(345)
Changes in net assets and liabilities to reconcile operating income to net cash provided by (used in) operations:		
Recoverable costs, current portion	1	(59)
Other assets	42	205
Accounts payable	27	(84)
Net change in operating assets & liabilities:	70	62
Net cash provided by (used in) operating activities	$ 126	$ (283)

The accompanying notes are an integral part of these financial statements.

1. Reporting Entity

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

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

DWR purchases power from wholesale suppliers under contracts entered into prior to January 1, 2003 for resale to ten million customers of Pacific Gas & Electric Company, Southern California Edison Company, and San Diego Gas & Electric Company (collectively referred to as the investor owned utilities or IOUs). The Code prohibits DWR from entering into new power purchase agreements, but allows DWR to enter into gas purchase contracts to provide fuel for power generation.

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

Under the terms of a rate agreement between DWR and the CPUC, the CPUC implements DWR's determination of its revenue requirements by establishing customer rates that meet DWR's revenue needs to assure the payment of debt service, power purchases, administrative expenses and changes in reserves.

2. Summary of Significant Accounting Policies

Basis of Presentation
The Fund is accounted for as an enterprise fund and is financed and operated in a manner similar to that of a private business enterprise. The Fund uses the economic resources measurement focus and the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred. As allowed by governmental accounting standards, the Fund has elected not to apply statements and related interpretations issued by the Financial Accounting Standards Board after November 30, 1989. The Fund is accounted for with a set of self-balancing accounts that comprise its assets, liabilities, fund equity, revenues and expenses.

The financial statements of the Fund are intended to present the financial position, and the changes in financial position and cash flows, where applicable, of only that portion of the business-type activities and major funds of the State of California that is attributable to the transactions of the Fund. They do not purport to, and do not, present fairly the financial position of the State of California as of September 30, 2009 and 2008, and the changes in its financial position and its cash flows, where applicable, for the periods then ended in conformity with accounting principles generally accepted in the United States of America.

Revenues and Recoverable Costs
DWR is required to at least annually establish a revenue requirement determination to recover all Fund costs, including debt service. The revenue requirement determination is submitted to the California Public Utilities Commission which then sets customer remittance rates. The Fund's financial statements are prepared in accordance with SFAS No. 71, "*Accounting for the Effects of Certain Types of Regulation*", which requires that the effects of the revenue requirement process be

recorded in the financial statements. Accordingly, all expenses and credits, normally reflected in the change in net assets as incurred, are recognized when recovered from IOU customers. Costs that are recoverable through future billings are recorded as long-term assets.

Amounts that have been earned but not collected by DWR are recorded as the current portion of recoverable costs.

Customer charges are separated into two primary components, power charges and bond charges. Power charge revenues recover the cost of power purchases, other expenses and operating reserves and are recognized when energy provided by DWR is delivered to the IOU customers. Certain customers of "direct access" Electric Service Providers (ESPs) are assessed a "cost responsibility surcharge" that is used by DWR for the same purposes as power charge revenues. Bond charge revenues recover debt service, debt service reserves and other bond related costs and are recognized when energy provided by either DWR or the IOU, or an ESP, is delivered to IOU or ESP customers. Costs are recovered over the life of the bonds (2022) as determined by DWR's revenue requirement process.

New Accounting Pronouncements

<u>GASB 53 Accounting and Financial Reporting for Derivative Instruments</u>

Effective July 1, 2009, DWR adopted GASB No. 53, *Accounting and Financial Reporting for Derivative Instruments* (GASB 53), which establishes accounting and financial reporting standards for the recognition, measurement, and disclosure of information regarding derivative instruments entered into by state and local governments (See note 5). GASB 53 requires governments to record certain derivative instruments on the statement of net assets as either assets or liabilities depending on the underlying fair value of the derivative. The fair value of a derivative instrument is either the value of its future cash flows in today's dollars or the price it would bring if it could be sold on an open market.

Prior to adopting GASB 53, DWR accounted for its derivative contracts under the provisions of GASB Technical Bulletin 2003-1 (GASB TB 03-1). The required treatment and disclosure have been superseded by GASB 53, thus certain disclosures that were necessary under GASB TB 03-1 and the treatment of certain financial instruments have been modified. Under GASB 53, derivative contracts that are considered normal purchases are excluded from the statement of net assets. Normal purchases and normal sales are contracts that are for the purchase or sale of a commodity such as natural gas or electricity, to be used in the normal course of operations, provided that is it probable that DWR will make or take delivery of the commodity specified in the derivative instrument.

The Fund is party to interest rate swap agreements which are considered to be derivatives and have been accounted for under the requirements of GASB 53. The fair values have been recorded on the statement of net assets as long-term assets or liabilities, according to the fair values detailed further in Note 5, along with a corresponding long-term deferred charge or credit.

DWR's natural gas hedging activities and positions are considered derivatives and have been accounted for under the requirements of GASB 53 and included on the statement of net assets for periods ended September 30 and June 30, 2009. DWR's natural gas hedges are considered effective. The fair value of these derivatives have been recorded on the balance sheet as assets or liabilities, along with a corresponding deferred charge or credit, and have been classified as current for contracts with under 12 months remaining until expiration, or as long-term for contracts with over 12 months remaining until expiration.

Under prior GASB TB 03-1 treatment, the natural gas financial options were already accounted for on the Fund's statement of net assets, but have been reclassified from other assets to derivative instruments, as required under GASB 53 for the period ended September 30, 2009. Under GASB TB 03-1 any change in the fair value of these options were recorded as a component of power costs. Reclassifying the options from other assets to derivatives has resulted in an increase to Power Costs and has been included in the statement of revenues, expenses and changes in net assets for period ended September 30, 2009. Because retroactive reclassification for prior periods presented would not be material, DWR has not made this adjustment for any prior periods.

All of DWR's power purchase agreements qualify for exemption from treatment as derivatives under the normal purchase/normal sales exclusion, and are not included on the Statement of Net Assets.

3. Restricted Cash and Investments

The State of California has a deposit policy for custodial credit risk. As of September 30, 2009, $22 million of the Fund's cash balances were uninsured and uncollateralized.

As of September 30, 2009, the Fund had the following investments (in millions):

Investment	Maturity		Amount
State of California Pooled Money Investment Account - State Money Investment Fund	5.5 months average	$	3,123
Cash			27
			3,150
Guaranteed investment contracts	May 1, 2022		200
Forward purchase agreement	November 1, 2009		100
		$	3,450
Reconciliation to Statement of Net Assets:			
Operating Reserve Account		$	543
Debt Service Reserve Account			950
Operating and Priority Contract Accounts			1,095
Bond Charge Collection and Bond Charge Payment Accounts			862
		$	3,450

Interest Rate Risk: In accordance with its investment policy, the State of California manages its exposure to declines in fair values by limiting investments to the maximum maturities, as follows: U.S. Treasury securities, 5 years; federal agency securities, 5 years; bankers acceptances – domestic and foreign, 180 days; certificates of deposits, 5 years; commercial paper, 180 days; corporate bonds and notes, 5 years; repurchase agreements and reverse repurchase agreements, 1 year.

Credit Risk: The PMIA funds are on deposit with the State's Centralized Treasury System and are managed in compliance with the California Government Code, according to a statement of investment policy which sets forth permitted investment vehicles, liquidity parameters and maximum maturity of investments. These investments consist of U.S. government securities, securities of federally-sponsored agencies, U.S. corporate bonds, interest bearing time deposits in California banks, prime-rated commercial paper, bankers' acceptances, negotiable certificates of deposit, repurchase and reverse repurchase agreements. The PMIA policy limits the use of reverse repurchase agreements to limits of no more than 10% of the PMIA and commercial paper to limits not to exceed 30% of the

PMIA. The PMIA does not invest in leveraged products or inverse floating rate securities. The PMIA is not rated.

The Fund's investments in the guaranteed investment contracts and forward purchase agreement are rated as follows, by Standard & Poor's (S&P) and Moody's, respectively, at September 30, 2009 (in millions):

	Amount	S&P	Moody's
GIC Providers			
FSA	$ 100	AAA	Aa3
Royal Bank of Canada	100	AA-	Aaa
	$ 200		
FPA Provider			
Merrill Lynch: FHLMC Discounted Notes	$ 100	AAA	Aa1

Concentration of Credit Risk: The PMIA's concentration of credit risk is limited by spreading the investment mix over different investment types and issuers to minimize the impact any one industry, investment class, or institution can have on the PMIA portfolio.

Interest on deposits in the PMIA varies with the rate of return of the underlying portfolio and approximated 0.75% and 2.78% at September 30, 2009 and 2008, respectively. Interest on the GICs is paid semi-annually at interest rates ranging from 5.3% to 5.5%. The FPA allows DWR to continuously reinvest funds in U.S. government or U.S. government agency securities through May 2022 to earn a minimum rate of return of 4.7%, as specified in the Reserve Fund Forward Purchase and Sale Agreement, dated May 1, 2004. The reinvested securities are to mature every six months.

4. Long-Term Debt

The following activity occurred in the long-term debt accounts during the three months ended September 30, 2009 (in millions):

	Revenue Bonds	Unamortized Premium	Deferred Loss on Defeasance	Total Revenue Bonds
Balance, June 30, 2009	$ 9,030	$ 142	(171)	$ 9,001
Amortization		(7)	4	(3)
Less current portion	(518)	(27)	16	(529)
Balance, September 30, 2009	$ 8,512	$ 108	$ (151)	$ 8,469

The tax exempt revenue bonds consist of the following at September 30, 2009 (in millions):

Series	Rates	Fiscal Year of Final maturity	Fiscal Year of First Call Date	Amount Outstanding 2009
A	Fixed (3.1-6.0%)	2018	2012	$ 2,458
B	Variable	2020	Callable	1,000
C	Variable	2021	Callable	2,229
F	Variable	2022	Callable	409
F	Fixed (4.375-5.0%)	2022	Callable	348
G	Variable	2018	Callable	646
G	Fixed (4.35-5.0%)	2016/18	Callable	173
H	Fixed (3.75-5.0%)	2022	Non-callable	1,007
I	Variable	2022	Callable	150
J	Variable	2018	Callable	330
K	Fixed (4.9-5.0%)	2018	Non-callable	279
				$ 9,030
Plus unamortized bond premium				135
Less deferred loss on defeasance				(167)
Less current maturities				(529)
				$ 8,469

Key terms

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

The Series A bonds are callable May 1, 2012 through October 31, 2012 at a redemption rate of 101%, from November 1, 2012 through April 30, 2013 at a redemption rate of 100.5% and thereafter, at 100%. The Series H bonds are callable in 2018 at a redemption rate of 100%. All other callable bonds are redeemable at 100%.

DWR's variable rate bonds have either daily or weekly rate reset modes. The variable rate bonds have a final stated maturity of 2022, but are scheduled to be retired in sinking fund installments from 2008 to 2022. The interest rates for the variable debt for the three months ended September 30, 2009, ranged from 0.04% to 2.50%.

The payment of principal and interest for all Series B bonds, $1.73 billion of Series C bonds, $409 million of Series F bonds, $46 million of Series G and all Series I and J bonds are paid from draws made under letters of credit. Draws made under the letters of credit are to be reimbursed on the same day by the Fund. Bonds purchased under the letters of credit are required to be redeemed in equal installments over a three year period beginning six months after the termination date of the letter of credit. There are no outstanding amounts on the letters of credit at June 30, 2009. The Fund pays fees of 0.45% per annum on the stated amount of the letters of credit for the Series B and C bonds, in a range from 0.35% to 0.38% per annum on the stated amount for the Series F and G bonds, and 0.53% per annum on the stated amount for the Series I and J bonds. All Series B, C, F, G, I and J letters of credit expire in fiscal year 2011.

Remarketing, credit support and related uncertainties

DWR bonds are remarketed by fourteen different broker-dealer remarketing agents, with credit enhancement provided by twenty one banks to spread its risk exposure among many firms. Remarketing agents can experience problems finding investors for certain bonds, including those with credit enhancement from banks and insurers that have perceived credit risk, as well as risk specific to their own company that carries negative perception with investors. Failed remarketings can result in the credit enhancing bank's required purchase of the bonds, and they become "bank bonds". If this occurs, DWR is required to pay a stated fixed interest rate quarterly until the bonds are successfully remarketed. If the agreements expire or are terminated, DWR is required to begin paying principal in quarterly installments nine months after termination. Early repayment requirements vary with each type of credit facility. Letters of credit require DWR to repay the bonds in eleven equal installments, while liquidity facilities require repayment in nineteen or twenty seven equal installments depending on the provider.

Negative credit market impacts can increase borrowing costs on variable rate bonds that experience interest rate resets at higher rates and on occasion will cause the remarketing failure of bonds resulting in those bonds becoming bank bonds. The level of bank bonds can fluctuate daily as the bonds are successfully remarketed. At September 30, 2009, there were no outstanding bank bonds.

At September 30, 2009, $496 million of Series C bonds and $600 million of Series G bonds are credit enhanced by bond insurance for the timely payment of principal and interest. All insured bonds are enhanced by FSA bond insurance which was rated AAA/Aa3 by S&P and Moody's at September 30, 2009. Liquidity support for these variable rate bonds is provided by bank liquidity facilities. Any funds paid under the bond insurance facilities are immediately due and payable by the Fund. Bonds purchased under the initial liquidity facilities are required to be redeemed in equal installments over a five or seven year period beginning six months after the termination date of the liquidity facilities. There are no outstanding amounts due under liquidity facilities at September 30, 2009. The liquidity facilities backing the $496 million of Series C bonds expire in fiscal year 2013. The Fund pays fees of 0.22% to 0.28% per annum under the Series C liquidity facilities. Four liquidity facilities backing $500 million of Series G bonds expire in fiscal year 2011 and the final liquidity facility underlying $100 million expires in fiscal year 2013. The Fund pays fees of between 0.15% to 0.19% per annum under the Series G liquidity facilities.

Future payment requirements on the revenue bonds are as follows at September 30, 2009 (in millions):

Fiscal Year	Principal	Interest [1]	Total
2010	518	174	692
2011	545	211	756
2012	573	193	766
2013	602	172	774
2014	636	144	780
2015-2019	3,601	459	4,060
2020-2022	2,555	126	2,681
	$ 9,030	$ 1,479	$ 10,509

[1] Variable portion of interest cost calculated using the September 30, 2009 Securities Industry and Financial Markets Association Swap Index (SIFMA).

5. Derivative Financial Instruments

As discussed in Note 2, DWR implemented GASB 53 during the three month period ended September 30, 2009. GASB 53 requires governments to record derivative instruments on the statement of net assets as either assets or liabilities depending on the underlying fair value of the derivative. The Fund is party to interest rate swap agreements and natural gas hedging positions that are considered to be derivatives under the provisions of GASB 53 and included on the statement of net assets for periods ended September 30, 2009 and June 30, 2009.

The fair values, classification and notional amounts outstanding for DWR's natural gas hedges and interest rate swaps accounted for as derivative financial instruments at September 30, 2009 and June 30, 2009 are summarized in the following table:

Cash Flow Hedges	Classification	Maturity	Fair Value at Sept 30, 2009	Notional Amount
Commodity forwards (effective hedge)	Deferred inflow	0-12 months	$ 169	172,890,000 mmBtu's
Commodity forwards (effective hedge)	Deferred inflow	over 12 months	$ 15	34,080,000 mmBtu's
Basis interest rate swaps (effective hedge)	Deferred inflow	over 12 months	$ 39	$ 1,006,400,000
		total deferred inflow	$ 223	
Commodity forwards (effective hedge)	Deferred outflow	0-12 months	$ (84)	100,021,500 mmBtu's
Commodity forwards (effective hedge)	Deferred outflow	over 12 months	$ (24)	23,205,000 mmBtu's
Pay-fixed interest rate swaps (effective hedge)	Deferred outflow	over 12 months	$ (305)	$ 3,812,100,000
		total deferred outflow	$ (413)	

Cash Flow Hedges	Classification	Maturity	Fair Value at June 30, 2009	Notional Amount
Commodity forwards (effective hedge)	Deferred inflow	0-12 months	$ 210	153,064,118 mmBtu's
Commodity forwards (effective hedge)	Deferred inflow	over 12 months	$ 16	36,835,902 mmBtu's
Basis interest rate swaps (effective hedge)	Deferred inflow	over 12 months	$ 41	$ 1,006,400,000
		total deferred inflow	$ 267	
Commodity forwards (effective hedge)	Deferred outflow	0-12 months	$ (184)	146,382,000 mmBtu's
Commodity forwards (effective hedge)	Deferred outflow	over 12 months	$ (36)	45,342,500 mmBtu's
Pay-fixed interest rate swaps (effective hedge)	Deferred outflow	over 12 months	$ (226)	$ 3,812,100,000
		total deferred outflow	$ (446)	

Natural Gas Hedging Instruments

The Fund enters into forward gas futures and options contracts to financially hedge the cost of natural gas. Implementing GASB 53 required reporting all of DWR financial natural gas hedges on the Statement of Net Assets as assets or liabilities depending on their fair value. It also required reclassifying all financial natural gas options as derivatives. DWR reclassified the options as derivatives for September 30, 2009, but did not make an adjustment for prior periods presented, since the impact would not be material to DWR.

All of DWR's gas hedging contracts are effective hedges, thus gains and losses are deferred on the statement of net assets as either current credits or charges for contracts with under 12 months remaining until expiration, or as long-term for contracts with over 12 months remaining until expiration. A long-term deferred charge or credit has also been recorded on the statement of net assets reflecting the deferred inflow or outflow associated with the derivative financial instruments.

Credit Risk: DWR has a portion of its open natural gas hedge positions with twelve different counterparties at June 30, 2009. All counterparties have credit ratings of at least A-/A2. At September 30, 2009, DWR has credit risk exposure to five counterparties, since the market values are in DWR's favor for between $1.3 million and $5.3 million. DWR management believes there is no substantial credit exposure to the remaining seven counterparties, as the sharp decrease of natural gas prices has resulted in valuations in the counterparties' favor. The remaining gas hedge positions have been entered into through DWR's brokerage accounts and the associated clearing accounts have collateral requirements that management believes does not expose DWR to any counterparty credit risk.

Termination Risk: With regards to gas hedge agreements, DWR or the counterparty may terminate an agreement if the other party fails to perform under the terms of the contract. In addition, the agreements allow either party to terminate in the event of a significant loss of creditworthiness by the other party. If a termination were to occur, DWR or the counterparty would owe the other a payment equal to the open positions fair value in their favor.

Interest Rate Swaps

DWR, on behalf of the Fund, entered into interest rate swap agreements with various counterparties to reduce variable interest rate risk. The pay-fixed swaps create a synthetic fixed rate for DWR. DWR has agreed to make fixed rate payments and receive floating rate payments on notional amounts equal to a portion of the principal amount of DWR's variable rate debt. DWR has also entered into swaps to mitigate basis risk and optimize debt service by changing the variable rate received by the Fund to a five year Constant Maturity Swap Index (CMS).

As discussed in Note 2, all of DWR's interest rate swaps are considered derivatives under GASB 53, and the fair values have been recorded on the statement of net assets as long-term assets or liabilities, depending on whether the fair values are in DWR favor or not. A long-term deferred charge or credit as also been recorded on the statement of net assets reflecting the deferred inflow or outflow.

The terms, fair values, and credit ratings of counterparties for the various pay fixed swap agreements at September 30, 2009 are summarized in the following table (in millions):

Outstanding Notional Amount	Fixed Rate Paid by Fund	Variable Rate [1] Received by Fund	Fair Value	Swap Termination Date	Counterparty Credit Rating S&P	Counterparty Credit Rating Moody's	Counterparty Credit Rating Fitch
$ 94	2.914%	67% of LIBOR	$ (4)	May 1, 2011	AAA	Aaa	AAA
234	3.024%	67% of LIBOR	(15)	May 1, 2012	AAA	Aaa	AAA
127	3.405%	SIFMA	(6)	May 1, 2013	AA-	Aa1	AA-
63	3.405%	SIFMA	(3)	May 1, 2013	A	A2	A
19	3.405%	SIFMA	(1)	May 1, 2013	A	A2	A+
194	3.204%	67% of LIBOR	(16)	May 1, 2014	A+	Aa3	A+
264	3.184%	66.5% of LIBOR	(19)	May 1, 2015	BBB	A3	A-
174	3.280%	67% of LIBOR	(15)	May 1, 2015	AAA	Aaa	AAA
202	3.342%	67% of LIBOR	(19)	May 1, 2016	AA	Aa1	AA
485	3.228%	66.5% of LIBOR	(42)	May 1, 2016	AA	Aa1	AA
202	3.389%	67% of LIBOR	(21)	May 1, 2017	A	A2	A
480	3.282%	66.5% of LIBOR	(42)	May 1, 2017	AA	Aa2	AA
515	3.331%	66.5% of LIBOR	(44)	May 1, 2018	A+	Aa1	AA-
306	3.256%	64% of LIBOR	(24)	May 1, 2020	A+	Aa1	AA-
453	3.325%	64% of LIBOR	(34)	May 1, 2022	AA-	Aaa	AA
$ 3,812			$ (305)				

[1] One month U.S. Dollar London Interbank Offered Rate or Securities Industry and Financial Markets Association (SIFMA)

The notional amounts of the swaps match the principal amounts of the associated debt. The swap agreements contain scheduled reductions in notional amounts that follow scheduled amortization of the associated debt.

As of September 30, 2009, the variable rates on DWR's hedged bonds ranged from 0.04% to 2.50%, while 64%, 66.5% and 67% of LIBOR received on a portion of the swaps was equal to 0.17%, 0.17%, and 0.18% respectively and SIFMA received on a portion of the swaps was 0.40%.

Fair Value: The reported fair values from the table above were determined based on quoted market prices for similar financial instruments.

Basis Risk: The Fund is exposed to basis risk on the swaps that have payments calculated on the basis of a percentage of LIBOR (a taxable rate index). The basis risk results from the fact that DWR's floating interest payments payable on the underlying debt are determined in the tax-exempt market, while DWR's floating receipts on the swaps are based on LIBOR, which is determined in the taxable market. When the relationship between LIBOR and the tax-exempt market change and move to convergence, or DWR's bonds trade at levels higher in rate in relation to the tax-exempt market, DWR's all-in costs would increase.

DWR has entered into basis swaps to mitigate this risk and optimize debt service by changing the variable rate received by the Fund to a five year Constant Maturity Swap Index (CMS). The terms, fair values, and credit ratings of counterparties for the various basis swap agreements at September 30, 2009 are summarized in the following table (in millions):

Outstanding Notional Amount	Variable Rate [1] Paid by Fund	Variable Rate [2] Received by Fund	Fair Value	Swap Termination Date	Counterparty Credit Rating S&P	Moody's	Fitch
$ 234	67% of LIBOR	62.83% of CMS	$ 7	May 1, 2012	AA	Aa1	AA
194	67% of LIBOR	62.70% of CMS	8	May 1, 2014	A+	Aa1	AA-
174	67% of LIBOR	62.60% of CMS	7	May 1, 2015	AA-	Aa1	AA-
202	67% of LIBOR	62.80% of CMS	8	May 1, 2016	AA	Aa1	AA
202	67% of LIBOR	62.66% of CMS	9	May 1, 2017	AA-	Aa1	AA-
$ 1,006			$ 39				

[1] One month U.S. Dollar London Interbank Offered Rate

As of September 30, 2009, 67% of LIBOR paid on the basis swaps was equal to 0.1750% while the variable rates received based on the 5 year CMS Index varied from 2.8350 to 3.0870%.

Credit Risk: The Fund has a total of twenty swap agreements with ten different counterparties at September 30, 2009. DWR's policies limit the amount of notional exposure to a single counterparty at no more than 25 percent. Approximately 23 percent of the swaps' total notional value is with a single counterparty with a credit rating of AA/Aa1/AA, while 21 percent of the total notional value is held with another counterparty with credit ratings of A+/Aa1/AA-. The remaining swaps are with separate counterparties, all having BBB/A3/A- ratings or better.

Termination Risk: The Fund's swap agreements do not contain any out-of-the-ordinary termination provisions that would expose it to significant termination risk. In keeping with market standards, DWR or the counterparty may terminate a swap agreement if the other party fails to perform under the terms of the contract. In addition, the swap documents allow either party to terminate in the event of a significant loss of creditworthiness by the other party. If a termination were to occur, at the time of the termination, the Fund would be liable for payment equal to the swap's fair value, if it had a negative fair value at that time. The counterparty would be liable for any payment equal to the swap's fair value, if it had positive fair value at that time. As of September 30, 2009, the ratings published by a ratings agency for one Fund swap counterparty, has fallen below the A-/A1 level that would allow DWR to terminate the swap. At this time DWR is not planning to terminate based on the swap having a valuation that would create a liability for the Fund and therefore, does not create any credit risk. In addition, a termination would mean that the Fund's underlying floating rate bonds would no longer be hedged and the Fund would be exposed to floating rate risk, unless it entered into a new hedge following termination.

Rollover Risk: Since the swap agreements have termination dates and notional amounts that are tied to equivalent maturity dates and principal amounts of amortizing debt, there is no rollover risk associated with the swap agreements, other than in the event of a termination.

Swap Payments and Associated Debt: As rates vary, variable-rate bond interest payments and net swap interest payments will vary. As of September 30, 2009, debt service requirements of the variable-rate debt and net swap payments, assuming current interest rates remain the same, for their term were as follows (in millions):

Fiscal Year	Variable Rate Bonds Principal	Variable Rate Bonds Interest	Interest Rate Swaps, Net	Total
2010	$ 80	$ 11	$ 101	$ 192
2011	241	15	98	354
2012	258	14	91	363
2013	54	13	88	155
2014	221	13	86	320
2015-2019	2,365	37	270	2,672
2020-2022	593	5	39	637
	$ 3,812	$ 108	$ 773	$ 4,693

6. Commitments and Contingencies

Litigation and Regulatory Proceedings
Certain pending legal and administrative proceedings involving DWR or affecting DWR's power supply program are summarized below.

California Refund Proceedings: During 2001 and 2002, DWR purchased power in bilateral transactions (both short term and long term), sold power to the CAISO, paid for power purchased by the CAISO and purchased power from the CAISO for sale to customers of the IOUs. In July 2001, the Federal Energy Regulatory Commission (FERC) initiated an administrative proceeding to calculate refunds for inflated prices in the CAISO and California Power Exchange (PX) markets during 2000 and 2001. FERC ruled that DWR would not be entitled in that proceeding to approximately $3.5 billion in refunds associated with DWR's approximately $5 billion of short term purchases because DWR made those purchases bilaterally, not in the PX or CAISO markets. The Ninth Circuit Court of Appeals affirmed FERC, but left open the possibility of refunds on DWR's bilateral purchases in other FERC proceedings. In contrast, FERC ruled that DWR is entitled to refunds on purchases made by the CAISO where DWR actually paid the bill.

Of DWR's $5 billion in short term bilateral purchases, $2.9 billion was imbalance energy which DWR sold to the CAISO at DWR's cost in order to meet the CAISO's emergency needs during 2001. DWR is treated in the FERC refund proceeding as a seller of that energy to CAISO, and in May 2004, FERC issued an order requiring DWR to pay refunds on the sales to the CAISO. However, because DWR would likely be the primary recipient of any refunds on energy it sold to the CAISO, DWR's potential net liability associated with its sales to the CAISO would be substantially reduced. Settlements executed to date with various sellers have reduced that potential liability even further.

Under FERC's orders, therefore, DWR both owes refunds (on the energy it sold to the CAISO) and is entitled to refunds (on the energy that the CAISO purchased but DWR paid for); the effect of offsetting the two is likely to be that DWR would receive refunds.

As to refunds owed, FERC has ruled that to the extent DWR could demonstrate that payment of refunds would result in DWR's costs exceeding its revenues remaining after payment of refunds, DWR could request FERC to reduce the refunds. DWR made a cost recovery filing that DWR believes demonstrates that its costs related to sales to the CAISO exceeded its revenues, a demonstration that, if approved by FERC, would eliminate any refund amount DWR might otherwise be required to pay. In January 2006, FERC deferred action on DWR's cost filing on the basis that

DWR, as described above, likely will be a net refund recipient, and net refund recipients, according to FERC, cannot make cost filings. Certain California parties have sought rehearing of that order.

In addition, in September 2005, the Ninth Circuit Court of Appeals ruled that FERC could not require governmental entities such as DWR to pay refunds.

Accordingly, although subject to uncertainty, DWR expects it will likely will be a net refund recipient in the FERC proceedings. Pending litigation could increase or decrease the level of the refunds DWR would be entitled to receive. DWR does not expect that FERC will order it to pay more in refunds than it receives on a market-wide basis.

Direct Access Proceeding: On February 28, 2008, the CPUC approved a decision concluding that the suspension of direct access cannot be lifted at the present time because DWR is still supplying power under the Act. However, the decision continued the proceeding to consider possible approaches to expediting DWR's exit from its role of supplying power under the Act. On November 21, 2008, the CPUC adopted a plan with the goal of the early exit of DWR from its role as supplier of power to retail electric customers. Under this plan, DWR's power purchase contracts would be replaced by agreements between the IOUs and DWR's power supplier counterparties that are not detrimental to ratepayers, through novation and/or negotiation. The decision sets a goal for the execution of replacement agreements for all of the Power Purchase Contracts by January 1, 2010. Although the CPUC decision sets a goal of January 1, 2010 for the removal of DWR from all of its power purchase contracts, that is not the target date for reopening direct access to bundled customers.

Provisions in 22 out of the 26 remaining DWR power purchase contracts would, if certain conditions are satisfied (including a minimum credit rating requirement for the IOU in some contracts), allow for DWR to novate the contract to a qualifying IOU. DWR's interest in and obligations under such a contract would be terminated upon such a novation. Four contracts currently lack such a provision, thus requiring negotiations with those counterparties before DWR's interest in and obligations under those contracts could be terminated prior to their scheduled termination. No assurance can be given that agreement could be reached with any of the counterparties to those four contracts or as to the timing of any such agreement

While the CPUC has set a goal of novating contracts as early as January 1, 2010, numerous conditions would need to be satisfied in order to complete the process. As such, timing and extent of future novation is uncertain. In the event of contract novation, management will reassess the impact on existing and future revenue requirements and consider modifying power charges accordingly. Management does not believe there will be a significant impact to the Fund's financial position in the event of novations of contracts.

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

Commitments
DWR has power purchase contracts that have remaining lives of up to seven years. Payments under these and gas purchase contracts approximated $0.9 billion and $1.3 billion for the three month period ended September 30, 2009 and 2008, respectively.

The remaining amounts of fixed obligations under the contracts as of September 30, 2009, are as follows (in millions):

For the Year Ending June 30,	Fixed Obligation (in millions)
2010	1,328
2011	1,463
2012	631
2013	61
2014	15
Thereafter	4
	$ 3,502

In addition to the fixed costs there are variable costs under several of the contracts. Management projected as of September 30, 2009 that the amount of future fixed and variable obligations associated with long-term power purchase contracts would approximate $6 billion. The difference between the fixed costs and the expected total costs of the contracts are primarily due to the variable factors associated with dispatchable contracts and the cost of natural gas.

7. Energy Settlements

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

Energy settlements in the three month period ended September 30, 2009 were $1 million as there were no large settlement actions. Future revenues under a number of settlements with larger suppliers including Mirant Corporation, Reliant Energy, Dynegy Inc, and Duke Energy Corporation, are subject to contingencies outlined in the underlying settlement and allocation agreements and will not be recognized until if and when the contingencies are resolved.

8. Related Party Transactions

The California State Teachers' Retirement System (STRS) and PERS, which are part of the California state government, participate in the Fund's letters of credit with three financial institutions. The total commitment for two letters of credit underlying the STRS' participation approximates $175 million and expires on November 30, 2010. The total commitment for the two letters of credit underlying the PERS' participation approximates $80 million and expires on April 15, 2011. There are no outstanding amounts on the letters of credit at September 30, 2009.