NORTHERN CALIFORNIA GAS AUTHORITY No. 1

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors of
Northern California Gas Authority No. 1
Sacramento, California

Report on the Financial Statements

We have audited the accompanying financial statements of Northern California Gas Authority No. 1 which comprise the Statements of Net Position as of December 31, 2015 and 2014, and the related Statements of Revenues, Expenses and Changes in Net Position, and Statements of Cash Flows for the years then ended and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control over financial reporting relevant to the Northern California Gas Authority No. 1'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 Northern California Gas Authority No. 1'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.

To the Board of Directors of
Northern California Gas Authority No. 1

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Northern California Gas Authority No. 1 at December 31, 2015 and 2014, and the changes in its financial position and its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America.

Other Matter

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis as listed in the table of contents be presented to supplement the financial statements. Such information, although not a part of the financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the 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 financial statements, and other knowledge we obtained during our audit of the 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.

Baker Tilly Virchow Krause, LLP

Madison, Wisconsin
February 19, 2016

NORTHERN CALIFORNIA GAS AUTHORITY No. 1
MANAGEMENT'S DISCUSSION AND ANALYSIS
(UNAUDITED)

Using this Financial Report

This annual financial report for Northern California Gas Authority No. 1 (Agency) consists of management's discussion and analysis and the financial statements, including notes to the financial statements. The basic Financial Statements consist of the Statements of Net Position, the Statements of Revenues, Expenses and Changes in Net Position and the Statements of Cash Flows.

The Agency's accounting records are maintained in accordance with Generally Accepted Accounting Principles for proprietary funds as prescribed by the Governmental Accounting Standards Board. The Agency's accounting records generally follow the Uniform System of Accounts for Public Licensees prescribed by the Federal Energy Regulatory Commission.

Overview of the Financial Statements

The following discussion and analysis of the financial performance of the Agency provides an overview of the financial activities for the years ended December 31, 2015 and 2014. This discussion and analysis should be read in conjunction with the Agency's financial statements and accompanying notes, which follow this section.

The Statements of Net Position provide information about the nature and amount of resources and obligations at a specific point in time.

The Statements of Revenues, Expenses and Changes in Net Position report all of the Agency's revenues and expenses during the periods indicated.

The Statements of Cash Flows report the cash provided and used by operating activities, as well as other cash sources such as investment income and debt financing, and other cash uses such as payments for debt service.

The Notes to Financial Statements provide additional detailed information to support the financial statements.

Nature of Operations

The Agency is a joint powers authority formed by the Sacramento Municipal Utility District (SMUD) and the Sacramento Municipal Utility District Financing Authority (SFA) in 2007. SFA is a joint powers agency formed between SMUD and the Modesto Irrigation District. The Agency was formed for the purpose of prepaying for a fixed quantity supply of natural gas to be delivered over a twenty-year period by Morgan Stanley Capital Group, Inc. (MSCG) under a Prepaid Gas Purchase and Sale Agreement (Prepaid Gas Supply) between the Agency and MSCG. The Agency then sells the natural gas to SMUD. The Agency issued bonds in May 2007, and commenced gas sales in June 2007.

SMUD purchases all of the natural gas delivered to the Agency pursuant to the Gas Supply Contract between SMUD and the Agency. The Agency has no staff and SMUD contributes to the Agency the actual costs of providing general and administrative services.

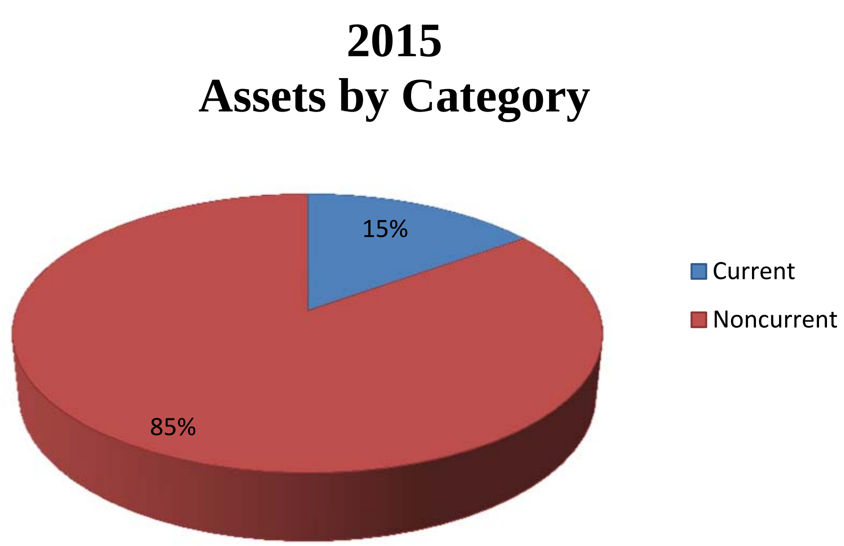
The Agency's Commission is comprised of SMUD's Board of Directors. The Agency is a separate legal entity; however, due to the extent of its operational and financial relationship with SMUD, it is included in the consolidated financial statements of SMUD.

FINANCIAL POSITION

Statements of Net Position Summary
(Dollars in thousands)

	December 31,			Change			
	2015	2014	2013	2015 vs. 2014		2014 vs. 2013	
Assets							
Current assets	$ 51,507	$ 43,479	$ 40,958	$ 8,028	18.5%	$ 2,521	6.2%
Noncurrent assets	289,108	316,997	342,009	(27,889)	-8.8%	(25,012)	-7.3%
Total assets	$ 340,615	$ 360,476	$ 382,967	$ (19,861)	-5.5%	$ (22,491)	-5.9%
Liabilities							
Long-term debt - net	$ 292,870	$ 318,795	$ 342,480	$ (25,925)	-8.1%	$ (23,685)	-6.9%
Current liabilities	33,524	27,297	26,219	6,227	22.8%	1,078	4.1%
Total liabilities	326,394	346,092	368,699	(19,698)	-5.7%	(22,607)	-6.1%
Net position							
Restricted	12,486	11,431	10,872	1,055	9.2%	559	5.1%
Unrestricted	1,735	2,953	3,396	(1,218)	-41.2%	(443)	-13.0%
Total net position	14,221	14,384	14,268	(163)	-1.1%	116	0.8%
Total liabilities and net position	$ 340,615	$ 360,476	$ 382,967	$ (19,861)	-5.5%	$ (22,491)	-5.9%

The following chart shows the breakdown of the Agency's assets by category:



2015 Compared to 2014

__ASSETS__

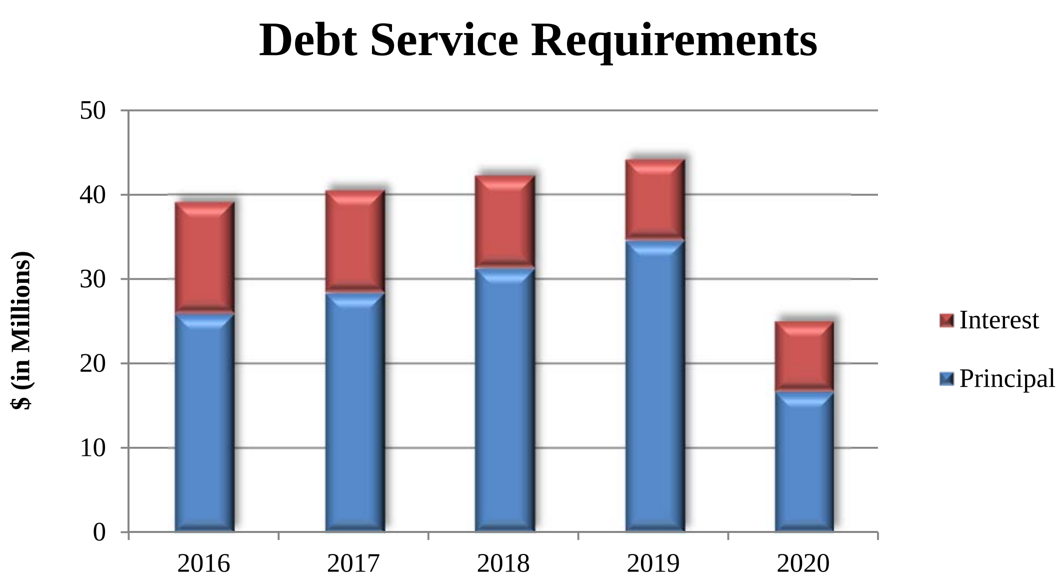
- Current Assets increased primarily due to higher restricted assets. The Agency's guaranteed investment contract with MSCG provides for MSCG to put up a collateral deposit if their credit ratings fall below agreed upon levels. At December 31, 2015, the Agency held a $4.2 million deposit from MSCG due to a credit rating downgrade. This increase is also due to a higher current portion of the amortization of the Prepaid Gas Supply.

- The Agency's main asset is its Prepaid Gas Supply, of which, the noncurrent portion was $287.8 million at December 31, 2015. Noncurrent Assets decreased due to the amortization of the Prepaid Gas Supply for gas delivered in 2015. The Prepaid Gas Supply (current and noncurrent portion) makes up about 93 percent of the Agency's assets at December 31, 2015.

__LIABILITIES & NET POSITION__

- Long-Term Debt – net decreased primarily due to $23.7 million of the scheduled principal payments for 2015. At December 31, 2015, the Agency had bonds outstanding of $318.8 million with maturities through 2027. At December 31, 2015, the 2007 Agency Bonds are rated "BBB+" by Standard & Poor's, "A" by Fitch and "A3" by Moody's. The Agency's bonds are tied to MSCG's credit rating.

  The following chart summarizes the debt service requirements of the Agency for the next five years:



- Current Liabilities increased due the credit support obligation to a collateral deposit from MSCG and a higher current portion of the Long-term debt due within one year.

2014 Compared to 2013

ASSETS

- Current Assets increased primarily due to a higher current portion of the amortization of the Prepaid Gas Supply.

- The Agency's main asset is its Prepaid Gas Supply, of which, the noncurrent portion was $315.6 million at December 31, 2014. Noncurrent Assets decreased due to the amortization of the Prepaid Gas Supply for gas delivered in 2014.

LIABILITIES & NET POSITION

- Long-Term Debt – net decreased primarily due to $22.4 million of the scheduled principal payments for 2014. At December 31, 2014, the Agency had bonds outstanding of $342.5 million with maturities through 2027.

RESULTS OF OPERATIONS

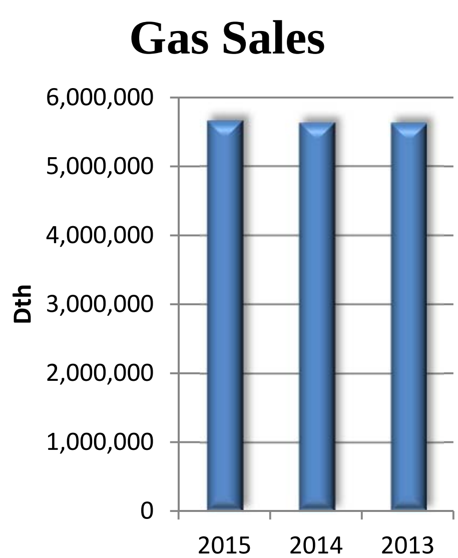
Summary of Revenues, Expenses and Changes in Net Position

(Dollars in thousands)

	December 31,			Change			
	2015	2014	2013	2015 vs. 2014		2014 vs. 2013	
Operating revenues	$ 38,871	$ 37,913	$ 37,913	$ 958	2.5%	$ -0-	0.0%
Operating expenses	(25,122)	(22,927)	(21,826)	(2,195)	-9.6%	(1,101)	-5.0%
Operating income	13,749	14,986	16,087	(1,237)	-8.3%	(1,101)	-6.8%
Interest and other income	649	621	610	28	4.5%	11	1.8%
Interest on debt	(13,965)	(14,901)	(15,767)	936	6.3%	866	5.5%
Change in net position before distributions and contributions	433	706	930	(273)	-38.7%	(224)	-24.1%
Distributions to Member	(698)	(672)	(672)	(26)	-3.9%	-0-	0.0%
Member contributions	102	82	75	20	24.4%	7	9.3%
Change in net position	(163)	116	333	(279)	-240.5%	(217)	-65.2%
Net position - beginning of year	14,384	14,268	13,935	116	0.8%	333	2.4%
Net position - end of year	$ 14,221	$ 14,384	$ 14,268	$ (163)	-1.1%	$ 116	0.8%

2015 Compared to 2014

The following chart shows gas sales in 2015, 2014, and 2013:



- Operating Revenue increased primarily due to higher swap revenues due to higher net swap price, partially offset by the lower gas sales to SMUD due to lower index prices.
- Operating Expense increased due to higher amortization of the Prepaid Gas Supply Contract.
- Interest expense decreased primarily due to lower bonds outstanding.
- Distributions to SMUD are based on interest earnings on the Debt Service fund not otherwise needed for another purpose, as specified in the indenture of trust. In 2015, the Agency distributed $0.7 million to SMUD.

2014 Compared to 2013

- Operating Expense increased due to higher amortization of the Prepaid Gas Supply Contract.

- Interest expense decreased primarily due to lower bonds outstanding.

NORTHERN CALIFORNIA GAS AUTHORITY No. 1
STATEMENTS OF NET POSITION

	December 31, 2015	December 31, 2014
ASSETS		
RESTRICTED ASSETS		
Debt service fund	$ 15,857,215	$ 15,042,358
Other restricted funds	4,228,144	-0-
Less current portion	(20,085,357)	(15,042,358)
Total restricted assets	2	-0-
CURRENT ASSETS		
Cash and cash equivalents:		
Restricted cash and cash equivalents	20,085,357	15,042,358
Receivables:		
Gas sales to Member	568,408	1,417,749
Accrued interest and other	2,965,312	2,006,067
Prepaid gas supply	27,767,785	24,892,581
Other prepayments	15,630	15,630
Regulatory costs to be recovered within one year	104,796	104,796
Total current assets	51,507,288	43,479,181
NONCURRENT ASSETS		
Prepaid gas supply	287,843,858	315,611,643
Regulatory costs for future recovery	1,100,363	1,205,160
Prepaid bond insurance costs	164,118	179,749
Total noncurrent assets	289,108,339	316,996,552
TOTAL ASSETS	$ 340,615,629	$ 360,475,733
LIABILITIES AND NET POSITION		
LONG-TERM DEBT - net	$ 292,870,000	$ 318,795,000
CURRENT LIABILITIES		
Accounts payable	2,648,605	2,892,573
Credit support for collateral obligation	4,228,142	-0-
Long-term debt due within one year	25,925,000	23,685,000
Accrued interest	722,419	718,973
Total current liabilities	33,524,166	27,296,546
TOTAL LIABILITIES	326,394,166	346,091,546
NET POSITION		
Restricted	12,486,193	11,430,812
Unrestricted	1,735,270	2,953,375
TOTAL NET POSITION	14,221,463	14,384,187
COMMITMENTS AND CONTINGENCIES (Notes 6 and 7)		
TOTAL LIABILITIES AND NET POSITION	$ 340,615,629	$ 360,475,733

NORTHERN CALIFORNIA GAS AUTHORITY No. 1
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION

	Years Ended December 31, 2015	Years Ended December 31, 2014
OPERATING REVENUES		
Gas sales to Member	$ 8,329,414	$ 18,653,774
Gas swap settlement, net	30,541,262	19,258,797
Total operating revenues	38,870,676	37,912,571
OPERATING EXPENSES		
Prepaid gas amortization	24,892,581	22,720,487
Administrative and general	124,174	101,948
Regulatory amounts collected in rates	104,797	104,796
Total operating expenses	25,121,552	22,927,231
OPERATING INCOME	13,749,124	14,985,340
NON-OPERATING REVENUES (EXPENSES)		
Interest and other income	648,776	620,874
Interest on debt	(13,965,137)	(14,900,717)
Total non-operating expenses	(13,316,361)	(14,279,843)
CHANGE IN NET POSITION BEFORE DISTRIBUTIONS AND CONTRIBUTIONS	432,763	705,497
Distributions to Member	(697,872)	(671,812)
Member contributions	102,385	82,183
CHANGE IN NET POSITION	(162,724)	115,868
NET POSITION - BEGINNING OF YEAR	14,384,187	14,268,319
NET POSITION - END OF YEAR	$ 14,221,463	$ 14,384,187

NORTHERN CALIFORNIA GAS AUTHORITY No. 1
STATEMENTS OF CASH FLOWS

	December 31, 2015		December 31, 2014	
CASH FLOWS FROM OPERATING ACTIVITIES				
Receipts from gas sales to Member	$	9,178,755	$	18,417,280
Receipts from others		29,582,156		19,477,537
Receipts for credit support collateral		4,228,142		-0-
Payments to vendors		(6,158)		(4,135)
Net cash provided by operating activities		42,982,895		37,890,682
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES				
Repayment of bonds		(23,685,000)		(22,380,000)
Interest payments on long-term debt		(14,205,659)		(15,127,986)
Distributions to Member		(697,872)		(671,812)
Net cash used in noncapital financing activities		(38,588,531)		(38,179,798)
CASH FLOWS FROM INVESTING ACTIVITIES				
Interest received		648,637		620,784
Net cash provided by investing activities		648,637		620,784
Net increase in cash and cash equivalents		5,043,001		331,668
Cash and cash equivalents - beginning of the fiscal year		15,042,358		14,710,690
Cash and cash equivalents - end of the year	$	20,085,359	$	15,042,358
CASH AND CASH EQUIVALENTS INCLUDED IN:				
Restricted cash and cash equivalents	$	20,085,359	$	15,042,358
Cash and cash equivalents - end of the year	$	20,085,359	$	15,042,358
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES				
Operating income	$	13,749,124	$	14,985,340
Adjustments to reconcile operating income to net cash provided by operating activities:				
Amortization of prepaid gas supply		24,892,581		22,720,487
Regulatory amortization		104,797		104,796
Receipts for credit support collateral		4,228,142		-0-
Amortization of prepaid bond insurance		15,631		15,630
Changes in operating assets and liabilities:				
Receivables		(109,765)		(17,754)
Payables and accruals		102,385		82,183
Net cash provided by operating activities	$	42,982,895	$	37,890,682
SUPPLEMENTAL DISCLOSURE OF NONCASH AND RELATED FINANCING ACTIVITIES				
Contributions from Member	$	102,385	$	82,183

NORTHERN CALIFORNIA GAS AUTHORITY No. 1
NOTES TO FINANCIAL STATEMENTS

NOTE 1. ORGANIZATION AND OPERATIONS

The Northern California Gas Authority No. 1 (Agency) is a Joint Powers Authority (JPA) formed by the Sacramento Municipal Utility District (SMUD) and the Sacramento Municipal Utility District Financing Authority (SFA) pursuant to the California Government Code (collectively, Members). SFA itself is a JPA formed by SMUD and the Modesto Irrigation District. The purpose of the Agency is to prepay for a supply of a fixed quantity of natural gas to be delivered over a twenty-year period (Gas Project) by Morgan Stanley Capital Group, Inc. (MSCG) under a Prepaid Gas Purchase and Sale Agreement (Prepaid Agreement) between the Agency and MSCG. The Prepaid Agreement terminates on May 31, 2027. MSCG is obligated to make payments to the Agency for any shortfall of gas not delivered or taken under the Prepaid Agreement for any reason, including force majeure.

The Agency has entered into a Gas Supply Contract (GSC) with SMUD that provides for the sale of all of the natural gas delivered to the Agency over the term of the Prepaid Agreement. SMUD is obligated to pay the Agency for the quantities of gas delivered under the GSC and to pay damages for gas that SMUD fails to take pursuant to the terms of the GSC. SMUD has no obligation to pay for gas that the Agency fails to deliver. The Agency anticipates that SMUD will be the only project participant with respect to the Gas Project during the term of the Prepaid Agreement. However, in the event of a default by SMUD under the GSC, the Agency has agreed to terminate the GSC and may enter into a replacement GSC with one or more municipal utilities on substantially the same terms as the GSC.

The Agency has no employees. The Gas Project is operated by SMUD’s staff. SMUD is obligated to contribute to the Agency the actual costs of providing administrative and general services. SMUD contributed $0.1 million in 2015 and also in 2014 for administrative and general services provided to the Agency by SMUD.

The JPA agreement will remain in effect until terminated by a supplemental written agreement of the parties; provided, that in no event shall the JPA agreement terminate while any contracts between the Agency and either of the parties or other parties are in effect, or while any bonds or notes of the Agency are outstanding. Gas Project revenues and the subsequent payments of principal and interest related to the Agency’s long-term debt are dependent upon the continued delivery of natural gas to the Gas Project under the Prepaid Agreement. Various termination events are specified in the Prepaid Agreement. Upon the occurrence of any such event, the Prepaid Agreement may be terminated by the Agency or MSCG. If the Prepaid Agreement is terminated, MSCG will be required to pay a scheduled termination payment to the Agency. Any termination of the Prepaid Agreement will result in the extraordinary mandatory redemption of the Agency’s long-term debt. Neither SFA nor SMUD has any obligation or liability to the Agency beyond that specifically provided for in the JPA agreement or the Gas Project agreement.

The Agency’s Commission is comprised of SMUD’s Board of Directors. The Agency is a separate legal entity; however, it is also included in the consolidated financial statements of SMUD as a component unit of SMUD’s financial reporting entity because of the extent of its operational and financial relationships with SMUD.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Method of Accounting. The accounting records of the Agency are maintained in accordance with Generally Accepted Accounting Principles for proprietary funds as prescribed by the Governmental Accounting Standards Board (GASB). The Agency’s accounting records generally follow the Uniform System of Accounts for Public Utilities and Licensees prescribed by the Federal Energy Regulatory Commission. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Natural gas sale revenues and purchase costs that are directly related to delivery of natural gas are reported as operating revenues and expenses. All other revenues and expenses are reported as non-operating revenues and expenses.

Use of Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America (U.S.) requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and revenues and expenses. Actual results could differ from those estimates.

Restricted Assets. The Agency's restricted assets are comprised of U.S. government securities and commercial paper which use is limited for specific purposes pursuant to the Indenture of Trust (Indenture) requirements. The Indenture specifies the flow of cash into the various Agency funds and dictates when they may become unrestricted.

Credit and Market Risk. The Agency entered into a guaranteed investment contract (see Note 3) in 2007 and is exposed to credit risk related to nonperformance by its investment provider. This contract requires the investment provider to post collateral if their credit ratings fall below agreed upon levels. At December 31, 2015, the Agency held $4.2 million on deposit by the investment provider. The amount is recorded as current restricted asset with an associated current liability.

Cash and Cash Equivalents. Cash and cash equivalents include all debt instruments purchased with an original maturity of 90 days or less and all investments in money market mutual funds. The debt instruments and money market funds are reported at amortized cost which approximates fair value.

Receivable from Member. The Agency records as a Receivable from Member the amounts due from SMUD for the purchase of natural gas from the Gas Project.

Prepaid Gas Supply. The Agency has prepaid for delivery of a natural gas supply with the proceeds from revenue bonds. The Agency provides for amortization on the historical cost of the Prepaid Gas Supply on a net present value (NPV) basis in which the change in the NPV of the Prepaid Agreement for the remaining term of its contract life from the beginning of the period to the end of the period is the amortization charged for the period. When the Agency amortizes its Prepaid Gas Supply, the amortization is recorded against the current portion of Prepaid Gas Supply.

Regulatory Deferrals. As a regulated entity, the Agency's financial statements are prepared in accordance with GASB Statement No. 62, ***"Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements"***, which require that the effects of the rate making process be recorded in the financial statements. Accordingly, certain expenses and credits normally reflected in the Change in Net Position as incurred, are recognized when included in rates and recovered from, or refunded to, SMUD through the PPA agreement. The Agency records regulatory assets and credits to reflect rate-making actions of the Commission. The account includes the unamortized debt issuance costs of previously issued bonds of the Agency. The regulatory asset is amortized using the straight line method over the remaining life of the associated bonds and recorded in Regulatory Amounts Collected in Rates in the Statements of Revenues, Expenses and Changes in Net Position.

Prepaid Bond Insurance Costs. The Agency recorded a prepaid asset for the prepaid bond insurance portion of unamortized debt issuance costs of previously issued bonds of the Agency. The prepaid bond insurance costs will be amortized using the straight line method over the remaining life of the associated bonds and recorded in Administrative and General in the Statements of Revenues, Expenses and Changes in Net Position.

Derivative Financial Instruments. The Agency enters into derivative financial instruments (interest rate swap and natural gas commodity price swap agreements) to manage its exposure to interest rate risk and market volatility of natural gas commodity prices. The Agency does not enter into these agreements for trading purposes. Due to the termination provisions of these agreements, they have no fair value, and therefore, there is no mark-to-market and the Agency does not record these derivative financial instruments on its Statement of Net Position. The Agency is exposed to the risk of early termination of the Prepaid Agreement if the counterparties default or if the swap agreements are terminated.

Interest Rate Swap Agreements. The Agency enters into interest rate swap agreements to modify the effective interest rates on outstanding debt. Interest expense is reported net of the swap payments received or paid as a component of Interest on Debt in the Statement of Revenues, Expenses and Changes in Net Position.

Natural Gas Commodity Price Swap Agreement. The Agency uses a forward contract to hedge the impact of market volatility on natural gas commodity prices on its natural gas sales to SMUD. Net swap payments received or paid are reported as a component of Operating Revenues in the Statement of Revenues, Expenses and Changes in Net Position.

Net Position. The Agency classifies its Net Position into two components as follows:

- Restricted – This component of net position consists of assets with constraints placed on their use, either externally or internally. Constraints include those imposed by debt indentures (excluding amounts considered in net capital), grants or laws and regulations of other governments, by law through constitutional provisions or enabling legislation, or by the Board. These restricted assets are reduced by liabilities and deferred inflows of resources related to those assets.
- Unrestricted – This component of net position consists of net amount of the assets, deferred outflows of resources, liabilities, and deferred inflows of resources that do not meet the definition of "Restricted."

Gas Sales to Member. Gas sales to Member are recorded as revenues when the natural gas is delivered.

Operating Expenses. Operating expenses include the cost of sales and services, administrative expenses and amortization on Prepaid Gas Supply assets and Regulatory Costs for Future Recovery and are recorded when incurred.

Distributions to Member. Amounts paid to SMUD from surplus funds are recorded as Distributions to Member.

Member Contributions. Amounts contributed by SMUD for the actual costs of providing administrative and general services are recorded as Member Contributions.

Subsequent Events. Subsequent events for the Agency have been evaluated through February 19, 2016, which is the date that the financial statements were available to be issued.

Recent Accounting Pronouncements. In February 2015, GASB issued Statement of Governmental Accounting Standards (SGAS) No. 72, ***"Fair Value Measurement and Application"*** (GASB No. 72). GASB No. 72 addresses accounting and financial reporting issues related to fair value measurements. This statement requires investments to be measured at fair value, which is described as an exit price. This statement requires valuation techniques that are appropriate in the circumstances and for which sufficient data are available to be used to measure fair value. The valuation techniques should be consistent with one or more of the following approaches: the market approach, the cost approach, or the income approach. This statement establishes a hierarchy of inputs to the valuation techniques used to measure fair value. The hierarchy has three levels. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are inputs, other than quoted prices, included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 3 inputs are unobservable inputs, such as management assumptions. A fair value takes into account the highest and best use for a nonfinancial asset. This statement requires disclosures to be made about fair value measurements, the level of fair value hierarchy, and valuation techniques. GASB No. 72 is effective for the Agency in 2016. The Agency is currently assessing the financial statement impact of adopting this statement, but does not believe that its impact will be material.

In June 2015, GASB issued SGAS No. 76, ***"The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments"*** (GASB No. 76). GASB No. 76 established the hierarchy of GAAP for state and local governments. This statement supersedes SGAS No. 55, ***"The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments"***. The GAAP hierarchy sets forth what constitutes GAAP for all state and local governmental entities. It establishes the order of priority of pronouncements and other sources of accounting and financial reporting guidance that a governmental entity should apply. Category A is comprised of GASB statements. Category B includes GASB Technical Bulletins, GASB Implementation Guides, and literature of the AICPA cleared by the GASB. GASB No. 76 is effective for the Agency in 2016. The Agency is currently assessing the financial statement impact of adopting this statement, but does not believe that its impact will be material.

NOTE 3. CASH, CASH EQUIVALENTS, AND INVESTMENTS

Cash Equivalents and Investments. The Agency's investments are governed by the California Government and Public Utilities Codes and its Indenture, which allow Agency investments to include: obligations which are unconditionally guaranteed by the U.S. Government or its agencies or instrumentalities; direct and general obligations of any state in the U.S. rated in the top two rating agency categories; certificates of deposit; repurchase and reverse repurchase agreements; bankers' acceptances; prime commercial paper; mortgage backed bonds and collateralized mortgage obligations; investment agreements; California State Local Agency Investment Fund; taxable government and tax-exempt money market portfolios; and other short-term investments rated at least P-1 or A-1 by Moody's and Standard & Poor's, respectively. The California Government Code also includes restrictions for investments relating to maximum amounts invested as a percentage of total portfolio and with a single issuer, maximum maturities, and minimum credit ratings.

Credit Risk. This is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. To mitigate the risk, the Agency limits investments to those rated, at a minimum, "A-1" or equivalent for short-term notes by a nationally recognized rating agency.

Custodial Credit Risk. This is the risk that in the event of the failure of a depository financial institution or counterparty to a transaction, the Agency's deposits may not be returned or the Agency will not be able to recover the value of its deposits, investments or securities that are in the possession of another party. The Agency does not have a deposit policy for custodial credit risk. At December 31, 2015 and 2014, the Agency had money market mutual funds of $7.8 million and $3.8 million which were uninsured, respectively. At December 31, 2015, $3.6 million of the money market mutual funds are held in trust for the benefit of the Agency and $4.2 million represents amounts held by the Agency as a collateral deposit by an investment provider.

Concentration of Credit Risk. This is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. The Agency places no limit on the amounts invested in any one issuer for federal agency securities. To limit the Agency's credit risk for commercial paper purchased under the Debt Service Fund Agreement, the aggregate maturity amount invested in any combination of one issuer, affiliate of issuer, or backed by any one credit support, cannot exceed $30 million. The following are the concentrations of risk greater than five percent in either year:

	December 31,	
Investment Type:	2015	2014
Commercial paper - Chesham Finance	100%	100%

Interest Rate Risk. This is the risk that investments are exposed to fair value losses arising from the increasing interest rates. Though the Agency has restrictions as to the maturities of some of the investments, it does not have a formal policy for interest rate risk. At December 31, 2015 and 2014, all of the Agency's investments had maturities of one year or less.

Debt Service Fund Agreement. The Agency has entered into a synthetic guaranteed investment contract, in the form of a forward supply agreement, in which it has agreed to purchase securities with the debt service deposit amounts for a guaranteed fixed rate of return of 5.148 percent. The agreement terminates on June 30, 2027.

The following schedules present credit risk by type of security held at December 31, 2015 and 2014. The credit ratings listed are from Standard & Poor's.

The Agency's cash and cash equivalents consist of the following:

	Credit Rating	December 31, 2015	December 31, 2014
Cash and Cash Equivalents:			
Money market mutual funds	Not Rated/AAAm	$ 7,771,383	$ 3,775,250
Commercial paper - Chesham Finance	A-1	12,313,976	11,267,108
Total cash and cash equivalents		$ 20,085,359	$ 15,042,358

The Agency's cash and cash equivalents are classified in the Statements of Net Position as follows:

	December 31, 2015	December 31, 2014
Total Cash and Cash Equivalents:		
Debt service fund	$ 15,857,215	$ 15,042,358
Other restricted funds:		
Collateral for credit support	4,228,142	-0-
Revenue Fund	2	-0-
Total other restricted funds	4,228,144	-0-
Total cash and cash equivalents	$ 20,085,359	$ 15,042,358

NOTE 4. PREPAID GAS SUPPLY

The Agency's prepaid gas supply is presented below:

	December 31, 2015	December 31, 2014
Prepaid gas supply	$ 313,190,414	$ 337,829,350
Prepaid gas supply revenue	2,421,229	2,674,874
Total prepaid gas supply	315,611,643	340,504,224
Less: amounts due within one year	(27,767,785)	(24,892,581)
Total prepaid gas supply - noncurrent portion	$ 287,843,858	$ 315,611,643

The following summarizes prepaid gas supply activity for the year ended December 31, 2015:

	December 31, 2014	Terminations	Amortization	December 31, 2015
Prepaid gas supply	$ 337,829,350	$ -0-	$ (24,638,936)	$ 313,190,414
Prepaid gas supply revenue	2,674,874	-0-	(253,645)	2,421,229
Total prepaid gas supply	$ 340,504,224	$ -0-	$ (24,892,581)	$ 315,611,643

The following summarizes prepaid gas supply activity for the year ended December 31, 2014:

	December 31, 2013	Terminations	Amortization	December 31, 2014
Prepaid gas supply	$ 360,310,836	$ -0-	$ (22,481,486)	$ 337,829,350
Prepaid gas supply revenue	2,913,875	-0-	(239,001)	2,674,874
Total prepaid gas supply	$ 363,224,711	$ -0-	$ (22,720,487)	$ 340,504,224

The prepaid gas supply is the discounted NPV of the fixed monthly natural gas prices per million British Thermal Units (mmbtu) as specified in, and over the remaining term of, the Prepaid Agreement. The prepaid gas supply revenue is the discounted NPV of $0.07 per mmbtu over the remaining term of the Prepaid Agreement.

NOTE 5. LONG-TERM DEBT

The Agency issued $668.5 million of 2007 Series B Gas project revenue bonds in May 2007 (Bonds) with variable interest rates, maturing July 2027.

The Agency's long-term debt is presented below:

	December 31, 2015	December 31, 2014
2007 Series B Gas project revenue bonds, variable rates, 2016-2027	$ 318,795,000	$ 342,480,000
Less: amounts due within one year	(25,925,000)	(23,685,000)
Total long-term debt - net	$ 292,870,000	$ 318,795,000

The following summarizes long-term debt activity for the year ended December 31, 2015:

	December 31, 2014	Extinguishments	Payments/ Amortizations	December 31, 2015
2007 Gas project revenue bonds	$ 342,480,000	$ -0-	$ (23,685,000)	$ 318,795,000
Total long-term debt	$ 342,480,000	$ -0-	$ (23,685,000)	$ 318,795,000

The following summarizes long-term debt activity for the year ended December 31, 2014:

	December 31, 2013	Extinguishments	Payments/ Amortizations	December 31, 2014
2007 Gas project revenue bonds	$ 364,860,000	$ -0-	$ (22,380,000)	$ 342,480,000
Total long-term debt	$ 364,860,000	$ -0-	$ (22,380,000)	$ 342,480,000

The annual debt service requirements to maturity for the Bonds are as follows at December 31, 2015:

Year	Principal	Interest	Total
2016	$ 25,925,000	$ 13,220,830	$ 39,145,830
2017	28,395,000	12,142,674	40,537,674
2018	31,305,000	10,953,300	42,258,300
2019	34,560,000	9,622,299	44,182,299
2020	16,675,000	8,368,752	25,043,752
2021-2025 (combined)	115,690,000	29,010,789	144,700,789
2026-2027 (combined)	66,245,000	3,637,257	69,882,257
Total	$ 318,795,000	$ 86,955,901	$ 405,750,901

Interest includes interest requirements for fixed rate debt at their stated rates and variable rate debt covered by interest rate swaps at their fixed swap rate.

The Agency had pledged future net revenues to repay $318.8 million and $342.5 million at December 31, 2015 and 2014, respectively, for Bonds issued in May 2007. Proceeds from the Bonds were used to purchase the Gas Project from MSCG at a price of $754.1 million with the remaining amounts used to fund the appropriate accounts for the Agency. The Bonds, payable through 2027, are secured solely by a pledge of and lien on the trust estate under the Indenture which includes bond proceeds, rights under the GSC, revenues, any termination payment and any investment income. Annual principal and interest payments on the Bonds are expected to require approximately 100 percent of the Agency's net revenues. The total principal and interest remaining to be paid on the Bonds was $405.8 million and $443.6 million at December 31, 2015 and 2014, respectively. Debt service payments on the Bonds are made quarterly on January 1, April 1, July 1 and October 1. Principal and interest paid was $37.9 million and $37.5 million for 2015 and 2014, respectively. Total net revenues were $39.5 million and $38.5 million for 2015 and 2014, respectively.

The ability of the Agency to pay related principal and interest payments associated with the Bonds is contingent upon the continued successful operation of the Gas Project. If the Prepaid Agreement were to terminate, a termination payment would be received into the trust estate from MSCG. The amount of the termination payment, together with the amounts required to be on deposit in certain funds and accounts held by the trustee, has been calculated to provide a sum sufficient to pay the redemption price of the Bonds upon early termination of the Prepaid Agreement. The amount of termination payment declines over time as MSCG performs its gas delivery obligations under the Prepaid Agreement. Agency Members are not obligated to pay debt service costs if the Gas Project is unable to operate pursuant to the Prepaid Agreement or if revenues generated by the Gas Project are insufficient to meet debt service obligations.

Interest Rate Swap Agreements – 2007 Series B Bonds. A summary of the Agency's three swap agreements are as follows:

Notional Amount	Agency Pays	Fixed Rate	Floating Rate	Termination Date	Credit Support Provider Credit Rating (S&P)
$ 54,320,000	Fixed	4.062%	67% of LIBOR +.60%	07/01/17	BBB+
$ 65,865,000	Fixed	4.144%	67% of LIBOR +.63%	07/01/19	BBB+
$ 198,610,000	Fixed	4.304%	67% of LIBOR +.72%	07/01/27	BBB+

At December 31, 2015, the Agency had three variable-to-fixed interest rate swap agreements with a counterparty. The Agency pays the counterparty a fixed rate on the notional amount and receives a floating rate equal to 67 percent of the three month London Interbank Offered Rates (LIBOR) (.61percent at December 31, 2015) plus an interest rate spread, as specified in each swap agreement. The total notional amounts of the three swaps at December 31, 2015 was $318.8 million and was equivalent to the outstanding principal balance on the Agency's Bonds. The swaps are amortized over the life of their respective swap agreements in a manner corresponding to the principal repayment schedule of the Bonds. Early termination of the swaps would occur upon termination of the Prepaid Agreement for any reason. Upon early termination, the swaps would have no value to either party.

Variable Rate 2007 Series B Bonds. The Agency's variable rate Bonds bear interest at quarterly rates, ranging from 1.01 percent to 1.13 percent at December 31, 2015.

NOTE 6. COMMITMENTS

Natural Gas Commodity Price Swap Agreement. The Agency has entered into a floating-to-fixed natural gas commodity price swap agreement (Gas Swap Agreement) with a counterparty for the purpose of fixing the variable price on the Agency's natural gas sales to SMUD under the GSC. The Agency pays an index-based natural gas price over the twenty-year period and receives a fixed natural gas price as specified in the Gas Swap Agreement, for notional quantities of natural gas at a pricing point corresponding to the daily contract quantity and the delivery point under the Prepaid Agreement. The Gas Swap Agreement terminates on May 31, 2027. The total notional amount of the Gas Swap Agreement remaining at December 31, 2015 was 45.1 million mmbtu. Presently, the Gas Swap Agreement is 15,585 mmbtu per calendar day, and this amount will change on June 1 of each remaining year of the Gas Swap Agreement and will range from 8,673 to 15,992 mmbtu per calendar day. Early termination of the Gas Swap Agreement would occur upon termination of the Prepaid Agreement for any reason whatsoever. Upon early termination, the Gas Swap Agreement would have no value to either party.

NOTE 7. CONTINGENCIES

General Contingencies. The Agency's ability to make principal and interest payments on its Bonds is contingent upon the continued delivery of natural gas to the Gas Project under the Prepaid Agreement. The Members are not obligated to make principal and interest debt service payments in the event the Gas Project does not operate and there are insufficient funds to pay the bondholders. The Agency expects that the natural gas will continue to be delivered as planned.

In the normal operation of business, the Agency is party to various claims, legal actions and complaints. Management and the Agency's legal counsel believe that there are no material loss contingencies that would have a material adverse impact on the financial position of the Agency.