

**PRELIMINARY OFFICIAL STATEMENT DATED \_\_\_\_\_, 2019****NEW ISSUE—BOOK-ENTRY ONLY****RATINGS: Moody's: \_\_\_\_\_****S&P: \_\_\_\_\_****Fitch: \_\_\_\_\_****See "RATINGS" herein**

*In the opinion of Jones Hall, A Professional Law Corporation, San Francisco, California, Bond Counsel, subject, however to certain qualifications described herein, under existing law, the interest on the Series 2019A-1 Bonds and the Series 2019C Bonds is excluded from gross income for federal income tax purposes and such interest is not an item of tax preference for purposes of the federal alternative minimum tax. In the further opinion of Bond Counsel, interest on the Bonds is exempt from California personal income taxes. See "TAX MATTERS" herein.*

**CITY OF SAN JOSE**

\$ \_\_\_\_\_ \*  
**GENERAL OBLIGATION BONDS, SERIES 2019A-1**  
**(DISASTER PREPAREDNESS, PUBLIC SAFETY, AND**  
**INFRASTRUCTURE)**

\$ \_\_\_\_\_ \*  
**TAXABLE GENERAL OBLIGATION BONDS, SERIES 2019A-2**  
**(DISASTER PREPAREDNESS, PUBLIC SAFETY, AND**  
**INFRASTRUCTURE)**

\$ \_\_\_\_\_ \*  
**TAXABLE GENERAL OBLIGATION BONDS, SERIES 2019B**  
**(DISASTER PREPAREDNESS, PUBLIC SAFETY, AND INFRASTRUCTURE)**

\$ \_\_\_\_\_ \*  
**GENERAL OBLIGATION BONDS, SERIES 2019C**  
**(REFUNDING, LIBRARIES, PARKS, AND PUBLIC SAFETY**  
**PROJECTS)**

\$ \_\_\_\_\_ \*  
**TAXABLE GENERAL OBLIGATION BONDS, SERIES 2019D**  
**(REFUNDING, LIBRARIES, PARKS, AND PUBLIC SAFETY**  
**PROJECTS)**

**Dated: Date of Delivery****Due: September 1, as shown on the inside front cover**

**Issuances.** The City of San José (the "City") is issuing the bonds captioned above (collectively, the "Bonds") to finance projects authorized under certain voter authorizations of the City and to refund all of the City's outstanding general obligation bonds, among other items, as described in this Official Statement.

**Security.** The Bonds are general obligations of the City payable from ad valorem taxes, and the City Council is empowered and is obligated to levy ad valorem taxes for the payment of interest on, and principal of, the Bonds upon all property subject to taxation by the City without limitation of rate or amount (except certain personal property which is taxable at limited rates). The City will direct the County of Santa Clara (the "County") to collect such ad valorem taxes in such amounts and at such times as is necessary to ensure the timely payment of debt service on the Bonds.

**Book-Entry Only.** The Bonds will be issued in book-entry form only, and will be initially issued and registered in the name of Cede & Co. as nominee of The Depository Trust Company, New York, New York (collectively referred to herein as "DTC"). Purchasers of the Bonds (the "Beneficial Owners") will not receive physical certificates representing their interest in the Bonds. The Bonds are issuable as fully registered securities in denominations of \$5,000 or any integral multiple thereof.

**Payments.** Interest on the Bonds will be payable on March 1, 2020 and semiannually thereafter on March 1 and September 1 of each year. Payments of principal of and interest on the Bonds will be paid by Wilmington Trust, N.A., as Fiscal Agent, to DTC for subsequent disbursement to DTC Participants which will remit such payments to the Beneficial Owners of the Bonds. See "THE BONDS — Book-Entry-Only System."

**Redemption.** The Bonds, other than the Taxable Series 2019A-2 Bonds, are subject to optional and mandatory redemption prior to maturity as described herein. The Taxable Series 2019A-2 Bonds are not subject to optional or mandatory redemption prior to maturity. See "THE BONDS — Optional Redemption" and "Mandatory Sinking Fund Redemption."

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**Maturity Schedules**  
 (See inside cover)

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**Cover Page.** This cover page contains certain information for general reference only. It is not a summary of all the provisions of the Bonds. Prospective investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision.

*The Bonds will be sold and awarded pursuant to a competitive bidding process to be held on [July 9], 2019, as set forth in the Official Notice Inviting Bids. The Bonds will be offered, when, as and if issued and accepted by the Purchasers, subject to the approval of Jones Hall, A Professional Law Corporation, San Francisco, California, Bond Counsel to the City. Jones Hall, A Professional Law Corporation, is also serving as Disclosure Counsel to the City. In addition, certain legal matters will be passed upon for the City by the City Attorney. It is anticipated that the Bonds will be available for delivery through the facilities of DTC on or about July 25, 2019.*

The date of this Official Statement is \_\_\_\_\_, 2019.

\* Preliminary; subject to change.

**DRAFT--Contact the Office of the City Clerk at (408) 535-1260 or CityClerk@sanjoseca.gov for final document.**

This Preliminary Official Statement and the information contained herein are subject to completion or amendment. These securities may not be sold nor may offers to buy be accepted prior to the time the Official Statement is delivered in final form. Under no circumstances will this Preliminary Official Statement constitute an offer to sell or a solicitation of an offer to buy nor will there be any sale of these securities in any jurisdiction in which such offer solicitation or sale would be unlawful.



## MATURITY SCHEDULES\*

CUSIP<sup>†</sup>  
(Base \_\_\_\_\_)

\$ \_\_\_\_\_

CITY OF SAN JOSE

### GENERAL OBLIGATION BONDS, SERIES 2019A-1 (DISASTER PREPAREDNESS, PUBLIC SAFETY, AND INFRASTRUCTURE)

<u>Maturity Date (September 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>Price</u>	<u>CUSIP<sup>†</sup></u>
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\$ \_\_\_\_\_ % Term Bonds due September 1, 20\_\_; \_\_%; CUSIP<sup>†</sup>: \_\_\_\_\_

\$ \_\_\_\_\_

CITY OF SAN JOSE

### TAXABLE GENERAL OBLIGATION BONDS, SERIES 2019A-2 (DISASTER PREPAREDNESS, PUBLIC SAFETY, AND INFRASTRUCTURE)

<u>Maturity Date</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>Price</u>	<u>CUSIP<sup>†</sup></u>
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\* Preliminary; subject to change.

<sup>†</sup> CUSIP Copyright 2019, CUSIP Global Services, and a registered trademark of American Bankers Association. CUSIP data herein is provided by CUSIP Global Services, which is managed on behalf of American Bankers Association by S&P Capital IQ. Neither the City nor the Purchasers take any responsibility for the accuracy of the CUSIP data.



**MATURITY SCHEDULES\***

(CONTINUED)

CUSIP<sup>†</sup>

(Base \_\_\_\_\_)

\$ \_\_\_\_\_

**CITY OF SAN JOSE**

**TAXABLE GENERAL OBLIGATION BONDS, SERIES 2019B**

**(DISASTER PREPAREDNESS, PUBLIC SAFETY, AND INFRASTRUCTURE)**

<u>Maturity Date</u> <u>(September 1)</u>	<u>Principal</u> <u>Amount</u>	<u>Interest</u> <u>Rate</u>	<u>Yield</u>	<u>Price</u>	<u>CUSIP<sup>†</sup></u>
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\$ \_\_\_\_\_ % Term Bonds due September 1, 20\_\_; \_\_%; CUSIP<sup>†</sup>: \_\_\_\_\_

\$ \_\_\_\_\_

**CITY OF SAN JOSE**

**GENERAL OBLIGATION BONDS, SERIES 2019C**

**(REFUNDING, LIBRARIES, PARKS, AND PUBLIC SAFETY PROJECTS)**

<u>Maturity Date</u> <u>(September 1)</u>	<u>Principal</u> <u>Amount</u>	<u>Interest</u> <u>Rate</u>	<u>Yield</u>	<u>Price</u>	<u>CUSIP<sup>†</sup></u>
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\$ \_\_\_\_\_ % Term Bonds due September 1, 20\_\_; \_\_%; CUSIP<sup>†</sup>: \_\_\_\_\_

\* Preliminary; subject to change.

<sup>†</sup> CUSIP Copyright 2019, CUSIP Global Services, and a registered trademark of American Bankers Association. CUSIP data herein is provided by CUSIP Global Services, which is managed on behalf of American Bankers Association by S&P Capital IQ. Neither the City nor the Purchasers take any responsibility for the accuracy of the CUSIP data.



**MATURITY SCHEDULES\***

(CONTINUED)

CUSIP†

(Base \_\_\_\_\_)

\$ \_\_\_\_\_

**CITY OF SAN JOSE**

**TAXABLE GENERAL OBLIGATION BONDS, SERIES 2019D**

**(REFUNDING, LIBRARIES, PARKS, AND PUBLIC SAFETY PROJECTS)**

<u>Maturity Date</u> <u>(September 1)</u>	<u>Principal</u> <u>Amount</u>	<u>Interest</u> <u>Rate</u>	<u>Yield</u>	<u>Price</u>	<u>CUSIP†</u>
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\$ \_\_\_\_\_ % Term Bonds due September 1, 20\_\_; \_\_%; CUSIP†: \_\_\_\_\_

\* Preliminary; subject to change.

† CUSIP Copyright 2019, CUSIP Global Services, and a registered trademark of American Bankers Association. CUSIP data herein is provided by CUSIP Global Services, which is managed on behalf of American Bankers Association by S&P Capital IQ. Neither the City nor the Purchasers take any responsibility for the accuracy of the CUSIP data.



## GENERAL INFORMATION ABOUT THIS OFFICIAL STATEMENT

**No Offering May Be Made Except by this Official Statement.** No dealer, broker, salesperson or other person has been authorized by the City to give any information or to make any representations with respect to the Bonds other than as contained in this Official Statement, and, if given or made, such other information or representation must not be relied upon as having been given or authorized by the City or the Purchasers.

**Use of this Official Statement.** This Official Statement is submitted in connection with the issuance and sale of the Bonds described in this Official Statement and may not be reproduced or used, in whole or in part, for any other purpose. This Official Statement does not constitute a contract between any owner of the Bonds and the City or the Purchasers.

**Preparation of this Official Statement.** The information contained in this Official Statement has been obtained from sources that are believed to be reliable, but this information is not guaranteed as to accuracy or completeness. The City anticipates that the Purchasers will provide the following sentence for inclusion in this Official Statement: The Purchasers have reviewed the information in this Official Statement in accordance with, and as part of, their responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Purchasers do not guarantee the accuracy or completeness of such information.

**Estimates and Forecasts.** When used in this Official Statement and in any continuing disclosure made by the City, the words or phrases “will likely result,” “are expected to,” “will continue,” “is anticipated,” “estimate,” “project,” “forecast,” “expect,” “intend” and similar expressions identify “forward looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements. Any forecast is subject to such uncertainties. Inevitably, some assumptions used to develop the forecasts will not be realized and unanticipated events and circumstances may occur. Therefore, there are likely to be differences between forecasts and actual results, and those differences may be material.

This Official Statement speaks only as of its date, and the information and expressions of opinion contained in this Official Statement are subject to change without notice. Neither the delivery of this Official Statement nor any sale of the Bonds will, under any circumstances, create any implication that there has been no change in the affairs of the City or the other parties described in this Official Statement, since the date of this Official Statement.

**Document Summaries.** All summaries of the Fiscal Agent Agreement and the other documents contained in this Official Statement are made subject to the provisions of such documents and do not purport to be complete statements of any or all such provisions. All references in this Official Statement to the Fiscal Agent Agreement and such other documents are qualified in their entirety by reference to such documents, which are on file with the City. Copies of documents referred to herein are available from the Finance Department—Debt Management, City of San José City Hall, 200 East Santa Clara Street, San José, CA 95113; Phone (408) 535-7010; or by e-mail at [debt.management@sanjoseca.gov](mailto:debt.management@sanjoseca.gov). The City may impose a charge for copying, mailing and handling.

**No Unlawful Offers or Solicitations.** This Official Statement does not constitute an offer to sell or a solicitation of an offer to buy in any jurisdiction in which such offer or solicitation is not authorized or in which the person making such offer or solicitation is not qualified to do so or to any person to whom it is unlawful to make such offer or solicitation.

**No Registration or Qualification.** The issuance and sale of the Bonds have not been registered under the Securities Act of 1933 or the Securities Exchange Act of 1934, both as amended, and the Fiscal Agent Agreement has not been qualified under the Trust Indenture Act of 1939, as amended, in reliance upon exemptions provided thereunder, for the issuance and sale of municipal securities.

**Public Offering Prices.** The Purchasers may offer and sell the Bonds to certain dealers and dealer banks and banks acting as agent at prices lower than the public offering prices stated on the cover page of this Official Statement, and the Purchasers may change those public offering prices from time to time.

**Internet Web Site.** The City maintains an internet website. However, the information presented on such website is not part of this Official Statement and should not be relied upon in making an investment decision with respect to the Bonds.



# **CITY OF SAN JOSE, CALIFORNIA**

## **CITY COUNCIL**

Sam Liccardo, Mayor

District 1: Charles "Chappie" Jones, Vice Mayor/Member	District 6: Devora "Dev" Davis, Member
District 2: Sergio Jimenez, Member	District 7: Maya Esparza, Member
District 3: Raul Peralez Member	District 8: Sylvia Arenas, Member
District 4: Lan Diep, Member	District 9: Pam Foley, Member
District 5: Magdalena Carrasco, Member	District 10: Johnny Khamis, Member

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## **CITY OFFICIALS**

David Sykes, City Manager  
Richard Doyle, City Attorney  
Toni Taber, City Clerk  
Julia H. Cooper, Director of Finance

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## **PROFESSIONAL SERVICES**

### **BOND AND DISCLOSURE COUNSEL**

Jones Hall, A Professional Law Corporation  
San Francisco, California

### **MUNICIPAL ADVISOR**

Public Resources Advisory Group  
Oakland, California

### **FISCAL AGENT**

Wilmington Trust, N.A.  
Costa Mesa, California

### **VERIFICATION AND BIDDING AGENT**

Causey Demgen & Moore P.C.  
Denver, Colorado







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JUNE 30, 2018

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APPENDIX F - DTC AND BOOK-ENTRY-ONLY SYSTEM



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## OFFICIAL STATEMENT

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### CITY OF SAN JOSE

\$ _____ *	\$ _____ *
GENERAL OBLIGATION BONDS, SERIES 2019A-1 (DISASTER PREPAREDNESS, PUBLIC SAFETY, AND INFRASTRUCTURE)	TAXABLE GENERAL OBLIGATION BONDS, SERIES 2019A-2 (DISASTER PREPAREDNESS, PUBLIC SAFETY, AND INFRASTRUCTURE)
\$ _____ *	
TAXABLE GENERAL OBLIGATION BONDS, SERIES 2019B (DISASTER PREPAREDNESS, PUBLIC SAFETY, AND INFRASTRUCTURE)	
\$ _____ *	\$ _____ *
GENERAL OBLIGATION BONDS, SERIES 2019C (REFUNDING, LIBRARIES, PARKS, AND PUBLIC SAFETY PROJECTS)	TAXABLE GENERAL OBLIGATION BONDS, SERIES 2019D (REFUNDING, LIBRARIES, PARKS, AND PUBLIC SAFETY PROJECTS)

The purpose of this Official Statement, which includes the cover page, inside cover page and attached appendices, is to set forth certain information concerning the sale and delivery of by the City of San José (the “**City**”) of its: (i) General Obligation Bonds, Series 2019A-1 (Disaster Preparedness, Public Safety, and Infrastructure) (the “**Series 2019A-1 Bonds**”); (ii) Taxable General Obligation Bonds, Series 2019A-2 (Disaster Preparedness, Public Safety, and Infrastructure) (the “**Taxable Series 2019A-2 Bonds**” and together with the Series 2019A-1 Bonds, the “**Series 2019A Bonds**”); (iii) Taxable General Obligation Bonds, Series 2019B (Disaster Preparedness, Public Safety, and Infrastructure) (the “**Taxable Series 2019B Bonds**”); (iv) General Obligation Bonds, Series 2019C (Refunding, Libraries, Parks, and Public Safety Projects) (the “**Series 2019C Bonds**”); and (v) Taxable General Obligation Bonds, Series 2019D (Refunding, Libraries, Parks, and Public Safety Projects) (the “**Taxable Series 2019D Bonds**,” and together with the Series 2019A Bonds, the Taxable Series 2019B Bonds, and the Series 2019C Bonds, the “**Bonds**”).

All capitalized terms used in this Official Statement, unless noted otherwise, have the meanings set forth in the Fiscal Agent Agreement (as defined below).

### INTRODUCTION

This Introduction is not a summary of this Official Statement. It is only a brief description of and guide to, and is qualified by, more complete and detailed information contained in the entire Official Statement, including the cover page and appendices hereto, and the documents summarized or described herein. A full review should be made of the entire Official Statement. The offering of Bonds to potential investors is made only by means of the entire Official Statement.



## The City

The City, with an estimated population as of January 1, 2019 of approximately 1,043,058 (as reported by the California Department of Finance), is the third largest city in the State of California (the “**State**”) and the tenth largest city in the United States. The territory of the City encompasses approximately 180 square miles. Located at the southern end of the San Francisco Bay, the City is the county seat of the County of Santa Clara (the “**County**”).

## Sources of Payment for Bonds

The Bonds are general obligations of the City payable from ad valorem taxes levied by the City and collected by the County. The City Council is empowered and is obligated to annually levy ad valorem taxes for the payment of the Bonds and the interest thereon upon all property within the City subject to taxation by the City, without limitation of rate or amount (except with respect to certain personal property which is taxable at limited rates). See “THE BONDS – Security for the Bonds” herein.

## Authority and Purpose

**Series 2019A-1 Bonds.** The Series 2019A-1 Bonds are being issued pursuant to a (i) resolution adopted by the City Council on [June 25], 2019 (the “**Bond Resolution**”), (ii) a Fiscal Agent Agreement dated as of July 1, 2019 (the “**Fiscal Agent Agreement**”), between the City and Wilmington Trust, N.A., as fiscal agent (the “**Fiscal Agent**”), (iii) Chapter 14.28 of the San José Municipal Code (the “**Act**”) and (iv) the authorization received by the City at the general election of the registered voters held on November 6, 2018 (the “**2018 Election**”), at which more than two-thirds of the persons voting on Measure T (San José Disaster Preparedness, Public Safety and Infrastructure Bond) (“**Measure T**”) voted to authorize the issuance and sale of not to exceed \$650,000,000 principal amount of general obligation bonds.

The Series 2019A-1 Bonds are the first series of general obligation bonds that the City is issuing pursuant to Measure T. After the issuance of the Series 2019A-1 Bonds, the Taxable Series 2019A-2 Bonds and the Taxable Series 2019B Bonds (as described below), a principal amount of \$410,000,000\* will remain authorized but unissued pursuant to the authorization under Measure T. See “THE BONDS – Authority for Issuance.”

The Series 2019A-1 Bonds are being issued by the City to (i) finance projects authorized under Measure T, as more fully described in this Official Statement, (ii) fund capitalized interest on the Series 2019A-1 Bonds, (iii) pay principal of and interest on the Taxable Series 2019A-2 Bonds, and (iv) pay costs of issuing the Series 2019A-1 Bonds. See “THE BONDS – Purpose of Issues.”

**Taxable Series 2019A-2 Bonds.** The Taxable Series 2019A-2 Bonds are being issued pursuant to the Bond Resolution, the Fiscal Agent Agreement, the Act and Measure T. The Taxable Series 2019A-2 Bonds are the second series of general obligation bonds that the City is issuing pursuant to Measure T. See “THE BONDS – Authority for Issuance.”

The Taxable Series 2019A-2 Bonds are being issued by the City to (i) finance projects authorized under Measure T, as more fully described in this Official Statement, and (ii)

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\* Preliminary; subject to change.



pay costs of issuing the Taxable Series 2019A-2 Bonds. See “THE BONDS – Purpose of Issues.”

**Taxable Series 2019B Bonds.** The Taxable Series 2019B Bonds are being issued pursuant to the Bond Resolution, the Fiscal Agent Agreement, the Act and Measure T. The Taxable Series 2019B Bonds are the third series of general obligation bonds that the City is issuing pursuant to Measure T. See “THE BONDS – Authority for Issuance.”

The Taxable Series 2019B Bonds are being issued by the City to (i) finance projects authorized under Measure T, as more fully described in this Official Statement, (ii) fund capitalized interest on the Taxable Series 2019B Bonds, and (iii) pay costs of issuing the Taxable Series 2019B Bonds. See “THE BONDS – Purpose of Issues.”

**Series 2019C Bonds.** The City is issuing the Series 2019C Bonds pursuant to (i) the Bond Resolution, (ii) the Fiscal Agent Agreement, and (iii) the Act.

In addition to the foregoing authorization, a portion of the Series 2019C Bonds are being issued to redeem the Prior Bonds (as defined below) pursuant to Articles 9 and 11 of Chapter 3 of Part 1 of Division 2 of Title 5 of the California Government Code, commencing with Section 53550 of said Code (the “**Refunding Law**”). Such Series 2019C Bonds are sometimes referred to in this Official Statement as, the “**Series 2019C Refunding Bonds**.”

The remaining Series 2019C Bonds are being issued pursuant to the following authorizations received by the City:

- The general election of the registered voters of the City held on November 7, 2000 (the “**2000 Election**”), pursuant to which more than two-thirds of the persons voting on Measure O (San José Neighborhood Libraries Bond) (“**Measure O (2000)**”) voted to authorize the issuance and sale of not to exceed \$211,790,000 principal amounts of general obligation bonds. \$5,905,000 aggregate principal amount of Series 2019C Bonds are being issued pursuant to the Measure O (2000) authorization and constitute the seventh and final series of general obligation bonds issued by the City under Measure O (2000). Such Series 2019C Bonds are sometimes referred to in this Official Statement as, the “**Series 2019C Libraries Bonds**.”
- The general election of the registered voters of the City held on March 5, 2002 (the “**2002 Election**”), pursuant to which more than two-thirds of the persons voting on Measure O (San José 911, Fire, Police, Paramedic and Neighborhood Security Act) (“**Measure O (2002)**”) voted to authorize the issuance and sale of not to exceed \$159,000,000 principal amount of general obligation bonds. \$3,325,000 aggregate principal amount of Series 2019C Bonds are being issued pursuant to the Measure O (2002) authorization and constitute the sixth and final series of general obligation bonds issued by the City pursuant to Measure O (2002). Such Series 2019C Bonds are sometimes referred to in this Official Statement as, the “**Series 2019C Public Safety Bonds**.”

See “THE BONDS – Authority for Issuance.”

The City will use a portion of the proceeds of the Series 2019C Refunding Bonds to redeem a portion of each of the following outstanding general obligation bonds previously issued by the City:



- City of San José General Obligation Bonds, Series 2001 (Libraries and Parks Project) (the “**Series 2001 Bonds**”), which are outstanding in the total aggregate principal amount of \$30,745,000;
- City of San José General Obligation Bonds, Series 2002 (Libraries, Parks and Public Safety Projects) (the “**Series 2002 Bonds**”), which are outstanding in the total aggregate principal amount of \$54,170,000;
- City of San José General Obligation Bonds, Series 2004 (Libraries, Parks and Public Safety Projects) (the “**Series 2004 Bonds**”), which are outstanding in the total aggregate principal amount of \$63,310,000;
- City of San José General Obligation Bonds, Series 2005 (Libraries and Public Safety Projects) (the “**Series 2005 Bonds**”), which are outstanding in the total aggregate principal amount of \$26,265,000;
- City of San José General Obligation Bonds, Series 2006 (Libraries and Parks Projects) (the “**Series 2006 Bonds**”), which are outstanding in the total aggregate principal amount of \$63,270,000;
- City of San José General Obligation Bonds, Series 2007 (Parks and Public Safety Projects) (the “**Series 2007 Bonds**”), which are outstanding in the total aggregate principal amount of \$57,000,000; and
- City of San José General Obligation Bonds, Series 2009 (Public Safety Projects) (the “**Series 2009 Bonds**”), which are outstanding in the total aggregate principal amount of \$6,300,000;

See “FINANCING AND REFUNDING PLANS – Refunding Plan.”

The Series 2019C Libraries Bonds and Series 2019C Public Safety Bonds are being issued by the City to finance projects authorized under Measure O (2000) and Measure O (2002), respectively, as more fully described in this Official Statement. See “THE BONDS – Purpose of Issues.”

The remaining proceeds of the Series 2019C Bonds will be used to (i) fund capitalized interest on a portion of the Series 2019C Bonds and (ii) pay costs of issuing the Series 2019C Bonds.

***Taxable Series 2019D Bonds.*** The City is issuing the Taxable Series 2019D Bonds pursuant to the Refunding Law, the Bond Resolution, and the Fiscal Agent Agreement. See “THE BONDS – Authority for Issuance.”

The City will use a portion of the proceeds of the Taxable Series 2019D Bonds to redeem the (i) remaining portion of the Series 2001 Bonds, the Series 2002 Bonds, the Series 2004 Bonds, the Series 2005 Bonds, the Series 2006 Bonds, the Series 2007 Bonds and the Series 2009 Bonds not redeemed by the City with proceeds of the Series 2019C Refunding Bonds, and (ii) all of the outstanding City of San José General Obligation Bonds, Series 2008 (Libraries and Parks Projects) (the “**Series 2008 Bonds**” and, together with the Series 2001 Bonds, the Series 2002 Bonds, the Series 2004 Bonds, the Series 2005 Bonds, the Series 2006 Bonds, the Series 2007 Bonds and the Series 2009 Bonds, the



**“Prior Bonds”**), which are outstanding in the total aggregate principal amount of \$22,050,000. See “FINANCING AND REFUNDING PLANS – Refunding Plan.”

The remaining proceeds of the Taxable Series 2019D Bonds will be used to pay costs of issuing the Taxable Series 2019D Bonds.

### **Offering and Delivery of the Bonds**

The Bonds are offered when, as and if issued, subject to approval of legality by Bond Counsel. It is anticipated that the Bonds will be available for delivery through DTC on or about July 25, 2019.

### **Description of the Bonds**

**Registration.** The Bonds will be issued in fully registered form only, registered in the name of Cede & Co. as nominee of The Depository Trust Company, New York, New York (“**DTC**”), and will be available to actual purchasers of the Bonds (the “**Beneficial Owners**”) in the denominations set forth on the inside cover pages hereof, under the book-entry system maintained by DTC only through brokers and dealers who are or act through DTC Participants as described herein. Beneficial Owners will not be entitled to receive physical delivery of the Bonds. See “THE BONDS – Book-Entry-Only System.” In the event that the book-entry-only system described below is no longer used with respect to the Bonds, the Bonds will be registered in accordance with the Fiscal Agent Agreement described herein. See “THE BONDS –Registration, Transfer and Exchange of Bonds.”

**Denominations.** Individual purchases of interests in the Bonds will be available to purchasers of the Bonds as fully registered securities in the denominations of \$5,000 each or any integral multiple thereof.

**Optional Redemption.** The Series 2019A-1 Bonds and the Series 2019C Bonds maturing on or before September 1, 2028, are not subject to redemption prior to their respective maturity dates. The Series 2019A-1 Bonds and Series 2019C Bonds maturing on or after September 1, 2029, shall be subject to redemption prior to their respective maturity dates as a whole, or in part, on any date, from any moneys provided at the option of the City, in each case on and after March 1, 2029, at a redemption price equal to the principal amount of Series 2019A-1 Bonds or the Series 2019C Bonds called for redemption, plus accrued interest to the date fixed for redemption, without premium.

The Taxable Series 2019A-2 Bonds are not subject to optional redemption prior to maturity.

The Taxable Series 2019B Bonds and the Taxable Series 2019D Bonds may be redeemed in whole or in part at any time, from any moneys that may be provided for such purpose, at a redemption price for such Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed determined by the Designated Investment Banker equal to the greater of (i) 100% of the principal amount of the Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed, or (ii) an amount equal to the sum of the present values of the remaining scheduled payments of principal and interest on each of Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed, not including any portion of those payments of interest accrued and unpaid as of the date on which the Taxable Series 2019B Bonds or Taxable Series 2019D Bonds are to be redeemed,



discounted to the date on which such Taxable Series 2019B Bonds or Taxable Series 2019D Bonds are to be redeemed on a semi-annual basis, assuming a 360-day year consisting of twelve 30-day months, at the applicable Treasury Rate plus 15 basis points, plus accrued and unpaid interest on the Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed on the redemption date.

See “THE BONDS – Optional Redemption” herein.

***Mandatory Sinking Fund Redemption.*** The Bonds maturing on September 1, 20\_\_ are subject to mandatory sinking fund redemption beginning on September 1, 20\_\_. See “THE BONDS – Mandatory Sinking Fund Redemption” herein.

***Payments.*** Interest on the Bonds accrues from the date of delivery, and with exception of all of the Taxable Series 2019A-2 Bonds, is payable on March 1, 2019 and semiannually thereafter on each March 1 and September 1. Principal on the Bonds, with exception of all of the Taxable Series 2019A-2 Bonds, is payable on September 1, commencing September 1, 2020, in the amounts and years set forth on the cover page hereof. Interest on the Taxable Series 2019A-2 Bonds accrues from the date of delivery, and is payable together with principal on such Taxable Series 2019A-2 Bonds on September 1, 2019.

#### **Continuing Disclosure**

The City will covenant for the benefit of bondholders to make available certain financial information and operating data relating to the City and to provide notices of the occurrence of certain enumerated events, if material, in compliance with the Securities Exchange Commission Rule 15c2-12(b)(5) (the “**Rule**”). See “CONTINUING DISCLOSURE” and APPENDIX E – “FORM OF CONTINUING DISCLOSURE CERTIFICATE.”

#### **Professionals Involved in the Offering**

Public Resources Advisory Group, Oakland, California (the “**Municipal Advisor**”), has served as municipal advisor to the City and has advised the City with respect to the financial structure of the issuance of the Bonds and as to other financial aspects of the transaction. See “MUNICIPAL ADVISOR.”

Wilmington Trust, N.A., Costa Mesa, California, will act as Fiscal Agent with respect to the Bonds.

All proceedings in connection with the issuance of the Bonds are subject to the approval of Jones Hall, A Professional Law Corporation, San Francisco, California, Bond Counsel to the City. Certain legal matters will also be passed upon for the City by Jones Hall, A Professional Law Corporation, San Francisco, California, as Disclosure Counsel to the City, and by the City Attorney of the City. *Payment of the fees and expenses of Bond Counsel, Disclosure Counsel and the Municipal Advisor is contingent upon the sale and delivery of the Bonds.*

#### **Other Information**

This Official Statement speaks only as of its date, and the information contained herein is subject to change. Copies of documents referred to herein and information concerning the Bonds are available from City of San José, Debt Management - Finance, 200 East Santa Clara Street, San José, California 95113-1905; phone (408) 535-7010; or by e-mail at [debt.management@sanjoseca.gov](mailto:debt.management@sanjoseca.gov). A charge will be made to cover the City's reasonable



costs of duplication and delivery. In addition, documents are available for inspection during business hours at the address above, or at the principal corporate trust office of the Fiscal Agent in Costa Mesa, California.

## **FINANCING AND REFUNDING PLANS**

### **Plan of Finance**

The net proceeds of the Series 2019A Bonds and the Taxable Series 2019B Bonds will be used by the City to finance projects authorized under Measure T. See “THE BONDS – Purpose of Issues.”

The net proceeds of the Series 2019C Libraries Bonds and Series 2019C Public Safety Bonds will be used by the City to finance projects authorized under Measure O (2000) and Measure O (2002), respectively. See “THE BONDS – Purpose of Issues.”

The City will use a portion of the net proceeds of the Series 2019C Refunding Bonds and all of the net proceeds of the Taxable Series 2019D Bonds to redeem all of the outstanding Prior Bonds. See “– Refunding Plan” below.

### **Refunding Plan**

**General.** The outstanding Prior Bonds are currently subject to optional redemption prior to their stated maturities on any date.

**Escrow Accounts.** In connection with the issuance of the Series 2019C Refunding Bonds and Taxable Series 2019D Bonds, the City will deliver Irrevocable Refunding Instructions (the “**Refunding Instructions**”) to Wells Fargo Bank, National Association, as fiscal agent of the Prior Bonds (in such capacity, the “**Prior Bonds Fiscal Agent**”). Pursuant to the Refunding Instructions, the City will cause the Fiscal Agent to deliver (i) a portion of the proceeds of the Series 2019C Refunding Bonds, along with other available amounts, to the Prior Bonds Fiscal Agent for deposit into an escrow subaccount (the “**Tax-Exempt Escrow Subaccount**”), and (ii) a portion of the proceeds of the Taxable Series 2019D Bonds, along with other available amounts, to the Prior Bonds Fiscal Agent for deposit into an escrow subaccount (the “**Taxable Escrow Subaccount**”), in each case established and held by the Prior Bonds Fiscal Agent under the Refunding Instructions.

**Defeasance and Redemption.** The Prior Bonds Fiscal Agent will invest a portion of the amounts on deposit in the Tax-Exempt Escrow Subaccount and the Taxable Escrow Subaccount in federal securities, and will hold the remainder in cash, uninvested. From the moneys on deposit in the Tax-Exempt Escrow Subaccount, the Prior Bonds Fiscal Agent will pay a portion of the outstanding principal amount of the Series 2001 Bonds, the Series 2002 Bonds, the Series 2004 Bonds, the Series 2005 Bonds, the Series 2006 Bonds, the Series 2007 Bonds and the Series 2009 Bonds, in each case with accrued interest thereon, on July 30, 2019 (the “**Redemption Date**”). From the moneys on deposit in the Taxable Prior Bonds Escrow Account, the Prior Bonds Fiscal Agent will pay (i) a portion of the outstanding principal amount of the Series 2001 Bonds, the Series 2002 Bonds, the Series 2004 Bonds, the Series 2005 Bonds, the Series 2006 Bonds, the Series 2007 Bonds and the Series 2009 Bonds not paid by the Prior Bonds Fiscal Agent, and (ii) all of the outstanding principal amount of the Series 2008 Bonds, in each case with accrued interest thereon, on the Redemption Date.



Pursuant to the fiscal agent agreements relating to the Prior Bonds (collectively, the **“Prior Bonds Fiscal Agent Agreements”**), upon (i) the deposits in the Tax-Exempt Escrow Subaccount and the Taxable Escrow Subaccount as described above (as confirmed by an independent certified public accountant (such as the Verification Agent) to be fully sufficient to pay and discharge the indebtedness on the Prior Bonds), and (ii) the giving of notice of redemption prior to maturity of the Prior Bonds as provided in the Prior Bonds Fiscal Agent Agreements, the pledge of the funds and moneys provided for in the Prior Bonds Fiscal Agent Agreement and all other obligations of the City thereunder with respect to outstanding Prior Bonds will cease and terminate.

*The amounts held in the Tax-Exempt Escrow Subaccount and the Taxable Escrow Subaccount by the Prior Bonds Fiscal Agent are pledged solely to the amounts due and payable by the City with respect to the outstanding Prior Bonds as described above. The funds deposited in the Tax-Exempt Escrow Subaccount and the Taxable Escrow Subaccount will not be available for the payment of debt service with respect to the Bonds.*

### **Verification of Mathematical Accuracy**

Causey Demgen & Moore P.C., Denver, Colorado, (the **“Verification Agent”**), will verify the sufficiency of the deposits in the Tax-Exempt Escrow Subaccount and the Taxable Escrow Subaccount for the purposes described above. Assuming the accuracy of the Verification Agent’s computations, as a result of the deposit and application of funds as provided in the Tax-Exempt Escrow Subaccount and the Taxable Escrow Subaccount, the obligations of the City with respect to the Prior Bonds will be discharged as described above.

The Verification Agent has restricted its procedures to examining the arithmetical accuracy of certain computations and has not made any study or evaluation of the assumptions and information upon which the computations are based and, accordingly, has not expressed an opinion on the data used, the reasonableness of the assumptions, or the achievability of the forecasted outcome.



## Sources and Uses of Funds

The estimated sources and uses of funds with respect to the Bonds will be applied as follows:

	Series 2019A-1 Bonds	Taxable Series 2019A-2 Bonds	Taxable Series 2019B Bonds	Series 2019C Bonds	Taxable Series 2019D Bonds	Total Bonds
<b>Sources of Funds</b>						
Principal Amount of Bonds						
<i>Plus:</i> [Net] Original Issue [Premium]/[Discount]						
Available Moneys Relating to Prior Bonds						
<i>Less:</i> Purchasers' Discount						
<i>Total Sources</i>						
<b>Uses of Funds</b>						
Series 2019A/B Infrastructure Account						
Deposit to Series 2019C Libraries Account						
Deposit to Series 2019C/D Public Safety Account						
Deposit to Taxable Series 2019D Libraries Account						
Deposit to Taxable Series 2019D Parks Account						
Deposit to Tax-Exempt Escrow Subaccount						
Deposit to Taxable Escrow Subaccount						
Deposit to Costs of Issuance Account <sup>(1)</sup>						
Deposit to Bond Service Fund <sup>(2)</sup>						
<i>Total Uses</i>						

<sup>(1)</sup> Includes bond and disclosure counsel fees, municipal advisor fees, rating fees, initial fees of the Fiscal Agent, fees of the City, verification and bidding agent fees, printing expenses and other costs of issuance with respect to the Bonds.

<sup>(2)</sup> To fund capitalized interest and, in the case of the Series 2019A-1 Bonds, also to pay principal of and interest on the Taxable Series 2019A-2 Bonds.



## THE BONDS

### Authority for Issuance

**Series 2019A Bonds and Taxable 2019B Bonds.** The City is issuing the Series 2019A-1 Bonds, the Taxable Series 2019A-2 Bonds and Taxable Series 2019B Bonds pursuant to the Bond Resolution, the Fiscal Agent Agreement, the Act and the authorization received by the City at the 2018 Election under Measure T.

Pursuant to the 2018 Election held on November 6, 2018, more than two-thirds of the persons voting on Measure T voted to authorize the issuance and sale of not to exceed \$650,000,000 principal amounts of general obligation bonds. The issuance of general obligation bonds in accordance with Measure T was approved by 70.95% of the voters. The Series 2019A-1 Bonds, the Series 2019A-2 Bonds and the Taxable Series 2019B Bonds are the first, second and third series of general obligation bonds, respectively, that the City is issuing pursuant to Measure T. After the issuance of the Series 2019A-1 Bonds, the Taxable 2019A-2 Bonds and the Taxable Series 2019B Bonds, a principal amount of \$410,100,000\* will remain authorized but unissued pursuant to the authorization under Measure T.

**Series 2019C Bonds.** The City is issuing the Series 2019C Bonds pursuant to (i) the Bond Resolution, (ii) the Fiscal Agent Agreement, and (iii) the Act. In addition, the portion of the Series 2019C Bonds that are Series 2019C Refunding Bonds are also being issued under the Refunding Law. The portion of the Series 2019C Bonds that are Series 2019C Libraries Bonds are also being issued under the authorization received at the 2000 Election under Measure O (2000). The portion of the Series 2019C Bonds that are Series 2019C Public Safety Bonds are also being issued under the authorization received at the 2002 Election under Measure O (2002).

As previously described, the City will use a portion of the net proceeds of the Series 2019C Refunding Bonds and the Taxable Series 2019D Bonds to redeem all of the outstanding Prior Bonds. The Prior Bonds were issued by the City pursuant to authorizations received at the 2000 Election, the 2002 Election and pursuant to the Measure P, as defined below.

Pursuant to the 2000 Election held on November 7, 2000, more than two-thirds of the persons voting on Measure O (2000) voted to authorize the issuance and sale of not to exceed \$211,790,000 principal amounts of general obligation bonds. The issuance of general obligation bonds in accordance with Measure O (2000) was approved by 75.8% of the voters. The Series 2019C Libraries Bonds are the seventh and final series of general obligation bonds that the City is issuing pursuant to Measure O (2000).

Pursuant to the 2002 Election held on March 5, 2002, more than two-thirds of the persons voting on Measure O (2002) voted to authorize the issuance and sale of not to exceed \$159,000,000 principal amount of general obligation bonds. The issuance of general obligation bonds in accordance with Measure O (2002) was approved by 71.7% of the voters. The Series 2019C Public Safety Bonds are the sixth and final series of general obligation bonds that the City is issuing pursuant to Measure O (2002).

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\* Preliminary; subject to change.



Pursuant to the 2000 Election held on November 7, 2000, at which more than two-thirds of the persons voting on Measure P (San José Safe Neighborhood Parks and Recreation Bond) ("**Measure P**") voted to authorize the issuance and sale of not to exceed \$228,030,000 principal amount of general obligation bonds and certain of the Prior Bonds were issued under such measure. The issuance of general obligation bonds in accordance with Measure P was approved by 78.7% of the voters. None of the Bonds are being issued by the City pursuant to the authorizations received at the 2000 Election under Measure P.

***Taxable Series 2019D Bonds.*** The City is issuing the Taxable Series 2019D Bonds pursuant to the Bond Resolution, the Fiscal Agent Agreement, and the Refunding Law.

### **Purpose of Issues**

***Series 2019A-1 Bonds.*** The net proceeds of the Series 2019A-1 Bonds will be used by the City to finance projects authorized under Measure T. Such projects include traffic, public safety and storm sewer improvements. The remaining proceeds of the Series 2019A-1 Bonds will be used to (i) fund capitalized interest on the Series 2019A-1 Bonds, (ii) pay principal of and interest on the Taxable Series 2019A-2 Bonds, and (iii) to pay costs of issuing the Series 2019A-1 Bonds.

***Taxable Series 2019A-2 Bonds.*** The net proceeds of the Series 2019A-1 Bonds will be used by the City to finance projects authorized under Measure T. Such projects include traffic, public safety and storm sewer improvements. The remaining proceeds of the Series 2019A-1 Bonds will be used to pay costs of issuing the Taxable Series 2019A-2 Bonds.

***Taxable Series 2019B Bonds.*** The net proceeds of the Taxable Series 2019B Bonds will be used by the City to (i) finance projects authorized under Measure T, and (ii) pay costs of issuing the Taxable Series 2019B Bonds. Such projects include the acquisition of open space in Coyote Valley, located at the southern end of the City and to the north of Morgan Hill, lighting improvements, and community centers/emergency shelters.

***Series 2019C Bonds.*** The City will use a portion of the net proceeds of the Series 2019C Bonds to redeem a portion of the Series 2001 Bonds, the Series 2002 Bonds, the Series 2004 Bonds, the Series 2005 Bonds, the Series 2006 Bonds, the Series 2007 Bonds and the Series 2009 Bonds. See "FINANCING AND REFUNDING PLANS – Refunding Plan" for additional information regarding the use of the proceeds of the Series 2019C Bonds and the Taxable Series 2019D Bonds to redeem the outstanding Prior Bonds.

The portion of the Series 2019C Bonds that are Series 2019C Libraries Bonds will be used by the City to finance projects authorized under Measure O (2000). Such projects include improvements at the three oldest branch libraries of the City: Biblioteca Latinoamericana, Alviso, and West Valley libraries.

The portion of the Series 2019C Bonds that are Series 2019C Public Safety Bonds will be used by the City to finance projects authorized under Measure O (2002). Such projects include the rehabilitation of fire stations.

The remaining proceeds of the Series 2019C Bonds will be used to (i) fund capitalized interest on the portion of the Series 2019C Bonds that are Series 2019C Libraries Bonds or Series 2019C Public Safety Bonds, and (ii) fund the costs of issuance relating to such bonds.



**Taxable Series 2019D Bonds.** The City will use a portion of the net proceeds of the Series 2019D Bonds to redeem (i) a portion of the Series 2001 Bonds, the Series 2002 Bonds, the Series 2004 Bonds, the Series 2005 Bonds, the Series 2006 Bonds, the Series 2007 Bonds and the Series 2009 Bonds not redeemed by the City with proceeds of the Series 2019C Refunding Bonds, and (ii) all of the outstanding Series 2008 Bonds. See “FINANCING AND REFUNDING PLANS – Refunding Plan” for additional information regarding the use of the proceeds of the Series 2019C Bonds and the Taxable Series 2019D Bonds to redeem the outstanding Prior Bonds.

The remaining proceeds of the Taxable Series 2019D Bonds will be used to fund the costs of issuance relating to such bonds.

### **Security for the Bonds**

**General.** The Bonds are general obligations of the City payable from *ad valorem* taxes levied by the City and collected by the County. The City Council is empowered and is obligated to levy *ad valorem* taxes upon all property within the City subject to taxation by the City, without limitation of rate or amount (except with respect to certain personal property which is taxed at limited rates), for the payment of the Bonds and the interest thereon, in accordance with all relevant provisions of law.

The City will direct the County to collect such *ad valorem* taxes in such amounts and at such times as is necessary to ensure the timely payment of debt service. Such taxes, when collected, will be deposited into the Debt Service Account, which is maintained by the City and which is irrevocably pledged for the payment of principal of and interest on the Bonds when due.

The amount of the annual *ad valorem* tax levied by the City and collected by the County to repay the Bonds will be determined by the relationship between the assessed valuation of taxable property in the City and the amount of debt service due on the Bonds. A reduction in the assessed valuation of taxable property in the City caused by economic factors beyond the City's control, such as economic recession, slower growth, or deflation of land values, a relocation out of the City by one or more major property owners, or the complete or partial destruction of such property caused by, among other eventualities or possibilities, an earthquake and flood (discussed below) or other natural disaster, could cause a reduction in the assessed value of the City and necessitate an unanticipated increase in the annual tax levy. For further information regarding the City's tax base, overlapping debt and other matters concerning taxation, see APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION.” For further information regarding pending reductions in assessed valuations of property located in the City, please see APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MAJOR GENERAL FUND REVENUE SOURCES – Assessed Values and Property Taxes” herein.

**Statutory Lien on Taxes (Senate Bill 222).** Pursuant to Section 53515 of the California Government Code, the Bonds will be secured by a statutory lien on all revenues received pursuant to the levy and collection of the *ad valorem* taxes levied for the Bonds. Section 53515 of the California Government Code provides that the lien will automatically arise, without the need for any action or authorization by the local agency or its governing board, and will be valid and binding from the time such bonds are executed and delivered. Section 53515 of the California Government Code further provides that the revenues



received pursuant to the levy and collection of the tax will be immediately subject to the lien, and the lien will immediately attach to the revenues and be effective, binding and enforceable against the local agency, its successor, transferees and creditors, and all others asserting rights therein, irrespective of whether those parties have notice of the lien and without the need for physical delivery, recordation, filing or further act. See “CERTAIN RISK FACTORS – Limitation on Remedies; Bankruptcy.”

**Teeter Plan.** The County operates on a Teeter Plan whereby taxing entities, including the City, receive 100% of their *ad valorem* tax levy assessed by the County. The Teeter Plan will remain in effect unless the County orders its discontinuance or unless the County receives a petition for its discontinuance joined in by resolutions adopted by at least two-thirds of the participating revenue districts in the County, in which event the Board of Supervisors of the County shall order discontinuance of the Teeter Plan effective at the commencement of the subsequent fiscal year. Additionally, the County may discontinue the procedures under the Teeter Plan with respect to any political subdivision in the County if the rate of secured property tax delinquency in that political subdivision in any year exceeds 3% of the total of all taxes and assessments levied on the secured rolls for that political subdivision. If the Teeter Plan is discontinued subsequent to its implementation, only those secured property taxes actually collected would be allocated to political subdivisions (including the City) for which the County acts as the tax-levying or tax-collecting agency. For further information, please see APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MAJOR GENERAL FUND REVENUE SOURCES – Assessed Values and Property Taxes” herein.

Under the Teeter Plan, the County funds current year delinquencies from certain moneys in its treasury, including, currently, tax payments from prior years’ delinquencies. There can be no assurance that the County will continue to utilize the Teeter Plan with respect to the tax levy for the Bonds or for the City. Further, the amounts expected to be available to the County may not be sufficient to fund all delinquencies in current tax levies, in which case the City may not receive the full amount required for the payment of debt service on the Bonds on a timely basis.

### **Payment of the Bonds**

The Bonds will be issued in book-entry form only and will be initially issued and registered in the name of Cede & Co. Purchasers will not receive certificates representing their interest in the Bonds. The Bonds shall be issued in the denomination of \$5,000 each or any integral multiple thereof. The Bonds mature on September 1, in the years and in the amounts shown on the inside cover pages of this Official Statement. See also “DEBT SERVICE SCHEDULES.”

Interest on the Bonds accrues from the date of delivery. Interest on the Taxable Series 2019-2 Bonds is payable on September 1, 2019. Interest on all of the other Bonds is payable on March 1, 2020, and semiannually thereafter on March 1 and September 1 of each year (the “**Interest Payment Dates**”). Interest on the Bonds shall be calculated on the basis of a 360-day year comprised of twelve 30-day months. Each Bond shall bear interest from the Interest Payment Date next preceding the date of registration and authentication thereof unless (i) it is registered and authenticated as of an Interest Payment Date, in which event it shall bear interest from such date, or (ii) it is registered and authenticated prior to an Interest Payment Date and after the close of business on the fifteenth day of the month preceding such Interest Payment Date, in which event it shall bear interest from such Interest Payment Date, or



(iii) it is registered and authenticated prior to August 15, 2019, in which event it shall bear interest from the date of delivery; *provided*, however, that if at the time of authentication of a Bond, interest is in default thereon, such Bond shall bear interest from the Interest Payment Date to which interest has previously been paid or made available for payment thereon.

Interest on the Bonds (including the final interest payment upon maturity or early redemption) is payable by check of the Fiscal Agent mailed on the Interest Payment Date to the owner thereof at such owner's address as it appears on the registration books maintained by the Fiscal Agent at the close of business on the fifteenth day of the month preceding the Interest Payment Date, or at such other address as the owner may have filed with the Fiscal Agent for that purpose; *provided* that an owner of \$1,000,000 or more aggregate principal amount of Bonds, or the owner of all of the Bonds at the time outstanding, shall, at his or her option, receive payment of interest by wire transfer to an account in the United States of America designated by such owner to the Fiscal Agent no later than the fifteenth day of the month immediately preceding the applicable Interest Payment Date. Principal of the Bonds is payable in lawful money of the United States of America at the principal office of the Fiscal Agent.

### **Book-Entry-Only System**

The Bonds will be initially registered in the name of "Cede & Co.," as nominee of DTC which has been appointed securities depository for the Bonds, and registered ownership may not thereafter be transferred except as provided in the Fiscal Agent Agreement. The Bonds are being issued in book-entry form only. Purchasers will not receive certificates representing their interests in the Bonds. Principal of and interest on the Bonds will be paid by the Fiscal Agent to DTC or its nominee, Cede & Co., which in turn is obligated to remit such principal and interest to its participants for subsequent disbursement to Beneficial Owners of the Bonds as described herein. See "APPENDIX F – DTC AND THE BOOK-ENTRY-ONLY SYSTEM" herein.

### **Fiscal Agent**

Wilmington Trust, N.A., Costa Mesa, California, will act as the registrar, transfer agent, and fiscal agent for the Bonds. As long as DTC's book-entry method is used for the Bonds, the Fiscal Agent will send any notice of redemption or other notices to owners only to DTC. Any failure of DTC to advise any DTC Participant, or of any DTC Participant to notify any Beneficial Owner, of any such notice and its content or effect will not affect the validity or sufficiency of the proceedings relating to the redemption of the Bonds called for redemption or of any other action premised on such notice.

The Fiscal Agent, the City, and the Purchasers of the Bonds have no responsibility or liability for any aspects of the records relating to or payments made on account of beneficial ownership, or for maintaining, supervising or reviewing any records relating to beneficial ownership, of interests in the Bonds.

In the event that either (i) DTC determines not to continue to act as securities depository for the Bonds, or (ii) the City determines to terminate DTC as a securities depository for the Bonds, then the City will discontinue the book-entry system with DTC. If the City fails to identify another securities depository to replace DTC, then the Bonds shall no longer be required to be registered in the name of DTC, but shall be registered in whatever name or



names the owners transferring or exchanging Bonds shall designate, in accordance with the provisions of the Fiscal Agent Agreement.

### **Optional Redemption\***

**Series 2019A-1 Bonds and the Series 2019C Bonds – Optional Redemption.** The Series 2019A-1 Bonds and the Series 2019C Bonds (collectively, the “**Tax-Exempt Bonds**” and each, a “**Tax-Exempt Bond**”) maturing on or before September 1, 20\_\_, are not subject to redemption prior to their respective maturity dates. The Tax-Exempt Bonds maturing on or after September 1, 20\_\_, shall be subject to redemption prior to their respective maturity dates as a whole, or in part, on any date, from any moneys provided at the option of the City, in each case on and after September 1, 20\_\_, at a redemption price equal to the principal amount of Tax-Exempt Bonds called for redemption, plus accrued interest to the date fixed for redemption, without premium.

**Taxable Series 2019A-2 Bonds – No Optional Redemption.** The Taxable Series 2019A-2 Bonds are not subject to optional redemption prior to maturity.

**Taxable Series 2019B Bonds and Taxable Series 2019D Bonds – Make-Whole Call Redemption.** The Taxable Series 2019B Bonds and the Taxable Series 2019D Bonds (and together with the Taxable Series 2019A-2 Bonds, the “**Taxable Bonds**”) may be redeemed in whole or in part at any time, from any moneys that may be provided for such purpose, at a redemption price for such Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed determined by the Designated Investment Banker equal to the greater of (i) 100% of the principal amount of the Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed, or (ii) an amount equal to the sum of the present values of the remaining scheduled payments of principal and interest on each of Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed, not including any portion of those payments of interest accrued and unpaid as of the date on which the Taxable Series 2019B Bonds or Taxable Series 2019D Bonds are to be redeemed, discounted to the date on which such Taxable Series 2019B Bonds or Taxable Series 2019D Bonds are to be redeemed on a semi-annual basis, assuming a 360-day year consisting of twelve 30-day months, at the applicable Treasury Rate plus 15 basis points, plus accrued and unpaid interest on the Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed on the redemption date.

**“Comparable Treasury Issue”** means, with respect to any redemption date for a particular Taxable Series 2019B Bond or Taxable Series 2019D Bond, the U.S. Treasury security or securities selected by the Designated Investment Banker that has or have an actual maturity closest to (one equal to or one earlier and one later than) the remaining average life of the Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed, and that would be utilized in accordance with customary financial practice in pricing new issues of debt securities of comparable maturity to the remaining average life of such Taxable Series 2019B Bonds or Taxable Series 2019D Bonds to be redeemed.

**“Comparable Treasury Price”** means, with respect to any redemption date for a particular Taxable Series 2019B Bond or Taxable Series 2019D Bond, the average of five Reference Treasury Dealer Quotations for that redemption date, after excluding the highest

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\* Preliminary; subject to change.



and lowest such Reference Treasury Dealer Quotations, or if the Designated Investment Banker obtains fewer than five Reference Treasury Dealer Quotations, the average of all such quotations.

**“Designated Investment Banker”** means a Reference Treasury Dealer appointed by the City.

**“Reference Treasury Dealer”** means each of five firms, specified by the City from time to time, that are primary U.S. Government securities dealers in the City of New York (each, a **“Primary Treasury Dealer”**); provided, however, that if any of them ceases to be a Primary Treasury Dealer, the City will substitute another Primary Treasury Dealer.

**“Reference Treasury Dealer Quotations”** means, with respect to each Reference Treasury Dealer and any redemption date for a particular Taxable Series 2019B Bond or Taxable Series 2019D Bond, the average, as determined by the Designated Investment Banker, of the bid and asked prices for the Comparable Treasury Issue or Comparable Treasury Issues, as applicable (expressed in each case as a percentage of its principal amount), quoted in writing to the City and the Fiscal Agent by such Reference Treasury Dealer at 3:30 p.m. (New York City time) on the Valuation Date.

**“Treasury Rate”** means, with respect to any redemption date for a particular Taxable Series 2019B Bonds or Taxable Series 2019D Bonds, the rate per annum, expressed as a percentage of the principal amount, equal to the actual or interpolated rate based on (a) the most recent yield data for the applicable U.S. Treasury maturity index or indices, as applicable, from the Federal Reserve Statistical Release H.15 Daily Update (or any comparable or successor publication) reported, as of 11:00 a.m. New York City time, on the Valuation Date; or (b) if the yield described in (a) above is not reported as of such date and time or the yield reported as of such date and time is not ascertainable, the semi-annual equivalent yield to maturity of the Comparable Treasury Issue or Comparable Treasury Issues, assuming that such Comparable Treasury Issue or Comparable Treasury Issues are purchased on the redemption date for a price equal to the applicable Comparable Treasury Price, as calculated by the Designated Investment Banker.

**“Valuation Date”** means a date, as determined by the City, after consultation with the Designated Investment Banker, that is no earlier than 45 days prior to the redemption date.

***Notice to Trustee and Selection.*** The City shall provide notice to the Fiscal Agent of any such optional redemption at least 30 days prior to the date set for redemption. In the case of a redemption in part, a City representative shall designate to the Fiscal Agent, in a written request of the City, those maturities to be redeemed in whole or in part (including as a maturity, for such purposes, principal due on the Bonds on a particular September 1 as a result of a scheduled mandatory sinking fund redemption). In the event a City representative does not designate the maturities of the Bonds to be redeemed, the Fiscal Agent shall select Bonds for redemption on a proportionate basis among maturities. In the event a particular maturity of the Tax-Exempt Bonds is to be redeemed in part only, the Fiscal Agent shall select the Bonds of such maturity to be redeemed by lot. In the event a particular maturity of the Taxable Bonds is to be redeemed in part only, the particular Taxable Bonds to be redeemed will be selected on a pro-rata pass-through distribution of principal basis in accordance with the rules and procedures of the book-entry system of the Depository.



## Mandatory Sinking Fund Redemption

**Series 2019A-1 Bonds.** The Series 2019A-1 Bonds maturing September 1, 20\_\_ are subject to mandatory sinking fund redemption in part, by lot, prior to their stated maturity dates, on each September 1 on and after September 1, 20\_\_, at a redemption price equal to 100% of the principal amount thereof called for redemption, plus accrued interest to the redemption date, without premium, as follows:

\$\_\_\_\_\_ Series 2019A-1 Term Bonds Maturing September 1, 20\_\_

Redemption Date  
(September 1)

Principal Amount of Bonds  
to be Redeemed

(Maturity)

**Taxable Series 2019B Bonds.** The Taxable Series 2019B Bonds maturing September 1, 20\_\_ are subject to mandatory sinking fund redemption in part, on a pro rata pass-through distribution of principal basis, prior to their stated maturity dates, on each September 1 on and after September 1, 20\_\_, at a redemption price equal to 100% of the principal amount thereof called for redemption, plus accrued interest to the redemption date, without premium, as follows:

\$\_\_\_\_\_ Taxable Series 2019B Term Bonds Maturing September 1, 20\_\_

Redemption Date  
(September 1)

Principal Amount of Bonds  
to be Redeemed

(Maturity)

**Series 2019C Bonds.** The Series 2019C Bonds maturing September 1, 20\_\_ are subject to mandatory sinking fund redemption in part, by lot, prior to their stated maturity dates, on each September 1 on and after September 1, 20\_\_, at a redemption price equal to 100% of the principal amount thereof called for redemption, plus accrued interest to the redemption date, without premium, as follows:

\$\_\_\_\_\_ Series 2019C Term Bonds Maturing September 1, 20\_\_

Redemption Date  
(September 1)

Principal Amount of Bonds  
to be Redeemed

(Maturity)



***Taxable Series 2019D Bonds.*** The Taxable Series 2019D Bonds maturing September 1, 20\_\_ are subject to mandatory sinking fund redemption in part, on a pro rata pass-through distribution of principal basis, prior to their stated maturity dates, on each September 1 on and after September 1, 20\_\_, at a redemption price equal to 100% of the principal amount thereof called for redemption, plus accrued interest to the redemption date, without premium, as follows:

\$\_\_\_\_\_ Taxable Series 2019D Term Bonds Maturing September 1, 20\_\_

Redemption Date  
(September 1)

Principal Amount of Bonds  
to be Redeemed

(Maturity)

### **Redemption Procedure**

Regardless of whether the City has deposited funds sufficient for any redemption with the Fiscal Agent, the Fiscal Agent shall cause notice of any redemption to be mailed, first class mail, postage prepaid, at least 20 days but not more than 60 days prior to the date fixed for redemption, to the respective owners of any Bonds designated for redemption, at their addresses appearing on the registration books maintained by the Fiscal Agent and to the Securities Depositories and the Municipal Securities Rulemaking Board (both as defined in the Fiscal Agent Agreement); but such mailing shall not be a condition precedent to such redemption and failure to mail or to receive any such notice shall not affect the validity of the proceedings for the redemption of such Bonds. The City shall have the right to cancel the notice of any optional redemption by providing written notice of such cancellation to the Fiscal Agent on or prior to the date fixed for redemption.

Such notice shall state the redemption date and the redemption price and the CUSIP numbers of the Bonds to be redeemed, and, if less than all of the then outstanding Bonds are to be called for redemption, shall designate the serial numbers of the Bonds to be redeemed by giving the individual number of each Bond or by stating that all Bonds between two stated numbers, both inclusive, or by stating that all of the Bonds of one or more maturities have been called for redemption, and shall require that such Bonds be then surrendered at the principal office of the Fiscal Agent for redemption at the said redemption price, giving notice also that further interest on such Bonds will not accrue from and after the redemption date. Any notice of optional redemption shall also state that it is subject to cancellation not less than the day prior to the date set for redemption. In the event term bonds are redeemed in part, the City shall deliver a revised sinking fund schedule to the Fiscal Agent.

### **Rescission of Redemption Notice**

The City has the right to rescind any notice of optional redemption of Bonds by written notice to the Fiscal Agent on or prior to the date fixed for redemption. Any notice of redemption shall be cancelled and annulled if for any reason funds will not be or are not available on the date fixed for redemption for the payment in full of the Bonds then called for redemption, and such cancellation shall not constitute an Event of Default. The City and the Fiscal Agent have



no liability to the Bond owners or any other party related to or arising from such rescission of redemption. The Fiscal Agent shall mail notice of such rescission of redemption in the same manner as the original notice of redemption was sent under the Fiscal Agent Agreement.

### **Partial Redemption of Bonds**

Upon surrender of Bonds redeemed in part only, the City shall execute and the Fiscal Agent shall authenticate and deliver to the owner, at the expense of the City, a new Bond or Bonds, of the same maturity, of authorized denominations in aggregate principal amount equal to the unredeemed portion of the Bond or Bonds.

### **Effect of Redemption of Bonds**

From and after the date fixed for redemption, if notice of such redemption shall have been duly given as provided in the Fiscal Agent Agreement and funds available for the payment of the principal of and interest (and premium, if any) on the Bonds so called for redemption shall have been duly provided, such Bonds so called shall cease to be entitled to any benefit under the Fiscal Agent Agreement other than the right to receive payment of the redemption price, and no interest shall accrue thereon on or after the redemption date specified in such notice.

### **Defeasance**

The City shall have the option to pay and discharge the entire indebtedness on all or any portion of the Bonds (including the principal due on the Bonds on any date as a result of a scheduled mandatory sinking fund redemption) in any one or more of the following ways:

- (a) by paying or causing to be paid the principal of, and interest and any premium on, such outstanding Bonds, as and when the same become due and payable;
- (b) by depositing with the Fiscal Agent or another escrow agent, in trust, at or before maturity, money which, together with, in the event of a discharge of all of the Bonds, the amounts then on deposit in the funds and accounts provided for in the Fiscal Agent Agreement is fully sufficient to pay such outstanding Bonds, including all principal, interest and redemption premiums; or
- (c) by irrevocably depositing with the Fiscal Agent or another escrow agent, in trust, cash and noncallable Defeasance Obligations (as defined below) in such amount as the City shall determine as confirmed by an independent certified public accountant will, together with the interest to accrue thereon and, in the event of a discharge of all of the Bonds, moneys then on deposit in the fund and accounts provided for in the Fiscal Agent Agreement, be fully sufficient to pay and discharge the indebtedness on such Bonds (including all principal, interest and redemption premiums) at or before their respective maturity dates.

If the City shall have taken any of the actions specified in (a), (b) or (c) above, and if such Bonds are to be redeemed prior to the maturity thereof notice of such redemption shall have been given as in the Fiscal Agent Agreement provided or provision satisfactory to the Fiscal Agent shall have been made for the giving of such notice, then, at the election of the City, and notwithstanding that any Bonds shall not have been surrendered for payment, the pledge of the funds and moneys provided for in the Fiscal Agent Agreement and all other obligations of the City under the Fiscal Agent Agreement with respect to such outstanding Bonds shall cease and



terminate. Notwithstanding the foregoing, the obligation of the City to pay or cause to be paid to the owners of the Bonds not so surrendered and paid all sums due thereon and all amounts owing to the Fiscal Agent pursuant to the Fiscal Agent Agreement shall continue in any event.

**“Defeasance Obligations”** means any of the following which at the time acquired or made are legal investments for the City, under applicable State laws and the Investment Policy (unless compliance with the City Investment Policy is waived in writing by the Director of Finance of the City), for the moneys held hereunder then proposed to be invested therein:

- (a) Cash;
- (b) Non-callable United States Treasury notes, bonds, bills or certificates of indebtedness or those for which the faith and credit of the United States are pledged for the payment of principal and interest;
- (c) Direct non-callable obligations of the Treasury which have been stripped by the Treasury itself, CATS, TIGRS and similar securities;
- (d) The interest component of Resolution Funding Corporation strips which have been stripped by request to the Federal Reserve Bank of New York in book entry form;
- (e) Pre-refunded municipal bonds provided that the pre-refunded municipal bonds must have been pre-refunded with cash, direct Federal obligations or U.S. obligations guaranteed by the Federal government; and
- (f) non-callable bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following federal agencies and provided such obligations are backed by the full faith and credit of the United States of America (stripped securities are only permitted if they have been stripped by the agency itself): (i) direct obligations or fully guaranteed certificates of beneficial ownership of the U.S. Export-Import Bank; (ii) certificates of beneficial ownership of the Rural Economic Community Development Administration (formerly the Farmers Home Administration); (iii) obligations of the Federal Financing Bank; (iv) debentures of the Federal Housing Administration; (v) participation certificates of the General Services Administration; (vi) guaranteed Title XI financings of the U.S. Maritime Administration; and (vii) project notes, local authority bonds, new communities debentures and U.S. public housing notes and bonds of the U.S. Department of Housing and Urban Development.

## **Registration, Transfer and Exchange of Bonds**

The Fiscal Agent shall keep or cause to be kept sufficient books for the registration and transfer of the Bonds, which shall at all times be open to inspection by the City upon reasonable notice; and, upon presentation for such purpose, the Fiscal Agent shall, under such reasonable regulations as it may prescribe, register or transfer or cause to be registered or transferred, on said books, the Bonds.



## Events of Defaults and Remedies

The following constitute Events of Default under the Fiscal Agent Agreement:

(a) if default shall be made by the City in the due and punctual payment of the principal of or redemption premium, if any, on any Bond when and as the same shall become due and payable, whether at maturity as therein expressed or by declaration or otherwise; or

(b) if default shall be made by the City in the due and punctual payment of any installment of interest on any Bond when and as such interest installment shall become due and payable.

Upon the occurrence of an Event of Default, any bondowner shall have the right, for the equal benefit and protection of all bondowners similarly situated:

(a) by mandamus, suit, action or proceeding, to compel the City and its members, officers, agents or employees to perform each and every term, provision and covenant contained in the Fiscal Agent Agreement and in the Bonds, and to require the carrying out of any or all such covenants and agreements of the City and the fulfillment of all duties imposed upon it; or

(b) by suit, action or proceeding in equity, to enjoin any acts or things which are unlawful, or the violation of any of the bondowners' rights.

Nothing in the Fiscal Agent Agreement, or in the Bonds, shall affect or impair the obligation of the City, which is absolute and unconditional, to pay the principal of and interest on the Bonds to the respective owners of the Bonds at the respective dates of maturity, or affect or impair the right of action, which is also absolute and unconditional, of such bondowners to institute suit to enforce such payment by virtue of the contract embodied in the Bonds. A waiver of any default by any bondowner shall not affect any subsequent default or impair any rights or remedies on the subsequent default. No delay or omission of any owner of any of the Bonds to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed to be a waiver of any such default or an acquiescence therein, and every power and remedy conferred upon the bondowners by the Fiscal Agent Agreement may be enforced and exercised from time to time and as often as shall be deemed expedient by the owners of the Bonds.

If a suit, action or proceeding to enforce any right or exercise any remedy be abandoned or determined adversely to the bondowners, the City and the bondowners shall be restored to their former positions, rights and remedies as if such suit, action or proceeding had not been brought or taken.

No remedy conferred upon the owners of Bonds under the Fiscal Agent Agreement shall be exclusive of any other remedy and that each and every remedy shall be cumulative and shall be in addition to every other remedy given hereunder or thereafter conferred on the bondowners.



## Amendments to Fiscal Agent Agreement

The Fiscal Agent Agreement and the rights and obligations of the City and of the owners of the Bonds may be modified or amended at any time by a Supplemental Fiscal Agent Agreement pursuant to the affirmative vote at a meeting of owners, or with the written consent without a meeting, of the owners of at least a majority in aggregate principal amount of the Bonds then outstanding, exclusive of Bonds disqualified as provided in the Fiscal Agent Agreement. No such modification or amendment shall (i) extend the maturity of any Bond or reduce the interest rate thereon, or otherwise alter or impair the obligation of the City to pay the principal of, and the interest and any premium on, any Bond, without the express consent of the owner of such Bond, or (ii) permit the creation by the City of any pledge or lien upon the *ad valorem* taxes of the taxes superior to or on a parity with the pledge and lien created for the benefit of the Bonds (except as otherwise permitted by the Act, the laws of the State or the Fiscal Agent Agreement), or reduce the percentage of Bonds required for the amendment of the Fiscal Agent Agreement. Any such amendment may not modify any of the rights or obligations of the Fiscal Agent without its written consent.

The Fiscal Agent Agreement and the rights and obligations of the City and of the bondowners may also be modified or amended at any time by a Supplemental Fiscal Agent Agreement, without the consent of any owners, only to the extent permitted by law and only for any one or more of the following purposes:

- (a) to add to the covenants and agreements of the City in the Fiscal Agent Agreement contained, other covenants and agreements thereafter to be observed, or to limit or surrender any right or power reserved to or conferred upon the City;
- (b) to make such provisions for the purpose of curing any ambiguity, or of curing, correcting or supplementing any defective provision contained in the Fiscal Agent Agreement, or in regard to questions arising under the Fiscal Agent Agreement, as the City and the Fiscal Agent may deem necessary or desirable and not inconsistent with the Agreement, and which shall not adversely affect the rights of the owners of the Bonds; and
- (c) to make such additions, deletions or modifications as may be necessary or desirable to assure compliance with Section 148 of the Code or otherwise as may be necessary to assure exclusion from gross income for federal income tax purposes of interest on the Series 2019A-1 Bonds and Series 2019C Bonds or to conform with the Regulations.



## DEBT SERVICE SCHEDULE

The following table shows the annual debt service schedule on the Bonds on an individual series basis, assuming no optional redemption thereof prior to maturity.

	Series 2019A-1 Bonds		Taxable Series 2019A-2 Bonds		Taxable Series 2019B Bonds		Series 2019C Bonds		Taxable Series 2019D Bonds		
Period Ending	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Principal	Interest	Aggregate Annual Debt Service

Total



## **CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS**

*Principal of and interest on the Bonds are payable from the proceeds of an ad valorem tax levied by the City for the payment thereof. See “THE BONDS — Security for the Bonds” herein. Articles XIII A, XIII B, XIII C and XIII D of the Constitution, and certain other provisions of law discussed below, are included in this section to describe the potential effect of these Constitutional and statutory provisions on the ability of the City to levy taxes and spend tax proceeds for operating and other purposes, and it should not be inferred from the inclusion of such materials that these laws impose any limitation on the ability of the City to levy taxes for payment of the Bonds. The tax levied by the City for payment of the Bonds was approved by the City’s voters in compliance with Article XIII A and all applicable laws.*

*The discussion of the Constitutional and statutory provisions and judicial decisions interpreting these provisions below is not intended to be an exhaustive analysis of these provisions.*

### **Article XIII A of the State Constitution**

Article XIII A of the State Constitution, known as Proposition 13, was approved by the voters in June 1978 and has been amended on occasions, including most recently on November 7, 2000 to reduce the voting percentage required for the passage of school bonds. Section 1(a) of Article XIII A limits the maximum *ad valorem* tax on real property to 1% of “full cash value,” and provides that such tax shall be collected by the counties and apportioned according to State statutes. Section 1(b) of Article XIII A provides that the 1% limitation does not apply to *ad valorem* taxes levied to pay interest or redemption charges on any (1) indebtedness approved by the voters prior to July 1, 1978, (2) bonded indebtedness for the acquisition or improvement of real property approved on or after July 1, 1978, by two-thirds of the votes cast by the voters voting on the proposition and (3) bonded indebtedness incurred by a school district, community college or county office of education district for the construction, reconstruction, rehabilitation or replacement of school facilities, including the furnishing and equipping of school facilities or the acquisition or lease of real property for school facilities, approved by 55% of the voters voting on the proposition.

Section 2 of Article XIII A defines “full cash value” to mean the county assessor’s valuation of real property as shown on the fiscal year 1975-76 tax bill, or thereafter, the appraised value of real property when purchased, newly constructed, or a change in ownership has occurred. The full cash value may be adjusted annually to reflect inflation at a rate not to exceed 2% per year, or to reflect a reduction in the consumer price index or comparable data for the taxing jurisdiction, or may be reduced in the event of declining property value caused by substantial damage, destruction or other factors. Section 51 of the Revenue and Taxation Code permits County assessors who have reduced the assessed valuation of a property as a result of natural disasters, economic downturns or other factors, to subsequently “recapture” such value (up to the pre-decline value of the property) at an annual rate higher than two percent, depending on the assessor’s measure of the restoration of value of the damaged property. The California courts have upheld the constitutionality of this procedure. Legislation enacted by the State Legislature to implement Article XIII A provides that, notwithstanding any other law, local agencies may not levy any *ad valorem* property tax except the one percent base tax levied by each County and taxes to pay debt service on indebtedness approved by the voters as described above.



Since its adoption, Article XIII A has been amended a number of times. These amendments have created a number of exceptions to the requirement that property be reassessed when it is purchased, newly constructed or undergoes a change in ownership. These exceptions include certain transfers of real property between family members, certain purchases of replacement dwellings for persons over age 55 and by property owners whose original property has been destroyed in a declared disaster, and certain improvements to accommodate disabled persons and for seismic upgrades to property.

Both the State Supreme Court and the United States Supreme Court have upheld the validity of Article XIII A. For further information regarding pending reductions in assessed valuations of property located in the City, please see APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MAJOR GENERAL FUND REVENUE SOURCES – Assessed Values and Property Taxes” herein.

### **Article XIII B of the State Constitution**

**General.** In addition to the limits Article XIII A imposes on property taxes that may be collected by local governments, certain other revenues of the State and most local governments are subject to an annual “appropriations limit” imposed by Article XIII B which effectively limits the amount of such revenues those entities are permitted to spend. Article XIII B, approved by the voters in June 1979, was modified substantially by Proposition 111 in 1990. The appropriations limit of each government entity applies to “proceeds of taxes,” which consist of tax revenues, State subventions and certain other funds, including proceeds from regulatory licenses, user charges or other fees to the extent that such proceeds exceed “the cost reasonably borne by such entity in providing the regulation, product or service.” “Proceeds of taxes” excludes tax refunds and some benefit payments such as unemployment insurance. No limit is imposed on the appropriation of funds which are not “proceeds of taxes,” such as reasonable user charges or fees, and certain other non-tax funds. Article XIII B also does not limit appropriation of local revenues to pay debt service on Bonds existing or authorized by January 1, 1979, or subsequently authorized by the voters, appropriations required to comply with mandates of courts or the federal government, appropriations for qualified capital outlay projects, and appropriation by the State of revenues derived from any increase in gasoline taxes and motor vehicle weight fees above January 1, 1990, levels. The appropriations limit may also be exceeded in case of emergency; however, the appropriations limit for the next three years following such emergency appropriation must be reduced to the extent by which it was exceeded, unless the emergency arises from civil disturbance or natural disaster declared by the Governor, and the expenditure is approved by two-thirds of the legislative body of the local government.

The State and each local government entity has its own appropriations limit. Each year, the limit is adjusted to allow for changes, if any, in the cost of living, the population of the jurisdiction, and any transfer to or from another government entity of financial responsibility for providing services.

Proposition 111 requires that each agency's actual appropriations be tested against its limit every two years. If the aggregate “proceeds of taxes” for the preceding two-year period exceeds the aggregate limit, the excess must be returned to the agency's taxpayers through tax rate or fee reductions over the following two years.

The City has never exceeded its appropriations limit.



## Articles XIII C and XIII D of the State Constitution

**General.** On November 5, 1996, the voters of the State approved Proposition 218, known as the “Right to Vote on Taxes Act.” Proposition 218 added Articles XIII C and XIII D to the California Constitution and contains a number of interrelated provisions affecting the ability of the City to levy and collect both existing and future taxes, assessments, fees and charges. The interpretation and application of Proposition 218 will ultimately be determined by the courts with respect to a number of the matters discussed below, and it is not possible at this time to predict with certainty the outcome of such determination.

On November 2, 2010, California voters approved Proposition 26, known as the “Supermajority Vote to Pass New Taxes and Fees Act.” Section 1 of Proposition 26 declares that Proposition 26 is intended to limit the ability of the State Legislature and local government to circumvent existing restrictions on increasing taxes by defining the new or expanded taxes as “fees.” Proposition 26 amended Articles XIII A and XIII C of the State Constitution. The amendments to Article XIII A limit the ability of the State Legislature to impose higher taxes (as defined in Proposition 26) without a two-thirds vote of the Legislature. With respect to local governments such as the City, Proposition 26’s amendments to Article XIII C broadly define “tax,” but specifically exclude, among other things:

- “(1) A charge imposed for a specific benefit conferred or privilege granted directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of conferring the benefit or granting the privilege.
- (2) A charge imposed for a specific government service or product provided directly to the payor that is not provided to those not charged, and which does not exceed the reasonable costs to the local government of providing the service or product.
- ...
- (6) A charge imposed as a condition of property development.
- (7) Assessments and property-related fees imposed in accordance with the provisions of Article XIII D.”

Article XIII C also removes limitations on the initiative power in matters of reducing or repealing local taxes, assessments, fees or charges. No assurance can be given that the voters of the City will not, in the future, approve an initiative or initiatives which reduce or repeal local taxes, assessments, fees or charges currently comprising a substantial part of the City’s General Fund.

**Article XIII C.** Article XIII C requires that all new local taxes be submitted to the electorate before they become effective. Taxes for general governmental purposes of the City require a majority vote and taxes for specific purposes, even if deposited in the City’s General Fund, require a two-thirds vote. The voter approval requirements of Article XIII C reduce the flexibility of the City to raise revenues for the General Fund, and no assurance can be given that the City will be able to impose, extend or increase such taxes in the future to meet increased expenditure needs.

**Article XIII D.** Article XIII D also adds several provisions making it generally more difficult for local agencies to levy and maintain property-related fees, charges, and assessments for municipal services and programs. These provisions include, among other things, (i) a prohibition against assessments which exceed the reasonable cost of the proportional special benefit



conferred on a parcel, (ii) a requirement that assessments must confer a “special benefit,” as defined in Article XIID, over and above any general benefits conferred, (iii) a majority protest procedure for assessments which involves the mailing of notice and a ballot to the record owner of each affected parcel, a public hearing and the tabulation of ballots weighted according to the proportional financial obligation of the affected party, and (iv) a prohibition against fees and charges which are used for general governmental services, including police, fire or library services, where the service is available to the public at large in substantially the same manner as it is to property owners. If the City were unable to continue to collect the property-related fees or assessments currently collected by the City, the services and programs funded with these revenues would have to be curtailed and/or the City’s General Fund might have to be used to support them. The City is unable to predict whether or not in the future it will be able to continue all existing services and programs funded by the fees, charges and assessments in light of Article XIID or, if these services and programs are continued, which amounts (if any) would be used from the City’s General Fund to continue to support these activities.

**Judicial Interpretation of Articles XIIC and XIID.** On April 12, 2002, the California Court of Appeal in *Howard Jarvis Taxpayers Association v. City of Roseville* (97 Cal. App. 4<sup>th</sup> 637; 98 Cal. App. 4<sup>th</sup> 476D (as modified on denial of rehearing on May 13, 2002; California Supreme Court review denied on July 10, 2002) (“**Roseville**”) held that the City of Roseville’s practice of charging “in-lieu franchise fees” against the budgets of the City-operated municipal utilities violated Article XIID. Annually, the City of Roseville transferred from the enterprise accounts for each of its water, refuse collection and sewer service utilities to its general fund an amount equivalent to 4% of each utility’s annual budget. The basis for these budgetary transfers was that if these utilities were privately operated, the city would receive a franchise fee to compensate it for the use of city streets and rights-of-way.

The *Roseville* court ruled that the “in-lieu franchise fees” were subject to Article XIID’s restrictions on “property-related” fees because the City of Roseville charged for water, refuse collection and sewer service regardless of whether the property owner used the particular service. Because the transfer from each utility’s enterprise account was a flat rate of 4% of the utility’s annual budget, the *Roseville* court also ruled that these budgetary transfers violated Proposition 218’s requirements that a property-related fee cannot exceed the amount necessary to provide the particular service and cannot be imposed to fund general governmental services, such as police, fire and the like. In rendering its decision, the *Roseville* court distinguished an earlier California appellate decision, *Howard Jarvis Taxpayers Assn. v. City of Los Angeles* (2000) 85 Cal. App. 4<sup>th</sup> 79 (“**Jarvis-L.A.**”). In *Jarvis-L.A.*, the court determined that the charges imposed by the Los Angeles Department of Water and Power were based on water consumption and as such were “commodity charges which do not fall within the scope of Proposition 218.”

On June 3, 2002, the California Court of Appeal in *Howard Jarvis Taxpayers Association v. City of Salinas*, 98 Cal. App. 4<sup>th</sup> 1351 (rehearing denied on July 2, 2002; California Supreme Court review denied on August 28, 2002) (“**Salinas**”) held that the City of Salinas’s imposition of storm drain fees without voter approval violated section 6(c) of Article XIID. In rendering its decision the *Salinas* Court held that (i) the Salinas storm drain fees were property-related fees subject to Article XIID’s requirements and (ii) these fees were not exempt from voter approval as “sewer fees.” The *Salinas* court, in holding that the imposition of storm drain fees required voter approval, determined that the voters in approving Article XIID intended that Article XIID’s exemption of sewer fees from voter approval applied only to the imposition of, or increases to, sanitary sewer fees.



The California Legislature in 2017 enacted SB 231, effective on January 1, 2018, to amend California Government Code provisions, known as “The Proposition 218 Omnibus Implementation Act.” The Proposition 218 Omnibus Implementation Act prescribes specific procedures and parameters for local jurisdictions in order to comply with Articles XIII C and XIII D and defines terms for these purposes. SB 231 amended Government Code Section 53750 to define sewer to include both storm and sanitary sewers and to set forth in Government Code Section 53751 certain findings of the Legislature concerning the Salinas court’s interpretation of the sewer for purposes of Article XIII D. There is no reported decision of a California appellate court applying the Government Code provisions enacted by SB 231 to a storm sewer fee and the City cannot predict, if or how, a California appellate court or the California Supreme Court, would apply these provisions.

Unlike the City of Salinas, the City imposed a storm sewer fee prior to the passage of Proposition 218. In 1999, the City’s storm sewer fees were restructured, without voter approval, in order to meet Article XIII D’s sewer fee requirements. Subsequent storm sewer fee increases have been adopted in accordance with Article XIII D’s requirements for sewer fee increases. In the event a court were to determine that despite the City’s restructuring of its storm sewer fees to meet Article XIII D’s sewer fee requirements, the City’s storm sewer fee increases require voter approval under Article XIII C, then the fees imposed after the passage of Proposition 218 could be at risk.

In July 2006, the California Supreme Court, in *Bighorn-Desert View Water Agency v. Verjil* (2006) 39 Cal. 4th 205 (“**Bighorn**”), addressed the validity of a local voter initiative measure that would have (a) reduced a water agency’s rates for water consumption (and other water charges), and (b) required the water agency to obtain voter approval before increasing any existing water rate, fee, or charge, or imposing any new water rate, fee, or charge. The *Bighorn* court held that the water agency’s charges for ongoing water delivery were “fees and charges” within the meaning of Article XIII D, and went on to hold that charges for ongoing water delivery which are fees and charges within the meaning of Article XIII D are also “fees” within the meaning of Article XIII C’s mandate that the initiative power of the electorate cannot be prohibited or limited in matters of reducing or repealing any local tax, assessment, fee or charge. Therefore, the court held that Article XIII C authorizes local voters to adopt an initiative measure that would reduce or repeal a public agency’s water rates and other water delivery charges. In reaching its decision, the *Bighorn* court expressly disapproved the *Jarvis-L.A.* decision discussed above, “to the extent that it was inconsistent” with its conclusion that charges for water delivery service are charges for a property-related service “whether the charge is calculated on the basis of consumption or is imposed as a fixed monthly fee.”

However, the court ultimately ruled in favor of the water agency and held that the entire initiative measure was invalid on the grounds that the second part of the initiative measure, which would have subjected future water rate increases to prior voter approval, was not supported by Article XIII C and was therefore invalid.

On April 20, 2015, the California Court of Appeal issued an opinion in *Capistrano Taxpayers Association, Inc. v. City of San Juan Capistrano* (“**Capistrano**”), 235 Cal.App.4th 1493 (as modified on May 19, 2015), upholding tiered water rates under Article XIII D provided that the tiers correspond to the actual cost of furnishing service at a given level of usage. The opinion was specific to the facts of the case, including a finding that the City of San Juan Capistrano did not attempt to calculate the actual costs of providing water at various tier levels.



**City's Current Practices.** The City has complied with Article XIID's noticing and protest procedure requirements for all sanitary and storm sewer rate increases that have been implemented since passage of Proposition 218. With respect to the City's municipal water utility, known as "San José Municipal Water", these noticing and protest procedures are also being followed for rate increases implemented after the *Bighorn* decision, even though the City, unlike the agency involved in *Bighorn*, does not collect delinquent charges through a property lien process.

Subsequent to the *Capistrano* decision, the City conducted a cost of service study for San José Municipal Water and in fiscal year 2017-18 implemented a new rate structure eliminating the prior tiered rate structure for residential customers, adjusting the percentage of costs recovered on a fixed basis through meter charges instead of the quantity charge for water, establishing quantity rates based on the cost of water supply in three service areas, and revising the reserves and reserve levels.

In the past, the City has made budgetary transfers from its municipal utilities to the City's General Fund similar to those described in the *Roseville* decision. For fiscal year 2007-08 the amount transferred was approximately \$4.6 million. For fiscal year 2008-09 the amount transferred was reduced to approximately \$2.8 million. For fiscal years 2009-10 through 2017-18, the City did not make any such transfers, and the City has no plans to make any such transfers in the future.

In June 2018, the trial court in two consolidated class action lawsuits against the City on behalf of current and former customers of San José Municipal Water challenging the fees charged for water service from 1997 to 2016 issued its decision denying the relief sought by the plaintiffs and de-certifying the class. The trial court's decision is currently pending appeal by the plaintiffs and cross-appeal by the City. A separate lawsuit filed by the same plaintiffs challenging the San José Municipal Water fees charged during fiscal year 2015-16 remains pending in the trial court. See APPENDIX A – "THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND CONSENT DECREES – Potentially Significant Litigation" for additional information.

## **Proposition 62**

On November 4, 1986, California voters adopted Proposition 62, a statutory initiative which, among other matters, requires: (a) that any tax for general governmental purposes imposed by local government entities be approved by a majority vote of the voters voting in an election on the issue, (b) that any special tax (defined as taxes levied for other than general governmental purposes) imposed by a local government entity be approved by a two-thirds of the voters voting in an election on the issue and (c) the revenues from a special tax be used for the purposes or for the services for which the special tax was imposed. Proposition 62 also provided that any tax imposed by any local government after August 1, 1985 and prior to November 5, 1986 (the effective date of proposition 62) can continue to be imposed only if approved by a majority vote of the voters voting in an election on the issue, and that any local government which fails to seek or obtain such approval shall cease to impose such tax on and after November 15, 1988.

Following its adoption by the voters, various provisions of Proposition 62 were declared unconstitutional by the appellate court level. On September 28, 1995, however, the California Supreme Court, in *Santa Clara County Local Transportation Authority v. Guardino*, 11 Cal. 4<sup>th</sup>



220 (1995) (“*Guardino*”), upheld the constitutionality of the portion of Proposition 62 requiring a two-thirds vote in order for a local government or district to impose a special tax, and by implication, upheld a parallel provision requiring a majority vote in order for a local government or district to impose any general tax. The *Guardino* decision did not address the question of whether or not Proposition 62 should be applied retroactively to taxes imposed during the period that certain of its provisions were held to be unconstitutional.

Following the *Guardino* decision several actions were filed challenging taxes imposed by public agencies after the adoption of Proposition 62. On June 4, 2001, the California Supreme Court rendered its opinion in *Howard Jarvis Taxpayers Association v. City of La Habra, et al.*, 25 Cal. 4th 809 (“*La Habra*”) holding that an action brought in 1996 challenging the imposition of a 1992 utility users tax imposed for general purposes, without voter approval, was not barred by a three-year statute of limitations period because the continued imposition and collection of the tax was an ongoing violation upon which the statute of limitations period began anew with each collection.

The *Guardino* and *La Habra* decisions did not decide the question of the applicability of Proposition 62 to charter cities such as the City. Two cases decided by the California Courts of Appeals in 1993, *Fielder v. City of Los Angeles* (1993) 14 Cal. App. 4th 137 (rev. den. May 27, 1993), and *Fisher v. County of Alameda* (1993) 20 Cal. App. 4th 120 (rev. den. Feb. 24, 1994) hold that Proposition 62’s restrictions on property transfer taxes do not apply to charter cities because charter cities derive their power to enact taxes under Article XI, Section 5 of the California Constitution relating to municipal affairs.

The City estimates that approximately \$63.8 million has been collected from June 30, 2015 through June 30, 2018 as a result of new or increased taxes imposed without voter approval between August 1, 1985 and January 1, 1995, the date on which the provisions of Proposition 218 applicable to voter approval of taxes were effective. Such increased or new taxes include hotel and business taxes (“**Post Proposition 62 Taxes**”).

If a court were to determine that a jurisdiction imposed a new or increased tax in violation of Proposition 62, Proposition 62 specifies that the portion of the one-percent ad valorem property tax levy allocated to that jurisdiction be reduced by \$1 for every \$1 in revenue attributable to the tax for each year that the tax is collected. This provision of Proposition 62 has not been interpreted by the California courts.

Proposition 62, is an initiative statute, does not have the same level of authority as a constitutional initiative, but is analogous to legislation adopted by the State Legislature (except that it may be amended only by a vote of the State’s electorate). However, Proposition 218, as a constitutional amendment, is applicable to charter cities and supersedes many of the provisions of Proposition 62 with respect to taxes imposed after January 1, 1995.

## **Proposition 1A**

Proposition 1A, proposed by the Legislature in connection with the State’s Fiscal Year 2004-05 Budget, approved by the voters in November 2004 and generally effective in fiscal year 2006-07, provides that the State may not reduce any local sales tax rate, limit existing local government authority to levy a sales tax rate or change the allocation of local sales tax revenues, subject to certain exceptions. Proposition 1A generally prohibits the State from shifting to schools or community colleges any share of property tax revenues allocated to local governments for any fiscal year, as set forth under the laws in effect as of November 3, 2004.



Any change in the allocation of property tax revenues among local governments within a county must be approved by two-thirds of both houses of the Legislature. Proposition 1A provides, however, that beginning in fiscal year 2008-09, the State may shift to schools and community colleges up to 8% of local government property tax revenues, which amount must be repaid, with interest, within three years, if the Governor proclaims that the shift is needed due to a severe state financial hardship, the shift is approved by two-thirds of both houses and certain other conditions are met. The State may also approve voluntary exchanges of local sales tax and property tax revenues among local governments within a county. Proposition 1A also provides that if the State reduces the motor vehicle license fee rate currently in effect, 0.65 percent of vehicle value, the State must provide local governments with equal replacement revenues. Further, Proposition 1A requires the State, beginning July 1, 2005, to suspend State mandates affecting cities, counties and special districts, excepting mandates relating to employee rights, schools or community colleges, in any year that the State does not fully reimburse local governments for their costs to comply with such mandates.

Proposition 1A may result in increased and more stable City revenues. The magnitude of such increase and stability is unknown and would depend on future actions by the State. However, Proposition 1A could also result in decreased resources being available for State programs. This reduction, in turn, could affect actions taken by the State to resolve budget difficulties. Such actions could include increasing State taxes, decreasing spending on other State programs or other action, some of which could be adverse to the City.

## **Proposition 22**

Proposition 22, entitled “The Local Taxpayer, Public Safety and Transportation Protection Act,” was approved by the voters of the State in November 2010. Proposition 22 amended the state Constitution to eliminate or reduce the State’s authority to (i) temporarily shift property taxes from cities, counties and special districts to schools, (ii) use vehicle license fee revenues to reimburse local governments for State-mandated costs (the State will have to use other revenues to reimburse local governments), (iii) redirect property tax increment from redevelopment agencies to any other local government, (iv) use State fuel tax revenues to pay debt service on State transportation bonds, or (v) borrow or change the distribution of State fuel tax revenues. Notwithstanding the passage of Proposition 22, the State successfully dissolved redevelopment agencies. See the discussion of the impact on the City of the redevelopment agency dissolution in Appendix A.

## **Possible Future Actions**

Propositions 62, 111, 218, 26, 1A and 22 were each adopted as measures that qualified for the ballot pursuant to the State’s initiative process. From time to time other initiative measures could be adopted, further affecting revenues of the City or the City’s ability to expend revenues. There is no assurance that the California electorate or Legislature will not at some future time approve additional limitations.



## CERTAIN RISK FACTORS

The following discussion of certain risk factors is not meant to be an exhaustive list of the risks associated with the purchase of the Bonds and does not necessarily reflect the relative importance of the various risks. Potential investors are advised to consider the following factors along with all other information in this Official Statement in evaluating the investment quality of the Bonds.

### Factors Affecting Property Tax Security for the Bonds

The annual property tax rate for repayment of the Bonds will be based on the total assessed value of taxable property in the City and the scheduled debt service on the Bonds in each year. Fluctuations in the annual debt service on the Bonds and the assessed value of taxable property in the City may cause the annual property tax rate applicable to the Bonds to fluctuate. Issuance by the City of additional authorized bonds payable from *ad valorem* property taxes may cause the overall property tax rate to increase.

In addition, the following risk factors may affect the City's ability to levy and collect sufficient taxes to pay scheduled debt service on the Bonds each year:

**Total Assessed Value of Taxable Property in the City.** The greater the assessed value of taxable property in the City, the lower the tax rate necessary to generate taxes sufficient to pay scheduled debt service on bonds. The net total assessed valuation of taxable property in the City in fiscal years 2018-19 is approximately \$182 billion. During economic downturns, declining market value of real estate, increased foreclosures, and increases in requests submitted to the Assessor and the Assessment Appeals Board for reductions in assessed value have generally caused a reduction in assessed value of some properties in the City. See APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – Assessed Values and Property Taxes” for information regarding the assessed values of property in the City for fiscal year 2018-19 and the previous ten fiscal years, and a list of the ten largest property taxpayers for fiscal year 2018-19 based on secured assessed valuations within the City.

Natural and economic forces can affect the assessed value of taxable property in the City. The City is located in a seismically active region, and damage from an earthquake in or near the City could cause moderate to extensive or total damage to taxable property. Other natural or man-made disasters, such as floods, climate change, fire, toxic dumping or acts of terrorism, could also cause a reduction in the assessed value of taxable property within the City. See “Development Risks” and “Environmental Risks” below.

**Concentration of Taxable Property Ownership.** The more property (by assessed value) is owned by a single assessee, the more exposure of tax collections to weakness in that taxpayer's financial condition and ability or willingness to pay property taxes. With respect to assessed values for fiscal year 2018-2019, no single assessee owned more than 0.69% of total taxable assessed value in the City. See APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MAJOR GENERAL FUND REVENUE SOURCES – Assessed Values and Property Taxes” herein.

**Property Tax Rates.** A factor in the ability of taxpayers to pay additional taxes for general obligation bonds such as the Bonds is the cumulative rate of tax. The total tax rate per \$100 of assessed value (including the *ad valorem* 1% rate required under Article IIIA) received



by the City is described in APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MAJOR GENERAL FUND REVENUE SOURCES – Assessed Values and Property Taxes” herein.

***Debt Burden on Owners of Taxable Property in the City.*** Another measure of the debt burden on taxpayers is total debt as a percentage of taxable property value. The Charter limits bonded indebtedness for general obligation bonds to 15% of the total assessed valuation of all real and personal property within the City. The total assessed value of taxable property on the City’s 2018-2019 tax roll was approximately \$182 billion, which results in a total debt limit of approximately \$27.3 billion. As of June 30, 2018, the City had outstanding approximately \$342.8 million in general obligation bonds, or approximately 0.2% of the total assessed value of taxable property on the for fiscal year 2018-2019. See APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MAJOR GENERAL FUND REVENUE SOURCES – Assessed Values and Property Taxes” herein.

***Additional Debt; Authorized but Unissued Bonds.*** Issuance of additional authorized bonds cause the overall property tax rate to increase. As of June 30, 2019, the City had voter approval to issue up to \$659.2 million in additional principal amount of bonds payable from *ad valorem* property taxes. A portion of such authorization will be reduced by the issuance of the Series 2019A Bonds, the Taxable Series 2019B Bonds, and the Series 2019C Bonds. See APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – BONDED AND OTHER INDEBTEDNESS.”

## **Development Risks**

***General.*** Economic forces can affect the assessed value of taxable property in the City.

The general economy of the City will also be subject to all of the risks generally associated with urban real estate development projects. Real estate development operations may be adversely affected by changes in general economic conditions, fluctuations in the real estate market and interest rates, unexpected increases in development costs and by other similar factors. Further, real estate development operations within the City could be adversely affected by limitations of infrastructure or future governmental policies, including governmental policies to restrict or control development.

In addition, if there is a decline in the general economy of the City, the owners of property within the City may be less able or less willing to make timely payments of property taxes or petition to reduce assessed valuation causing a delay in or reduce the property taxes received by the City. At various times, the contraction of the technology business sector has led to significant reductions in property values both in Silicon Valley and in the City. The continued importance of technology business to the area economy may continue to affect property values. See “– Trade Policy” for a discussion of recent trade tariffs with China which could have a negative impact on the local economy.

Historical patterns in the City also suggest that assessed value increases and decreases in the City may lag economic conditions. For example, assessed values in the City continued to increase for two fiscal years following the significant economic decline that began in April 2000 (commonly referred to as the “dot com bust”).

In addition, the total assessed value can be reduced through the reclassification of taxable property to a class exempt from taxation, whether by ownership or use (such as



exemptions for property owned by State and local agencies and property used for qualified educational, charitable or religious purposes.

**Governmental Policy Risks.** Development in the City may be limited by the City's General Plan and subordinate land use policies that could affect when land may be developed for particular uses, particularly residential development. Additionally, the City charges a number of area wide mitigation fees in addition to project-specific mitigation fees and may consider the imposition of other fees. Other issues, such as the availability of water supply to certain areas of the City, may also adversely affect the pace of development. See "– Water Supply Risks" below.

**Water Supply Risks.** Because water is supplied to the City from imported sources purchased from wholesalers, as well as local groundwater, Statewide and local conditions could impact the availability of water supply for future development in the City. Imported water supplies to portions of the City include: water that is delivered by the San Francisco Public Utilities Commission ("**SFPUC**") to the San José Municipal Water System ("**SJMWS**"); water from the State Water Project ("**SWP**") and Central Valley Project ("**CVP**") that is delivered by the Santa Clara Valley Water District to water retailers in the City; and water transfers that may be delivered by both wholesalers to retailers in the City. All of these sources of supply are subject to limitations during periods of drought. On a long-term basis, supplies may also be limited due to the impacts of climate change. The supply of SWP and CVP water is also subject to regulatory constraints imposed to manage flows and water quality in the Sacramento-San Joaquin River Delta. In addition, the supply of SFPUC water to SJMWS for service in North San José is limited by two July 2009 contracts: (i) an individual water sales contract between the City and County of San Francisco and the City; and (ii) a master wholesale contract between the City and County of San Francisco and all wholesale customers, including the City. Under these contracts, the supply of water could be interrupted by the supplier thereof in certain circumstances. The 2009 master wholesale contract is in the process of being amended, but without a change to the general structure.

See also "–Environmental Risks" below.

## **Environmental Risks**

The value of the property in the City in the future can be adversely affected by a variety of factors, including environmental factors, some of which are listed below.

**Seismic Hazards.** The City is in a region of very high seismic activity. The seismically active San Francisco Bay region has been subjected to recurring large earthquakes. In 2014, the Working Group on California Earthquake Probabilities updated the 30-year earthquake forecast for California. They concluded that there is a 72 percent probability of at least one earthquake of magnitude 6.7 or greater striking somewhere in the region before 2043. Seismic hazards includes risks of (i) surface fault rupture, (ii) ground shaking and (iii) liquefaction and ground failure.

**Surface Fault Rupture.** Surface fault rupture, displacement at the earth's surface resulting from fault movement, is typically observed close to or on an active fault. There are several active faults in the greater San Francisco Bay Area that have the potential to cause serious earthquakes, which could result in damage to buildings, roads, bridges, and property within the City. Areas within the City are located within 6 to 12 miles of the Hayward, Calaveras, and San Andreas faults, all of which are known to be active faults



and pose the greatest potential for surface rupture in the Bay Area. According to the U.S. Geological Survey (“**USGS**”), the San Francisco Bay Area has experienced at least nine recorded earthquakes with a magnitude of 6.0 or greater since 1836. The South Napa earthquake with a magnitude of 6.0 according to the USGS, occurred on August 24, 2014. Prior to the South Napa earthquake, the City experienced the Loma Prieta earthquake on October 17, 1989, which had a magnitude of 6.9 according to the USGS. No significant damage was noted in the City from either the South Napa or the Loma Prieta earthquakes.

*Ground Shaking.* Ground shaking can be described in terms of peak acceleration, earthquake ground shaking intensity (Modified Mercalli Scale), and displacement of the ground. Ground shaking may affect areas hundreds of miles away from an earthquake’s epicenter. The risks to a structure from a seismic event are dependent upon several factors, including the distance of the structure from the active fault, the character of the earthquake, the nature of construction of the structure, and the geologic conditions underlying the structure. Ground surface rupture tends to occur along lines of previous faulting, where fault displacement intersects the ground surface. Displacement may either occur suddenly during an earthquake or it may occur slowly as the fault “creeps” over a long period of time. The northern segment of the Quaternary Silver Creek fault transects a portion of the downtown area of the City, east of 17th Street. The fault is buried deeply beneath alluvial deposits. Evidence of active Holocene (within the past 11,000 years) displacement of the northern segment of the Silver Creek fault is lacking (USGS, 2010). Therefore, the potential hazard of surface rupture from the Silver Creek fault in the subject area is low. The northern segment of the Silver Creek fault is not zoned for fault rupture hazard by the State or City. The potentially active Piercy fault may transect a small portion of the Edenvale area within the City. Surface rupture studies may be required by the City prior to development of any properties near mapped traces of the Piercy fault.

*Liquefaction and Ground Failure.* “Liquefaction” is the transformation of soil from a solid state to a liquid state during a major earthquake. Liquefaction hazard zones are regulatory zones where historic occurrence of liquefaction or local geologic, geotechnical and ground water conditions indicate a potential for permanent ground displacements during a major earthquake. Liquefaction may result in differential settlement, sand boils, ground fissures, lateral spreading, and other surface deformations. Pursuant to applicable State law, the California Geological Survey (“**CGS**”) has prepared maps to identify certain areas as liquefaction hazard zones. Much of the City, including the Civic Center and City Hall, is within the State of California *Seismic Hazard Zone of Required Investigation for Liquefaction* (CGS, 2002). As such, in accordance with the State of California Seismic Hazards Mapping Act, the City requires a geotechnical investigation report addressing liquefaction potential to be submitted by a land developer, for review and approval by the City Geologist, prior to approval of a development project. The report must be prepared in accordance with State guidelines. In areas of high liquefaction potential, multi-story/high rise buildings typically include the installation of various types of soil improvement structures beneath the building, or deep pile foundations, to mitigate liquefaction hazards.

The City has a variety of structures/uses that were designed with different importance factors based on occupancy, assembly, and its essential use to be operational after a seismic event. Also, many structures survived the Loma Prieta earthquake but triggered new City ordinances requiring higher levels of seismic strength,



resulting in increased building costs for development projects in the City. Many structures survived the Loma Prieta earthquake with relatively minor damage. However, unreinforced masonry structures sustained significant damage and the City created a structural seismic upgrade ordinance for property owners who own unreinforced masonry buildings. The ordinance required structural analysis to be submitted by May 1992 and complete structural upgrade or demolition to occur by November 1997.

In addition, other City ordinances amend the structural portion of the building code for more stringent requirements in consideration of near earthquake faults and geological conditions. However, one type of older structure that may be vulnerable in the event of seismic risk and that is not subject to the more stringent requirements of more recent building codes is the multifamily “soft story” structure. Soft story structures pose a particular concern because one floor of the building (usually the ground floor parking or commercial space) has significantly less lateral rigidity than stories on top. Accordingly, these buildings have a greater risk than average of collapsing during an earthquake. At the June 26, 2018 City Council meeting, Council accepted staff’s report and recommendation on potential ways to incentivize the seismic retrofit of multifamily soft story buildings in the City, and directed staff to return to Council with the framework of a mandatory multifamily soft story seismic mitigation ordinance. The staff report, referring to a study conducted in 2002 by San Jose State University’s Engineering Department, estimated that the City had approximately 1,100 soft story multifamily buildings at the time of the study.

The City is in the process of issuing a Request for Proposal for a consultant to assist the City with the drafting of the ordinance mandating the retrofitting of multifamily soft story buildings and to do an inventory identifying the number of multifamily soft story buildings in the City. At this time, it is anticipated that the Request for Proposal will be issued by June 30, 2019, and that the initial development of a soft story retrofit program will be completed by the end of fiscal year 2019-2020 with implementation to occur over several more years.

There can be no guarantee that structural seismic upgrades that have been completed or that may be completed in the future to address soft story structures are sufficient for future seismic events. Because the City is located within an area near active earthquake faults, the possibility does exist for operations to be disrupted or for structures to be damaged by a strong earthquake.

**Flood Hazards.** Flooding hazards may be considered in two categories: natural flooding and dam inundation.

Natural Flooding. Natural flooding hazards are those associated with major rainfall events, which result in the flooding of developed areas due to overflows of nearby waterways, or inadequacies in local storm drain facilities. The City and the Santa Clara Valley have a history of flooding due to heavy rain and inadequate storm drains and flood protection conveyance systems, which has resulted in property damage. The Santa Clara Valley Water District (the “**District**”) is responsible for flood protection infrastructure in the County on streams and waterways. The District coordinates flood hazard mitigation efforts for the major creeks and waterways in the City and assists the City in the review of development proposals that could impact flood protection efforts. District staff also prepare and maintain reports of severe flood events. These reports dating back to 1955 can be found on the District website under Flood Protection. *Such*



*website is not incorporated into this Official Statement. It is referenced for informational purposes only. The City and the Purchasers make no representation whatsoever as to the accuracy or completeness of any of the information on such website.*

The Federal Emergency Management Agency (“**FEMA**”) oversees the delineation of flood zones. FEMA publishes Flood Insurance Rate Maps (“**FIRMs**”) that show the expected frequency and severity of flooding by area, typically for the existing land use and drainage/flood control facilities. The maps prepared by FEMA for the San José area indicate that during a 100-year flood event (area subject to a flood that has a 1% chance of being equaled or exceeded in any given year), sections of the City could be subject to flooding from creek overbanking, inadequate storm drains and levees or inundation from the San Francisco Bay. These areas are labeled on the FIRM as zones A, AE, AH, AO, AR, A99, V, and VE. The FIRMs and the zone definitions are available on the FEMA website. Approximately 20,000 parcels (or approximately 10% of the total number of properties within the City) are within the 100-year flood hazard area established by FEMA. The other zones on the FIRM include zone X shaded - also known as the 500-year flood event (or the 0.2% annual chance floodplain), zone X unshaded – an event beyond the 500-year flood (areas outside the 0.2% annual chance floodplain), and zone D - areas where flood hazards are undetermined but possible. In areas designated as Zone D, no analysis of flood hazards have been conducted. While flood insurance is available for structures in all flood zones, it is only federally required by lenders for loans to structures in zones represented by letters A and V. In addition to flood insurance, new and substantially improved structures in zones A and V are subject to construction requirements per the City's floodplain ordinance, Chapter 17.08 Special Flood Hazard Area Regulations.

**Dam Inundation.** Dam inundation hazards are those associated with the downstream inundation that would occur given a major structural failure in a nearby dam/reservoir. Parts of the City are in the dam inundation area for Guadalupe Dam, Lenihan Dam and Anderson Dam. The District is also responsible for these dams. In a catastrophic event, damage to one or more of these dams could result in flooding within the City as shown on inundation maps originally prepared by the District in the early 1970's and mid 1990's (the map for Guadalupe Dam was further updated in 2014, the maps for Lenihan Dam and Anderson Dam in 2016). These inundation maps are on file with the California Office of Emergency Services and with the City.

The District commenced seismic stability studies on nine of the District's dams in 2007. On July 6, 2011, the District issued a press release announcing the results of a seismic study of the Anderson Dam, an earth and rockfill structure constructed in 1950, which concluded that the dam could be affected by a major earthquake with a magnitude of 7.25 on the Calaveras Fault within two kilometers of the dam. The study further stated that the analysis found loosely compacted layers of liquefiable materials in the foundation of the dam. These materials are susceptible to a reduction in strength when subjected to severe earthquake shaking. If the foundation were damaged, part of the dam could experience 15 to 25 feet of vertical deformation, with an additional 15 feet of potential cracking. The study stated that if the reservoir were full at the time, there could be an uncontrolled release of water. Although the chances are very remote, a complete failure of the Anderson Dam could send a wall of water 35 feet high into downtown Morgan Hill in 14 minutes, and 8 feet deep into the City within three hours.

The Anderson Dam is regulated by the State of California Division of Safety of Dams, which performs yearly reviews and requires maintenance and safety standards to



be enforced by the dam owners and operators. Additionally, the Federal Energy Regulatory Commission has dam safety jurisdiction at the Anderson Dam. Currently, these regulatory agencies have set a reservoir elevation restriction equivalent to 58% of capacity, or 52,553 acre-feet of water. These agencies set these storage elevation restrictions understanding that reservoirs cannot physically be kept below a restricted level at all times; for example, they understand that storms produce rainfall runoff into reservoirs that will temporarily increase the amount of water in them and that they have not requested the District do anything beyond releasing water from the dam's existing outlet as quickly as possible, to help bring water levels back down.

In response to the seismic study, the District initiated a project to retrofit the Anderson Dam. The planning phase of the Anderson Dam Seismic Retrofit project has been completed and currently the project is in the engineering design phase, which identified significant new issues with the dam that will require a much more extensive retrofit of the embankment. The modified project is scheduled for completion in 2027 at an estimated cost of approximately \$563 million. City staff has (and will continue to) meet with District staff to ask questions about the project in an effort to promote the safety of City residents both during and after construction of the project.

On October 10, 2017, the District approved a short-term flood risk reduction option for Coyote Creek for the 2017-2018 Winter Season. In particular, the District approved a plan to lower reservoir storage levels at Anderson Dam Reservoir significantly below the current seismic restriction before the winter season, and maintaining the lower level to provide more storage volume through the winter season. This same short-term flood risk reduction continued to be implemented in the 2018-19 Winter season.

Coyote Reservoir and Dam, also operated by the District, lie immediately upstream of Anderson Reservoir and are located on the Calaveras fault. Coyote Reservoir was constructed in the 1930's and is currently operated under a State of California Division of Safety of Dams storage restriction limit equivalent to 53% of capacity. When Coyote Reservoir exceeds 100% of storage capacity due to extreme wet weather, spillway flows from Coyote Reservoir enter the south end of Anderson Reservoir. Coyote Reservoir has a total storage capacity of 23,244 acre-feet, which is approximately 25% of the storage capacity of Anderson Reservoir, which can store a total of 90,373 acre-feet. In the event of a total failure of Coyote Reservoir Dam, the resulting water that would be released because of such failure would be expected to be contained within the channel that leads to Anderson Reservoir. If Anderson Reservoir lacked the storage capacity to contain the Coyote Reservoir water flows resulting from a dam failure event, the Anderson Reservoir spillway would convey those flows to Coyote Creek below the Anderson Reservoir and ultimately into San José.

On October 26, 2011, the District announced preliminary findings from a seismic study indicating that its Calero and Guadalupe dams could be subject to significant damage if a major earthquake occurred near either dam. In response to these preliminary findings, the District has further restricted reservoir levels at the Calero and Guadalupe dams. In 2012, the District initiated a project to retrofit Calero and Guadalupe dams. The planning phase of the project has been completed. The design phase of the project commenced in 2015 and is currently projected to continue through 2027. Construction of the Calero dam retrofit project is currently scheduled for to begin after 2024. Construction of the Guadalupe dam retrofit project is scheduled for



construction in 2022, with a scheduled completion in 2024. The estimated costs for the combined projects is approximately \$240 million.

Reports or studies were completed for the Almaden Dam in October 2012, the Lenihan Dam in December 2012, and the Stevens Creek Dam in December 2013, that concluded that the dams are in suitable condition and that no retrofit work is required. The District continues to work with the State of California Division of Safety of Dams to study seismic stability of its other dams and is adapting operations accordingly.

In April 2017, State water officials directed the District to perform comprehensive spillway condition assessments for nine dam spillways, including with respect to the Guadalupe Dam, Lenihan Dam and Anderson Dam.

2017 Flooding. Due to significant rainfall in the Santa Clara Valley during fall 2016 and winter 2017, Anderson Dam's water capacity exceeded the capacity restriction and the District released water from it. On February 18, 2017, Anderson Dam exceeded 100% of its capacity, and as a result of the uncontrollable, but predictable release of water over the spillway, the City experienced significant flooding along Coyote Creek.

The uncontrollable spillway release lasted 10 days. The reservoir spillway event began on February 18, 2017 and reached its peak on February 21, 2017 before declining and eventually stopping on February 28, 2017. Beginning February 28, 2017, the reservoir levels slowly retreated as the District used the outlet structure at the base of the Anderson Dam to draw down water levels at a rate of approximately 425 cubic feet per second (fully opened).

This flooding required a combination of advisory and mandatory evacuations of approximately 14,000 residents in three areas of the City: Rock Springs; neighborhoods in the William Street area (Olinder, Brookwood Terrace, and Naglee Park); and three mobile home parks in the Rincon area. The flood significantly impacted both privately and publicly owned property and facilities in the Rock Springs and William Street neighborhoods. Flooding also occurred on Highway 101, south of the City, causing the closure of the freeway for most of the day in this location on February 21, 2017.

Due to the damages that occurred at the above locations, the City proclaimed a state of local emergency with respect to this flooding event and requested that the Governor of the State proclaim a state of emergency for the City and that he request a federal declaration for assistance. Subsequently, the President declared disasters for the California winter storms including the Coyote Creek flood, making the City eligible to file for public assistance claims for costs incurred for emergency response. On February 27, 2017, the City submitted to the State a preliminary damage estimate of \$73 million, including \$50 million in damage to private property and \$23 million in public assistance damage for emergency protective measures, debris removal, and infrastructure damage incurred by the City. These estimates were preliminary and continue to be revised.

There has been no further significant flooding that has impacted entire neighborhoods in San José since the February 2017 flood event on Coyote Creek. See APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND CONSENT DECREES – Potentially Significant Litigation” for additional information related to lawsuits and claims filed against the City arising from the February 2017 flood event on Coyote Creek.



**Wildfire Areas.** The California Department of Forestry and Fire Protection (“**CAL FIRE**”) classifies State Responsibility Areas (in which the State is financially responsible for preventing and suppressing fires) as either Moderate, High, or Very High “Fire Hazard Severity Zones” (“**FHSZ**”). CAL FIRE has designated approximately 85.64 square miles of State Responsibility Area within the City as FHSZ of which, 4.08 square miles is Moderate, 81.12 square miles is High, and 0.44 square miles is Very High. CAL FIRE has identified 5.16 square miles within the City’s Local Responsibility Area (in which the City is financially responsible for preventing and suppressing fires) as Very High FHSZ. The City has not taken action to date to designate this area as Very High FHSZ.

Local enforcing agencies, including the San José Fire Department, may designate areas within its jurisdiction as Wildland Urban Interface (“**WUI**”) areas in which there is a significant risk to property from wildfires. The City, through its Fire Department, has designated approximately 54.5 square miles of the City’s 180 square miles of incorporated area as WUI. These areas are in the southwestern and southeastern areas of the City known as the Almaden Valley and East Foothills. The City’s designation of areas as WUI allows for the enforcement of heightened construction standards that mitigate the spread of wildfires.

**Wildfire Risk.** In a report entitled: “Wildfires and Climate Change: California’s Energy Future -- A Report from Governor Newsom’s Strike Force” published on April 12, 2019 (the “**Wildfire Report**”), the Governor’s Strike Force made a number of recommendations to address the challenges presented by catastrophic wildfires in California. The Wildfire Report notes that “Climate change, widespread tree mortality, weak utility infrastructure, and the proliferation of homes in the WUI [Statewide] magnify the wildfire threat and place substantially more people and property at risk than ever before.”

**Wildfire Response.** The San José Fire Department is the local enforcing agency for applicable sections of the California Code of Regulations, as adopted by the City Council, including the California Fire Code, Building Code, and Residential Code. All WUI areas in the City receive fire response from the San José Fire Department, which has emergency operations, policies, and procedures established for wildland firefighting. Wildland fires also receive full wildland fire response from CAL FIRE.

### ***Wildfire Prevention and Mitigation.***

**Building Requirements.** New construction and building permits in the City’s designated WUI areas must be compliant with construction regulations in Chapter 7A of the California Building Code and Section R337 of the California Residential Code, as adopted by San José Municipal Code Chapter 24.03, Part 1 and Chapter 24.09, Part 1, respectively. These sections contain heightened requirements for material and construction methods for buildings subject to exterior wildfire exposure. The City does not have data on the percentage of structures in the WUI which are required to meet these heightened standards.

In addition to complying with Chapter 7A of the California Building Code and Section R337 of the California Residential Code, buildings and structures within the FHSZ of a State Responsibility Area must comply with defensible space regulations in the Public Resources Code. There are currently no defensible space regulations for structures in the WUI that are not also within the FHSZ of a State Responsibility Area. Defensible space regulations contain specific requirements for maintaining and clearing



vegetation and fuel around buildings and structures to reduce their vulnerability to wildfires.

## **Hazardous Substances**

Owners and operators of real property may be required by law to remedy conditions of the property relating to releases or threatened releases of hazardous substances. The federal Comprehensive Environmental Response, Compensation and Liability Act of 1980, sometimes referred to as “CERCLA” or the “Superfund Act,” is the most well-known and widely applicable of these laws, but California laws with regard to hazardous substances area also stringent and similar. Under many of these laws, the owner (or operator) is obligated to remedy a hazardous substance condition of property whether or not the owner (or operator) has anything to do with creating or handling the hazardous substance. Further, such liabilities may arise not simply from the existence of a hazardous substance but from the method of handling it. All of these possibilities could significantly and adversely affect assessed values of property in the City and the operations and finances of the City.

## **Natural Gas Transmission Pipelines**

On September 9, 2010, a Pacific Gas and Electric Company (“**PG&E**”) high pressure natural gas transmission pipeline exploded in San Bruno, California, with catastrophic results. In a final Pipeline Accident Report, adopted by the National Transportation Safety Board (the “**NTSB**”) on August 30, 2011, the NTSB found recurring deficiencies in PG&E’s pipeline integrity management program, which the NTSB concluded were evidence of a systemic problem. Publicly available information on PG&E’s website indicates there are several similar natural gas transmission pipelines located throughout the City.

The effects of any failure of the high pressure natural gas transmission pipelines in the City are difficult to predict, but could include explosion and concussive force, fire, smoke, transportation delays and detours on routes to and from the City, and potential forced evacuation of nearby structures for temporary or lengthy periods of time. This could lead to a decrease in assessed values of the land in the City and decreased tax revenues generated thereby.

The City is not able to independently confirm the information contained in the NTSB’s Pipeline Accident Report or on the PG&E website, including the exact distances of any high pressure transmission lines from the City, and can provide no assurances as to the accuracy or completeness of such information. Information available in the NTSB’s Pipeline Accident Report and from PG&E’s website is not part of this Official Statement nor has such information been incorporated by reference herein, and should not be relied upon in making an investment decision with respect to the Bonds. Further, the City cannot provide any assurances as to the condition of PG&E pipelines and other facilities in or within the vicinity of the City, or predict the extent of the damage to any property that would occur if a PG&E pipeline were to experience any type of failure, including a possible fire or explosion.

## **PG&E Chapter 11 Bankruptcy Filing**

On January 29, 2019, PG&E filed for bankruptcy protection under Chapter 11 of the Bankruptcy Code (the “**PG&E Bankruptcy Proceeding**”). The PG&E Bankruptcy Proceeding may result in, among other things, delays in the payments of amounts owed to the City or even nonpayment of amounts owed the City if such amounts owing were incurred by PG&E prior to



PG&E filing for bankruptcy protection, commonly referred to as pre-petition debt, and the amounts owing are discharged as part of the PG&E Bankruptcy Proceeding or the City is unable to collect in whole or in part as a creditor. At the present time, the City estimates that PG&E's pre-petition debt owed the City consists mostly of unpaid permit fees and other miscellaneous items and is approximately \$230,000. However, the City is in the process of reviewing PG&E's remittance of franchise fees and the City's utility users taxes. Depending on the outcome of the City's review, the estimate of PG&E's pre-petition debt owed to the City could increase.

In addition, under the State's inverse condemnation doctrine, government agencies, as well as utilities such as PG&E, are subject to strict liability for damages caused by public use. In *Cobb v. City of Stockton*, the U.S. Court of Appeals for the Ninth Circuit recently held that the City of Stockton could treat an inverse condemnation claim in the same manner as other unsecured claims in its bankruptcy case and could discharge such claims. As a result, to the extent inverse condemnation claims are brought by owners of property within the City for damage to such property during the pendency of the PG&E Bankruptcy Proceeding, it is possible that such claims will be reduced or discharged. A reduction or discharge of any such claims could delay the restoration of assessed values of any damaged property in the City and decrease property tax revenues.

The City cannot provide any assurance regarding the effect the PG&E Bankruptcy Filing will have on the City or its finances.

### **PG&E Public Safety Power Shutoffs**

PG&E has adopted a Community Wildfire Safety Program in effort to prevent wildfires in the State. As part of its Community Wildfire Safety Program, PG&E has notified customers, including the City, that PG&E has implemented additional precautionary measures to help reduce the risk of wildfires. In particular, PG&E has notified the City that, if extreme fire danger conditions threaten a portion of the electric system serving a community, PG&E may turn off electricity in the interest of public safety (referred to as a "**Public Safety Power Shutoff**"). According to PG&E, a Public Safety Power Shutoff could impact customers in an area that is not experiencing high winds or other extreme weather conditions because PG&E's system relies on power lines working together to provide electricity across cities, counties and regions, including the City and the County.

As the third largest city in State and the largest in Northern California, the City is PG&E's largest customer. The City serves a population of over 1 million people. Reliable electric service is essential to the residents, government operations, and businesses in the City's community. In the event a Public Safety Power Shutoff in the City or surrounding areas, the general economy of the City could be adversely affected and result in a reduction in tax revenues to the City, such as sales tax revenues resulting from the interruption of businesses within the City. See "APPENDIX A – THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MAJOR GENERAL FUND REVENUE SOURCES" for a description of the City's major general fund sources, including sales tax revenues.

Additionally, the City operates a community choice energy program, San José Clean Energy ("**SJCE**"), that supplies the City and City residents and businesses with cleaner electricity options through PG&E's infrastructure. Certain start-up costs of SJCE were financed with proceeds from commercial paper notes issued by the City of San José Financing Authority (the "**Financing Authority**"). Although SJCE's operating costs, including repayment of financing costs (such as the commercial paper notes issued by the Financing



Authority to finance start-up costs) are anticipated to be borne by SJCE customers/ratepayers, such commercial paper notes are secured by lease payments payable from the City's General Fund. In the event a Public Safety Power Shutoff occurs in the State, SJCE's ability to supply electricity to City residents and business could be interrupted and thereby delay or reduce SJCE's revenues available to repay financing costs, including the commercial paper notes issued by the Financing Authority.

The City has requested additional information from PG&E regarding, among other items, the location of areas and infrastructure that could be subject to de-energization in an effort to understand the possible impact Public Safety Power Shutoffs may have on the City and its residents. The impact that any Public Safety Power Shutoffs in the City and surrounding areas will have on the City and its finances is unknown and the City cannot provide any assurance regarding the effect such shutoffs will have on the City or its finances.

See APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MUNICIPAL GOVERNMENT” and “– BONDED AND OTHER INDEBTEDNESS – San José Clean Energy Debt,” for further discussion regarding SJCE and a description of outstanding debt of the City that is secured by or payable from SJCE revenues.

## **Climate Change**

The change in the earth's average atmospheric temperature, generally referred to as “climate change,” is expected to, among other things, increase the frequency and severity of extreme weather events and cause substantial flooding.

In 2005, the Governor signed Executive Order S-3-05 setting the stage for multiple legislative actions to reduce greenhouse gas emissions (“**GHG**”) to 80% below 1990 levels by 2050. The adoption of the California Global Warming Solutions Act of 2006 (“**AB 32**”) and subsequent companion bills, including but not limited to the Sustainable Communities and Climate Protection Act of 2008 (“**SB 375**”) that builds upon AB 32 to reduce GHG emissions by linking transportation funding to land use planning, demonstrate the commitment by the State to take action and reduce GHG emissions to 1990 levels by 2020 and to 80% below 1990 levels by 2050. Additionally, the State adopted Senate Bill No. 32, which established a revised statewide GHG emission reduction target of 40% below 1990 levels by 2030.

In 2009, the California Natural Resources Agency released its California Climate Adaptation Strategy, as updated in 2010, 2013, and 2018. California Climate Adaptation Strategy summarizes the best known science on climate change impacts in the State to assess vulnerability and outlines possible solutions that can be implemented within and across State agencies to promote resiliency.

In 2011, the City prepared its Greenhouse Gas Reduction Strategy in conjunction with the preparation of the Envision San José 2040 General Plan (“**General Plan**”) process to ensure that the implementation of the General Plan update aligns with the implementation requirements of AB 32 and SB 375. The General Plan is the City's comprehensive and long-range plan to guide physical development within San José. The purposes of the Greenhouse Gas Reduction Strategy were to: (i) capture and consolidate GHG reduction efforts already underway by the City; (ii) distill policy direction on GHG reduction from the General Plan update; (iii) quantify GHG reductions that could result from land use changes



incorporated in the General Plan's Land Use/Transportation diagram; (iv) create a framework for the ongoing monitoring and revision of this Greenhouse Gas Reduction Strategy; and (v) achieve General Plan-level environmental clearance for future development activities (through the year 2020) occurring within San José. The City updated the Greenhouse Gas Reduction Strategy in 2015 and is in the process of further updating the Greenhouse Gas Reduction Strategy to comply with all current legal requirements and to achieve General Plan-level environmental clearance for future development activities in San José through the year 2030.

In February 2018, City Council accepted the Climate Smart San José Plan ("**Climate Smart**") which is intended to provide a framework to address global warming, establish a sustainable water supply, reduce dependency upon fossil fuels, and create cleaner air by 2050. Under a fully-implemented Climate Smart Plan, the City would exceed the AB 32 and AB 375 targets and achieve an estimated 88 percent reduction in GHG levels in 2050 as compared to 1990.

Climate Smart outlines future strategies for the City which align with the Paris Climate Agreement. The City Council has approved one of the major Climate Smart initiatives, SJCE. As previously described, SJCE is a community choice energy program operated by the City's Community Energy Department which supplies the City and City residents and businesses with cleaner electricity options through PG&E's infrastructure. In August 2017, the City Council approved the Financing Authority's issuance of lease revenue commercial paper notes for the purpose of financing start-up costs relating to SJCE, including capitalization and related costs, in the principal amount of \$10 million. SJCE launched services to the City in September 2018 and to City residents and businesses in February 2019, and its operating costs, including repayment of financing costs, are anticipated to be borne by SJCE customers/ratepayers. See APPENDIX A – "THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MUNICIPAL GOVERNMENT" and "– BONDED AND OTHER INDEBTEDNESS – San José Clean Energy Debt," for further discussion regarding SJCE and a description of outstanding debt of the City that is secured by or payable from SJCE revenues.

Other strategies in Climate Smart include encouraging densification of development and increasing residents' access to mass transit to reduce vehicle miles travelled. Climate Smart also contemplates support for State requirements for Zero Net Carbon new residential construction, as well as strategies for retrofitting existing residential buildings to improve energy usage. If all of the actions in Climate Smart are implemented, the cost to residents and the City (estimated to be \$264 billion or 2.55% of gross domestic product ("**GDP**") cumulative through 2050) is anticipated to be offset by long-term savings and avoided costs (estimated at \$269 billion or 2.6% of GDP cumulative through 2050.) As to the City, the estimated annual cost for full implementation is \$435 million, with ninety-five percent of this cost (\$413.25 million) attributed to SJCE, as discussed above. The remaining cost is for staff facilitation and coordination activities.

In addition, climate change may increase sea levels in the Alviso area of North San José. To reduce the potential for flooding, the US Army Corps of Engineers and the Santa Clara Valley Water District are designing, constructing, and funding the South San Francisco Bay Shoreline Levee (the "**Levee**"). The Levee will be partially constructed on property currently owned by the City and the City of Santa Clara, as joint owners of the San José-Santa Clara Regional Wastewater Facility ("**RWF**"). The City anticipates that as a result of the Levee project, the San Francisco Regional Water Quality Board will require the RWF to close inactive, legacy lagoons used until the 1970s for drying residual solids and



remediate environmental contamination. Cost of remediation is unknown at this time, but it is anticipated that the City's portion of such costs would be borne by ratepayers, or may be mitigated by the RWF's sale of land and easements to facility the Levee project.

The City cannot predict the timing, extent, or severity of climate change and its impact on the City's operations and finances, or property within the City.

## **Cybersecurity**

The City relies on a large and complex technology environment to conduct its operations. As a recipient and provider of personal, private, and sensitive information, the City and its departments may be subject to cyber threats from time to time, including, but not limited to, hacking, viruses, malware and other attacks on computers and other sensitive digital networks and systems. [The City's Information Technology Department has no knowledge or notice of any significant data breaches on City information and systems assets to date.]

In 2018, the City established a Cybersecurity Office and hired its first Chief Information Security Officer (the "**CISO**"), within the City's Information Technology Department, to coordinate cybersecurity preparation and response across City departments. Under the direction of the CISO, the City has completed its Information Security Standards Handbook that establishes a security baseline for the City. The Cybersecurity Office also worked with City departments to improve IT system and infrastructural changes by establishing a new City-wide Change Control Board ("**CCB**") in August 2018. The CCB's main objective is to communicate and inform changes to computer systems as part of maintenance or upgrades to all impacted departments. Additionally, a Cybersecurity Advisory Board with leaders from the public and private sectors was established to validate and to work with the City to refine the City's Cybersecurity strategy, policies approach, and roadmap. [In its 2019-20 Adopted Operating Budget, the City has also allocated additional funding totaling approximately \$1.1 million and an Enterprise Supervising Technology Analysts to support the City's Cybersecurity program.]

The City has conducted training with City employees who handle credit card transactions and cybersecurity awareness campaigns aimed at City employees. The Cybersecurity Office is preparing to provide cybersecurity training and testing with all City employees including phishing email tests, tests against psychological manipulation to perform actions or divulge confidential information, periodic cybersecurity newsletters, and workshops. These efforts will couple with the Cybersecurity's Office's ongoing information technology security assessment and "penetration testing" to identify and remediate any potential weaknesses in its networks.

No assurances can be given that any organization's cybersecurity and operational controls will be completely successful in guarding against cyber threats, attack, and/or advanced persistent threats. The results of any attack on the City's computer and information technology systems could impact its operations and damage the City's digital networks and systems, and the costs of remedying any such damage could be substantial. Hence, the City's cybersecurity work focuses on prevention and resilience, as described above.



## Loss of Tax Exemption/Risk of Audit of Municipal Issuer

As discussed under the caption “TAX MATTERS,” interest on Series 2019A-1 Bonds and Series 2019C Bonds could fail to be excluded from gross income of the Owners thereof for purposes of federal income taxation retroactive to the date of the issuance of the Series 2019A-1 Bonds and Series 2019C Bonds as a result of future acts or omissions of the City in violation of its covenants to comply with requirements of the Internal Revenue Code of 1986, as amended. Additionally, subsequent to the issuance of the Bonds, there might be federal, state or local statutory changes (or judicial or regulatory interpretations of federal, state or local law) that affect the federal, state or local tax treatment of the Series 2019A-1 Bonds and Series 2019C Bonds or the market value of the Bonds. Tax reform proposals are being considered by Congress. It is possible that legislative changes might be introduced in Congress, which, if enacted, would result in additional federal income imposed on owners of tax-exempt state or local obligations, such as the Series 2019A-1 Bonds and Series 2019C Bonds. The introduction or enactment of any of such changes could adversely affect the market value or liquidity of the Series 2019A-1 Bonds and Series 2019C Bonds. No assurance can be given that subsequent to the issuance of the Bonds such changes (or other changes) will not be introduced or enacted or interpretations will not occur. Should such an event of taxability occur, the Series 2019A-1 Bonds and Series 2019C Bonds are not subject to special redemption or any increase in interest rate and will remain outstanding until maturity or until redeemed under one of the redemption provisions contained in the Fiscal Agent Agreement. Before purchasing any of the Series 2019A-1 Bonds and Series 2019C Bonds, all potential purchasers should consult their tax advisors regarding possible statutory changes or judicial or regulatory changes or interpretations, and their collateral tax consequences relating to the Series 2019A-1 Bonds and Series 2019C Bonds.

The Internal Revenue Service (the “IRS”) has a program for the auditing of tax-exempt bond issues, including both random and targeted audits. It is possible that the Series 2019A-1 Bonds and Series 2019C Bonds or other obligations of the City may be selected for audit by the IRS. It is also possible that the market value of the Series 2019A-1 Bonds and Series 2019C Bonds could be affected as a result of such an audit or audits.

## Trade Policy

In 2018, the United States imposed tariffs on \$250 billion worth of Chinese products, equivalent to half the nation’s imports from China, triggering Chinese retaliatory tariffs on over \$50 billion of exports from the United States. In May 2019, the United States raised such tariffs on \$200 billion worth of Chinese products. In response, China announced tariff increases on over \$60 billion worth of U.S. goods in retaliation for new U.S. tariffs.

Silicon Valley is a region in the Southern San Francisco Bay Area of Northern California that serves as a global center of high technology, innovation, and social media. It corresponds roughly to the geographical Santa Clara Valley. The San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (the “**San José MSA**”) in the Silicon Valley has a large concentration of high-tech companies, many of which have ties to global markets for both sales and manufacturing. According to data published by the U.S. Census Bureau – U.S. Department of Commerce, in 2017, exports from the San José MSA exceeded \$21.4 billion, ranking 16th in the nation. China is the top export market for the San José MSA totaling \$2.5 billion in exports followed by Mexico (\$2.2 billion), Canada (\$1.7 billion), Republic of Korea (\$1.6 billion), and Japan (\$1.4 billion). Ongoing trade tariffs with China could have negative effects on the economy of the San José MSA, which includes the City. The City cannot estimate the potential



loss from existing or future trade policies of the United States or any of the countries to which the San José MSA exports goods.

## **[2020 Census**

In March 26, 2018, the U.S. Secretary of Commerce, Wilbur Ross, issued a memorandum directing the Census Bureau to add a citizenship question to the 2020 Census. The City has large immigrant, and particularly Hispanic, communities and it is expected that the citizenship question will negatively affect the census count of persons residing in the City and in turn federal funding based on population, such as funding through the Workforce Innovation and Opportunity Act and Community Development Block Grants, as well as funding available to the City's Office of Emergency Management from FEMA.

In April 2018, the City and Black Alliance for Just Immigration sued the U.S. Commerce Secretary, the U.S. Commerce Department, the Census Bureau, and the Director of the Census Bureau to enjoin the Secretary's decision to include a citizenship question on the 2020 Census on the basis that its inclusion violated the Administrative Procedures Act ("**APA**") and the Enumeration Clause of the U.S. Constitution. A trial was held in the case in January 2019, and in March 2019, Judge Richard Seeborg issued his decision finding that the Secretary had violated the APA and the Enumeration Clause in deciding to include the question, and enjoined the Commerce Department from using the question on the 2020 Census.

Prior to the trial before Judge Seeborg, a U.S. District Court judge in New York ("**New York Census Case**") issued a decision holding that the inclusion of the citizenship question on the 2020 Census violated the APA and ordered the Commerce Department to remove a citizenship question from the 2020 Census. The federal government subsequently filed an appeal directly to the U.S. Supreme Court, which the Court granted. Oral argument in the New York Census Case was heard in April 2019 and a decision is anticipated to be issued before June 30, 2019.

In the event that the U.S. Supreme Court reverses the decision in the New York Census Case and allows the citizenship question to be included in the 2020 Census, the City anticipates federal funding to the City would be negatively impacted. The City has performed and anticipates continuing to perform outreach to residents in an attempt to mitigate the risk of a population undercount. The City cannot estimate the potential loss of federal funds nor provide any assurance that such outreach will mitigate such risk.

See APPENDIX A – "THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND CONSENT DECREES – Affirmative Litigation – Census Litigation."]

## **Limitation on Remedies; Bankruptcy**

**General.** The rights of the owners of the Bonds are subject to limitations on legal remedies against the City, including applicable bankruptcy or similar laws affecting the enforcement of creditors' rights generally, now or hereafter in effect. Bankruptcy proceedings, if initiated, could subject the owners of the Bonds to judicial discretion and interpretation of their rights in bankruptcy proceedings or otherwise, and consequently may entail risks of delay, limitation or modification of the rights of the owners of the Bonds.

Bankruptcy courts are courts of equity and as such have broad discretionary powers. If the City were to become the debtor in a proceeding under Chapter 9 of the Bankruptcy Code,



the parties to the proceedings may be prohibited from taking any action to collect any amount from the City (including ad valorem tax revenues or Loan Repayments) or to enforce any obligation of the City, without the bankruptcy court's permission. In such a proceeding, as part of its plan of adjustment in bankruptcy, the City may be able to alter the priority, interest rate, principal amount, payment terms, collateral, maturity dates, payment sources, covenants (including tax-related covenants), and other terms or provisions of the Bonds and other transaction documents related to the Bonds, as long as the bankruptcy court determines that the alterations are fair and equitable. In addition, in such a proceeding, as part of such a plan, the City may be able to eliminate the obligation of the City to raise taxes if necessary to pay the Bonds. There also may be other possible effects of a bankruptcy of the City that could result in delays or reductions in payments on the Bonds. Moreover, regardless of any specific adverse determinations in any City bankruptcy proceeding, the fact of a City bankruptcy proceeding, could have an adverse effect on the liquidity and market price of the Bonds.

As stated above, if the City were to go into bankruptcy, the bankruptcy petition would be filed under Chapter 9 of the Bankruptcy Code. Chapter 9 provides that it does not limit or impair the power of a state to control, by legislation or otherwise, a municipality of or in such state in the exercise of the political or governmental powers of such municipality, including expenditures for such exercise. For purposes of the language of Chapter 9, the City is a municipality. State law provides that the ad valorem taxes levied to pay the principal and interest on the Bonds shall be used for the payment of principal and interest of the City's general obligation bonds and for no other purpose. If this restriction on the expenditure of such ad valorem taxes is respected in a bankruptcy case, then the ad valorem tax revenue could not be used by the City for any purpose other than to make payments on the Bonds. It is possible, however, that a bankruptcy court could conclude that the restriction should not be respected.

**Statutory Lien.** Pursuant to Section 53515 of the California Government Code (which became effective on January 1, 2016, as part of Senate Bill 222), the Bonds will be secured by a statutory lien on all revenues received pursuant to the levy and collection of the ad valorem taxes levied for the Bonds. Section 53515 provides that the lien will automatically arise, without the need for any action or authorization by the local agency or its governing board, and will be valid and binding from the time the bonds are executed and delivered. See "THE BONDS – SECURITY FOR THE BONDS." Although a statutory lien would not be automatically terminated by the filing of a Chapter 9 bankruptcy petition by the City, the automatic stay provisions of the Bankruptcy Code would apply and payments that become due and owing on the Bonds during the pendency of the Chapter 9 proceeding could be delayed (unless the Bonds are determined to be secured by a pledge of "special revenues" within the meaning of the Bankruptcy Code and the pledged taxes are applied to pay the Bonds in a manner consistent with the Bankruptcy Code).

**Special Revenues.** If the tax revenues that are pledged to the payment of the Bonds (see "THE BONDS – SECURITY FOR THE BONDS") are determined to be "special revenues" within the meaning of the Bankruptcy Code, then the application in a manner consistent with the Bankruptcy Code of the pledged ad valorem revenues that are collected after the date of the bankruptcy filing should not be subject to the automatic stay. "Special revenues" are defined to include, among others, taxes specifically levied to finance one or more projects or systems of the debtor, but excluding receipts from general property, sales, or income taxes levied to finance the general purposes of the debtor. The City has specifically pledged the taxes for payment of the Bonds. Additionally, the ad valorem taxes levied for payment of the Bonds are permitted under the State Constitution only where the applicable bond proposition is approved by at least two-thirds of the votes cast. State law prohibits the use of the tax proceeds for any



purpose other than payment of the Bonds and the Bond proceeds can only be used to fund the acquisition or improvement of real property and other capital expenditures included in the proposition so such tax revenues appear to fit the definition of special revenues. However, there is no binding judicial precedent dealing with the treatment in bankruptcy proceedings of ad valorem tax revenues collected for the payments of bonds in California, so no assurance can be given that a bankruptcy court would not hold otherwise.

In addition, even if the ad valorem tax revenues are determined to be “special revenues,” the Bankruptcy Code provides that special revenues can be applied to necessary operating expenses of the project or system, before they are applied to other obligations. This rule applies regardless of the provisions of the transaction documents. Thus, a bankruptcy court could determine that the City is entitled to use the ad valorem tax revenues to pay necessary operating expenses of the City before the remaining revenues are paid to the owners of the Bonds.

**Possession of Revenues; Remedies.** If the City goes into bankruptcy and has possession of tax revenues (whether collected before or after commencement of the bankruptcy), and if the City does not voluntarily pay such tax revenues to the owners of the Bonds, it is not entirely clear what procedures the owners of the Bonds would have to follow to attempt to obtain possession of such tax revenues, how much time it would take for such procedures to be completed, or whether such procedures would ultimately be successful.

## **TAX MATTERS**

### **Tax-Exempt Bonds**

**Federal Tax Status.** In the opinion of Jones Hall, A Professional Law Corporation, San Francisco, California, Bond Counsel, subject, however to the qualifications set forth below, under existing law, the interest on the Series 2019A-1 Bonds and the Series 2019C Bonds (collectively referred to in this Official Statement as, the Tax-Exempt Bonds) is excluded from gross income for federal income tax purposes and such interest is not an item of tax preference for purposes of the federal alternative minimum tax.

The opinions set forth in the preceding paragraph are subject to the condition that the City comply with all requirements of the Internal Revenue Code of 1986, as amended (the “**Tax Code**”) that must be satisfied subsequent to the issuance of the Bonds in order that the interest thereon be, and continue to be, excludable from gross income for federal income tax purposes. The City has made certain representations and covenants in order to comply with each such requirement. Inaccuracy of those representations, or failure to comply with certain of those covenants, may cause the inclusion of such interest in gross income for federal income tax purposes, which may be retroactive to the date of issuance of the Tax-Exempt Bonds.

**Tax Treatment of Original Issue Discount and Premium.** If the initial offering price to the public at which a Tax-Exempt Bond is sold is less than the amount payable at maturity thereof, then such difference constitutes “original issue discount” for purposes of federal income taxes and State of California personal income taxes. If the initial offering price to the public at which a Tax-Exempt Bond is sold is greater than the amount payable at maturity thereof, then such difference constitutes “original issue premium” for purposes of federal income taxes and State of California personal income taxes. *De minimis* original issue discount and original issue premium are disregarded.



Under the Tax Code, original issue discount is treated as interest excluded from federal gross income and exempt from State of California personal income taxes to the extent properly allocable to each owner thereof subject to the limitations described in the first paragraph of this section. The original issue discount accrues over the term to maturity of the Tax-Exempt Bond on the basis of a constant interest rate compounded on each interest or principal payment date (with straight-line interpolations between compounding dates). The amount of original issue discount accruing during each period is added to the adjusted basis of such Tax-Exempt Bonds to determine taxable gain upon disposition (including sale, redemption, or payment on maturity) of such Tax-Exempt Bond. The Tax Code contains certain provisions relating to the accrual of original issue discount in the case of purchasers of the Tax-Exempt Bonds who purchase the Tax-Exempt Bonds after the initial offering of a substantial amount of such maturity. Owners of such Tax-Exempt Bonds should consult their own tax advisors with respect to the tax consequences of ownership of Tax-Exempt Bonds with original issue discount, including the treatment of purchasers who do not purchase in the original offering to the public at the first price at which a substantial amount of such Bonds is sold to the public.

Under the Tax Code, original issue premium is amortized on an annual basis over the term of the Tax-Exempt Bond (said term being the shorter of the Tax-Exempt Bond's maturity date or its call date). The amount of original issue premium amortized each year reduces the adjusted basis of the owner of the Tax-Exempt Bond for purposes of determining taxable gain or loss upon disposition. The amount of original issue premium on a Tax-Exempt Bond is amortized each year over the term to maturity of the Tax-Exempt Bond on the basis of a constant interest rate compounded on each interest or principal payment date (with straight-line interpolations between compounding dates). Amortized Tax-Exempt Bond premium is not deductible for federal income tax purposes. Owners of premium Tax-Exempt Bonds, including purchasers who do not purchase in the original offering, should consult their own tax advisors with respect to State of California personal income tax and federal income tax consequences of owning such Tax-Exempt Bonds.

**California Tax Status.** In the further opinion of Bond Counsel, interest on the Tax-Exempt Bonds is exempt from California personal income taxes.

**Other Tax Considerations.** Current and future legislative proposals, if enacted into law, clarification of the Tax Code or court decisions may cause interest on the Tax-Exempt Bonds to be subject, directly or indirectly, to federal income taxation or to be subject to or exempted from state income taxation, or otherwise prevent beneficial owners from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such legislative proposals, clarification of the Tax Code or court decisions may also affect the market price for, or marketability of, the Tax-Exempt Bonds. It cannot be predicted whether or in what form any such proposal might be enacted or whether, if enacted, such legislation would apply to bonds issued prior to enactment.

The opinions expressed by Bond Counsel are based upon existing legislation and regulations as interpreted by relevant judicial and regulatory authorities as of the date of such opinion, and Bond Counsel has expressed no opinion with respect to any proposed legislation or as to the tax treatment of interest on the Tax-Exempt Bonds, or as to the consequences of owning or receiving interest on the Tax-Exempt Bonds, as of any future date. Prospective purchasers of the Tax-Exempt Bonds should consult their own tax advisors regarding any pending or proposed federal or state tax legislation, regulations or litigation, as to which Bond Counsel expresses no opinion.



Owners of the Tax-Exempt Bonds should also be aware that the ownership or disposition of, or the accrual or receipt of interest on, the Tax-Exempt Bonds may have federal or state tax consequences other than as described above. Other than as expressly described above, Bond Counsel expresses no opinion regarding other federal or state tax consequences arising with respect to the Tax-Exempt Bonds, the ownership, sale or disposition of the Tax-Exempt Bonds, or the amount, accrual or receipt of interest on the Tax-Exempt Bonds.

***Form of Bond Counsel Opinions.*** At the time of issuance of the Tax-Exempt Bonds, Bond Counsel expects to deliver an opinion for the Bonds in substantially the form set forth in Appendix D.

## **Taxable Bonds**

***General.*** The interest on the Taxable Series 2019A-2 Bonds, the Taxable Series 2019B Bonds, and the Taxable Series 2019D Bonds (collectively referred to in this Official Statement as, the Taxable Bonds) is not intended by the City to be excluded from gross income for federal income tax purposes. However, in the opinion of Bond Counsel, interest on the Taxable Bonds is exempt from California personal income taxes.

Owners of the Taxable Bonds should also be aware that the ownership or disposition of, or the accrual or receipt of interest on, the Taxable Bonds may have federal or state tax consequences other than as described above. Other than as expressly described above, Bond Counsel expresses no opinion regarding other federal or state tax consequences arising with respect to the Taxable Bonds, the ownership, sale or disposition of the Taxable Bonds, or the amount, accrual or receipt of interest on the Taxable Bonds.

***Form of Bond Counsel Opinion.*** At the time of issuance of the Taxable Bonds, Bond Counsel expects to deliver opinions for the Bonds in substantially the form set forth in Appendix D.

## **APPROVAL OF LEGAL PROCEEDINGS**

Certain legal matters incident to the authorization, issuance and sale of the Bonds are subject to the approval of Jones Hall, A Professional Law Corporation, San Francisco, California, Bond Counsel. Jones Hall, A Professional Law Corporation, San Francisco, California, is also serving as Disclosure Counsel in connection with the sale, issuance and delivery of the Bonds. Certain legal matters will be passed upon for the City by the City Attorney.

Copies of the approving opinion of Bond Counsel will be available at the time of delivery of the Bonds. The form of the opinions are set forth in APPENDIX D – “FORM OF OPINION OF BOND COUNSEL.” Except as expressly described in certain opinions delivered to the City, Bond Counsel is not passing upon and undertakes no responsibility for the accuracy, completeness or fairness of the information contained in the Official Statement. Bond Counsel and Disclosure Counsel will receive compensation that is contingent upon the sale, issuance and delivery of the Bonds.

## **FINANCIAL STATEMENTS**

The City’s Basic Financial Statements for Fiscal Year 2017-18 included in this Official Statement have been audited by Macias, Gini & O’Connell LLP, independent auditors, as stated



in their report included in the Financial Statements. See APPENDIX C – “BASIC FINANCIAL STATEMENTS OF THE CITY OF SAN JOSE FOR THE FISCAL YEAR ENDED JUNE 30, 2018.” Macias Gini & O’Connell LLP has not been requested to consent to the use or to the inclusion of its report in this Official Statement and has not reviewed this Official Statement.

## CONTINUING DISCLOSURE

The City will covenant for the benefit of owners of the Bonds to provide to the Electronic Municipal Market Access System (“**EMMA System**”) certain financial information and operating data relating to the City by not later than April 1 after the end of each fiscal year of the City (currently June 30th), commencing not later than April 1, 2020 with the report for the 2018-19 Fiscal Year (the “**Annual Report**”), and to provide notices of the occurrence of certain listed events. The specific nature of the information to be contained in the Annual Report or the notices of listed events is summarized in APPENDIX F – “FORM OF CONTINUING DISCLOSURE CERTIFICATE.” These covenants have been made in order to assist the Purchasers in complying with the Rule. The Fiscal Agent has no obligation to enforce the undertakings of the City in the Continuing Disclosure Certificate, and a failure by the City to provide any information required thereunder shall not constitute an Event of Default under the Fiscal Agent Agreement.

The City engaged third-party consultants to conduct an analysis of the historical compliance of the City and the Successor Agency to the Redevelopment Agency of the City of San José (the “**Successor Agency**”) with their respective continuing disclosure obligations over the past five years. During this time, both the City and the Successor Agency were obligated to provide continuing disclosure. The City was obligated to provide continuing disclosure pursuant to undertakings for numerous bond issuances, including bond issuances of the City, the City of San José Financing Authority, the San José-Santa Clara Clean Water Financing Authority, and various City of San José special assessment and community facilities districts and a convention center facilities district. However, the City was not obligated under the Successor Agency’s prior undertakings under the Rule, nor was the Successor Agency obligated under the City’s prior undertakings under the Rule. The Successor Agency is not obligated under the Continuing Disclosure Certificate for the Bonds.

During the five year period preceding the date of this Official Statement:

(i) The Successor Agency failed to file, or file on a timely basis, notices of rating changes, or insurer-related changes or rating withdrawals with respect to numerous series of bonds. The Successor Agency also failed to file on a timely basis certain annual operating data for Fiscal Year 2015-16 with respect to numerous series of bonds. In addition, the Successor Agency failed to correctly link all applicable CUSIP numbers to a notice of defeasance that was otherwise timely filed by the Successor Agency in connection with the defeasance of a series of bonds. The Successor Agency has correctly linked all applicable CUSIP numbers to such notice.

(ii) The City failed to file, on a timely basis, notices of rating changes, or insurer-related rating changes or rating withdrawals with respect to numerous series of bonds. In addition, the assessed value of taxable property and top ten real property tax assesses information contained in the Annual Reports for each of the past five years reflects information as of the “prior” fiscal year instead of the “current” fiscal year, as may have been required by the terms of the City’s undertakings relating to previous issues of general obligation bonds.



## LITIGATION AND SIGNIFICANT CLAIMS

[No litigation is pending against the City with service of process accomplished or threatened in writing concerning the validity of the Bonds, or questioning the political existence of the City or seeking to restrain or enjoin the issuance or execution of the Bonds. The City will furnish to the purchaser of the Bonds a certificate as to the foregoing as of the time of the original delivery of the Bonds.]

There are a variety of civil cases in which the City is a named defendant pending at any given time, including without limitation, the litigation described in Appendix A. See APPENDIX A – “THE CITY OF SAN JOSE: DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND CONSENT DECREES.” Additionally, there are numerous claims filed with the City or with other agencies in which the claimants allege that they have been damaged by the City. If these cases or these claims which develop into civil actions were determined adversely to the City, it is possible there could be an adverse effect on the City’s revenues and cash flow.

## RATINGS

The Bonds have received ratings of “\_\_\_” by Moody's Investors Service, “\_\_\_” by S&P Global Ratings, and “\_\_\_” by Fitch.

These ratings reflect only the views of the respective rating agency and any desired explanation of the significance of these ratings should be obtained from the rating agencies. There is no assurance that any ratings will continue for any given period of time or will not be revised downward or withdrawn entirely by the rating agencies, if in the judgment of the rating agencies, circumstances so warrant. Any such downward revision or withdrawal of any ratings may have an adverse effect on the market price of one or more series of the Bonds.

## MUNICIPAL ADVISOR

The City has retained Public Resources Advisory Group, Oakland, California, as Municipal Advisor in connection with the authorization and delivery of the Bonds. The Municipal Advisor is not obligated to undertake, and has not undertaken to make, an independent verification or to assume responsibility for the accuracy, completeness or fairness of the information contained in the Official Statement. The fees and expenses of the Municipal Advisor are contingent upon the successful issuance and delivery of the Bonds.

## COMPETITIVE SALE OF BONDS

**Series 2019A-1 Bonds.** The Series 2019A-1 Bonds were sold pursuant to a competitive bidding process held on [July 9], 2019, pursuant to the terms set forth in an Official Notice Inviting Bids for the Bonds (the “**Official Notice Inviting Bids**”).

The Series 2019A-1 Bonds were awarded to \_\_\_\_\_ (“\_\_\_\_\_”), whose proposal represented the lowest true interest cost for the Series 2019A-1 Bonds as determined in accordance with the Official Notice Inviting Bids. \_\_\_\_\_ has agreed to purchase the Series 2019A-1 Bonds at a price of \$\_\_\_\_\_ (being the principal amount of the Series 2019A-1 Bonds



plus a [net] original issue premium of \$\_\_\_\_\_ and less a purchasers' discount of \$\_\_\_\_\_). \_\_\_\_\_ will purchase all of the Series 2019A-1 Bonds, Taxable Series 2019A-2 Bonds, and Taxable Series 2019B Bonds if any are purchased.

**Taxable Series 2019A-2 Bonds.** The Taxable Series 2019A-2 Bonds were sold pursuant to a competitive bidding process held on \_\_\_\_\_, 2019, pursuant to the terms set forth in the Official Notice Inviting Bids.

The Taxable Series 2019A-2 Bonds were awarded to \_\_\_\_\_ ("\_\_\_\_\_"), whose proposal represented the lowest true interest cost for the Taxable Series 2019A-2 Bonds as determined in accordance with the Official Notice Inviting Bids. \_\_\_\_\_ has agreed to purchase the Taxable Series 2019A-2 Bonds at a price of \$\_\_\_\_\_ (being the principal amount of the Taxable Series 2019A-2 Bonds plus a [net] original issue premium of \$\_\_\_\_\_ and less a purchasers' discount of \$\_\_\_\_\_). \_\_\_\_\_ will purchase all of the Series 2019A-1 Bonds, Taxable Series 2019A-2 Bonds, and Taxable Series 2019B Bonds if any are purchased.

**Taxable Series 2019B Bonds.** The Taxable Series 2019B Bonds were sold pursuant to a competitive bidding process held on \_\_\_\_\_, 2019, pursuant to the terms set forth in the Official Notice Inviting Bids.

The Taxable Series 2019B Bonds were awarded to \_\_\_\_\_ ("\_\_\_\_\_"), whose proposal represented the lowest true interest cost for the Taxable Series 2019B Bonds as determined in accordance with the Official Notice Inviting Bids. \_\_\_\_\_ has agreed to purchase the Taxable Series 2019B Bonds at a price of \$\_\_\_\_\_ (being the principal amount of the Taxable Series 2019B Bonds plus a [net] original issue premium of \$\_\_\_\_\_ and less a purchasers' discount of \$\_\_\_\_\_). \_\_\_\_\_ will purchase all of the Series 2019A-1 Bonds, Taxable Series 2019A-2 Bonds, and Taxable Series 2019B Bonds if any are purchased.

**Series 2019C Bonds.** The Series 2019C Bonds were sold pursuant to a competitive bidding process held on \_\_\_\_\_, 2019, pursuant to the terms set forth in the Official Notice Inviting Bids.

The Series 2019C Bonds were awarded to \_\_\_\_\_ ("\_\_\_\_\_"), whose proposal represented the lowest true interest cost for the Series 2019C Bonds as determined in accordance with the Official Notice Inviting Bids. \_\_\_\_\_ has agreed to purchase the Series 2019C Bonds at a price of \$\_\_\_\_\_ (being the principal amount of the Series 2019C Bonds plus a [net] original issue premium of \$\_\_\_\_\_ and less a purchasers' discount of \$\_\_\_\_\_). \_\_\_\_\_ will purchase all of the Series 2019C Bonds if any are purchased.

**Taxable Series 2019D Bonds.** The Taxable Series 2019D Bonds were sold pursuant to a competitive bidding process held on \_\_\_\_\_, 2019, pursuant to the terms set forth in the Official Notice Inviting Bids.

The Taxable Series 2019D Bonds were awarded to \_\_\_\_\_ ("\_\_\_\_\_") and, together with \_\_\_\_\_, \_\_\_\_\_ and \_\_\_\_\_, the "**Purchasers**"), whose proposal represented the lowest true interest cost for the Taxable Series 2019D Bonds as determined in accordance with the Official Notice Inviting Bids. \_\_\_\_\_ has agreed to purchase the Taxable Series 2019D Bonds at a price of \$\_\_\_\_\_ (being the principal amount of the Series 2019D Bonds plus a [net] original issue premium of \$\_\_\_\_\_ and less a purchasers' discount of \$\_\_\_\_\_). \_\_\_\_\_ will purchase all of the Series 2019D Bonds if any are purchased.



The Purchasers may offer and sell any Bonds to certain dealers and others at a price lower than the offering price stated on the inside cover pages of this Official Statement. The offering price may be changed from time to time by the Purchasers.

### **ADDITIONAL INFORMATION**

Quotations from and summaries and explanations of the Bonds, the Fiscal Agent Agreement providing for issuance of the Bonds, and the constitutional provisions, statutes and other documents referenced herein, do not purport to be complete, and reference is made to said documents, constitutional provisions and statutes for full and complete statements of their provisions.

Some of the data contained herein has been taken or constructed from City records. Appropriate City officials, acting in their official capacities, have reviewed this Official Statement and have determined that, as of the date hereof, the information contained herein is, to the best of their knowledge and belief, true and correct in all material respects and does not contain an untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made herein, in light of the circumstances under which they were made, not misleading. This Official Statement has been approved by the City Council.

CITY OF SAN JOSE, CALIFORNIA

By: \_\_\_\_\_  
Title: City Manager



**APPENDIX A**

**THE CITY OF SAN JOSE  
DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION**



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## INTRODUCTION TO APPENDIX A

This Appendix A is the part of the Official Statement that provides investors with information concerning the City of San José (the “**City**”). Investors are advised to read the entire Official Statement, including Appendix A, to obtain information essential to making an informed investment decision.

When used in this Appendix A and in any continuing disclosure made by the City, the words or phrases “will likely result,” “are expected to,” “will continue,” “is anticipated,” “estimate,” “project,” “forecast,” “expect,” and “intend,” and similar expressions identify “forward-looking statements.” Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements. Any forecast is also subject to such risks and uncertainties. Inevitably, some assumptions used to develop the forecasts will not be realized and unanticipated events and circumstances may occur. Therefore, there are likely to be differences between forecasts and actual results, and those differences may be material. This Appendix A speaks only as of its date, and the information and expressions of opinion contained in this Official Statement are subject to change without notice.

This Appendix A summarizes portions of the following documents of the City:

- Basic Financial Statements for the Fiscal Year ended June 30, 2018 (included in this Official Statement as Appendix C);
- Comprehensive Annual Financial Report for the Fiscal Year ended June 30, 2018;
- Comprehensive Annual Debt Report for the Fiscal Year ended June 30, 2018;
- Adopted Operating Budget for the Fiscal Years ended June 30, 2018 and June 30, 2019;
- Annual Report for the Fiscal Years ended June 30, 2017 and June 30, 2018;
- 2018-2019 Mid-Year Budget Review;
- 2019-2020 City Manager’s Budget Request & 2020-2024 Five-Year Forecast and Revenue Projections;
- 2019-2020 Mayor’s March Budget Message;
- 2019-2020 Proposed Operating Budget, as modified and adopted by the City Council on June 11, 2019; and
- 2019-2020 Mayor’s June Budget Message.

Copies of documents listed above are available from the Finance Department – Debt Management, City of San José City Hall, 200 East Santa Clara Street, San José, CA 95113; Phone (408) 535-7010; email: [debt.management@sanjoseca.gov](mailto:debt.management@sanjoseca.gov).

The City maintains a number of websites. However, the information presented on the City’s websites is not part of this Appendix A and should not be relied upon in making an investment decision with respect to the Bonds.



## INTRODUCTION TO THE CITY OF SAN JOSE

The City is the oldest city in the State of California (the “**State**”), developing from a Spanish pueblo established in 1777. Situated between the Diablo and Santa Cruz mountain ranges, the City encompasses approximately 180 square miles at the south end of the San Francisco Bay and is the county seat of Santa Clara County (the “**County**”). With a 2019 estimated population of approximately 1,043,058<sup>1</sup>, the City is the third most populous city in the State and the tenth most populous in the United States.

The City has transformed from the agricultural setting of its early years into the largest city in the Silicon Valley. Silicon Valley is a region in the Southern San Francisco Bay Area of Northern California which serves as a global center of high technology, innovation, and social media. It corresponds roughly to the geographical Santa Clara Valley. The San José-Sunnyvale-Santa Clara Metropolitan Statistical Area (the “**San José MSA**”) in the Silicon Valley has a large concentration of high-tech employment with 326,100 workers out of a total civilian employment level of 1.14 million<sup>2</sup>. Silicon Valley is home to many of the world’s largest technology companies and is a global center of technology innovation. Commercial, retail, professional, high-tech manufacturing, electronic assembly, and service businesses all have a presence in the City. On the international front, the City attracts significant foreign investment from throughout the globe. For additional information regarding the recent economic environment, see “DEMOGRAPHIC AND ECONOMIC INFORMATION – Economic Overview.”

## FISCAL PRESSURES

### Fiscal Overview - 2009 to 2019

Between 2008-2009 and 2011-2012, the City faced significant budget challenges, particularly in the General Fund, as the growth in revenues did not keep pace with the increase in expenditures. The Great Recession, commencing in 2008, led to declines and weaknesses in the City’s economically-sensitive revenues, particularly Property Tax and Sales Tax receipts which are the City’s two largest General Fund revenue sources. For example, between 2008-2009 through 2010-2011 Property Tax decreased by \$16 million and between 2007-2008 and 2009-2010 Sales Tax dropped by approximately \$27 million. While revenues were dropping, General Fund expenditures were increasing, which was driven primarily by increases in retirement and benefit costs. The City’s employer retirement contributions for all City funds increased 87% from \$136.4 million in 2008-2009 to \$255.1 million in 2011-2012, with the largest increases experienced in 2010-2011 and 2011-2012. See APPENDIX B – “THE CITY OF SAN JOSE: RETIREMENT PLANS.”

Between 2008-2009 and 2011-2012, the City projected General Fund shortfalls ranging from \$29.6 million to \$118.5 million annually, totaling \$347.5 million over the four-year period. These projected shortfalls were addressed each year in the development of the Adopted Budget. The City addressed the annual budget shortfalls by implementing significant service and position reductions, employee compensation reductions, changes to service delivery models across the organization, and undertaking efforts to maintain and increase revenues,

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<sup>1</sup> State of California, Department of Finance, E-1 Population Estimates for Cities, Counties, and State with Annual Percentage Change - January 1, 2018 and 2019 (Released May 2019).

<sup>2</sup> State of California, Employment Development Department, Labor Market Information Division, June 2018.



including four voter-approved tax measures. These four tax measures include: (1) modifications to the telephone utility tax to decrease the tax rate and expand the types of charges subject to the tax; (2) imposition of a telephone line tax to replace the fee to fund 911 services; (3) an increase of the gross receipts tax rate on cardroom businesses from 13% to 15% and an increase in the number of tables allowed City-wide from 80 to 98; and (4) imposition of a gross receipts tax on marijuana businesses up to a maximum rate of 10%. The reduction in staffing reduced services to the community, such as police, fire, and library services as well as the City's administrative functions. See "MAJOR GENERAL FUND REVENUE SOURCES – Utility Taxes" and "– Business Taxes" for a discussion regarding the City's utility taxes, cardroom business taxes and marijuana business taxes.

The actions described above, along with improved economic conditions, resulted in some improvement in the City's fiscal condition in 2012-2013, during which elements of the City's Fiscal Reform Plan were implemented including the elimination of the Supplemental Retiree Benefit Reserve and changes to existing healthcare plans for active employees and retirees. The Fiscal Reform Plan was a successor to a prior plan approved by the City Council in 2008 aimed at the elimination of the structural deficit in the General Fund. The Fiscal Reform Plan presented a strategy to achieve long-term financial stability, restore key City services to January 1, 2011 service levels for police, fire, libraries, and community centers, and open facilities that were recently completed or under construction. The Fiscal Reform Plan identified cost reduction strategies, which were primarily related to the City's retirement costs. It also identified revenue strategies that would require a voter-approved ballot measure such as a sales tax measure and other tax measures. Despite such changes, the City continued to face uncertainties related to the implementation of the retirement reform measures, including those approved by the voters with the passage of Measure B in June 2012, which enacted the Sustainable Retirement Benefits and Compensation Act ("**Measure B**"), and changes to the lowest cost healthcare plans offered to active employees and retirees. See "– Measure B and Status of Retirement Reforms" below for further discussion regarding Measure B.

Since 2012-2013, annual deficits or surpluses ranging from a deficit of \$10.0 million to a surplus of \$10.4 million have been forecasted each year, representing approximately 1% or less of the General Fund expenditure budget. This reflected rising costs and strong increases in several revenue categories as a result of favorable economic conditions and/or changes in taxes, including voter approved ballot measures to implement a new local sales tax and to increase the existing business tax. For example, Property Tax receipts increased by \$101.2 million (2012-2013; \$205.0 million and 2017-2018; \$306.2 million) and Transient Occupancy Tax receipts increased by \$9.4 million (2012-2013; \$10.1 million and 2017-2018; \$19.5 million) due to positive economic conditions. In addition, Sales Tax grew by \$62.5 million (2012-2013; \$163.8 million and 2017-2018; \$226.3 million), which was primarily due to the approval of a 0.25% transaction and use tax (commonly referred to as a sales tax) approved by San José voters in June 2016, as well as general economic growth. Finally, Business Tax revenue has grown by \$25.5 million (2012-2013; \$45.2 million and 2017-2018; \$70.7 million), which was primarily the result of an increase to the City's local business tax that was approved by San José voters on November 8, 2016 to provide for additional funding in the City's General Fund to support city services. See "MAJOR GENERAL FUND REVENUE SOURCES – Sales and Use Taxes" and "– Business Taxes."

The increases in General Fund expenditures were driven primarily by increases in retirement and benefit costs for City employees. In particular, the City's employer retirement contributions for all City funds increased 35% from \$245.4 million in 2012-2013 to \$372.3 million in 2017-18. See APPENDIX B – "THE CITY OF SAN JOSE: RETIREMENT PLANS."



In addition, the City is the only major city in the country that has a smaller daytime population than nighttime population commonly referred to as “bedroom communities.” Large cities are typically job centers. In contrast, the City has job centers around it. This imbalance between jobs and residents creates fiscal challenges for the City because the City has to provide services to its one million residents, a significant portion of who then go and work and spend dollars outside the City. The City’s general plan, Envision San José 2040 General Plan (the “**General Plan**”), includes a set of major strategies to address long-term development of the City in a manner that promotes greater land use within the City for employment, housing (in urban villages, the Downtown area of the City, North San José, and certain other specific plan areas) and improves the ability of City residents to commute to work without vehicles. A portion of the net proceeds of the Taxable Series 2019B Bonds will be used to finance the acquisition of open space in Coyote Valley, located at the southern end of the City and to the north of Morgan Hill, thereby further reducing the land within the City available for employment purposes. See “RECENT ECONOMIC DEVELOPMENT ACTIVITIES – Development Challenges” for a discussion of recent economic development in the City and challenges relating to development in the City. See also “THE BONDS – Purpose of Issues” for a discussion regarding the use of net proceeds of the Taxable Series 2019B Bonds and the other Bonds.

## **Measure B and Status of Retirement Reforms**

In June 2012, approximately 70% of San José voters passed Measure B. Measure B amended the City’s Charter provisions related to the Retirement Plans to provide for, among other modifications: (1) additional employee contributions from employees who remain members of the existing Retirement Plans; (2) alternative plans to which existing employees could opt in, subject to approval by the Internal Revenue Service; (3) parameters for Tier 2 plans within both Retirement Plans; (4) limitations on disability retirements; (5) elimination of supplemental retiree benefits; (6) requirements for retiree healthcare contributions; and (7) suspension of cost of living adjustments in the event the City declares a fiscal emergency. See APPENDIX B – “THE CITY OF SAN JOSE: RETIREMENT PLANS” for information about the City’s retirement plans.

Measure B was subsequently the subject of various legal challenges. In November 2016, the voters approved the Alternative Pension Reform Act (“**Measure F**”) that the City Council placed on the ballot as a result of settlement frameworks entered into with the City’s bargaining groups related to Measure B. The City Council adopted ordinances to implement the terms of the settlement frameworks and Measure F in February and May 2017. The City also approved a settlement in November 2017 in connection with a lawsuit brought by individual retirees and a retiree association. The legal challenges to Measure B have been resolved. See APPENDIX B – “THE CITY OF SAN JOSE: RETIREMENT PLANS – RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS” for further discussion regarding Measure B, Measure F and the settlement of the legal challenges brought in connection with Measure B.

## **Current Outlook**

Looking forward, the City is forecasting small incremental General Fund surpluses and shortfalls in the next five fiscal years. In the 2020-2024 Five-Year Forecast and Revenue Projections, the City forecasted such surpluses and shortfalls to range between a surplus of \$11.4 million to a shortfall of \$15.6 million. These margins are relatively narrow when put into context with the size of the projected General Fund budget, ranging from -1.2% to 0.9% of the projected annual budget of \$1.2 billion to \$1.4 billion. However, as noted in the 2020-2024 Five-



Year Forecast and Revenue Projections, there are significant expenditure components that are not incorporated into such forecast, including programs funded on a one-time basis in fiscal year 2018-2019, unmet/deferred infrastructure needs and any potential decreases in federal funding to the City that may result in the event a citizenship question is added by the Census Bureau to the 2020 Census. Over the five-year period, the City projected a total General Fund shortfall of approximately \$16.2 million, or an average of approximately \$3.2 annually. Portions of the 2020-2024 Forecast related to 2019-2020 and 2020-2021 were modified by the 2019-2020 Proposed Operating Budget released on May 1, 2019, including the projected General Fund incremental surplus or shortfall in the next five fiscal years as shown in Table 10b. See “BUDGET – Budget Outlook – 2020-2024 Forecast” for a discussion regarding the City’s General Fund forecast for the next five fiscal years. See also “– SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND CONSENT DECREES – Affirmative Litigation – Census Litigation” for a discussion regarding litigation relating to the proposed addition of the citizenship question to the 2020 Census.

## DEMOGRAPHIC AND ECONOMIC INFORMATION

### Introduction

The information provided in the section entitled “DEMOGRAPHIC AND ECONOMIC INFORMATION” has been collected from sources that the City believes to be reliable and is the most current information available from those sources. The City has included this information to provide context about the City’s finances.

For current estimates regarding the City’s General Fund revenue sources, see “BUDGET – Budget Outlook” and “MAJOR GENERAL FUND REVENUE SOURCES,” below.

### Economic Overview

**General.** The Silicon Valley, including the City, continues to show positive economic performance, but some economic indicators are beginning to moderate from the extremely strong performance experienced in recent years and the local economy is expected to enter a period of slower economic growth. Local unemployment levels, which have consistently been well below national levels are anticipated to remain low. While the employment growth level is a bit slower than was previously experienced, it is still positive. Employment levels in Silicon Valley are determined largely by the flow of venture capital funding and the overall health of the U.S. economy. As both of these contributors continue to remain healthy, local unemployment levels are projected to remain at low levels.

**Employment.** The April 2019 employment level in the San José MSA was 1.15 million or 2.7% higher than the April 2018 employment of approximately 1.12 million. Between April 2018 and April 2019, 29,900 jobs were added in the San José MSA. This includes 9,200 jobs in the information sector, 5,500 manufacturing jobs, and other major industries and employment growth including professional and business services (up 3,900 jobs), leisure and hospitality (up 3,500 jobs), government (up 3,000 jobs) and financial activities (up 1,200 jobs).<sup>3</sup> See “– Employment” below for employment figures for the City and the County and unemployment rates for the City, the County, the State and the United States for the five most recent calendar years available.

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<sup>3</sup> State of California Employment Development Department Labor Market Information Division Press Release, May 17, 2019.



**Unemployment.** The unemployment rate at the local level remains low. The unemployment rate in the San José MSA was 2.4% in April 2019, down from the 3.0% unemployment rate experienced in March 2019. This compares with an unadjusted unemployment rate of 3.9% for the State, 3.3% for the nation and 2.3% for the County in March 2019.<sup>4</sup>

**Construction.** Local construction activity through March 2019 decreased 17.4% from the high levels experienced in fiscal year 2017-2018 during the same period. In particular, residential permits for new dwelling units through March 2019 totaled 2,473 versus 2,620 in the prior year. Correspondingly, the valuation of new residential construction and alteration activity have also decreased to approximately \$449.5 million in fiscal year 2018-2019 from \$530.0 million in fiscal year 2017-2018. See “– Construction” below for a history of construction valuation and new dwelling units for the most recent five calendar years.

**Home Prices and Sales.** After seven years of year-over-year home price growth, the local real estate market is beginning to slow down. According to data from the Santa Clara County Association of Realtors, the median single-family home price peaked at \$1.3 million in May 2018, which represented a 30% increase from the May 2017 median home price, but then steadily began decreasing. In April 2019, the median single-family home price totaled \$1.15 million, which represents a 10% decrease from the April 2018 median single-family home price of \$1.28 million, but is approximately 17% above the April 2017 price of \$980,000.

The number of property transfers (sales) has also continued to decline. The total number of property transfers that occurred year-to-date through April 2019 has dropped over 9% compared to the prior year. In April 2019, the number of property transfers totaled 659. However, while homes continue to sell quickly, it appears they are on the market longer than in fiscal year 2017-2018. For example, the average days-on-market for single-family and multi-family dwellings in April 2019 totaled 28 days, which is more than twice as long as the 11 days experienced in April 2018.

Table 1 on the following page shows the average monthly median price for a single family home in the County for 2007-2008 through 2017-2018, and 2018-19 as of April 2019.

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<sup>4</sup> State of California Employment Development Department Labor Market Information Division Press Release, May 17, 2019.



**Table 1**  
**County of Santa Clara**  
**Average Monthly Median Price of Single Family Home**

<b>Fiscal Year</b>	<b>Average Median Price</b>	<b>Percentage Change</b>
2007-2008 .....	\$695,708	--
2008-2009 .....	463,008	(33.5)%
2009-2010 .....	503,592	8.8
2010-2011 .....	498,187	(-1.1)
2011-2012 .....	499,620	0.3
2012-2013 .....	630,001	26.1
2013-2014 .....	724,450	15.0
2014-2015 .....	781,708	7.9
2015-2016 .....	870,042	11.3
2016-2017 .....	921,019	5.9
2017-2018 .....	1,131,704	22.9
2018-2019 .....	1,109,222 <sup>(1)</sup>	-2.0

<sup>(1)</sup> As of April 2019.

Source: Santa Clara Association of Realtors.

## Population

City residents account for over half of the population of the County, which is the most populous of the San Francisco Bay Area counties. While the period from 1960 to 1980 was characterized by extremely rapid population growth in both the City and County, the last three decades reflect a trend of slower but steady growth. Table 2 shows the population of the City, the County and the State according to the U.S. Census Bureau for the years 1960, 1970, 1980, 1990, 2000 and 2010 and according to the California Department of Finance for the years 2016, 2017, 2018 and 2019.

**Table 2**  
**City, County and State Population Statistics**

	<b>City of San José</b>	<b>% Change</b>	<b>County of Santa Clara</b>	<b>% Change</b>	<b>State of California</b>	<b>% Change</b>
1960 .....	204,196	--	642,315	--	15,717,204	--
1970 .....	459,913	125.23%	1,064,714	65.76%	19,953,134	26.95%
1980 .....	629,442	36.86	1,295,071	21.64	23,667,902	18.62
1990 .....	782,248	24.28	1,497,577	15.64	29,760,021	25.74
2000 .....	895,131	14.43	1,682,585	12.35	33,873,086	13.82
2010 .....	945,942	5.68	1,781,642	5.89	37,253,956	9.98
2016 .....	1,035,312	9.45	1,924,582	8.02	39,179,627	5.17
2017 .....	1,042,782	0.72	1,937,473	0.67	39,500,973	0.82
2018 .....	1,042,900	0.01	1,947,798	0.53	39,740,508	0.61
2019 .....	1,043,058	0.02	1,954,286	0.33	39,927,315	0.47

Sources: U.S. Census Bureau (1960-2010), California Department of Finance (2016-2019).



## Employment

Table 3 shows employment figures for the City and the County and unemployment rates for the City, the County, the State and the United States for the five most recent calendar years available. The City's unemployment rate increased from 6.7% in 2008 to 12.2% in 2010 during the most recent recession, but has decreased to 2.4% as of April 2019.

<b>Table 3</b>					
<b>Estimated Average Annual Employment and Unemployment of Resident Labor Force<sup>(1)</sup></b>					
<b>Civilian Labor Force</b> <i>(in thousands)</i>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
<b>City of San José</b>					
Employed .....	498	513	524	517	540
Unemployed .....	31	25	23	19	15
Total <sup>(2)</sup> .....	529	538	547	536	555
<b>County of Santa Clara</b>					
Employed .....	941	968	985	1,009	1,021
Unemployed .....	51	9742	39	33	27
Total <sup>(2)</sup> .....	992	1,010	1,024	1,042	1,048
<b>Unemployment Rates</b>					
City .....	5.8%	4.6%	4.2%	3.6%	2.7%
County .....	5.2	4.2	3.8	3.2	2.6
State .....	7.5	6.2	5.5	4.8	4.2
United States .....	6.2	5.3	4.9	4.4	3.9

<sup>(1)</sup> Data is not seasonally adjusted.

<sup>(2)</sup> Totals may not add due to independent rounding.

Source: California Employment Development Department, Labor Market Information Division; United States Department of Labor, Bureau of Labor Statistics.

The City is the largest city in the County. The high-technology industry component of the City's economy is diversified in research, development, manufacturing, marketing, and management. Development of high technology has been supported by the area's proximity to San José State University, Stanford University, Santa Clara University, and other institutions of higher education, and such research and development facilities as SRI International (formerly the Stanford Research Institute), the Stanford Linear Accelerator Center and NASA Ames Research Center.

While the region is known worldwide as "Silicon Valley," the silicon-based semiconductor industry is only a part of the industrial picture. Other industries include information systems, solar, manufacturing, computers, peripherals, instruments, software and a wide array of communication electronics.



Table 4 shows the composition of employment in the San José MSA by general category for the most recent three years available.

**Table 4**  
**San José-Sunnyvale-Santa Clara Metropolitan Statistical Area**  
**Estimated Average Annual Employment by Industry**

<b>Industry</b>	<b>2016</b>	<b>Percent of Total</b>	<b>2017</b>	<b>Percent of Total</b>	<b>2018</b>	<b>Percent of Total</b>
Farm .....	6,100	0.56%	5,800	0.52%	5,800	0.51%
Natural Resources & Mining.....	300	0.03	200	0.02	200	0.02
Construction.....	48,300	4.45	49,300	4.44	49,400	4.37
Manufacturing .....	166,600	15.34	166,400	14.98	172,300	15.23
Wholesale Trade .....	35,200	3.24	32,900	2.96	31,700	2.80
Retail Trade .....	85,800	7.90	85,800	7.72	86,300	7.63
Transportation, Warehousing, Utilities ...	15,500	1.43	15,400	1.39	16,000	1.41
Information.....	74,700	6.88	84,700	7.63	91,700	8.11
Financial Activities.....	35,600	3.28	36,100	3.25	37,100	3.28
Professional & Business Services .....	233,000	21.45	237,400	21.37	237,300	20.98
Educational & Health Services .....	162,500	14.96	168,800	15.20	172,700	15.27
Leisure & Hospitality.....	100,600	9.26	103,400	9.31	105,000	9.28
Other Services .....	27,600	2.54	28,900	2.60	28,800	2.55
Government .....	94,100	8.66	95,500	8.60	96,800	8.56
Total <sup>(1)</sup> .....	1,086,000		1,110,700		1,131,000	

<sup>(1)</sup> Totals may not add due to independent rounding.

Source: California Employment Development Department, Labor Market Information Division.



## Major Employers

Table 5 shows fifteen selected major employers in the City, ranked by the number of their employees, estimated as of May 2019. Because there is no official source for this information, it has been gathered by the City's Office of Economic Development on an informal basis from sources believed to be reliable. However, the City can provide no assurances as to the accuracy or completeness of the information shown in Table 5.

**Table 5**  
**City of San José**  
**Selected Major Employers as of May 2019**

	<b>Company/Organization</b>	<b>Approximate Number of Employees</b>	<b>Percent of Total City Employment</b>
1	Santa Clara County	18,570	4.1%
2	Cisco Systems	9,500	2.1%
3	City of San José	6,400	1.5%
4	San Jose State University	3,600	0.8%
5	eBay	3,400	0.8%
6	PayPal	3,300	0.7%
7	Adobe Systems	2,900	0.6%
8	Kaiser Permanente	2,585	0.6%
9	Target Stores	2,400	0.5%
10	Good Samaritan Hospital	2,240	0.5%
11	Western Digital	2,200	0.5%
12	Super Micro Computer	2,000	0.4%
13	Safeway	1,800	0.4%
14	Cadence Design Systems	1,750	0.4%
15	Regional Medical Center	1,625	0.4%

*Source: City of San José, Office of Economic Development, San José business tax filings, and company surveys. City of San José 2018-19 Adopted Budget.*



## Household Income

Household income, as measured by the U.S. Census Bureau, includes the income of the householder and all other people 15 years and older in the household, whether or not they are related to the householder. The median is based on the income distribution of all households, including those with no income. Table 6 shows the top ten median household incomes by metropolitan statistical area in the United States in 2017, the most recent American Community Survey available. The San José MSA had the highest median household income in 2017, which was well above the national median.

**Table 6**  
**United States**  
**2017 Top Ten Median Household Income**

1.	<b>San José-Sunnyvale-Santa Clara, CA Metro Area</b>	<b>\$117,474</b>
2.	San Francisco-Oakland-Fremont, CA Metro Area	101,714
3.	Washington-Arlington-Alexandria, DC-VA-MD-WV Metro Area	99,669
4.	Bridgeport-Stamford-Norwalk, CT Metro Area	91,198
5.	Napa, CA Metro Area	86,562
6.	Boston-Cambridge-Newton, MA-NH Metro Area	85,691
7.	Oxnard-Thousand Oaks-Ventura, CA Metro Area	82,857
8.	Seattle-Tacoma-Bellevue Metro Area	82,133
9.	California-Lexington Park, MD Metro Area	81,495
10.	Urban Honolulu, HI Metro Area	81,284
	U.S. Median	\$60,336

*Source: U.S. Census Bureau, Income and Poverty in the United States 2017 American Community Survey 2017.*

## Retail Sales

Table 7 sets forth a history of taxable sales for the City for calendar years 2013 to 2017 as reported by the California State Board of Equalization (the “**BOE**”) for years 2013 through 2016 and the California Department of Tax and Fee Administration (“**CDTFA**”) for 2017. [Information regarding taxable sales for the City for calendar year 2018 is not yet available.] Taxable sales are reported using the North American Industry Classification System codes.

For 2017-2018, sales tax receipts of the City totaled approximately \$226 million, an increase of approximately \$18 million over sales tax receipts of approximately \$208 million for fiscal year 2016-2017. For additional information regarding sales tax receipts, see “MAJOR GENERAL FUND REVENUE SOURCES – Sales and Use Taxes.”



**Table 7**  
**City of San José**  
**Taxable Sales**  
**Calendar Years 2012 to 2016**  
**(in thousands)**

	2013	2014	2015	2016	2017
Motor Vehicle and Parts Dealers .....	\$1,686,882	\$1,819,198	\$1,969,242	\$2,034,428	\$2,134,572
Home Furnishings and Appliance Stores .....	571,857	616,670	730,134	727,764	728,521
Bldg. Matrl. and Garden Equip. and Supplies....	826,743	853,791	910,837	945,772	972,171
Food and Beverage Stores .....	490,554	514,184	549,792	559,060	577,938
Gasoline Stations .....	1,293,598	1,245,370	1,048,492	954,475	1,050,645
Clothing and Clothing Accessories Stores .....	909,595	962,662	999,094	998,722	971,102
General Merchandise Stores.....	1,209,364	1,238,634	1,111,272	1,071,528	1,110,193
Food Services and Drinking Places.....	1,549,971	1,673,477	1,812,304	1,940,194	2,045,134
Other Retail Group .....	993,150	1,010,789	1,024,576	1,014,199	968,095
Total Retail and Food Services .....	9,531,713	9,934,775	10,155,744	10,246,143	10,558,372
All Other Outlets .....	4,427,791	4,759,064	5,017,109	4,878,198	4,495,992
Total All Outlets .....	<u>\$13,959,504</u>	<u>\$14,693,838</u>	<u>\$15,172,853</u>	<u>\$15,124,341</u>	<u>15,054,364</u>

Source: California State Board of Equalization. Taxable Sales in California (Sales & Use Tax) for years 2013-2016. State Department of Tax and Fee Administration for year 2017.

## Construction Activity

A history of construction valuation and new dwelling units for the most recent five calendar years appears in Table 8.

**Table 8**  
**City of San José**  
**Construction Valuation and New Dwelling Units**  
**(in thousands)**

	2014	2015	2016	2017	2018
<b>Valuation:<sup>(1)</sup></b>					
Residential .....	\$ 861,789	\$ 483,399	\$ 563,521	\$ 694,998	\$536,303
Non-Residential ..	581,288	870,199	1,535,204	1,658,682	795,116
Total	<u>\$ 1,443,077</u>	<u>\$ 1,353,598</u>	<u>\$ 2,098,725</u>	<u>\$2,353,680</u>	<u>\$1,331,419</u>
<b>New Dwelling Units:</b>					
Single Family .....	393	160	226	201	315
Multi-Family .....	4,058	1,860	1,862	2,896	2,658
Total	<u>4,451</u>	<u>2,020</u>	<u>2,088</u>	<u>3,097</u>	<u>2,973</u>

<sup>(1)</sup> Valuation figures are adjusted to 2018 dollars (per June San Francisco-Oakland-Hayward Consumer Price Index).

Source: City of San José, Department of Planning, Building and Code Enforcement.



More information regarding building permits and fees is set forth below in the section entitled “MAJOR GENERAL FUND REVENUE SOURCES – Licenses and Permits.”

## **Education**

The residents in the City are highly educated. According to the United States Census Bureau’s American Community Survey for 2017, approximately 43% of the City’s population have a bachelor’s degree or higher, compared to approximately 34% in the State and approximately 32% in the United States.

For the 2017-2018 school year, the residents of the County are served by 257 elementary schools; 68 middle schools and junior high schools; 55 high schools; 31 K-12, community, alternative, special education, continuation and juvenile hall schools, 65 charter schools (for the 2016-2017 school year) and a number of private schools. The City is served by 15 of the 32 public school districts in the County. Many of these school districts cross municipal boundaries. Principal public school systems serving the City are the San José Unified School District (grades K-12) and the East Side Union High School District.

In addition, the City includes or is in close proximity to the County’s seven community colleges, which are within four community college districts (San José-Evergreen, Foothill-DeAnza, Gavilan Joint, and West Valley-Mission). Major universities in the County include Stanford University, Santa Clara University (currently ranked the number 1 Regional University in the West region of the United States by U.S. News & World Report), and San José State University.

## **Transportation**

**General.** The San José area is served by a network of freeways providing regional, national and international access. Bayshore Freeway (Highway 101), a major north-south highway between San Francisco and Los Angeles, provides access to air passenger and cargo facilities at Norman Y. Mineta San José International Airport (the “**Airport**”) and San Francisco International Airport. Interstate 880 connects the City with the Oakland International Airport and the Port of Oakland. Interstates 280 and 680 provide access to the peninsula and eastern regions of the San Francisco Bay Area, respectively, and State Route 17 serves to connect San José with the Pacific Coast at Santa Cruz. Additional freeways serving the local area are State Routes 85, 87 and 237.

**Public Transportation.** The Santa Clara Valley Transportation Authority (the “**VTA**”) provides public transit service throughout the County, which is readily accessible to residents of the City as most residences and businesses in the City are within a quarter mile of bus or light rail service. VTA also partners with Altamont Commuter Express and Caltrain to provide commuter rail service, with Santa Cruz Metro to provide regional bus service from Santa Cruz to Downtown San José, and with the Dumbarton Express for bus services between the East Bay and northern Santa Clara County work centers and communities.

Caltrain, a commuter rail service with 32 stations, runs from Gilroy through the City and north to San Francisco, with an average weekday ridership of 62,000 (2017). Caltrain operates 92 weekday trains, including 22 Baby Bullet express route trains that travel from the City to San Francisco in less than an hour. Electrification of the Caltrain system is under construction, with electric trains anticipated to be in service in 2022.



Bay Area Rapid Transit (“**BART**”) and California High-Speed Rail both have planned routes to the City. In April 2012, construction began on phase one of the BART Silicon Valley Extension. This extension of the BART system begins at the Warm Springs Station in Fremont, proceeds through Milpitas and ends in the Berryessa area in North San José. It includes two new BART stations that are part of two bigger, new transit centers: the Milpitas Transit Center and the Berryessa Transit Center. When BART service to the County begins, the Milpitas and Berryessa/North San José BART Stations are intended to be served by two lines providing direct and connecting service to the entire BART system. Construction activities are complete. [VTA and BART have begun the system testing phase with passenger service expected to begin by the end of 2019.]

Phase two of the BART Silicon Valley Extension is anticipated to consist of a six-mile, four-station extension that will expand BART operations from Berryessa/North San José through downtown San José to the City of Santa Clara. As part of phase two, VTA plans to locate a BART station at the historic Diridon Station with proposed completion by [2026]. In addition, the California High-Speed Rail Authority (the “**High-Speed Rail Authority**”) has announced plans to construct a 520-mile high-speed rail system in the State extending from Southern California to San Francisco and to locate a high-speed rail station at the Diridon Station to provide service to the Central Valley and Southern California. Neither the BART nor the high-speed rail projects at the Diridon Station is fully funded and there is no assurance that such funding will be obtained. In May 2019, the High-Speed Rail Authority released its “SB1029 Project Update Report,” in which the High-Speed Rail Authority acknowledged that it does not have all the funding in hand to construct the full 520-mile high-speed rail system from San Francisco to Los Angeles or even the Silicon Valley to Central Valley segment. The lack of funding is due in part to the cancellation by the United States federal government of a grant totaling approximately \$1 billion previously awarded to the State to fund a portion of the costs to construct the high-speed rail system in the State. In May 2019, the State filed a lawsuit against the federal government claiming that the U.S. Transportation Department lacks the authority to withhold the grant and seeking an injunction to keep the grant intact. As a result, the High-Speed Rail Authority has recommended a building block approach to delivering the system and focus on delivering an interim operating segment in the Central Valley. Currently, the historic Diridon Station, is served by CalTrain, VTA light rail, Altamont Corridor Express and Amtrak.

**Airport.** The Airport is located on approximately 1,050 acres of land four miles north of Downtown San José, between the Bayshore Freeway (Highway 101) and Interstate 880. It is a commercial service and general aviation airport and is classified by the Federal Aviation Administration as a “medium hub” (an airport that enplanes at least 0.25% but less than 1.0% of the total number of passenger boardings at all commercial service airports in the United States). The Airport is located approximately four miles north of downtown San José and serves the counties of Alameda, Monterey, San Benito, San Mateo, Santa Clara and Santa Cruz. According to statistics published by the Airports Council International-North America, in calendar year 2017, the Airport was the 37th busiest airport nationwide in terms of total passengers.

To accommodate the large increase in air traffic, the Airport is constructing a 30,000 square-foot extension to the south end of Terminal B containing six gates and capacity for over 1,300 passengers. The addition brings the total number of boarding gates to 36, provides capacity to accommodate additional growth in routes and alleviates congestion on the number of aircraft operations per gate per day. [The project was placed in use on June 13, 2019.]



## RECENT ECONOMIC DEVELOPMENT ACTIVITIES

### Overview

New industrial development in the City significantly increased in fiscal year 2017-2018, while new residential and commercial development remained strong. However, current trends suggest levels have plateaued and the rate of new development may begin to slow as described below.

As previously described, local construction activity through March 2019 decreased 17.4% from the high levels experienced in fiscal year 2017-2018 during the same period. In particular, residential permits for new dwelling units through March 2019 totaled 2,473 versus 2,630 in the prior year. Correspondingly, the valuation of new residential construction and alteration activity have also decreased to approximately \$449.5 million in fiscal year 2018-2019 from \$530,0 million in fiscal year 2017-2018.

Overall, new residential units are forecasted to decline in fiscal years 2020-2024 based on building permits issued in 2018- 2019 and the current housing market, which has slowed due to increases in the costs associated with new construction, and the flattening of rents relative to these increased costs. New commercial and retail construction may also decline as the market absorbs existing big-box vacancies (such as those created by the closures of national chains Toys R Us, Babies R Us, Orchard Supply Hardware and others), and as consumer shopping habits shift online.

*The following sections include descriptions of certain proposed and pending construction and development projects in the City. The City cannot neither provide assurance as to the timing of completion of such projects, if ever, or that such projects when completed will conform to the descriptions herein.*

### Downtown Development

In 2011, after three years of extensive community input from more than 5,000 residents and more than 50 public meetings, the City Council unanimously adopted the General Plan to determine how San José would develop in the next three decades. A critical component of the General Plan focused on creating a vibrant Downtown destination including expansion of the relatively small Downtown to a size and density more appropriate for a city of one million people. The General Plan called for adding 48,500 jobs, along with 10,360 housing units, to Downtown.

Three years later, in 2014, the City Council adopted the Diridon Station Area Plan to transform the 250-acre area of Downtown's western side (the "**Diridon Station Area**") into an area for people to live, work and visit. The Diridon Station Area Plan provides for the development of the Diridon Station Area into mixed-used developments with improved parks, trails and public spaces, among other items.

In December 2018, the City Council approved General Plan amendments and adopted the Downtown Strategy 2040 to replace the 2005 Downtown Strategy. The Downtown Strategy 2040 and associated General Plan amendments increased the Downtown housing unit capacity from 10,360 to 14,360 and 48,500 jobs to 58,500 jobs. The housing and job capacity were



transferred from other General Plan Growth Areas to the Downtown to accommodate anticipated Downtown growth to year 2040.

**Google Mixed-Use Development in Diridon Station Area.** In early 2017, Google Inc. (“Google”) expressed to the City an interest in purchasing land in the Diridon Station Area for the purpose of creating a mixed-use office development. Early discussions by the City with Google indicated their interest in planning and building a master planned, transit-oriented development that could include between 6 and 8 million square feet of office/R&D space and retail/commercial amenities. Such potential development could support approximately 20,000 new Downtown employees, significantly aiding the City's critical need for local jobs and supporting ridership on existing and new public transportation investments.

In 2018, the City entered into purchase and sale agreements or option agreements with Google with respect to three properties in the Diridon area owned by the City, including a fire training facility, totaling approximately 15 acres (collectively, the “**Diridon City Properties**”), and five properties previously owned by the Former Agency totaling approximately 6.5 acres (collectively, the “**Diridon SARA Properties**”). In December 2018, all of the Diridon City Properties, other than the fire training facility, and all of the SARA Properties were sold to Google. The City's sale of the fire training facility to Google closed in June 2019. As part of the sale, Google agreed to lease the fire training facility to the City through June 2022.

In December 2018, the City and Google entered into a Memorandum of Understanding (the “**Google MOU**”) for the purpose of memorializing guiding principles and shared goals of the City and Google's collaboration and to act as a basis for negotiating a potential future development agreement between the City and Google with respect to Diridon Station Area. The shared goals set forth in the Google MOU include, optimizing development density and creating a complementary mix of uses in order to create a transit-oriented urban neighborhood and destination and to grow and preserve housing in the City to help address rising housing costs and displacement. See “– Transportation” above for a discussion regarding the lack of funding for construction of the full 520-mile high-speed rail system and the High-Speed Rail Authority's focus on delivering an interim operating segment in the Central Valley, which would not include Diridon Station.

The Google MOU expires upon the mutual execution of a development agreement between the City and Google or December 31, 2022, whichever occurs first. Project planning and design are anticipated to occur over the next two years. The City cannot provide any assurance as to when such a development agreement will be entered into, if ever.

Google has completed the purchase of numerous other properties in the Diridon Station Area. Google, either directly or through a partnership with Trammell Crow, began buying properties in the City in December 2016 when it spent \$55 million for a telephone company building on South Montgomery Street in the City. It is estimated that Google and its affiliates have spent at least \$319.5 million purchasing an array of sites in the Downtown area that are expected to provide the land for Google's planned transit village.

Google is not the only party interested in investing in the Downtown core. Since 2016, investors have spent at least \$546 million on land-development sites. Spurred on by transit access and urban amenities, developers were proposing roughly 8 million square feet of office space as of May 2019, not including the potential Google campus. The largest preliminary proposal is a 3.4 million square foot redevelopment of the 1970s-era CityView Plaza from developer Jay Paul Co., which has built more than 11 million square feet of Class A office space



in California. While Downtown is still a relatively small office market (it had a daytime employment of roughly 43,000 as of 2018), these potential projects could substantially increase its size. However, the City can provide no assurance that any such projects will obtain land use entitlements or as to the timing of completion, if ever. In addition, investors had spent over \$560 million on existing office buildings since 2015, often investing additional dollars into renovations after purchasing them. During the current economic cycle, several large residential projects have been built Downtown, and there are currently 2,200 apartments or for-sale condominium units under construction with an additional 3,450 residential units with approved land use entitlements that have not proceeded to construction.

**Adobe North Tower.** Adobe intends to begin construction of a fourth office tower in Downtown San José, to serve as office space for Adobe's employees. Adobe, a provider of cloud-based software and services, already owns a three-tower campus in the Downtown area that serve as Adobe's headquarters and is preparing to begin construction of a fourth high-rise on an adjacent lot. The groundbreaking for the tower, which Adobe calls the North Tower, is targeted for late [June 2019], and is anticipated to accommodate approximately 4,000 employees with approximately 700,000 square feet of office space. Adobe's new tower is expected to provide ground floor retail. The retail could total about 8,100 square feet, according to information that Adobe sent to the City. The City cannot predict when construction of the North Tower will be complete, if ever.

### **Other City Development**

**North San José.** North San José is the City's main employment district. It contains approximately 100,000 jobs and is home to major companies such as Cisco Systems Inc., Broadcom Inc., Maxim Integrated Products Inc., and Cadence Design Systems Inc. North San José has traditionally been singularly employment-focused, but it has seen nearly 8,000 residential units constructed between 2009 and 2017 as part of a planning policy change to allow workers to live near jobs. In addition, developers have constructed the equivalent of roughly 4.5 million square feet of office and research and development ("**R&D**") space in this area during this period. Much of this activity followed the adoption in 2005 of the North San José Area Development Policy (the "**NSJ ADP**"), which provides development capacity for 32,000 homes and 26.7 million square feet of industrial (office/R&D), metered out in phases. Commercial occupancy has been boosted by tenant leases, acquisitions or expansions including Hewlett Packard Enterprise, Micron, Bloom Energy, and Roku.

Beginning in 2015 and continuing through 2018, Apple Inc. acquired roughly 86 acres of contiguous land (most of it undeveloped) in North San José. In 2016, the City Council approved a 15-year development agreement with Apple, Inc., that provides capacity for up to 4.1 million square feet of industrial/office/R&D space. Apple Inc. has not submitted a development application to the City and the City cannot provide any assurance that Apple will move forward with a development proposal with respect to its land in North San José.

As mentioned above, the NSJ ADP provides for a specified amount of new development, including an additional 26.7 million square feet of new office/R&D development, as well as an additional 32,000 residential units, 2.7 million sq. ft. of retail development and 1,000 hotel rooms. The full build out of all new development within the NSJ ADP area is divided into four roughly equivalent phases. The NSJ ADP does not establish a timeline for these phases. Rather, each phase is defined by various amounts of development capacity for industrial, commercial and residential development that are also tied to specified transportation improvements occurring within a reasonable time of development. For this reason, the NSJ



ADP includes a phasing plan that limits how much industrial and residential development may occur in advance of the construction of supporting infrastructure improvements. As of this date, development in North San José remains in Phase I primarily because commercial and industrial development has not reached Phase I capacity. Additionally, the NSJ ADP requires that 85% of the infrastructure improvements for each phase must be reasonably assured and that all of the improvements from any preceding phase must be constructed before the industrial or residential development of the next phase may be issued building permits. Currently, the residential capacity of Phase I has been utilized and the City Council has directed staff to explore mechanisms to advance as many as 8,000 residential units prior to the conclusion of Phase I.

There are also currently three settlement agreements relating to transportation improvements in the North San José Area Development Policy area. The first is a 2006 settlement agreement among the City, the County, and the City of Santa Clara, while the second is a 2006 settlement agreement between the City and the County. Both settlement agreements provide that the City contribute \$1.5 million towards a Santa Clara County project to fund the design work for the construction of the Montague/Mission/101 Interchange Project as contemplated in the County's Project Study Report for the project, which funds have been set aside by the City for that purpose. These two settlement agreements also require the City to fund and complete the widening of Montague Expressway to eight lanes between Lick Mill and Trade Zone, including all portions of the Expressway regardless of City boundaries, including interchange modifications at I-880 and the Trimble Road flyover as part of Phase I of the NSJ ADP. Some of this work has already been completed, with the remaining work to be completed on Montague Expressway between Lick Mill Boulevard and North 1st Street. The City has set aside funding in an amount estimated to be adequate to complete the design and improvements on this County expressway. Both settlement agreements also require the City to complete the McCarthy-O'Toole Interchange as part of implementation of Phase III of the North San José Area Development Policy. To date, development in North San José has not reached the limits of Phase I of the North San José Area Development Policy,

**West San José.** The City's west side has continued to build on its retail-heavy base in recent years, anchored by Valley Fair mall and mixed-use Santana Row development. Unibail-Rodamco-Westfield began construction in 2016 on a \$1.1 billion expansion and renovation of Valley Fair, which will expand the 1.5-million-square-foot mall by 650,000 square feet. It is slated for completion in 2019. The expansion is anticipated to include a new Bloomingdale's department store, a new flagship Apple store, 150 retail shops and restaurants and additional parking. A portion of Valley Fair lies in the City of Santa Clara; the Bloomingdale's, Apple Store and most of the new stores are anticipated to be located on the portion of Valley Fair within the City.

Other projects in the City's west side include the expansion of Santana Row by Federal Realty Investment Trust. Federal Realty Investment Trust continues to expand Santana Row, completing a 284,000 square foot building (recently leased to Splunk) at the 2.1-million-square-foot center, which includes 622 residential units, a 212-room hotel, 360,000 square feet of office, and 650,000 square feet of retail. Federal Realty Investment Trust has also entitled a roughly 1-million-square-foot office campus on a 13.4-acre site across from Santana Row. The City believes that Federal Realty Investment Trust is considering whether to move forward with construction on such site.

**South San José.** The southern region of the City ("**South San José**"), includes the Edenvale industrial district. While South San José has not seen as much development activity as other business districts in the City, several major projects have added significant housing,



retail and industrial/warehouse space. The largest of these sits on former buffer lands surrounding the Western Digital manufacturing campus totaling roughly 400 acres. Master-planned projects on these buffer lands include roughly 3,700 housing units, 500,000 square feet of retail (including a new Costco store that opened in 2017), and 386,000 square feet of data center space. These projects are now either complete or under construction, and the City believes the build-out will continue for several more years. Western Digital has also expanded with two buildings totaling 240,000 square feet. In addition, in Edenvale, developers constructed the first new warehouse/industrial projects in the City in many years: three warehouse buildings totaling roughly 420,000 square feet; the third building was completed in 2018. Several data center proposals are currently under review by the City, including a proposed China Telecom project that would include 65,000 square feet of office and 217,000 square feet of data center space.

## **Development Challenges**

Future development within the City is not without some challenges. While San José has seen strong development activity since the Great Recession, some recent proposals have struggled to obtain financing and have not broken ground as expected. These challenges, which are not unique to San José, are due in large part to escalating construction costs and, in the case of residential projects, an inability to project future rent growth to offset rising costs. An April 2018 study prepared for the City by Keyser Marston Associates found that direct construction costs would need to decrease by 15% to 20%, or average rents would need to increase by 10% to 15% (or some combination of the two) to ensure sufficient returns to drive new construction. Despite challenges in the current market, unique circumstances could enable certain projects to proceed, such as projects with a low land basis due to long-term ownership, or projects viewed as longer-term investments. Moreover, real estate development economics are constantly changing with respect to construction costs, land values, rent potential, and cost of capital. If, for example, market values improve relative to costs, more projects would be able to achieve an acceptable return and break ground.

## **MUNICIPAL GOVERNMENT**

The City is a charter city, which means the City, through its charter (the “**Charter**”), may regulate municipal affairs, subject only to restrictions and limitations provided in the Charter. In matters other than municipal affairs or in matters of statewide concern, the City is subject to State law. The form of municipal government established by the Charter is known as the “Council-Manager” form of government.

The City Council consists of a Mayor and ten other council members. The Mayor is elected at large for a four-year term. Council members are elected by district for staggered four-year terms. The Mayor and the council members are limited to two consecutive four-year terms. Under the Charter, the Mayor recommends policy, program, and budget priorities to the Council, which in turn approves policy direction for the City. The City Manager is appointed by the Council and serves as the chief administrative officer of the organization responsible for the administration of City affairs, day-to-day operations, and implementation of Council policies. In addition to the City Manager, the City Attorney, City Clerk, City Auditor, and Independent Police Auditor are appointed by and report directly to the Council.

The Charter provides that the boards of administration for each of the City’s retirement plans, the Federated City Employees’ Retirement System and the Police and Fire Department



Plan, hire and prescribe the duties of the chief executive officer and chief investment officer within the Office of Retirement Services who serve at the pleasure of the retirement boards. The Charter also specifies certain duties and obligations of each retirement board and authorizes the chief executive officer to hire and oversee the Office of Retirement Services' employees, subject to any applicable Civil Service Rules.

The City organization is structured into six City Service Areas ("**CSAs**") that integrate services provided by separate departments and offices into key alignments from the community's perspective. The CSAs consists of Community and Economic Development, Environmental and Utility Services, Neighborhood Services, Public Safety, Transportation and Aviation Services, and Strategic Support. The City provides a range of municipal services, including police and fire protection, sanitation services, environmental management, maintenance of streets and infrastructure, and the administration of library services, recreational activities, and cultural facilities. The City also operates a parking program, a municipal water system, a wastewater treatment facility, the Airport, and three municipal golf courses.

In addition, in June 2018, the City established San José Clean Energy ("**SJCE**"), a Community Choice Aggregation program operated by the City's Community Energy Department for the provision of electrical power within the City's boundaries. Community Choice Aggregation programs such as SJCE permit local governments to supply electricity to serve the needs of participating customers within their jurisdiction while existing investor-owned utilities continue to provide such service to existing customers, such as billing, transmission and distribution. SJCE is one of the major initiatives under the City's Climate Smart San José Plan, which outlines future strategies for the City which align with the Paris Climate Agreement. See "CERTAIN RISK FACTORS – Climate Change" in the forepart of this Official Statement and see "– BONDED AND OTHER INDEBTEDNESS" a description of outstanding debt of the City that is secured by or payable from SJCE revenues.

The City also provides oversight in the management of convention, cultural event, sport and hospitality facilities that include the San José McEnery Convention Center, Center for the Performing Arts, California Theatre, Mexican Heritage Plaza, Solar4America Ice Centre, and the SAP Center at San José – home of the San José Sharks of the National Hockey League and the San José Barracuda minor league hockey team. The City leases the San José Municipal Stadium to the San José Giants, a minor league baseball team. The City has served as host City for major sporting events, including the 2019 College Football Playoff National Championship, the 2019 National Hockey League All-Star Game, and the first and second rounds of the 2019 NCAA Men's Division I Basketball Championship.

## **REDEVELOPMENT DISSOLUTION**

On June 29, 2011, Assembly Bill No. 26 ("**AB X1 26**") was enacted, together with a companion bill, Assembly Bill No. 27 ("**AB X1 27**"). The provisions of AB X1 26 provided for the dissolution of all redevelopment agencies statewide as of February 1, 2012. The provisions of AB X1 27 permitted redevelopment agencies to avoid such dissolution by the payment of certain amounts. A lawsuit was brought in the California Supreme Court, *California Redevelopment Association, et al., v. Matosantos, et al.*, 53 Cal. 4th 231 (Cal. Dec. 29, 2011), challenging the constitutionality of AB X1 26 and AB X1 27. The California Supreme Court largely upheld AB X1 26, invalidated AB X1 27, and held that AB X1 26 may be severed from AB X1 27 and enforced independently. As a result of AB X1 26 and the decision of the California Supreme Court in the *California Redevelopment Association* case, as of February 1, 2012, all



redevelopment agencies in the State were dissolved, including the Redevelopment Agency of the City of San José (the “**Former Agency**”).

The primary provisions enacted by AB X1 26 relating to the dissolution and wind down of former redevelopment agency affairs are found in Parts 1.8 (commencing with Section 34161) and 1.85 (commencing with Section 34170) of Division 24 of the California Health and Safety Code of the State, as amended on June 27, 2012 by Assembly Bill No. 1484 (“**AB 1484**”), enacted as Chapter 26, Statutes of 2012 and as further amended on September 22, 2015 by Senate Bill 107 (“**SB 107**”), enacted as Chapter 325, Statutes of 2015. The provisions of Part 1.85 as amended by AB 1484 and SB 107 are referred to in this Official Statement as the “**Dissolution Act**.”

On January 24, 2012, the City Council authorized the City to serve as the Successor Agency to the Redevelopment Agency of the City of San José (the “**Successor Agency**”). The City Council acts as the Successor Agency Board.

Under the Dissolution Act, certain actions require approval and are subject to the direction of an oversight board. Pursuant to SB 107, the functions of such board were assumed by an oversight board established for all successor agencies within the County (the “**Oversight Board**”) commencing on July 1, 2018. The county-wide Oversight Board as of July 1, 2018 is comprised of seven member representatives with one member appointed by each of the following: County Board of Supervisors, the city selection committee established pursuant to Section 50270 of the Government Code, the independent special district selection committee established pursuant to Section 56332 of the Government Code, the County Superintendent of Education, the Chancellor of the California Community Colleges, a public appointment made by the County Board of Supervisors, and the recognized employee organization representing the largest number of successor agency employees in the county.

Prior to its dissolution on February 1, 2012, the Former Agency engaged in various redevelopment activities within or for the benefit of its various redevelopment project areas in the City. These activities included the issuance of bonds, the incurrence of other indebtedness, and the financing of redevelopment projects through the use of tax increment revenues. Upon the dissolution of the Former Agency pursuant to the Dissolution Act, the Successor Agency succeeded to those obligations.

On December 21, 2017, the Successor Agency issued the following refunding tax allocation bonds (collectively, the “**2017 Tax Allocation Refunding Bonds**”): (i) \$70,825,000 original principal amount 2017 Series A Senior Tax Allocation Refunding Bonds; (ii) \$1,333,325,000 original principal amount 2017 Series A-T Senior Taxable Tax Allocation Refunding Bonds; and (iii) \$264,390,000 original principal amount 2017 Series B Subordinate Tax Allocation Refunding Bonds. The net proceeds of the 2017 Tax Allocation Refunding Bonds were used to refund and defease or prepay 23 series of tax allocation bonds previously issued by the Former Agency, and certain other obligations of the Former Agency, including certain pledge and reimbursement agreements entered into by the Former Agency to support, in part, bonds previously issued by the City of San José Financing Authority (the “**Financing Authority**”).

The 2017 Tax Allocation Refunding Bonds are secured solely by tax increment revenues generated within the project areas established by the Former Agency and certain funds and accounts held by the trustee for such refunding bonds. In the event that there are not sufficient tax increment revenues to pay debt service on such refunding bonds, the City is under no



obligation to make any such payments, and the City is in no manner liable for the payment of debt service on 2017 Tax Allocation Refunding Bonds.

The Successor Agency has additional obligations payable from tax increment revenues generated within the project areas established by the Former Agency on a basis subordinate to the 2017 Tax Allocation Refunding Bonds. Such obligations include loans (the “**SERAF Loans**”) made by the City to the Former Agency to meet its obligations pursuant to Assembly Bill No. 26x4 adopted by the State legislature in 2009 (the “**SERAF Legislation**”), which mandated that redevelopment agencies in the State make deposits to the Supplemental Educational Revenue Augmentation Fund (“**SERAF**”) and loans made from the City’s Parking Fund to the Former Agency (“**Parking Fund Loans**”). The SERAF Loans and Parking Fund Loans are currently outstanding in the total amount of approximately \$46.6 million. The City anticipates that the tax increment revenues generated within the project areas established by the Former Agency will be sufficient to pay the total amount due to the City under both the SERAF Loans and Parking Fund Loans by January 2020. The City cannot and does not provide any assurance that these loans will be repaid to the City as anticipated, if ever. However, the 2019-2020 [Proposed] Operating Budget assumes the repayment of these funds to the City in 2019-2020.

See Note IV. C. 4 to the City’s Basic Financial Statements for the Fiscal Year ended June 30, 2018, included in this Official Statement as Appendix C, for additional information regarding the 2017 Tax Allocation Refunding Bonds and other obligations of the Successor Agency.

## **BUDGET**

The City is legally required to have a balanced budget in place before the beginning of each fiscal year and has used a variety of strategies to balance its budget. The City Council adopted a balanced budget for 2019-2020 on June 11, 2019, marking the eighth consecutive year that the operating budget did not include significant reductions in services, staffing, and compensation to achieve a balanced budget. See “FISCAL PRESSURES” above for a discussion regarding budgetary and fiscal pressures experienced by the City in recent years.

### **City’s Budgetary Process**

**General.** The City’s fiscal year extends from July 1 through June 30. In the third quarter of each fiscal year, the City Manager releases the “City Manager’s Budget Request and Five-Year Forecast and Revenue Projections for the General Fund and Capital Improvement Program.” Since 1986, the City has used the five-year forecast to assist in projecting revenue levels and expenditures based on certain assumptions and expectations.

Pursuant to the Charter, the Mayor releases an annual “budget message.” This document describes the budget process, the current fiscal situation of the City, the strategy for developing the proposed budget, recommendations on specific budget items, and other related issues. The City Council reviews the Mayor’s Budget Message, and a public hearing is held to discuss the budget message prior to the City Council taking action. The City Council, by majority vote, may make revisions to the Mayor’s Budget Message.

The Charter requires that the City Manager release the Proposed Capital Budget, the Capital Improvement Program and the Proposed Operating Budget at least thirty days prior to



the beginning of each fiscal year, or at such earlier time as the City Council may specify. As currently directed by the City Council, the City Manager releases the Proposed Capital Budget in April and the Proposed Operating Budget and Proposed Fees and Charges Report in May. The Proposed Operating and Capital Budgets contain the complete financial plan for the City for the next fiscal year, and account for all revenue received by the City and the uses for all revenue. The Operating Budget describes each department's activities and budget and recommended additions or reductions to the budget. The Capital Budget describes the capital projects that are funded, including the project cost and source of funds, a project description, and the timing of the project. The Fees and Charges Report documents the majority of fees and charges accruing to the City's General Fund and selected fees within other funds. Such report does not, however, include a number of fees assessed by the City's enterprise operations (e.g., Airport, Downtown Parking, and Convention Center facilities). The City Council holds a number of study sessions in mid-May to discuss the proposed Operating and Capital Budgets and the Fees and Charges Report, and holds two public hearings on the budget, the first of which generally occurs in mid-May and the second of which generally occurs in early June.

In early June, the Mayor releases the final budget modification message for City Council deliberation. It contains changes to the Proposed Budget recommended by the Mayor after review and discussion of the document during the budget hearings. The City Council approves the Mayor's June Budget Message, with any revisions supported by a majority vote. By June 30, the City Council adopts the operating and capital budgets for the next fiscal year, along with the implementing appropriation ordinances and funding sources resolutions that appropriate the budgeted amounts to the respective departments.

Current City practice calls for the preparation of Bi-Monthly Financial Reports, which are presented to the City Council Public Safety, Finance, and Strategic Support Committee. Additionally, the Mid-Year Budget Review document is released in January and considered by the City Council in February. The Mid-Year Budget Review contains an assessment of the City's budget condition based on actual performance during the first six months of the fiscal year.

Based on this assessment, any necessary budget revisions are recommended to address projected revenue and expenditure variances, account for new grants and reimbursements, and address any other budgetary needs. City Council reviews the mid-year status of the operating and capital budgets, and takes actions as necessary to maintain a balanced budget. At any public meeting, the City Council may amend or supplement the budget by affirmative vote of at least a majority of the total members of the City Council.

In accordance with the City Charter, an Annual Report is issued in late September that reports on the financial status of the City at the end of the prior fiscal year, including a comparison of actual revenue collections and expenditures to projections and appropriations included in the City's budget. Recommended budget actions are brought forward in the City's Annual Report for City Council consideration to implement required fund balance reconciliations as well as necessary re-budget and clean-up adjustments based on the final year-end financial performance of the City's funds. Budget actions are also typically brought forward to adjust the current year budget to align revenues and expenditures with the most current information, make technical adjustments, and recognize new and adjust existing grant, reimbursement, or fee activity revenues and expenditures.



## **2018-2019 Adopted Operating Budget**

The City Council adopted the 2018-2019 Adopted Operating Budget (the “**2018-2019 Adopted Operating Budget**”) on June 12, 2018, after a series of City Council Budget Study Sessions to consider the many proposals set forth in the 2018-2019 Proposed Budget.

The 2018-2019 Adopted Operating Budget is a balanced budget that continues efforts to address the highest priority community and organization needs while maintaining budget stability. The 2019-2023 Five-Year Forecast was used as the starting point in the development of the budget. For the General Fund, a revised shortfall of \$4.3 million was projected for 2018-2019, and was addressed in the 2018-2019 Adopted Operating Budget. However, the 2018-2019 Adopted Operating Budget also reflects the City’s limited capacity to expand services and address a significant backlog of deferred infrastructure and maintenance needs.

As directed in the Mayor’s March Budget Message for 2018-2019, as approved by the City Council, the 2018-2019 Adopted Operating Budget includes investments across multiple City funds that support long-term, major initiatives, including: (i) Homelessness and Housing; (ii) Public Safety; (iii) Environment; (iv) Innovation and Technology; (v) Education and Our Youth; (vi) Community Engagement; and (vii) Saving and Improving Fiscal Sustainability.

The 2018-2019 Adopted Operating Budget takes a multi-year approach with one-time funding set aside in fiscal year 2018-2019 (of approximately \$15.5 million) to address the projected General Fund shortfall in 2019-2020 at the time the 2018-2019 Adopted Operating Budget was adopted by the City Council. It also maintains existing service levels, enhances service delivery in limited areas, and invests in the City’s infrastructure and technology. The 2018-2019 Adopted Operating Budget notes that with limited resources, it is critical that the City continue to innovate and leverage resources to achieve its service delivery goals.

## **2018-2019 Interim Financial Status Reports**

***Mid-Year Budget Review Report.*** The 2018-2019 Mid-Year Budget Review Report was released on January 31, 2019, and was approved by the City Council on February 12, 2019. The 2018-2019 Mid-Year Budget Review Report provided an assessment of the City’s budget condition in the 2018-2019 fiscal year as compared to the 2018-2019 Modified Operating Budget based on actual performance during the first six months of 2018-2019. Based on this analysis, budget revisions are recommended to: implement required technical/rebalancing actions to align existing revenue estimates and expenditure budgets with the most current tracking information, implement City Council direction, or reallocate funding among appropriations based on updated needs; implement a number of technical and net-zero adjustments between revenue categories and expenditure appropriations; account for new or adjusted grants, reimbursements, or fees; and fund a limited number of new projects in special and capital funds.

According to the 2018-2019 Mid-Year Budget Review Report, through the first half of the year, City funds were generally performing within expected 2018-2019 budgeted levels. Based on then current collection trends and information, General Fund revenues were anticipated to end the year approximately \$20 million to \$25 million above budgeted levels. The primary drivers of this additional revenue were higher than estimated Property Tax, Sales Tax, and revenue from local agencies. An additional \$18.7 million was also projected to be generated from the Successor Agency and City owned property sales.



Overall, General Fund expenditures as of the date of the 2018-2019 Mid-Year Budget Review Report were also tracking within estimated anticipated levels and were expected to generate minimal savings by year-end of approximately \$4 million to \$6 million. The combination of additional revenues (excluding new property sale revenues), expenditure savings, and the liquidation of prior year carryover encumbrances were expected to generate a 2018-2019 Ending Fund Balance of at least \$25 million, which were used as a funding source in the Five-year General Fund Forecast and the 2019-2020 Proposed Operating Budget.

Table 9 on the following page summarizes the City's actual General Fund Budget performance for 2017-2018, the City's 2018-2019 Modified Operating Budget and the City's 2019-2020 [Proposed] Operating Budget.



**Table 9**  
**City of San José**  
**General Fund Budget Summaries<sup>(1)</sup>**  
**2017-2018 Actuals, 2018-2019 Budgeted and 2019-2020 Budgeted**  
**(in thousands)**

<b>SOURCE OF FUNDS</b>	<b>2017-2018 Actuals</b>	<b>2018-2019 Modified Operating Budget<sup>(2)</sup></b>	<b>2019-2020 [Proposed] Operating Budget</b>
<b>FUND BALANCE</b>			
Encumbrance Reserve .....	\$48,886	\$38,466	\$38,467
Carryover .....	241,173	249,953	143,812
Total Fund Balance .....	\$290,058	\$288,420	\$182,279
<b>GENERAL REVENUES</b>			
Property Tax .....	\$306,222	\$324,450	\$354,000
Sales and Use Tax .....	226,337	250,500	258,300
Transient Occupancy Tax .....	19,531	19,700	22,500
Franchise Fees .....	51,180	50,475	48,641
Utility Taxes .....	99,753	102,400	99,645
Telephone Line Tax .....	20,481	20,000	20,000
Business Taxes .....	70,673	69,400	72,200
Licenses and Permits .....	60,505	60,894	62,037
Fines and Forfeitures .....	14,354	14,983	16,213
Revenue from Use of Money and Property .....	7,930	6,897	13,144
Revenue from Local Agencies .....	38,623	16,105	12,483
Revenue from the State Government .....	15,825	14,354	12,435
Revenue from the Federal Government .....	5,591	6,206	792
Fees, Rates and Charges .....	51,081	55,822	55,784
Other Revenue .....	218,951	210,937	19,778
Total General Revenue .....	\$1,207,036	\$1,223,122	\$1,069,952
Overhead Reimbursements .....	\$47,245	\$50,456	\$56,133
Transfers to the General Fund .....	26,306	25,969	27,013
Reimbursements for Services .....	17,328	18,225	17,081
Total Interfund Transfers and Reimbursements .....	90,879	94,650	100,227
<b>TOTAL SOURCE OF FUNDS</b> .....	<b>\$1,587,973</b>	<b>\$1,606,193</b>	<b>\$1,352,458</b>
<b>USE OF FUNDS</b>			
<b>DEPARTMENTAL</b>			
General Government .....	\$96,187	\$118,830	\$122,897
Public Safety .....	603,457	643,650	685,234
Capital Maintenance .....	80,199	85,970	87,063
Community Services .....	159,281	175,736	189,942
Total Departmental .....	\$939,124	\$1,024,186	\$1,085,137
<b>NON-DEPARTMENTAL</b>			
Citywide .....	\$293,674	\$268,284	\$81,809
Capital Expenditures .....	32,408	38,884	280,380
Transfers to Other Funds .....	34,347	47,831	36,178
Earmarked Reserves .....	--	151,541	43,987
Encumbrance Reserve .....	38,467	38,467	38,467
Contingency Reserve .....	--	37,000	38,500
Total Non-Departmental and Reserves .....	398,895	582,007	267,321
<b>TOTAL USE OF FUNDS</b> .....	<b>\$1,338,020</b>	<b>\$1,606,193</b>	<b>\$1,352,458</b>

<sup>(1)</sup> Totals may not add due to independent rounding.

<sup>(2)</sup> As of March 31, 2019.

Sources: City of San José 2019-2020 [Proposed] Operating Budget.



## Budget Outlook

**2020-2024 Five-Year Forecast.** On March 7, 2019, the City Manager released the 2018-2019 City Manager's Budget Request & 2020-2024 Five-Year Forecast and Revenue Projections. The 2020-2024 Five-Year Forecast and Revenue Projections (the "**2020-2024 Forecast**") reflects the City Manager's best estimates on the projected revenues and expenditures over the next five fiscal years based on the information available as of March 7, 2019. The 2020-2024 Forecast was built on the assumption of slowing, but still positive, economic growth. Table 10a below shows the projected General Fund revenues and expenditures over the next five years and the total cumulative shortfall as set forth in the 2020-2024 Forecast as of March 7, 2019.

In addition to the cumulative shortfall, the incremental shortfall or surplus (assuming each preceding shortfall or surplus is addressed completely with ongoing solutions in the year it appears) for each year of the forecast is included. Because it is the City's goal to remain in balance on an ongoing basis, the incremental figure is useful in that it shows the additional shortfall and/or surplus attributed to a particular fiscal year. To the extent that a shortfall is not resolved or a surplus is not expended on an ongoing basis, it is important to understand that the remaining budget gap or surplus will carry over to the following year.

**Table 10a**  
**City of San José**  
**2020-2024 General Fund Five-Year Forecast <sup>(1)</sup>**  
**As of March 7, 2019**  
**(in millions)**

	<b>2019-2020</b>	<b>2020-2021</b>	<b>2021-2022</b>	<b>2022-2023</b>	<b>2023-2024</b>
Projected Revenues	\$1,207.8	\$1,244.8	\$1,279.7	\$1,314.3	\$1,351.5
Projected Expenditures	1,204.3	1,257.0	1,305.6	1,328.7	1,367.7
<b>Total Cumulative Surplus/(Shortfall) <sup>(2)</sup></b>	\$3.5	\$(12.2)	\$(25.9)	\$(14.4)	\$(16.2)
<b>Total Incremental Surplus/(Shortfall)</b>	\$3.5	\$(15.6)	\$(13.7)	\$11.4	\$(1.7)
<b>% of Budget (Based on Expenditure)</b>	0.3%	(1.2%)	(1.0%)	0.9%	(0.1%)

<sup>(1)</sup> Does not include (a) costs associated with services that were funded on a one-time basis in 2018-2019; (b) costs associated with unmet/deferred infrastructure and maintenance needs; and (c) one-time revenue sources or expenditure needs. It should also be noted that no net impacts associated with the Development Fee Programs are included due to the cost-recovery nature of these programs.

<sup>(2)</sup> The City's goal is to remain in balance on an ongoing basis. The incremental figure shows the additional shortfall or surplus attributed to a fiscal year. In addition to the cumulative shortfall, incremental shortfalls and surplus assume each preceding shortfall or surplus is addressed completely with ongoing solutions in the year it appears.

Source: City of San José 2020-2024 Five-Year Forecast and Revenue Projections, which are generated internally by City staff.

As shown in Table 10a above, small incremental General Fund surpluses and shortfalls between a surplus of \$11.4 million to a shortfall of \$15.6 million were projected in the 2020-2024 Forecast. These margins are relatively narrow when put into context with the size of the projected General Fund budget, ranging from -1.2% to 0.3% of the projected annual budget of \$1.2 billion to \$1.4 billion. However, there are significant expenditure components that are not incorporated into the 2020-2024 Forecast, including programs funded on a one-time basis in 2018-2019, unmet/deferred infrastructure needs and any potential decrease in federal funding to the City that may result in the event a citizenship question is added by the Census Bureau to the 2020 Census. The General Fund position as forecasted in the 2020-2024 Forecast is fairly



consistent with the 2019-2023 Forecast issued in March 2018. In the 2019-2023 Forecast, shortfalls ranging from \$7.3 million to \$15.5 million were projected for four years of such forecast with one surplus of \$10.8 million projected in 2022-2023. See “– SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND CONSENT DECREES – Affirmative Litigation – Census Litigation” for a discussion regarding litigation relating to the proposed addition of the citizenship question to the 2020 Census.

Portions of the 2020-2024 Forecast related to 2019-2020 were modified by the 2019-2020 Proposed Operating Budget released on May 1, 2019, including the projected General Fund incremental surplus or shortfall in the next five fiscal years as shown in Table 10b below.

**Table 10b**  
**City of San José**  
**2020-2024 General Fund Five-Year Forecast as Modified By**  
**2019-2020 Proposed Operating Budget <sup>(1)</sup>**  
*(in millions)*

	<u>2019-2020</u>	<u>2020-2021</u>	<u>2021-2022</u>	<u>2022-2023</u>	<u>2023-2024</u>
<b>Total Incremental Surplus/(Shortfall)</b>	\$5.1	\$(10.9) <sup>(2)</sup>	\$(13.7)	\$11.4	\$(1.7)
<b>% of Budget (Based on Expenditure)</b>	0.4%	(0.9%)	(1.0%)	0.9%	(0.1%)

<sup>(1)</sup> Does not include (a) costs associated with services that were funded on a one-time basis in 2018-2019; (b) costs associated with unmet/deferred infrastructure and maintenance needs; and (c) one-time revenue sources or expenditure needs. It should also be noted that no net impacts associated with the Development Fee Programs are included due to the cost-recovery nature of these programs.

<sup>(2)</sup> These figures were revised from the \$3.5 million surplus and \$15.6 million deficit in 2019-2020 and 2020-2021, respectively, as presented in the February 2019 Forecast. The figure for 2019-2020 was revised as a result of continued analysis of projected revenues and expenditures; the 2020-2021 figure was revised downward to account for the \$4.7 million of unallocated ongoing surplus in 2019-2020.

Source: City of San José 2019-2020 Proposed Operating Budget.

For a further discussion of the 2019-2020 Proposed Operating Budget, see “– Proposed 2019-2020 Operating Budget,” below.

Given the decreasing level of precision to be expected in the later years of a multi-year forecast, the significance of the projections in the out years is not so much in terms of their absolute amounts, but rather in the relative size of the decrease or increase from the prior year. This information should be used to provide a multi-year perspective to budgetary decision-making, rather than as a precise prediction of what will occur.

To model the range of budgetary scenarios possible under varying economic conditions, two alternative forecasts have been developed in addition to the “Base Case,” “Optimistic” and “Pessimistic” cases model economic scenarios considered possible, but less likely to occur than the “Base Case.” These alternatives are presented in the 2020-2024 Forecast to provide a framework that gives perspective to the Base Case. The Base Case Forecast is still considered, however, the most likely scenario and is being used for planning purposes for the 2019-2020 Proposed Operating Budget.

- **Base Case.** The Base Case is built on the assumption of slowing, but still positive, economic growth. In recent years, several of the City’s economically sensitive revenues experienced strong growth as the City recovered from the severe recession that started in the latter half of the last decade. This region has also benefitted from continued venture capital investment in the technology industry, solid employment growth, and a



strong real estate market. Over the forecast period, activity in most of these areas is expected to moderate, which will result in a slowing rate of local expansion and ultimately lower growth in the City's revenues. In the Base Case, General Fund revenue collections are anticipated to experience slow growth over the forecast period.

- *Optimistic Case.* The Optimistic Case assumes somewhat faster economic growth than anticipated in the Base Case, but still slower than that experienced in recent years. On a national level, economic growth is slightly higher with increased defense spending. This increased defense spending positively impacts technology sectors, which benefits the local economy. Local conditions are very strong and the area's largest technology employers are doing much better than in the Base Case scenario. Venture capital expenditures are steady, as is the flow of foreign funds into the region. Local employment continues to expand and, because of this solid employment growth, housing prices remain at high levels and grow through the entire forecast period. Inflation is also expected to be higher than in the Base Case. This stronger growth results in increased collections in the economically sensitive revenue categories, such as Property Tax and Transient Occupancy Tax.
- *Pessimistic Case.* The Pessimistic Case assumes that a combination of adverse factors results in lower economic growth rates than in the Base Case. Significantly lower growth is assumed for several of the key determinants of the City's revenue; local employment, local housing prices and number of sales, and local inflation are all lower than those of the Base Case. However, this scenario does not assume an economic crash at the local, national, or international levels. In this scenario, the City's revenues, particularly Property Tax, Sales Tax, and Transient Occupancy Tax, are significantly impacted by an economic slowdown.
- *Recession Scenario.* While not modeled over the 2020-2024 Forecast period, a Recession Scenario is included to provide additional context on the potential impacts of an economic downturn. In this scenario, a recession is experienced in 2021-2022, impacting the City's economically sensitive revenues. Sales Taxes, Transient Occupancy Tax, and Business Taxes experience declines in both 2021-2022 and 2022-2023 and Property Tax growth rates dramatically slow. On the expenditure side, the discount rate for the retirement plans declines by one eighth percent in both 2020-2021 and 2021-2022. In this scenario, the total General Fund shortfall over the five-year period totals \$153.1 million.

The following table shows the General Fund operating margins for 2019-2020 through 2023-2024, based on the scenarios described above and assuming that the City does not prefund the employer retirement contributions in such fiscal year and do not include the revisions to the projected General Fund incremental surplus or shortfall shown in Table 10b above.



**Table 11**  
**City of San José**  
**General Fund Operating Margins**  
*(Base, Optimistic, Pessimistic, and Recession Scenarios)*

	<b>2019-2020</b>	<b>2020-2021</b>	<b>2021-2022</b>	<b>2022-2023</b>	<b>2023-2024</b>	<b>Five-year Surplus/ (Shortfall)</b>
Base Case	\$3.45 M	(\$15.65 M)	(\$13.7 M)	\$11.4 M	(\$1.7 M)	(\$16.2 M)
Optimistic Case	\$6.5 M	(\$12.1 M)	(\$2.1 M)	\$22.1 M	\$17.1 M	31.5 M
Pessimistic Case	(\$3.6 M)	(\$27.9 M)	(\$28.1 M)	(\$1.5M)	(\$11.5 M)	(\$72.5 M)
Recession Scenario	(\$3.6 M)	(\$38.9 M)	(\$76.6 M)	(\$25.2 M)	(\$8.8 M)	(\$153.1 M)

*Source: City of San José 2020-2024 Five-Year Forecast and Revenue Projections, which are generated internally by City staff.*

**2019-2020 Mayor’s March Budget Message.** On March 8, 2019, the Mayor released the March Budget Message for 2019-2020 (the “**Mayor’s March Budget Message**”). Public comment on the Mayor’s March Budget Message was received on March 19, 2019, and the City Council completed the final review and approval of the message on March 19, 2019. This document provided direction to the City Manager to submit a proposed budget for 2019-2020 that is balanced and guided by the policy direction and framework of priorities outlined in the Mayor’s March Budget Message.

The Mayor’s March Budget Message highlighted recent improvements in the City’s fiscal position in the last four years through changes in pension and healthcare benefits for new employees and focused spending, strategic investments, and restoration of key services leading to a projected budget surplus of approximately \$3.5 million in fiscal year 2019-2020. However, in the Mayor’s March Budget Message, the Mayor cautioned that in the 2020-2024 Forecast, the City projects a cumulative budget deficit of approximately \$16 million in the next five fiscal years. In addition, the Mayor’s March Budget Message highlighted the City’s accomplishments in slowing the growth in its pension and healthcare benefit costs in recent years, but warns that actual costs may be higher than those currently projected by the plan actuaries.

For the reasons described above, the Mayor’s March Budget Message directed the City Manager to propose a budget for 2019-2020 that focuses on savings through building reserves, and paying down debt and thereby reduce the General Fund’s interest expense. Such reserves include the contribution of any one-time funds not otherwise prioritized to the Budget Stabilization Reserve of a minimum amount of \$10 million.

In addition, the Mayor’s March Budget Message directed the City Manager to propose a budget for 2019-2020 that focuses on public safety, confronting the high cost of housing and living, homelessness, combatting blight, and the environment.

### **2019-2020 Proposed Operating Budget**

On May 1, 2019, the City Manager released the 2019-2020 Proposed Operating Budget (the “**2019-2020 Proposed Operating Budget**”). The 2019-2020 Proposed Operating Budget is a balanced budget that continues efforts to address the highest priority community and organizational needs while maintaining budget stability. It follows the direction provided by the Mayor and City Council with the adoption of the



Mayor's March Budget Message. It also considers other City Council priorities, organizational priorities, and forecasts for future revenues and expenditures.

The 2020-2024 Forecast was used as the starting point in the development of the 2019-2020 Proposed Operating Budget. For the General Fund, a revised surplus of \$5.1 million is projected for 2019-2020, and has been allocated in the 2019-2020 Proposed Operating Budget. Small shortfalls ranging from \$1.7 million to \$13.7 million and one surplus of \$11.4 million in 2022-2023 are projected for the remaining four years of the 2020-2024 Forecast (see Table 10b above). With minimal projected shortfall and surplus figures, the City's budget is in a fairly stable position. However, there is limited capacity to expand much needed services to City residents and fully address the backlog of the City's deferred infrastructure and maintenance needs. With the passage of Measure T, however, there is a significant amount of resources to address some of the City's most critical infrastructure needs. The 2019-2020 Proposed Operating Budget begins the delivery of these improvements. However, even with the passage of Measure T, the City's infrastructure backlog number is still estimated to be at \$1.5 billion. This is an increase from the \$1.4 billion projected in 2018.

The 2019-2020 Proposed Operating Budget follows City Council direction to focus on targeted, strategic spending as well as saving for the future. It takes a multi-year approach with a combination of ongoing and one-time funding set aside in 2019-2020 to address the projected General Fund shortfall in 2020-2021. It also increases the Budget Stabilization Reserve, maintains existing service levels, enhances service delivery in limited areas, and invests in the City's infrastructure and technology. With limited resources, it is critical that the City continue to innovate and leverage resources to achieve its service delivery goals.

The 2019-2020 Proposed Operating Budget includes investments across multiple City funds that support certain long-term, major initiatives, including: (i) Emergency Management and Preparedness; (ii) Creating Housing and Preventing Homelessness; and (iii) Safe, Vibrant, and inclusive Neighborhoods and Public Life. These initiatives are also in alignment with the investment priorities identified in the Mayor's March Budget Message, as approved by the City Council, including: (1) Saving; (2) Public Safety; (3) Confronting the High Cost of Housing and Living; (4) Homelessness; (5) Combatting Blight; and (6) Environment.

The availability of one-time funding in 2019-2020, primarily generated from the sale of various properties in 2018-2019, has provided extra capacity to address the priorities outlined in the Mayor's March Budget Message. This funding is being used strategically to better position the City moving forward by setting aside funding in reserves as well as addressing some of the City's highest priority infrastructure and service delivery needs. The small surplus for 2019-2020 also helps better position the City moving forward as the majority of this funding is allocated to one-time items as directed in the Mayor's March Budget Message, which will reduce the projected shortfall in 2020-2021 from \$15.6 million to \$10.9 million.

### **2019-2020 Mayor's June Budget Message**

On June 3, 2019, the Mayor released the June Budget Message for 2019-2020 (the **"Mayor's June Budget Message"**), outlining his final recommendations and changes to the 2019-2020 Proposed Operating Budget. The public hearing on the Mayor's June Budget Message occurred on June 10, 2019, and the City Council completed the final review and approval of the message on June 11, 2019.



In the Mayor's June Budget Message, the Mayor recommends a series of one-time investments focused on the following areas: (1) Public Safety; (2) Homelessness; (3) Educational Opportunity and Enrichment for Youth; (4) Inclusive, Age-Friendly, and Family-Friendly Services; (5) Blight; (6) Neighborhood Empowerment and Community Building; (7) Economic and Cultural Vitality; (8) Innovation and Technological Implementation; and (9) Debt Reduction. These include programs that build on the Mayor's commitment to expand opportunity for City residents who struggle with the rising cost of living, including free summer learning youth programs, pre-apprenticeships construction trades programs for young adults, street-cleaning jobs for homeless residents, and child care for working parents. He also advocates for substantial investments in public safety, including the return of "foot patrols" to restore "community policing" in some high-crime neighborhoods. The Mayor's June Budget Message also makes new investments to counter sexual assault, to prevent crime through community engagement, and traffic safety infrastructure.

In addition, the Mayor's June Budget Message Mayor also calls for an "equity screen" to focus scarce resources for such services as blight eradication, pedestrian safety, parks rehabilitation, and crime prevention initiatives on the City's most vulnerable neighborhoods. In connection with the approval of the Mayor's June Budget Message, the City Council gave direction on setting a study session on the concept of equity and how the City can address inequities in City spending and programs.

### **2019-2020 Adopted Operating Budget**

The City Council adopted the 2019-2020 Proposed Operating Budget with certain modifications on June 11, 2019, after a series of City Council Budget Study Sessions to consider the many proposals set forth in the 2019-2020 Proposed Operating Budget. The 2019-20 Proposed Operating Budget as modified and adopted by the City Council on June 11, 2019 is referred to in this Official Statement as the "**2019-2020 Adopted Operating Budget.**" Such modifications include the changes to the 2019-2020 Proposed Operating Budget set forth in the Mayor's June Budget Message. The City anticipates publishing the 2019-2020 Adopted Operating Budget in the Fall of 2019.

The 2019-2020 Adopted Operating Budget is a balanced budget that continues efforts to address the highest priority community and organization needs while maintaining budget stability. The 2020-2024 Five-Year Forecast was used as the starting point in the development of the budget.

The 2018-2019 Adopted Operating Budget includes investments across multiple City funds that support the following major initiatives as identified in the Mayor's March Budget Message for Fiscal Year 2019-2020: Saving; Public Safety; Confronting the High Cost of Housing and Living; Homelessness; Combatting Blight; and the Environment.

### **State Budget**

The City receives a portion of its funding from the State. The City's 2019-2020 [Adopted] Operating Budget projects that approximately [1%] of the City's General Fund revenues will come from State sources.

Voters approved Proposition 1A in November 2004 to amend the State Constitution to place constraints on the State's ability to divert certain specified revenues from local agencies to the State. Subsequently, in November 2010, voters approved Proposition 22 to amend the



State Constitution to further constrain or eliminate the State's ability to redirect revenues from local agencies, including property tax revenues from redevelopment agencies.

On May 9, 2019, the Governor released the 2019-2020 May Revision (the "**May Revision**") to the Governor's Proposed 2019-2020 Budget. [At this time, the City cannot estimate the impact, if any, that the revisions proposed by the May Revision to the Governor's Proposed 2019-2020 Budget will have on the finances of the City.]

## **MAJOR GENERAL FUND REVENUE SOURCES**

Following is a discussion of the City's principal General Fund revenue sources. As discussed more fully in the forepart of this Official Statement under "**CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS**," there are limitations on the ability of the City to increase revenues payable to the General Fund. Legal limitations under the State Constitution generally restrict the ability of cities to raise or increase taxes without voter approval and to increase fees in excess of the amount needed to provide the service with respect to which such fees are charged, and increases to property-related fees may be subject to majority protest. Additional limitations may also be imposed through legislation or initiatives. Furthermore, existing revenues may be subject to certain risk factors.

The table on the following page summarizes the actual revenues for 2017-2018 and budgeted revenues for 2018-2019 and 2019-2020. Included in this presentation are Interfund Transfers and Reimbursements as a source of revenue to the General Fund. The percentage of General Fund revenues for the revenue sources shown in the tables below include Interfund Transfers and Reimbursements.



**Table 12**  
**City of San José**  
**General Fund Revenues<sup>(1)</sup>**  
**2017-2018 Actuals, 2018-2019 Budgeted, and 2019-2020 Budgeted**  
*(in thousands)*

	<b>2017-2018 Actuals</b>	<b>% of Total</b>	<b>2018-2019 Modified Operating Budget<sup>(2)</sup></b>	<b>% of Total</b>	<b>2019-2020 [Proposed] Operating Budget</b>	<b>% of Total</b>
Property Tax .....	\$306,222	23.61%	\$324,450	22.98%	\$354,000	30.25%
Sales and Use Tax .....	226,337	17.45	250,500	17.74	258,300	22.07
Other Revenue .....	218,951	16.88	210,937	14.94	19,778	1.69
Utility Taxes .....	99,753	7.69	102,400	7.25	99,645	8.52
Franchise Fees .....	51,180	3.95	50,475	3.58	48,641	4.16
Business Taxes .....	70,673	5.45	69,400	4.92	72,200	6.17
Licenses and Permits .....	60,503	4.66	60,894	4.31	62,037	5.30
Revenue from Local Agencies .....	38,623	2.96	16,105	1.14	12,483	1.07
Fees, Rates and Charges .....	51,081	3.91	55,822	3.95	55,784	4.77
Telephone Line Tax .....	20,481	1.58	20,000	1.42	20,000	1.71
Revenue from the Federal Government .....	5,591	0.43	6,206	0.44	792	0.07
Fines and Forfeitures .....	14,354	1.11	14,983	1.06	16,213	1.39
Revenue from the State Government .....	15,825	1.21	14,354	1.02	12,435	1.06
Transient Occupancy Tax .....	19,531	1.51	19,700	1.40	22,500	1.92
Revenue from Use of Money and Property .....	7,930	0.61	6,897	0.49	13,144	1.12
Total General Revenues .....	<u>\$1,207,036</u>	<u>92.99</u>	<u>\$1,223,122</u>	<u>86.64</u>	<u>\$1,069,952</u>	<u>91.43</u>
Overhead Reimbursements .....	47,245	3.64	\$52,550	3.72	\$56,133	4.80
Transfers to the General Fund .....	26,306	2.03	23,562	1.67	27,013	2.31
Reimbursements for Services .....	17,328	1.34	18,225	1.29	17,081	1.46
Total Interfund Transfers and Reimbursements .....	<u>90,879</u>	<u>7.01</u>	<u>94,338</u>	<u>6.68</u>	<u>100,227</u>	<u>8.57</u>
<b>TOTAL GENERAL FUND REVENUES<sup>(3)</sup> .....</b>	<b><u>\$1,297,915</u></b>	<b><u>100.00%</u></b>	<b><u>\$1,317,772</u></b>	<b><u>100.00%</u></b>	<b><u>\$1,170,179</u></b>	<b><u>100.00%</u></b>

<sup>(1)</sup> Totals may not add due to independent rounding.

<sup>(2)</sup> As of March 31, 2019.

<sup>(3)</sup> Does not include the Beginning Fund Balance and Reserve for Encumbrances.

Source: City of San José 2019-2020 [Proposed] Operating Budget.



## Assessed Values and Property Taxes

**Assessed Values.** The assessed valuation of property is established by the County Assessor and reported at 100% of the full cash value as of January 1, except for public utility property, which is assessed by the State Board of Equalization.

The County collects the ad valorem property taxes. Taxes arising from the 1% levy are apportioned among local taxing agencies based on a formula established by State law in 1979. Under this formula, the City receives a base year allocation plus an allocation based on growth in assessed value (consisting of new construction, change of ownership and inflation). Taxes relating to voter-approved indebtedness are allocated to the relevant taxing agency. Beginning in 1990-1991 (with the adoption of new State legislation), the County deducts the pro-rata cost of collecting property taxes from the City's allocation.

Table 13 sets forth the City's net assessed valuation for fiscal year 2018-2019 and the previous ten fiscal years.

<b>Table 13</b> <b>City of San José</b> <b>Net Assessed Property Value</b> <b>(in thousands)</b>		
<b>Fiscal Year</b>	<b>Total Net Assessed Valuation<sup>(1)</sup></b>	<b>Percentage Change</b>
2008-2009 .....	\$124,189,474	--
2009-2010 .....	121,995,117	(1.8)%
2010-2011 .....	118,508,779	(2.9)
2011-2012 .....	119,519,391	0.9
2012-2013 .....	121,132,767	1.3
2013-2014 .....	131,817,441	8.8
2014-2015 .....	140,740,876	6.8
2015-2016 .....	150,039,891	6.6
2016-2017 .....	160,547,694	7.0
2017-2018 .....	170,460,819	6.2
2018-2019 .....	181,926,524	6.7
<sup>(1)</sup> Valuations are as of the end of the fiscal year, are net of exemptions and include properties in the Former Agency' project areas.		
Source: California Municipal Statistics, Inc.		

Under current County policy, the City's allocation of total ad valorem taxes is received in approximately the following cumulative percentages: 40% by mid-December, 50% by the first week of January, 85% by the third week of April, 90% by the end of April and 100% by the end of June.

The County Board of Supervisors approved the implementation of an alternative method of distribution of tax levies and collections of tax sale proceeds (a "**Teeter Plan**"), as provided for in Section 4701 et seq. of the California Revenue and Taxation Code. Under the County's



Teeter Plan, the County apportions secured property taxes on an accrual basis when due (irrespective of actual collections) to its local political subdivisions, including the City, for which the County acts as the tax-levying or tax-collecting agency. The County then receives all future delinquent payments, penalties and interest. The Teeter Plan was effective in the County beginning the fiscal year commencing July 1, 1993.

The Teeter Plan is applicable to all tax levies for which the County acts as the tax-levying or tax-collecting agency, or for which the County treasury is the legal depository of tax collections. As adopted by the County, the Teeter Plan excludes Mello-Roos Community Facilities Districts and tax levy for certain 1915 Act assessment bonds.

The Teeter Plan is to remain in effect unless the County Board of Supervisors orders its discontinuance or unless, prior to the commencement of any fiscal year of the County (which commences on July 1), the Board of Supervisors receives a petition for its discontinuance joined in by resolutions adopted by at least two-thirds of the participating revenue districts in the County, in which event the Board of Supervisors is to order discontinuance of the Teeter Plan effective at the commencement of the subsequent fiscal year. The Board of Supervisors may, by resolution adopted no later than July 15 of the fiscal year for which it is to apply, after holding a public hearing on the matter, discontinue the procedures under the Teeter Plan with respect to any political subdivision in the County if the rate of secured property tax delinquency in that political subdivision in any year exceeds 3% of the total of all taxes and assessments levied on the secured rolls for that political subdivision. If the Teeter Plan were discontinued subsequent to its implementation, only those secured property taxes actually collected would be allocated to political subdivisions (including the City) for which the County acts as the tax-levying or tax-collecting agency.

**Property Taxes.** Property Tax receipts collected for the City by the County in the recent fiscal years and as budgeted for 2018-2019 and 2019-20 are set forth in Table 14.

**Table 14**  
**City of San José**  
**Property Tax Receipts**  
**(in thousands)**

<b>Fiscal Year</b>	<b>Property Tax Receipts</b>	<b>Percentage of General Fund Revenues</b>	<b>Percentage Change (Y/Y)</b>
2015-2016 Actual .....	262,950	24.9%	6.3%
2016-2017 Actual .....	276,388	24.9	5.1
2017-2018 Actual .....	306,222	23.6	10.8
2018-2019 Modified Operating Budget.....	324,450 <sup>(1)</sup>	22.9	6.0
2019-2020 [Proposed] Operating Budget.....	354,000	30.25	9.1

<sup>(1)</sup> Increase in Property Tax Receipts as budgeted for 2018-2019 is due, in part, to increases in residual property taxes resulting from debt service savings achieved as a result of the issuance of the 2017 Tax Allocation Refunding Bonds by the Successor Agency.

Source: City of San José 2019-2020 [Proposed] Operating Budget.



Under California law, property owners are entitled to an assessment based on the lower of the fair market value of their property as of the property tax lien date (January 1) or the assessed value as determined at the time of purchase or construction, and increased by no more than 2% annually. A reduction of a property's assessed valuation may occur upon the request of the property owner or the County Assessor may unilaterally reduce the assessed valuations of properties in response to declining market values. In the event a property owner's request for a reduction in assessed value is denied, the property owner may file an appeal.

The County Assessor issued its "2018-19 Assessor's Annual Report" documenting taxable fiscal year 2018-2019 real and business property values for the City and the Successor Agency. The Assessor's Annual Report indicated that there was an increase to the City's assessment roll of 6.69% from fiscal year 2017-2018. The increase for the City is attributable to a combination of factors including changes in ownership, exemptions, new construction, the California Consumer Price Index, and the values of business personal property.

The estimate of Property Tax receipts for 2018-2019 shown in Table 14 takes into account the County Assessor's projections regarding changes in assessed valuations of property located in the City.

**Largest Secured Property Taxpayers.** Table 15 presents a list of the ten largest property taxpayers for 2018-2019 based on secured assessed valuations within the City, which collectively account for approximately 4% of the total secured assessed property valuation for 2018-2019. Some of the properties owned by these property owners are located in redevelopment project areas established by the Former Agency.

**Table 15**  
**City of San José**  
**Ten Largest Local Secured Property Taxpayers**

<b>Name</b>	<b>Assessed Property Valuation</b>	<b>Percentage of Total<sup>(1)</sup></b>
Essex Portfolio LP	\$ 1,199,313,696	0.69%
Cisco Technology Inc.	1,112,096,507	0.64
FRIT San Jose Town & Country Village LLC	789,185,823	0.45
River View Apartments	663,819,040	0.38
Sobrato Interests	639,209,644	0.37
VF Mall LLC	633,636,794	0.37
San Jose Water Works	617,019,170	0.36
Apple Inc.	437,199,590	0.25
Adobe Systems Inc.	434,634,648	0.25
Hitachi Global Storage Techs Inc.	433,810,294	0.25
<b>Total</b>	<b>\$6,959,925,206</b>	<b>4.01%</b>

<sup>(1)</sup> 2018-2019 Local Secured Assessed Valuation: \$173,497,937,003.

Source: California Municipal Statistics, Inc.



## Sales and Use Taxes

The sales tax is an excise tax imposed on retailers for the privilege of selling tangible personal property. The use tax is an excise tax imposed on a person for the storage, use or other consumption of tangible personal property purchased from any retailer. The proceeds of sales and use taxes (collectively, “**Sales Tax**”) imposed within the boundaries of the City are distributed by the State to various agencies as shown in Table 16. The total Sales Tax rate applicable within the City is currently 9.250% and is allocated as follows:

<b>Table 16</b> <b>City of San José</b> <b>Sales Tax Rates</b>	
State – General Fund .....	3.9375%
State – Local Revenue Fund .....	1.5625
State – County Transportation Funds .....	0.2500
State – City or County Operations .....	1.0000
Public Safety Fund (Proposition 172) <sup>(1)</sup> .....	0.5000
<b>Sub-Total Statewide Sales and Use Tax .....</b>	<b>7.2500</b>
Local – City of San José <sup>(2)</sup> .....	0.2500
Santa Clara County Transit District <sup>(3)</sup> .....	0.5000
Santa Clara County Valley Transportation Authority <sup>(4)</sup> .....	0.5000
Santa Clara VTA BART Operating and Maintenance Transactions and Use Tax <sup>(5)</sup> .....	0.1250
Santa Clara County Retail Transactions and Use Tax <sup>(6)</sup> .....	0.1250
Silicon Valley Transportation Solutions Tax <sup>(7)</sup> .....	0.5000
<b>Total .....</b>	<b>9.2500%</b>

<sup>(1)</sup> Approximately 0.18% of this tax is allocated to the City. In 2018-2019, the Santa Clara County share of the statewide allocation is 6.37%; the City receives approximately 2.78% of the allocation to the County.  
<sup>(2)</sup> Approved by voters in June 2016, and effective October 1, 2016, (limited to 15 years) to fund essential City services.  
<sup>(3)</sup> Approved by voters in 1976; does not expire. Imposed by VTA.  
<sup>(4)</sup> Approved by voters in November 2000, and effective April 1, 2006 (limited to 30 years). Imposed by VTA.  
<sup>(5)</sup> Approved by voters in November 2008 to support BART was implemented on July 1, 2012 (limited to 30 years). Imposed by VTA.  
<sup>(6)</sup> Approved by voters in November 2012 and effective April 1, 2013 (limited to 10 years).  
<sup>(7)</sup> Approved by voters in June 2016, and effective April 1, 2017 (limited to 30 years). Imposed by VTA.  
Source: California Department of Tax and Fee Administration; City of San José.

Between fiscal year 2004-2005 and the 2015-2016, the State diverted one-quarter of the City’s 1.00% local share of the sales tax and replaced the lost revenue with a shift of local property taxes to the City from local school district funding. This diversion scheme was commonly referred to as the “Triple Flip.” The Triple Flip ended on December 31, 2015. After such date, the full 1.00% local share of the sales tax is distributed to the City’s General Fund.

At the November 1993 election, Proposition 172 was approved by voters, allowing for the permanent extension of the half-cent sales tax that was originally imposed on July 15, 1991, which was scheduled to sunset on June 30, 1993. (On July 1, 1993, a six-month extension of the tax was granted by the State in order to provide a source of one-time funding for cities and counties to partially offset 1993-1994 ongoing property tax reductions.) The passage of the Proposition 172 legislation, effective January 1, 1994, required that the proceeds from the half-cent tax be diverted from the State to counties and cities on an ongoing basis for funding public safety programs.



At the June 2016 election, Measure B was approved by voters amending the City's Municipal Code to enact a 0.25% transactions and use tax, also referred to as the Local Sales Tax, in the City beginning October 1, 2016 for 15 years to fund essential City services, such as: improving public safety (e.g., additional police officers to improve emergency response times, reduce violent and non-violent crimes, increase neighborhood patrols, and increase fire resources to improve fire and emergency medical response times); maintaining and repairing major streets (e.g., increase pavement maintenance funding for major streets to significantly slow the incidence of pothole formation and general pavement deterioration); and increasing neighborhood services (e.g., additional resources for reducing homelessness, increasing youth and senior services, and other high priority neighborhood services, such as blight eradication and gang prevention). The 0.25% transactions and use tax will terminate automatically on September 30, 2031, unless extended by voters.

The City's budgeting forecast of Sales Tax receipts is based on the forecast of local economists, information from the City's Sales Tax consultant, State officials' estimates, and an analysis of current and historical performance and economic trends. The City develops estimates for General Sales Tax category, which reflects the 1.0% allocation, the .25% Local Tax and the Proposition 172 Sales Tax category, which reflects the portion of the 0.5% public safety sales tax that is allocated to the City.

Table 17 shows actual and budgeted Sales Tax receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2015-2016.

<b>Table 17</b> <b>City of San José</b> <b>Sales Tax Receipts</b> <i>(in thousands)</i>			
<b>Fiscal Year</b>	<b>Sales Tax Receipts</b>	<b>Percentage of General Fund Revenues</b>	<b>Percentage Change (Y/Y)</b>
2015-2016 Actual.....	\$201,797	19.1%	11.9%
2016-2017 Actual.....	207,695	18.7	2.9
2017-2018 Actual.....	226,337	17.4	9.0
2018-2019 Modified Operating Budget.....	250,500	19.0	10.7
2019-2020 [Proposed] Operating Budget.....	258,300	22.07	3.1

Source: City of San José 2019-2020 [Proposed] Operating Budget.

In June 2018, the United States Supreme Court published its decision in *South Dakota v. Wayfair* (the “**Wayfair Decision**”), in which the Supreme Court held that sales to a customer in a particular state alone are sufficient to create a nexus for purposes of determining whether a seller is required to collect sales taxes of the applicable state. Prior to the Wayfair Decision, courts had interpreted the dormant Commerce Clause of the United States Constitution to



require that a company have physical nexus in a state in order for the seller to be liable for the collection of that state's sales tax. Physical nexus is defined as having either property or payroll in the state, including a resident employee working from home or inventory stored in that state.

The State has issued guidance in response to the Wayfair Decision pursuant to Assembly Bill 147 ("**AB 147**"). Under AB 147, beginning April 1, 2019, retailers located outside of the State are required to register with the CDTFA, collect the California use tax, and pay the tax to the CDTFA based on the amount of their sales into California, even if they do not have a physical presence in the state. The new collection requirements apply to retailers if during the preceding or current calendar year certain sales thresholds are met. The new collection requirements apply to taxable sales of tangible personal property to California consumers on and after April 1, 2019, and are not retroactive. AB 147 also imposes collection obligations on retailers that contract with sellers to sell goods and services on their on-line platforms (i.e. "marketplace facilitators") commencing October 1, 2019.

Sales Tax receipts estimates for Fiscal Year 2018-2019 do not include any additional revenue anticipated as a result of the Wayfair Decision. However, Fiscal Year 2019-2020 Sales Tax receipts estimates do factor in an additional revenue of \$5.0 million for out-of-state internet sales.

### **Other Revenue**

The Other Revenue category in 2017-2018 totaled approximately \$219 million, and included the issuance of a \$150.0 million TRAN (the "**2017 TRAN**") to prefund employer retirement contributions for the City's pension plans.

The 2018-2019 Modified Operating Budget projects Other Revenue to decrease to approximately \$211 million, and includes the issuance of a \$150.0 million TRAN (the "**2018 TRAN**") to prefund employer retirement contributions for the City's pension plans. The City has decided to not prefund the employer retirement contributions for the City's pension plans for fiscal year 2019-2020.

Net of the 2018 TRAN, Other Revenues in 2018-2019 represent 1.3% of General Fund revenues for such fiscal year. For a discussion of the 2018 TRAN, see "BONDED AND OTHER INDEBTEDNESS." In addition to TRAN proceeds, the Other Revenue category includes a number of unrelated revenue sources, including proceeds from the sale of property.

### **Utility Taxes**

The Utility Tax is charged to all users of a given utility (electricity, gas, water, and telephone) other than the corporation providing the utility (e.g., a utility company's consumption of all utilities used in the production or supply of its service is not taxed). Except as described below with respect to the City's telephone utility user's tax, the consumers of these services pay a tax at the rate of 5% of the utility charges to the utility company that acts as a collection agent for the City. The utility company collects the tax from consumers on a monthly basis and is required to remit that amount to the City by the 25<sup>th</sup> of the following month. The tax is not applicable to Federal, State, County, or City agencies. Per State law, insurance companies and banks are also exempted from the tax.

On November 4, 2008, voters approved Measure K, a ballot measure that replaced the existing tax on telephone service with an updated telecommunications user's tax. The updated



telecommunication user's tax took effect on April 1, 2009 and reduces the 5.0% tax rate to 4.5%, and applies the tax to all intrastate, interstate and international communications services regardless of technology used to provide such services, such as private communication services, voicemail, paging, and text messaging, and continues to tax existing communication services including landline, wireless, Voice over Internet Protocol, and bundled services, where taxable and non-taxable services are bundled together.

In February 2009, the City Council adopted an ordinance amending the new voter approved telecommunications user's tax to cap the maximum amount of telecommunications user's tax payable by customers that meet certain threshold requirements in order to mitigate any disproportionate financial impact on customers. The ordinance went into effect on April 3, 2009, with an original expiration date of December 31, 2012 that the City Council extended through December 31, 2017. On January 9, 2018, the City Council approved a further extension of the ordinance through December 31, 2022, and changed the annual increase of the cap from 2% to 3%, to take effect retroactively on January 1, 2018.

Table 18 shows Utility Tax receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2015-2016.

<b>Table 18</b> <b>City of San José</b> <b>Utility Tax Receipts</b> <i>(in thousands)</i>			
<b>Fiscal Year</b>	<b>Utility Tax Receipts</b>	<b>Percentage of General Fund Revenues</b>	<b>Percentage Change (Y/Y)</b>
2015-2016 Actual.....	\$93,397	8.8%	2.0%
2016-2017 Actual.....	100,786	9.1	7.9
2017-2018 Actual.....	99,753	7.7	(1.0)
2018-2019 Modified Operating Budget.....	102,400	8.2	2.7
2019-2020 [Proposed] Operating Budget.....	99,645	8.6	(2.7)
<i>Source: City of San José 2019-2020 [Proposed] Operating Budget.</i>			

## Franchise Fees

Franchise Fees are collected mainly from utility providers for the use of public rights-of-way. Franchise Fees include revenues from electricity, gas and water utility services, commercial solid waste, cable television, and nitrogen pipelines. Actual collections are subject to significant fluctuations from the impact of weather conditions and/or rate changes because the largest sources of Franchise Fees are based on utility revenues. Table 19 shows Franchise Fee receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2015-2016.



**Table 19**  
**City of San José**  
**Franchise Fees**  
**(in thousands)**

<b>Fiscal Year</b>	<b>Franchise Fee Receipts</b>	<b>Percentage of General Fund Revenues</b>	<b>Percentage Change (Y/Y)</b>
2015-2016 Actual.....	\$48,949	4.6%	4.4%
2016-2017 Actual.....	49,641	4.5	1.4
2017-2018 Actual.....	51,180	3.9	3.1
2018-2019 Modified Operating Budget.....	50,475	4.0	(1.4)
2019-2020 [Proposed] Operating Budget.....	48,641	4.2	(3.6)

*Source: City of San José 2019-2020 [Proposed] Operating Budget.*

## **Business Taxes**

This category comprises four major subcategories: general business taxes, cardroom business taxes, marijuana business taxes, and disposal facility taxes.

**General Business Tax.** On November 8, 2016, voters approved Measure G, a ballot measure to increase the general business tax imposed on all persons (broadly defined) engaged in business in San José. The general business tax is an excise tax based on the number of persons employed or on the number of units, lots or square feet leased in the City, as applicable. It is not a tax on gross receipts. Prior to Measure G, most businesses paid an annual base tax of \$150 for up to 8 employees with an additional \$18 for each employee thereafter, capped at \$25,000 annually. For landlords of residential real estate, mobile home parks, or commercial real estate the tax was based on the number of units, lots, or square feet leased in San Jose, capped at \$5,000 annually.

Measure G enacted an ordinance, effective on July 1, 2017, that: (1) increased the minimum base tax from \$150 to \$195, set graduated rates for businesses with more employees paying higher rates, increased rates for landlords who pay more per unit, lot and square feet of leased space, (2) raised the annual cap on the maximum amount of tax payable to \$150,000; and (3) instituted an annual adjustment for inflation based on the consumer price index beginning on July 1, 2018, subject to certain limits. Measure G maintained various exemptions for nonprofits and a financial hardship exemption for small business owners, while adding a financial hardship exemption for certain small businesses with limited household incomes.

General Business Tax revenues are estimated to reach \$25.7 million in 2018-2019 and \$28.0 million in 2019-2020.

**Cardroom Tax.** Two cardroom clubs exist in the City. Currently, the number of tables allowed in the City is 98 and the number of tables allowed at each cardroom is 49. The City imposes an annual “base tax” on each cardroom permittee in an annual minimum amount of \$150 per year, plus an additional tax in the amount of \$18 per employee based on the average number of employees, not to exceed a maximum of \$25,000. In addition, if the annual gross revenue of the cardroom exceeds \$10,000, the City imposes a tax equal to 15% of the



cardroom's gross revenues. Cardroom Tax revenues are estimated to reach \$18.7 million in 2018-2019 and remain steady in 2019-2020.

***Marijuana Business Tax.*** On November 2, 2010, San José voters approved Measure U, which allows the City to impose a tax on all marijuana businesses in the City at a rate of up to 10% of gross receipts from the planting, cultivation, harvesting, transporting, manufacturing, compounding, converting, processing, preparing, storing, packaging, and sales of marijuana and ancillary products in the City. On December 13, 2010, the City Council approved a 7% rate and the tax became effective on March 1, 2011 and on June 4, 2013, the City Council adopted an ordinance increasing to the rate to 10% effective on July 1, 2013.

While the maximum tax rate on all marijuana businesses approved by the voters of San José is 10% of gross receipts, the City Council has discretion to set a lower tax rate for different categories of marijuana activities.

On January 15, 2019, the City Council approved amendments to the Municipal Code to add manufacturing, distribution, and laboratory testing to the categories of regulated cannabis businesses in the City. The City currently uses the term "cannabis businesses" instead of the prior term "marijuana businesses." The City Council also directed the City Administration to work with the City Attorney and return to City Council before June 30, 2019 with an ordinance amending the Municipal Code to enact a revised tax rate structure for cultivation, manufacturing, distribution and laboratory testing of cannabis. On May 21, 2019, the City Council adopted an ordinance amending the Municipal Code to revise the Chapter setting forth the Marijuana Business Tax to reduce the tax rate from 10% of gross receipts to 4% of gross receipts derived from cultivation, 3% of gross receipts derived from manufacturing, 2% of gross receipts derived from distribution, and 0% of gross receipts derived from laboratory testing and to replace the term "marijuana" with "cannabis." The reduction of the tax rate for these activities is effective July 1, 2019. The City is unable to project the impact, if any, on tax revenues as the number of businesses that will engage in these activities is unknown. [The 2019-2020 [Proposed] Budget includes Marijuana Business Tax revenues of \$13.5 million in 2018-2019 and remaining flat in 2019-2020 due to the unknowns mentioned above.]

***Disposal Facility Tax.*** On May 26, 1987, the City Council adopted the Disposal Facility Tax, which went into effect on July 1, 1987. The tax is based on the weight of solid waste disposed. The tax rate is \$13.00 per ton and is assessed on landfills located in San José. Disposal Facility Tax revenues are estimated to reach \$12.0 million in 2018-2019 and remain flat in 2019-2020. Table 20a shows Business Tax receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2015-2016.



**Table 20a**  
**City of San José**  
**Business Tax Receipts**  
*(in thousands)*

<b>Fiscal Year</b>	<b>Business Tax Receipts</b>	<b>Percentage of General Fund Revenues</b>	<b>Percentage Change (Y/Y)</b>
2015-2016 Actual.....	\$50,864	4.8%	7.4%
2016-2017 Actual.....	54,159	4.9	6.5
2017-2018 Actual.....	70,673	5.4	30.5
2018-2019 Modified Operating Budget.....	69,400	5.5	(1.8)
2019-2020 [Proposed] Operating Budget.....	72,200	6.2	4.0

*Source: City of San José 2019-2020 [Proposed] Operating Budget.*

Table 20b shows Business Tax receipts by major subcategory since 2015-2016.

**Table 20b**  
**City of San José**  
**Business Tax Receipts By Major Subcategory**  
*(in thousands)*

<b>Subcategory</b>	<b>2015-2016</b>	<b>2016-2017</b>	<b>2017-2018</b>	<b>2018-2019 Modified Operating Budget</b>	<b>2019-2020 [Proposed] Budget</b>
Cardroom Tax	\$17,979	\$18,484	\$18,891	\$18,700	\$18,700
Business Tax	11,840	13,047	26,486	25,700	28,000
Disposal Facility Tax	12,172	12,157	12,278	11,500	12,000
Marijuana Business Tax	8,873	10,471	13,018	13,500	13,500
<b>Total</b>	<b>\$50,864</b>	<b>\$54,159</b>	<b>\$70,673</b>	<b>\$69,400</b>	<b>\$72,200</b>

*Sources: City of San José 2019-2020 [Proposed] Operating Budget.*

## Licenses and Permits

The City requires payment for the issuance of Building Permits, Fire Permits, and miscellaneous health and safety-related licenses and permits. For most licenses and permits, the various fees charged by a given department are based on full recovery of the estimated costs for providing each service. Where appropriate, license and permit fees take into consideration approved exceptions to the City Council's full cost recovery policy, as well as applicable State laws. Specific prices and rates are determined by ordinance and each of the charges is fully explained in the City's Fees and Charges Report, which is released in May of each year. Table 21 shows Licenses and Permits receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2015-2016.



**Table 21**  
**City of San José**  
**Licenses and Permits Receipts**  
**(in thousands)**

<b>Fiscal Year</b>	<b>Licenses and Permits Receipts</b>	<b>Percentage of General Fund Revenues</b>	<b>Percentage Change (Y/Y)</b>
2015-2016 Actual.....	\$53,766	5.1%	13.2%
2016-2017 Actual.....	58,075	5.2	8.0
2017-2018 Actual.....	60,505	4.7	4.2
2018-2019 Modified Operating Budget.....	60,894	4.9	0.6
2019-2020 [Proposed] Budget.....	62,037	5.3	1.9

Sources: City of San José 2019-2020 [Proposed] Operating Budget.

## Revenue from Local Agencies

This revenue category includes revenue received from a variety of other local government agencies. For example, the City receives payments from the Central Fire District for fire services provided to the Central Fire District residents by the San José Fire Department. Table 22 shows Revenue from Local Agencies, its respective percentage of General Fund revenues, and year-over-year changes since 2015-2016.

**Table 22**  
**City of San José**  
**Revenue from Local Agencies**  
**(in thousands)**

<b>Fiscal Year</b>	<b>Revenue from Local Agencies</b>	<b>Percentage of General Fund Revenues</b>	<b>Percentage Change (Y/Y)</b>
2015-2016 Actual.....	\$17,143	1.6%	(57.0)%
2016-2017 Actual.....	27,717	2.5	(61.7)
2017-2018 Actual.....	38,623 <sup>(1)</sup>	3.0	38.7
2018-2019 Modified Operating Budget.....	16,105	1.1	(58.1)
2019-2020 [Proposed] Operating Budget.....	12,483	1.0	(22.5)

<sup>(1)</sup> The increase in Revenue from Local Agencies from fiscal year 2016-2017 to fiscal year 2017-2018 is primarily due to a reimbursement payment by the Successor Agency to the City of approximately \$13.6 million to pay debt service on City of San José Financing Authority Lease Revenue Bonds, Series 2001F (Convention Center Refunding Project) (the “**2001F Convention Center Bonds**”), the debt service on which the Successor Agency was obligated to reimburse the City from tax increment revenues from the Former Agency’s project areas. A portion of the net proceeds of the 2017 Tax Allocation Refunding Bonds were used to refund the 2001F Convention Center Bonds in full. In fiscal year 2017-2018, the City also received a reimbursement from the Successor Agency for enforceable obligations totaling approximately \$12.2 million.

Sources: City of San José 2019-2020 [Proposed] Operating Budget.



## Transient Occupancy Tax

The Transient Occupancy Tax is assessed as a percentage of the rental price for transient lodging charged when the period of occupancy is 30 days or less. The tax rate is currently 10%

The General Fund portion of the Transient Occupancy Tax totaling approximately 40%, was enacted as a general tax. The other 60% of the Transient Occupancy Tax is restricted for use in cultural development, supporting a convention and visitors bureau, and supporting the convention and cultural facilities of the City.

Table 23 shows Transient Occupancy Tax receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2015-2016.

<b>Table 23</b> <b>City of San José</b> <b>Transient Occupancy Tax</b> <b>(in thousands)</b>			
<b>Fiscal Year</b>	<b>Transient Occupancy Tax</b>	<b>Percentage of General Fund Revenues</b>	<b>Percentage Change (Y/Y)</b>
2015-2016 Actual.....	\$16,565	1.6%	12.4%
2016-2017 Actual.....	18,275	1.6	10.3
2017-2018 Actual.....	19,531	1.5	6.9
2018-2019 Modified Operating Budget.....	19,700	1.4	0.9
2019-2020 Adopted Operating Budget.....	22,500	1.9	14.2
<i>Sources: City of San José 2019-2020 [Proposed] Operating Budget.</i>			

## FINANCIAL OPERATIONS

### Financial Statements

Since 2001-2002, the City has prepared its audited Basic Financial Statements (referred to as General Purpose Financial Statements in previous years) in accordance with Governmental Accounting Standards Board Statement No. 34. The Basic Financial Statements provide both government-wide financial statements with a long-term perspective on the City's activities while retaining the more traditional fund-based financial statements that focus on near-term inflows, outflows, and balances of spendable financial resources. The government-wide financial statements report on a full accrual basis and include comprehensive reporting of the City's infrastructure and other fixed assets.

Tables 23 and 24 on the following pages summarize financial information contained in the City's Basic Financial Statements as of June 30 for 2013-2014 through 2017-2018. The tables include information solely on the General Fund of the City.



**Table 24**  
**City of San José**  
**General Fund**  
**Balance Sheet**  
**2013-2014 through 2017-2018**  
*(in thousands)*

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018
<b>ASSETS</b>					
Cash and Pooled Investments.....	\$282,631	\$308,829	\$281,607	\$299,728	\$296,597
Receivables:					
Taxes .....	38,918	39,953	72,606	55,039	54,281
Accrued Interest .....	304	510	629	1,440	1,986
Grants .....	2,851	1,207	1,352	822	3,081
Other .....	33,439	35,160	36,963	39,782	39,965
Less: allowance for uncollectibles .....	(18,678)	(21,715)	(28,759)	(27,904)	(26,398)
Due from Other Funds .....	2,078	1,942	1,450	1,823	1,797
Due from Outside Agencies.....	783	655	459	341	185
Loans Receivable (net of allowance for uncollectibles)	1,491	1,241	1,241	1,241	1,241
Advances and Deposits	219	203	186	170	153
Advances to Other Funds.....	3,297	3,297	3,297	3,297	3,297
Advances to Receivable from SARA .....	13,109	6,404	26,182	28,950	13,863
Restricted Assets:					
Cash and Pooled Investments .....	1,264	1,269	1,277	1,289	1,308
Cash and Investments held with fiscal agent.....	19,260	19,250	4,564	2,852	682
<b>TOTAL ASSETS</b>	<b>\$380,966</b>	<b>\$398,205</b>	<b>\$403,054</b>	<b>\$408,870</b>	<b>\$392,038</b>
<b>LIABILITIES</b>					
Accounts Payable.....	6,994	14,805	14,105	14,125	9,001
Accrued Salaries, Wages and Payroll Taxes.....	14,681	20,260	23,305	30,536	33,975
Due to Other Funds .....	10,149	--	--	--	--
Due to Successor Agency .....	15	--	--	--	--
Due to Outside Agency.....	373	373	373	373	372
Unearned Revenue.....	6,792	6,363	6,205	6,302	6,483
Advance, Deposits, and Reimbursement Credits.....	7	7	7	7	7
Advances from Other Funds.....	8,111	8,112	--	--	--
Other Liabilities .....	29,780	32,331	29,803	32,553	36,736
<b>TOTAL LIABILITIES</b>	<b>\$76,902</b>	<b>\$82,251</b>	<b>\$73,798</b>	<b>\$83,896</b>	<b>\$86,574</b>
<b>DEFERRED INFLOW OF RESOURCES</b>	--	--	10,217	12,142	12,442
<b>FUND EQUITY</b>					
Fund Balances:					
Nonspendable .....	219	203	186	170	153
Restricted .....	19,629	10,599	1,265	690	1,057
Committed .....	121,991	94,748	84,998	96,026	97,809
Assigned .....	111,587	143,398	167,239	136,093	111,509
Unassigned .....	50,638	67,006	65,351	79,853	82,494
<b>TOTAL FUND EQUITY</b>	<b>304,064</b>	<b>315,954</b>	<b>319,039</b>	<b>312,832</b>	<b>293,022</b>
<b>TOTAL LIABILITIES AND FUND EQUITY</b>	<b>\$380,966</b>	<b>\$398,205</b>	<b>\$403,054</b>	<b>\$408,870</b>	<b>\$392,038</b>

Source: City of San José Comprehensive Annual Financial Reports, 2013-2014 through 2017-2018.



**Table 25**  
**City of San José**  
**General Fund**  
**Statement of Revenues, Expenditures and Changes in Fund Balance**  
**2013-2014 through 2017-2018**  
*(in thousands)*

	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018
<b>REVENUES</b>					
Taxes:					
Property Taxes .....	\$223,645	\$247,258	\$263,300	\$276,388	\$306,222
Sales Taxes and Shared Revenue .....	173,412	180,407	201,797	207,695	226,337
Utility Taxes .....	114,486	112,645	113,474	121,045	120,234
State of California in-lieu Tax.....	434	419	410	467	551
Franchise Taxes .....	45,749	46,909	48,949	49,642	51,180
Business Taxes .....	45,501	47,431	50,864	54,159	70,673
Miscellaneous Taxes.....	11,873	14,734	16,565	18,275	19,531
Total Taxes.....	615,099	649,803	695,359	519,976	568,391
Licenses, Permits, and Fines .....	66,826	62,000	69,856	75,173	74,859
Intergovernmental .....	18,951	11,385	9,103	11,132	11,773
Charges for Current Services.....	42,806	42,731	48,110	46,049	52,303
Interest and Investment income.....	3,795	1,749	4,658	2,222	2,228
Other Revenues.....	39,461	40,998	44,582	38,821	42,905
<b>TOTAL REVENUES</b>	<b>\$786,938</b>	<b>\$808,666</b>	<b>\$871,668</b>	<b>\$901,068</b>	<b>\$978,796</b>
<b>EXPENDITURES</b>					
Current:					
General Government.....	75,559	71,792	92,093	95,861	100,732
Public Safety .....	462,187	485,327	513,921	536,068	593,162 <sup>(1)</sup>
Capital Maintenance .....	64,845	75,493	85,324	111,737	120,158
Community Services .....	107,512	122,614	132,115	133,409	139,593
Sanitation .....	1,041	1,291	1,690	2,444	4,148
Capital Outlay .....	3,685	21,766	26,832	14,535	14,264
Debt Service:					
Principal .....	--	13,623	1,463	1,526	39,119 <sup>(2)</sup>
Interest.....	499	1,250	1,200	1,328	2,184
<b>TOTAL EXPENDITURES</b>	<b>\$715,328</b>	<b>\$793,156</b>	<b>\$854,638</b>	<b>\$896,908</b>	<b>\$1,013,360</b>
<b>Excess (Deficiency) of Revenues over Expenditures</b>	<b>71,610</b>	<b>15,510</b>	<b>17,030</b>	<b>4,160</b>	<b>(34,564)</b>
<b>OTHER FINANCING SOURCES (USES)</b>					
Transfers In.....	9,784	9,124	10,253	20,461	11,409
Proceeds from capital lease financing .....	19,286	--	--	--	--
Proceeds for sale of capital assets.....	2,221	37,482	3,848	157	38,187
Transfers Out .....	(25,731)	(50,226)	(28,046)	(30,985)	(34,842)
<b>TOTAL OTHER FINANCING SOURCES (USES)</b>	<b>\$5,560</b>	<b>\$(3,620)</b>	<b>\$(13,945)</b>	<b>\$(10,367)</b>	<b>\$14,754</b>
<b>Excess (Deficiency) of Revenues and Other Sources over Expenditures and Other Uses</b>	<b>77,170</b>	<b>11,890</b>	<b>3,805</b>	<b>(6,207)</b>	<b>(19,810)</b>
<b>Fund Balance - July 1</b>	<b>226,894</b>	<b>304,064</b>	<b>315,954</b>	<b>319,039</b>	<b>312,832</b>
<b>Fund Balance - June 30</b>	<b>\$304,064</b>	<b>\$315,954</b>	<b>\$319,039</b>	<b>\$312,832</b>	<b>\$293,022</b>

<sup>(1)</sup> Increase in 2017-2018 is due primarily to an increase in salary and benefits paid to the City's safety employees as required under their collective bargaining agreements. See "– LABOR RELATIONS."

<sup>(2)</sup> Increase in 2017-2018 is due primarily to repayment and defeasance of the Series 2008F Bonds in the amount of \$37.1 million.

Source: City of San José Comprehensive Annual Financial Reports, 2013-2014 through 2017-2018.



## Financial and Accounting Information

**General.** The accounts of the City are organized on the basis of funds, each of which is considered a separate accounting entity. The fund financial statements provide information about the City's funds, including fiduciary funds. Separate statements for each fund category, such as governmental, proprietary and fiduciary, are presented. The emphasis of fund financial statements are on the major governmental and enterprise funds of the City and are reported separately in the accompanying financial statements. All remaining governmental funds are aggregated and reported as nonmajor funds in the City's accompanying financial statements.

Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts.

The basis of accounting determines when transactions are reported in the financial statements. The government-wide, proprietary and fiduciary funds (excluding agency funds) financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Agency funds do not have a measurement focus but are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash flows take place. Non-exchange transactions, in which the City gives (or receives) value without directly receiving (or giving) equal value in exchange, include property and sales taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenues from sales and use, transient occupancy and utility user taxes are recognized when the underlying transactions take place. Revenues from grants, entitlements and donations are recognized in the fiscal year in which all eligibility requirements have been satisfied. Governmental funds are reported using the current financial resources measurement focus and modified accrual basis of accounting. This focus is on the determination of, and changes in financial resources, and generally only current assets and current liabilities are included in the balance sheet. Revenues are recognized in the accounting period in which they become both measurable and available to finance expenditures of the fiscal period. For this purpose, the City considers revenues as available if they are collected within sixty days after the end of the current fiscal period. Expenditures are generally recorded when a liability is incurred. However, principal and interest on long-term debt and certain estimated liabilities, such as compensated absences and self-insurance claims, are recorded when payment is due.

**Implementation of GASB 68.** In June 2012, the Governmental Accounting Standards Board issued Statement No. 68, Accounting and Financial Reporting for Pensions - an amendment of GASB Statement No. 27 ("**GASB Statement No. 68**"), which addresses the accounting and financial reporting requirements for pensions. The provisions of GASB Statement No. 68 separate accounting and financial reporting from how pensions are funded and require changes in the notes to the financial statements and required supplementary information. Significant changes include an actuarial calculation of the total and net pension liability. It also includes comprehensive footnote disclosure regarding the pension liability, the sensitivity of the net pension liability to the discount rate, and the pension expense and related deferred outflows/inflows of resources disclosures. When the City implemented this statement in fiscal year 2015, the City also implemented GASB Statement No. 71, Pension Transition for Contributions Made Subsequent to the Measurement Date – an amendment of GASB Statement No. 68, which resolves transition issues in GASB Statement No. 68.



The implementation by the City of GASB Statement No. 68 resulted in the recognition of a net pension liability in the amount of \$1.699 billion, the deferred outflows of resources related to pension contributions made subsequent to the measurement date of June 30, 2014 in the amount of \$244.1 million, and the deferred inflows of resources related to differences between projected and actual earnings on pension investments in the amount of \$275.8 million as of June 30, 2015.

See APPENDIX B – “THE CITY OF SAN JOSE: RETIREMENT PLANS.”

**Implementation of GASB 75.** In June 2015, the GASB issued Statement No. 75, Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions (other postemployment benefits or OPEB) (“**GASB Statement No. 75**”). This statement replaces the requirements of Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, as amended, and No. 57, OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans. The scope of this statement addresses accounting and financial reporting for other post-employment benefits (“**OPEB**”) that is provided to the employees of state and local governmental employers. The GASB Statement No. 75 requires the liability for OPEB obligations, known as the net OPEB liability, to be recognized on the Statement of Net Position. In addition, an OPEB expense is to be recognized in the Statement of Activities and the statement of changes in net position of proprietary and fiduciary funds. The OPEB expense in GASB Statement No. 75 is no longer equal to the annual required contribution and has shorter amortization periods. There is a recognition of OPEB expense that incorporates deferred outflows of resources and deferred inflows of resources related to OPEB over a defined, closed period, rather than a choice between an open or closed period. For defined benefit OPEB, this statement identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. This statement requires that the notes to financial statements of a single employer that sponsors an OPEB plan include descriptive information, such as the types of benefits provided and the number and classes of employees covered by the benefit terms. This statement also requires that a single employer that sponsors an OPEB plan to present in Required Supplementary Information the sources of changes in the net OPEB liability and the components of the net OPEB liability and related ratios.

As of June 30, 2018, total net OPEB liability was \$1.071 billion, which included \$957.6 million in governmental activities and \$113.7 million in business-type activities. As a result of the implementation of GASB Statement No. 75, the prior year net OPEB obligation of \$478.5 million under Governmental Accounting Standards Board Statement No. 45 was eliminated and replaced with the net OPEB liability.

See APPENDIX B – “THE CITY OF SAN JOSE: RETIREMENT PLANS.”

## **City Audit and Management Report**

The City Council engages an independent certified public accountant (the “**Accountant**”) who examines books, records, inventories and reports of all officers and employees who receive, control, handle, or disburse public funds and of any other officers, employees or departments as the City Council directs. These duties are performed both annually and upon request. For the financial statements for 1999-2000 to 2014-2015, the City retained Macias Gini & O’Connell LLP as the Accountant. For 2015-2016 and 2016-2017, the City engaged Grant Thornton LLP as the Accountant. For 2017-2018, the City engaged Macias Gini & O’Connell



LLP. Within 180 days following the end of each fiscal year, the Accountant submits the final audit to the City Council. The City then publishes the City's financial statements as of the close of the fiscal year in the Comprehensive Annual Financial Report.

In addition to the annual audit of the City's financial statements, the Accountant issues an annual audit report of the City's internal controls over financial reporting (the "**Management Report**") to the City Council.

The 2017-2018 Management Report noted five "significant deficiencies." A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. The Accountant found such deficiencies relating to the City's financial reporting process, as well as the City's controls over information technology.

Specifically, in the 2017-2018 Management Report, the Accountant commented that between 2006 and 2015, the City reduced its budgeted positions by 25 percent and that "[t]his reduction and displacement of staff through the Civil Service Rules resulted in a significant disruption in the City's ability to maintain appropriate financial internal controls." The Accountant further commented that, "[w]hile the City has been successful in recruiting professionals over the past two years, it has been challenged with retaining these professionals." As a result, the workload of the remaining seasoned professionals has increased and resulted in numerous late and significant adjusting entries after the close of the City's financial records.

The City's management, in its response to this finding, agreed with the Accountant's comment and acknowledged that staffing turnover negatively impacted timely and accurate reconciliation of accounts and completion of audit documents. Staff believes that the staffing challenges coupled with increased workload has led to the high staff turnover with several departures to other City departments and to outside public agencies with better compensation packages when compared to the City. The City's management further noted that despite these challenges, the City's Finance Department is undertaking steps to address this finding. Such steps include the hiring of the Deputy Director of Finance, Accounting, position which had been vacant since June 2018. The City's management further noted that it anticipates during 2018-2019, to institute changes to address to internal control issues, including training and cross training of professional accounting staff in core job assignments. Additionally, to address this finding, the 2019-2020 [Proposed] Operating Budget includes the addition of two accountants which is anticipated to provide more capacity for management positions in the City's Accounting Division to provide support and training to accounting staff in other departments.

The Accountant also found significant deficiencies regarding the City's control over the City-wide information security program; account management; password configuration; board privileged access; password configuration; shared accounts; and audit logging/monitoring. Specifically, in the 2017-2018 Management Report, the Accountant commented that management had not assigned security responsibilities associated with its decentralized control environment; had not finalized, published, and communicated formal policies and procedures related to information technology control process; did not have a process implemented to perform continuous monitoring such as periodic risk and vulnerability assessments; defined City-wide password security configurations; defined requirements for privileged user accounts, shared accounts, logging/monitoring; and maintain a process to consistently document and retain evidence related to change management activities.



The City's management, in response to this finding, commented that it has made progress in certain areas related to information technology governance and control. Such progress includes budgeting a new cybersecurity program overseeing information and systems and security for the entire organization, the hiring of the City's first Chief Information Security Officer in April 2018, and the drafting of the City Information Security Standards Handbook. In addition, the City has also completed vulnerability scans and initiated new periodic checks of vulnerabilities. The City's management also commented that the City has taken steps to improve its change control process and a new City-wide Change Control Board was formed in August 2018 to maintain enterprise level visibility.

Significant deficiencies substantially the same as those set forth in the 2017-2018 Management Report and described above were made in the Management Report for 2016-2017.

## **INSURANCE AND SELF-INSURANCE PROGRAMS**

The City reassesses its insurance coverage annually. Therefore, the City makes no representations that the insurance coverages described below will be maintained in the future.

### **Citywide Insurance**

**General Liability.** The City is self-insured for workers' compensation, general liability, auto liability, and certain other risks. The current portion of claims liability is accounted for in the General Fund and the enterprise funds on the basis of settlements reached or judgments entered within the current fiscal year. In the government-wide financial statements and the enterprise fund financial statements, the estimated liability for all self-insurance liability claims is recorded as a liability.

The City self-insures for liability (other than for the Airport and the San José-Santa Clara Regional Wastewater Facility (the "**Plant**")), personal injury, and workers' compensation. The City currently maintains an all-risk property policy including boiler and machinery exposures, coverage for loss due to business interruption and flood. The City does not carry earthquake insurance as it was not available at reasonable rates.

A summary of insurable coverage for the policy period October 1, 2018 to October 1, 2019 is provided in Table 26.



**Table 26**  
**City of San José**  
**Summary of Citywide Property Insurance Coverage**  
*(For Policy period October 1, 2018 – October 1, 2019)*

	<b>Coverage Per Occurrence</b>	<b>Deductible Per Occurrence</b>
Property, including Business Interruption <sup>(1)</sup>	\$1.5 billion	\$100,000
Flood Zone, SFHA <sup>(3)</sup>	\$25 million (and annual aggregate)	5% of TIV (\$1 Million minimum deductible) <sup>(2)</sup>
Flood, Other Locations	\$100 million (and annual aggregate)	\$100,000

<sup>(1)</sup> Acts of terrorism are covered.

<sup>(2)</sup> TIV: Total Insured Value; Deductible applies per affected location.

<sup>(3)</sup> SFHA: Special Flood Hazard Area as defined by the Federal Emergency Management Agency.

Source: City of San José, Finance Department - Risk & Insurance Management.

**Airport Liability Policy.** The City also maintains an airport liability policy (the “**Airport Liability Policy**”) covering the Airport, which provides a \$200,000,000 combined single limit for bodily injury and property damage subject to a deductible of \$0 per occurrence and annual aggregate with a sublimit of \$50,000,000 per occurrence and in the annual aggregate for personal injury, and a limit of \$200,000,000 per occurrence and in the annual aggregate as respects to war liability.

In addition, the Airport Liability policy also provides excess liability coverage with a limit of \$50,000,000 in excess of the underlying limit of \$1,000,000, which is provided by a separate automobile policy issued to provide coverage for the off-premise operations of scheduled Airport vehicles including shuttle bus fleets with a limit of \$1,000,000 per occurrence, combined single limit for bodily injury and property damage, and no deductible. [Physical damage coverage is available for the Airport Shuttle Bus Fleet and is subject to a \$10,000 comprehensive and \$25,000 collision deductible. As part of general support services, the City charges the Airport for the cost of liability and property insurance coverage. Settled claims have not exceeded the City’s commercial insurance coverage in any of the past 4 years.]

**Crime Coverage.** The City maintains government fidelity/crime coverage for City losses arising from employee bad acts. Coverage is for financial or property losses and provides a \$5,000,000 per occurrence limit for losses resulting from employee theft, forgery or alteration and inside the premises- theft of money and securities, and provides for a \$1,000,000 per occurrence limit for computer fraud, funds transfer fraud, money orders, and counterfeit money. All claims have a \$100,000 deductible per occurrence.

**Workers’ Compensation.** As noted above, the City is self-insured and self-administered for workers’ compensation with claims paid on a “pay as you go” basis. The City budgets for workers’ compensation payouts based on prior year payout history.

Pursuant to City Council direction, the City’s Worker’s Compensation Program has been fully outsourced to Intercare, a third-party administrator (“**Intercare**”). As of September 1, 2018,



all in-house claims were electronically transferred to Intercare with all open claims administered by Intercare staff.

As of March 1, 2019, open claims data for Intercare were at 2,599. The total number of open claims has been significantly reduced (by approximately 17%) since June 30, 2018 when the open claim inventory was 3,120 (Intercare - 1,488, City of San Jose - 1,632). This was in large part a result of Intercare's triage process.

The City conducted a Request for Proposal process for a third-party administrator to provide all services related to the City's Workers' Compensation Program to commence on July 1, 2019, which is pending Council approval in June 2019. A new agreement with a third-party administrator is anticipated be in place for the 2019-2020 fiscal year.

As a result of the transfer of all claims administration to Intercare, the City anticipates no longer being subject to state audits related to the City's workers' compensation program in the future. The last state audit of the City's workers' compensation program was in 2016. The City anticipated the possibility of being subject to a re-audit by the State in the end of 2018. The City is not aware of any pending audits by the State of the City's workers' compensation program.

**Third Party Liability Claims.** The City is also self-insured for third party liability claims other than those involving the Airport and the Plant. Generally, third party liability claims are handled by the City Attorney's Office. The City maintains an emergency reserve provide funding for potential workers' compensation or general liability claims that exceed the budgeted amounts as the City, for the most part, is self-insured. As of June 30, 2018, the workers' compensation and general liability catastrophic reserve accounts totaled \$15,000,000 of the unassigned fund balance.

Claims liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. The result of the process to estimate the claims liability is not an exact amount as it depends on many complex factors, such as inflation, changes in legal doctrines, newly discovered information and damage awards. Accordingly, claims are reevaluated periodically to consider the effects of inflation, recent claims settlement trends (including frequency and amount of pay-outs), economic and social factors, newly discovered information and changes in the law. The estimate of the claims liability also includes increases or decreases to previously reported unsettled claims. The workers' compensation estimate includes allocated loss adjustment expenses, which represent the direct cost associated with the defense of individual claims, which may be years into the future and have been discounted to their present value using a rate of 3.1% for the amounts recorded.

With respect to the general liability accrual, the City has numerous unsettled lawsuits filed or claims asserted against it as of June 30, 2018. The City Attorney and, with respect to workers' compensation claims, the City's Department of Human Resources have reviewed these claims and lawsuits in order to evaluate the likelihood of an unfavorable outcome to the City and to arrive at an estimate of the amount or range of potential loss to the City. The City has included a provision for losses in its claims liability for loss contingencies that are both probable and can be reasonably estimated. As of June 30, 2018, the provision for losses in its claims liability for loss contingencies totaled approximately \$142.4 million. Because the City recognizes estimated liabilities, such as compensated absences and self-insurance claims, when payment is due, the claims liability for loss contingencies as of June 30, 2018 includes only claims for which payment is due but not estimated reported claims that are not yet due.



See “SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND COURT DECREES” below for a description of certain claims filed against the City.

***Unemployment Insurance.*** The City self-insures to the limits required by State statute. The City budgets for each year’s anticipated unemployment insurance claims. By policy, the City also funds a reserve for claims equal to at least one year of claims payments.

***Dental Insurance.*** The City self-insures one of its two dental plans. The City budgets each year for anticipated claims and a claims reserve as recommended by an actuary. Currently, the claims reserve is an amount equal to three months of claims.

***Medical Insurance.*** The City self-insures one medical plan. Similar to the dental plan, an actuary advises the City on claims projections and reserves for claims. Based on the projected revenues and expenditures in the fund that accounts for the self-insured medical plan, the claims are budgeted, but the reserve for claims is not budgeted and a General Fund subsidy has been required each fiscal year since 2017-2018. The City is actively pursuing a fully insured replacement for this plan effective January 1, 2020; however, the City cannot predict whether a fully insured medical plan to replace the self-insured medical plan will be implemented.

Effective January 1, 2017 the City has maintained a stop loss insurance policy that protects the City from liability for large claims with two forms of coverage, individual and aggregate. The individual coverage is for all claims over \$300,000 incurred by one member in the calendar year. The aggregate coverage applies once total claims for all members exceed an attachment point that is a function of expected claims per member and is fixed each year in the policy. For calendar year 2019, the attachment point is \$13,484,577. The liability thresholds for triggering the aggregate coverage have not been met in any of the completed calendar years that the City has maintained the stop loss insurance policy and the City does not anticipate reaching the liability threshold for calendar year 2019. Since January 2017, individual claims have exceeded \$300,000 on a few occasions resulting in payments from the insurance carrier of \$82,433 in 2017-2018 and \$14,842 in 2018-2019.

#### **[Airport Owner-Controlled Insurance Programs]**

***North Concourse Project.*** On March 31, 2004, the City bought certain liability insurance coverages for major components of the Airport’s North Concourse project (the “**North Concourse Project**”) through an owner-controlled insurance program (“**OCIP**”) from Chartis, formerly American International Group, AIU Holdings, Inc. and AIU LLC. The OCIP is a single insurance program that provides commercial general liability, excess liability and worker’s compensation insurance coverage for construction jobsite risks of the project owner, general contractors and all subcontractors associated with construction at the designated project site.

Due to delays in completing the North Concourse Project, the City was also required to establish a claims loss reserve for the North Concourse Project in the aggregate amount of \$3,900,000 available in a cash working fund. The full amount of the claims loss reserve had been deposited with the insurance carrier and was recorded as advances and deposits in the accompanying Airport enterprise fund statements of net position. The claims loss reserve funds are available to Chartis to pay claims within the City’s deductible of up to \$250,000 per occurrence to an aggregate maximum loss exposure within coverage limits to the City of \$3,900,000. The City was able to negotiate the return of a large portion of the unused claims reserve in advance of the 10-year coverage term. Since March 2010, Chartis has returned



\$3,458,000 to the Airport as of April 30, 2019. The balance of the North Concourse Project reserve fund as of April 30, 2019 was approximately \$14,000.

The North Concourse Project has been completed and the policies expired on December 31, 2008. Closeout procedures on the North Concourse Project are in process. The City has requested that any remaining funds be distributed to the City.

**Terminal Area Improvement Program.** On March 15, 2007, the City obtained additional liability insurance through Chartis for major components of the Airport's Terminal Area Improvement Program ("TAIP") through another OCIP (the "TAIP OCIP"). The coverage for this program is as follows:

**Table 27**  
**City of San José**  
**Summary of Airport Owner-Controlled Insurance Program – TAIP**

<b>Coverages</b>	<b>Limit</b>	<b>Deductible Per Occurrence</b>
General Liability	\$2 million per occurrence \$4 million aggregate	\$250,000
Workers' Compensation	Statutory	\$250,000
Employers' Liability	\$1 million per accident	\$250,000
Excess Liability	\$200 million	None

*Source: City of San José, Finance Department - Risk & Insurance Management.*

The liability under the TAIP OCIP is based upon an estimated payroll of \$92,500,000 for the covered projects and a construction period of 45 months, commencing on March 15, 2007 through December 31, 2010. The terms of the TAIP OCIP require the City to fund a claims loss reserve fund with Chartis in the amount of \$8,900,000. The claims loss reserve fund is available to Chartis to pay claims within the City's deductible subject to an aggregate maximum loss exposure within coverage limits to the City of \$8,900,000. The City was able to negotiate to fund 74% of the claims loss reserve and interest generated remains in the fund. The full amount of \$6,500,000 was deposited with Chartis in fiscal year 2008-2009 and was recorded as advances and deposits in the accompanying Airport enterprise fund statement of net position. Since August 2013, as part of the annual loss reserve analysis by Chartis, a total amount of \$2,297,000 has been returned to the Airport as of April 30, 2019. The balance of the TAIP reserve fund as of April 30, 2019 was approximately \$1.5million.

The TAIP Project has been completed and the policies expired on June 30, 2011. Chartis will continue to hold the remaining funds in the claims loss reserve until such time as the exposure to risk of claims ceases or the City opts to cash out the remaining funds in exchange for accepting responsibility for potential future claims.

**RWF OCIP.** Pursuant to an agreement executed between the City and City of Santa Clara in 1959 (the "**1959 Agreement**"), the City is co-owner and administering agency of the Plant. On June 30, 2017, the City bound certain liability insurance coverage for the major components of the San José-Santa Clara Regional Wastewater Facility Capital Improvement Program through an owner-controlled insurance program ("**RWF OCIP**") with the primary carrier Old Republic General Insurance Corporation ("**Old Republic**"). The RWF OCIP is a single



insurance program that the City sponsors and provides commercial general liability, excess liability and worker's compensation insurance coverage for construction jobsite risks of the project owner, general contractors and all subcontractors associated with construction at the designated project site. In addition, the City procured builder's risk, contractor's pollution liability, and owners protective indemnity insurance to cover liabilities associated with the work.

The City was also required to establish and post a cash collateral fund of \$2,657,000, to be paid in five annual installments and subject to the Old Republic's quarterly requests to adjust based on expenditure of funds up to the maximum aggregate loss of \$4,385,000. The cash collateral fund is available to Old Republic to pay claims within the City's deductible of up to \$250,000 per occurrence to an aggregate maximum loss exposure within coverage limits to the City of \$4,385,000. The coverage for this program is as follows:

<b>Table 28</b> <b>City of San José</b> <b>Summary of José-Santa Clara Regional Wastewater Facility Capital Improvement Program</b>		
<b>Coverages</b>	<b>Limit</b>	<b>Deductible Per Occurrence</b>
General Liability	\$2 million per occurrence \$4 million aggregate	\$250,000
Workers' Compensation	Statutory	\$250,000
Employers' Liability	\$1 million per accident	\$250,000
Excess Liability	\$100 million	None
<i>Source: City of San José, Finance Department - Risk &amp; Insurance Management.</i>		

The premiums of the RWF OCIP are calculated based on the estimated hard cost of construction valued at \$535,000,000 for the covered capital improvement projects to be enrolled and for work to be performed up to March 30, 2023.]



## LABOR RELATIONS

### Overview

Currently, the City has 10 recognized employee bargaining units. The table below shows the representation and agreement expiration dates for the 10 bargaining units. In addition to its represented employees, the City has 326 unrepresented employees budgeted for 2018-2019.

**Table 29**  
**City of San José**  
**Summary of Labor Agreements**

	<b>Agreement Expiration Date</b>	<b>Full-Time Equivalent Employment<sup>(1)(2)</sup></b>
International Union of Operating Engineers, Local #3 <sup>(3)</sup>	9/30/19	727
San José Police Officers' Association	6/30/20	1,149
Association of Maintenance Supervisory Personnel	6/30/21	113
Association of Engineers and Architects <sup>(4)</sup>	6/30/21	307
Association of Legal Professionals	6/30/21	41
International Brotherhood of Electrical Workers	6/30/21	80
City Association of Management Personnel	6/30/21	454
Municipal Employees Federation <sup>(5)</sup>	6/30/21	2,426
Assoc. of Building, Mechanical and Electrical Inspectors	6/30/23	87
International Association of Firefighters, Local 230	6/30/23	703
<b>Total</b>		<b>6,087</b>

<sup>(1)</sup> Full-time Equivalents ("FTE's") are the combined total number of budgeted full-time positions. For example, one full-time position equals one FTE. Similarly, two half-time positions equal one FTE. The FTE numbers are based upon the 2018-2019 Adopted Operating Budget, and have been rounded to the nearest FTE.

<sup>(2)</sup> The total number of employees does not include 326 unrepresented positions budgeted in 2018-2019.

<sup>(3)</sup> If and when the Park Rangers become a new bargaining unit, there will be 18 full-time equivalent positions represented by that bargaining unit. The bargaining unit will be comprised of the classifications of full-time Senior Park Ranger and full-time Park Ranger.

<sup>(4)</sup> The City has two separate agreements with AEA; the first agreement is related to employees of Unit 41 and Unit 42 and the second agreement is related to employees in Unit 43. Both agreements expire on June 30, 2021.

<sup>(5)</sup> Effective October 7, 2018, the Confidential Employees' Organization ("CEO") was merged with the Municipal Employees' Federation ("MEF"). All classifications and employees represented by CEO were reassigned to MEF and are entitled to the benefits per the MEF Memorandum of Agreement.

*Source: City of San José, Office of Employee Relations, City Manager's Budget Office.*

### State Law Requirements Related to Labor Negotiations

Under California law, sworn police and fire employees are not permitted to strike. The City Charter provides that police and fire bargaining units have the right to binding interest arbitration of labor disputes once either the City or the applicable bargaining unit declares that the negotiations are at impasse. A summary of the City Charter's binding interest arbitration provisions is set forth below in "– City Charter Binding Interest Arbitration Provisions." The agreements with the Association of Building, Mechanical and Electrical Inspectors ("ABMEI"),



Association of Engineers and Architects (“**AEA**”), International Brotherhood of Electrical Workers (“**IBEW**”), Municipal Employees’ Federation (“**MEF**”), the Association of Maintenance Supervisory Personnel (“**AMSP**”), the City Association of Management Personnel (“**CAMP**”), and Operating Engineers, Local #3 (“**OE#3**”) include “no strike” clauses during the terms of their respective agreements.

Also under California law (the Meyers-Milias-Brown Act), the City and the bargaining units have the mutual obligation to meet and confer promptly upon request by either party and to endeavor to reach agreement on matters within the scope of representation, which generally include wages, hours, benefits and other terms and conditions of employment. Some bargaining units have limitations in their contracts on whether or not they are required to meet and confer on certain items during the term of a contract. In the event that the City and a bargaining unit are unable to reach an agreement, the parties are required to follow the impasse procedures set forth in the City’s resolution governing employer-employee relations which specifies mediation of the dispute. The non-public safety bargaining units do not have the right to binding interest arbitration of disputes. Prior to January 2012, if mediation with a non-public safety bargaining group did not result in an agreement, the City Council could choose to implement the City’s last, best and final offer. Implementation of any such terms, however, does not result in a bargaining agreement.

Effective January 2012, State law was amended to provide for an additional step before the City Council may impose a last, best and final offer. State law currently requires a non-binding fact-finding process upon election by a bargaining unit. A three-person fact-finding panel, comprised of representatives selected by the employer, bargaining unit and a chairperson selected by the Public Employee Relations Board or by mutual agreement of the parties, is charged with making written findings of fact and advisory recommendations covering unresolved issues during negotiations. The panel is empowered to conduct investigations, hold hearings and issue subpoenas requiring the attendance and testimony of witnesses and the production of evidence. In arriving at their findings and recommendations, the panel is required to consider and apply numerous factors, including without limitation: (a) state and federal laws applicable to the employer; (b) local rules, regulations and ordinances; (c) stipulations of the parties; (d) the interests and welfare of the public; (e) the financial ability of the public agency; (f) wages, hours and conditions of employment of employees performing similar services for comparable public agencies; (g) the consumer price index for goods and services; and (h) the overall compensation presently received by employees. After applicable mediation and fact finding procedures have been exhausted, but no earlier than 10 days after the issuance of the panel’s written findings and recommendations, a public agency may implement its last, best and final offer. Prior to doing so, the City must hold a public hearing regarding the impasse. It is expected that the fact finding process could significantly lengthen the negotiation process.

### **Negotiations Related to Successor Bargaining Unit Agreements**

The City anticipates that it will be in negotiations with two bargaining units for successor agreements related to wages and other terms and conditions of employment, including but not limited to, wage increases and operational issues. Specifically, the City will be in negotiations with OE#3 as its agreement expires on September 30, 2019, and with the San José Police Officers’ Association, as its agreement expires on June 30, 2020. In addition, it is anticipated that negotiations will begin with a potentially new bargaining unit representing the City’s Park Rangers in the event that the Park Rangers submit an updated Petition for Recognition in compliance with the City’s Employer-Employee Resolution No. 39367 to recognize the full-time



Senior Park Ranger and full-time Park Ranger classifications as a separate bargaining unit, and the City issues a decision to recognize the new bargaining unit. .

The City cannot predict the outcome of the negotiations with any of its bargaining units.

### **City Charter Binding Interest Arbitration Provisions**

In November 2010, the voters approved a Charter amendment to revise the Charter's binding interest arbitration provisions for the City's public safety bargaining units to, among other things, change the selection process for the neutral arbitrator member of the Arbitration Board (as defined below) and the factors to be weighed by the Arbitration Board in making its award, and to place limits on the Arbitration Board's authority. The Charter's provisions governing arbitration, as amended, are described below.

These provisions have been utilized on two occasions since they were enacted. In 2013, the City and the San José Police Officers Association (the "**POA**") reached an impasse during the negotiations for a successor memorandum of agreement ("**MOA**"). An arbitration hearing was held regarding certain terms of the MOA under dispute in May 2013. In July 2013, the Arbitration Board issued its decision on those terms within the limitations of Charter Section 1111. In 2014, the City and the International Association of Firefighters, Local 230 ("**IAFF, Local 230**") held an arbitration hearing related to implementation of a new tier of retirement benefits for new Fire employees hired or rehired by the City after the effective date of the implementing ordinance. At the conclusion of the hearing, the Arbitration Board adopted the City's proposal for a new tier of pension retirement benefits for Fire employees. The reduced retirement benefits awarded through these arbitration proceedings have been superseded by the retirement benefits that were implemented through the voters' approval of Measure F in November, 2018. See APPENDIX B – "THE CITY OF SAN JOSE: RETIREMENT PLANS." In addition, in 2013, prior to the commencement of the arbitration for a tier two retirement plan for police officers, the POA and the City reached an agreement on new retirement benefits for new Police employees that was subsequently approved by the Arbitration Board as a stipulated arbitration award

Under the City's Charter, the City and the bargaining unit each select one arbitrator and jointly select a third neutral arbitrator. The neutral arbitrator serves as the Chair of the three-person arbitration board ("**Arbitration Board**"). If the City and the bargaining unit cannot reach agreement on the selection of the neutral arbitrator, then either party may request the Superior Court to appoint the third arbitrator who shall be a retired judge of the Superior Court.

At the conclusion of the arbitration hearings, the Arbitration Board shall direct each of the parties to submit, within such time limit as the Board may establish, a last offer of settlement on each of the issues in dispute. The Arbitration Board shall decide each issue by majority vote by selecting whichever last offer of settlement on that issue it finds by the preponderance of the evidence submitted to the Arbitration Board is consistent with the City Charter, satisfies the factors below, is in the best interest and promotes the welfare of the public, and most nearly conforms with those factors traditionally taken into consideration in the determination of wages, hours, and other terms and conditions of public and private employment, including, but not limited to, changes in the average consumer price index for goods and services, the wages, hours, and other terms and conditions of employment of other employees performing similar services.



The primary factors in decisions regarding compensation shall be the City's financial condition and, in addition, its ability to pay for employee compensation from on-going revenues without reducing City services. No arbitration award may be issued unless a majority of the Arbitration Board determines, based upon a fair and thorough review of the City's financial condition and a cost analysis of the parties' last offers, that the City can meet the cost of the award from on-going revenues without reducing City services. The arbitrators shall also consider and give substantial weight to the rate of increase or decrease of compensation approved by the City Council for other bargaining units.

Additionally, the Arbitration Board cannot issue an award that would (1) increase the projected cost of compensation at a rate that exceeds the rate of increase in revenues from the sales tax, property tax, utility tax and telephone tax averaged over the prior five fiscal years; (2) retroactively increase or decrease compensation, excluding base wages; (3) create a new or additional unfunded liability for which the City would be obligated to pay; or (4) deprive or interfere with the discretion of the Police or Fire Chiefs to make managerial, operational or staffing decisions, rules, order and policies in the interest of the effective and efficient provision of police and fire services to the public.

## **SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND COURT DECREES**

### **Significant Litigation**

The City is involved in a variety of pending actions and there are also a number of claims filed against the City. The specific pending cases, described below, are the most significant in terms of potential risk of loss, using a threshold of \$10 million.

***Great Oaks Water Company Litigation.*** Great Oaks Water Company, a private water company in the City, sued both the City and the Former Agency claiming that they illegally used their respective authority to deny permits, licenses and other authorizations to the water company and its potential customers, in an effort to cause property owners and developers to use the City's Municipal Water System instead of the private water company in two areas of the City. The water company alleged that the City and/or the Former Agency inversely condemned the water company's property, interfered with its contracts and business opportunities, and violated various provisions of the State Water Code. In 2008, the water company agreed to dismiss its case without prejudice and entered into an agreement with the City tolling the statute of limitations while the parties attempted to settle the matter. The agreement was extended annually from 2008 through December 31, 2018. The agreement has expired and it is unclear whether the water company intends to re-file the lawsuit. Discovery concerning the water company's alleged damages was not completed before the case was dismissed. If the effort to reach a settlement fails, and the water company re-files its case and ultimately prevails, the City is unable to predict the nature or amount of the damages that can be proven.

***Tributary Agencies' Litigation.*** As previously described, pursuant to the 1959 Agreement, the City is co-owner and administering agency of the Plant. The Plant also provides wastewater treatment services to other neighboring agencies through five outside user agreements ("**Master Agreements**") with City of Milpitas, West Valley Sanitation District, Cupertino Sanitary District, Burbank Sanitary District, and CSD 2-3 (the "**Tributary Agencies**"). Contributions from the City of Santa Clara and the Tributary Agencies are made pursuant to



agreements with each agency based on the anticipated operation and maintenance, and capital budget. The Tributary Agencies' proportional contribution for the operation and maintenance cost is based on the amount and characteristics of the sewage discharged into the Plant. Each Tributary Agency's capital contribution is based on each agency's reserved capacity in the Plant. The balance of the Plant budget is shared between the cities of San José and Santa Clara based on the respective City's assessed property value relative to the total assessed property value in both jurisdictions.

On January 22, 2016 and September 7, 2016, the City, as the administering agency, received claims from the Tributary Agencies alleging a breach of contract and inequity under the Master Agreements. The administrative claims primarily arise out of disagreements regarding the interpretation of how the capital cost to rehabilitate the Plant as generally described in the Plant Master Plan should be apportioned, and whether the Master Agreements must be amended to require the Tributary Agencies to pay for their respective portions of the capital cost.

The Master Agreements require that any allegation of breach of contract or inequity ("**Claim**") be filed with the legislative bodies of the agencies that committed the alleged breach, and with the Treatment Plant Advisory Committee ("**TPAC**"). TPAC is an advisory body, comprised of representatives of the City, Santa Clara and three of the Tributary Agencies that was established by the Master Agreements to provide policy and budget guidance to the City, as the Plant's administering agency.

The Master Agreements specify the procedures for consideration of the Claims. TPAC is required to conduct a hearing regarding a claim within two months. TPAC is then required to prepare a full report of its findings and recommendations to the San José and Santa Clara City Councils. The report is advisory. If any of the parties to the claim disagree with the report, the legislative bodies of the agencies that are parties to the claim are required to meet jointly within two months of receiving the report. If the joint meeting fails to resolve the claim, the agency alleging the claim can file a lawsuit in court after giving the other party or parties to the claim three months to cure the breach or alleged breach.

TPAC conducted a hearing on March 24, 2016, and issued its report on June 9, 2016 to deny the January 22, 2016 Claim. The Tributary Agencies disagreed with the report, and requested a joint meeting of the legislative agencies of the City, Santa Clara and all the Tributary Agencies. The City, Santa Clara, and the Tributary Agencies agreed to mediate the Claims and potential amendments to the Master Agreements but were unable to reach a resolution. On May 19, 2017, TPAC conducted a hearing on the Tributary Agencies' September 7, 2016 Claim, and issued its report on September 14, 2017 to deny the September 7, 2016 Claim. On June 13, 2017, the City, Santa Clara and the Tributary Agencies agreed to waive the hearings before the joint legislative bodies for both Claims.

The Tributary Agencies filed a complaint against the City and Santa Clara on March 23, 2018, and served both cities on May 18, 2018. The allegations in the complaint are substantially similar to the claims raised and heard through the administrative hearing process. The Tributary Agencies allege the City breached their respective contracts, which set the terms for treating the Agencies' wastewater by, among other allegations, charging them for expenditures they allege the contracts do not authorize and concealing how the funds are used. They also allege the City breached the implied covenant of good faith and fair dealing and violated certain California Constitutional provisions limiting local agencies' imposition of property related fees, charges and taxes. The Tributary Agencies further allege their payments resulted in unjust enrichment to the



City and Santa Clara, and that the court should provide declaratory relief in support of their allegations.

The City and Santa Clara filed a demurrer to the complaint on August 9, 2018, which the court denied and in March 2019 the City and Santa Clara filed and served their answer to the complaint. The City has also filed and served a cross-complaint against each Tributary Agency seeking declaratory relief from the court as to each of the causes of action alleged by the Tributary Agencies in their complaint. Discovery in the case has commenced.

The Tributary Agencies have fully paid their portion of the capital cost for the projects to rehabilitate the Plant to date. The City cannot predict the outcome or the timeline for resolution of this litigation.

### **Potentially Significant Litigation**

In addition to the specific matters described above, there are a number of pending cases or claims that could result in litigation that are anticipated to be scheduled for trial or appellate court hearing during the next twelve to twenty-four months in which the City's potential exposure for damages or attorneys' fees, collectively, could total \$10 million or more. For all of the matters described below, the City is unable to predict their actual outcome or when they will be resolved.

- ***Retirement Benefits Litigation.*** On November 30, 2016, twenty-one individuals who are retired members of Federated Plan and their spouses, a surviving spouse of a Federated Plan retiree and an association representing Federated Plan retired members or to-be-retired Federated Plan members, their qualified spouses, domestic partners, dependents and beneficiaries filed a claim against the City and the Federated Plan Board and have since filed a lawsuit against the City. The lawsuit arises from the limitations on pension payments payable by tax-qualified retirement plans imposed by Internal Revenue Code Section 415 ("**Section 415**"). The lawsuit alleges that the City has failed to provide the plaintiffs with their fully-earned vested retirement pension benefits as a result of the application of Section 415 limitations. The lawsuit further alleges that the City should have established a separate plan as allowed under Section 415 or should have taken other lawful action as appropriate to pay the plaintiffs with the amount of the compensation that would exceed the Section 415 limitations.

Following a motion for judgment on the pleadings brought by the City as to the original complaint, an amended complaint was filed to which the City demurred. The amended complaint contains five causes of action including unconstitutional impairment or breach of contract; impairment by terminating or disregarding the grandfathered status of plaintiffs; equitable estoppel; promissory estoppel; and breach of fiduciary duty. On the City's demurrer, the judge found that the Government Claims statute applies to and bars most of the causes of action against the City except for the claim of unconstitutional impairment or breach of contract. Certain causes of action remain for two plaintiffs who have a "grandfathered" option under an earlier plan, and the City Manager remains a defendant with respect to estoppel and fiduciary duty claims. Discovery is ongoing and the City's outside counsel intends to file a summary judgment motion with respect to the remaining causes of action once discovery has



concluded. At this time, the City is unable to state the potential exposure for damages in this case.

- ***Coyote Creek Flood Litigation.*** The City has received almost 400 claims for property loss and damage, personal injuries, and emotional distress allegedly caused by flooding in some areas of the City following heavy rains in February 2017. Several lawsuits have been filed against the City, the County, Santa Clara Valley Water District, and state agencies on behalf of hundreds of plaintiffs. The allegations against the City primarily relate to a failure to warn of the potential for flooding, but also include a failure to clean and maintain Coyote Creek in a manner that would prevent flooding. The City has immunities to certain liability claims and filed demurrers and motions to strike to plaintiffs' complaints which were heard on May 31, 2019. The court ruled on the demurrer filed by the City and held as a matter of law that the plaintiffs have not stated a claim for failure to warn, for breach of mandatory duty, for negligent infliction of emotional distress and negligence, but have stated a cause of action for inverse condemnation, nuisance and dangerous condition of public property. The court has not ruled on the merits of the last three causes of action only that the plaintiffs have stated a legally sufficient claim. Discovery has not yet begun pending appointment of a special master. A case management conference has been scheduled for July 19, 2019.
- ***Hernandez v. City of San Jose, et al.*** This is a lawsuit against the City in which the plaintiff alleges that she was raped by a then San José police officer after he escorted her from her home to a local hotel in response to a domestic violence situation. Criminal charges were filed against the former officer and therefore, the civil lawsuit against the City and the former officer was stayed. In 2016, a criminal trial against the former officer resulted in a hung jury. The criminal case was retried in April and May 2018 and resulted in a mistrial with the jury deadlocked 9 to 3 in favor of a guilty verdict. The civil case that had been stayed during the pendency of the criminal proceedings proceeded to discovery. There has been an initial mediation in the civil case that did not resolve the case. No further mediation sessions are currently scheduled. The trial court has ordered a settlement conference that is scheduled to occur on July 24, 2019 and the case is set for trial on July 29, 2019.
- ***San José Municipal Water Litigation.*** A class action lawsuit was filed against the City on behalf of current and former customers of the City's water utility known as "San Jose Municipal Water" challenging the fees charged for water service from 1997 to 2016. The plaintiffs claim that the water service fees violate Proposition 218 in that a portion of the fees were transferred from the Water Utility Fund and used for general purposes, rather than for purposes related to the provision of water service. The plaintiffs also challenge the City's prior practice of transferring monies for rate of return and enterprise fund in lieu fees to the General Fund.

The plaintiffs filed a second lawsuit essentially identical to the original lawsuit, regarding alleged overcharges and improper transfers in fiscal year 2015-2016. In both cases, the plaintiffs seek a refund of water fees from 1997 onward in the amount of approximately \$38 million. Both cases were tried before a judge in Fall 2017. The trial court issued the statement of decision and judgment



(collectively, the “**Decision**”) on June 19, 2018 denying the relief sought by the plaintiffs. The court did rule that the City’s tiered water rate structure violated Proposition 218 but it decertified the class and held that plaintiffs were entitled to no relief. The plaintiffs have appealed the Decision and the City has filed a cross-appeal.

In addition to these two lawsuits, the plaintiffs filed a third lawsuit with similar allegations related to the water fees charged in fiscal year 2016- 2017 which the judge stayed during the pendency of the trial. Discovery commenced in September 2018. In this lawsuit, plaintiffs will be challenging the tiered water rate structure and late penalty charges. A case management conference is set for June [14], 2019 at which time it is anticipated that a hearing date will be scheduled for consideration of class certification. SEE “CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS – Articles XIIIC and XIID of the State Constitution” in the forepart of this Official Statement.

- **Employment Litigation.** There is one lawsuit brought against the City by a former employee alleging a wrongful discharge and seeking back pay and attorneys’ fees in which the City has prevailed after several years of litigation. The former employee has filed an appeal.
- **Cardroom Litigation.** A cardroom business has filed lawsuits against the City challenging the constitutionality of the City’s regulatory fees and seeking declaratory and injunctive relief finding the imposition of the regulatory fees to be a special tax and refund of the fees that have been paid. The refund of the regulatory fees paid would be approximately \$1 million for each of the fiscal years 2012 through 2018, with the exception of fiscal year 2013 for which no claim has been made. In addition, the cardroom business is seeking interest at the legal rate and attorneys’ fees.

A bench trial commenced in January 2018. The case was bifurcated with the court first considering the plaintiff’s claims that the cardroom regulatory fee is an illegal tax under the California Constitution before proceeding with the plaintiff’s constitutional claims under 42 U.S.C. Section 1983.

On August 22, 2018, the court issued its Statement of Decision, denying all of plaintiff’s claims and the plaintiff has appealed. See “CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS — Articles XIIIC and XIID of the State Constitution” in the forepart of this Official Statement.

- **FLSA Litigation and Claims.** There are currently nine federal court cases brought by firefighters alleging that the City failed to pay them adequate overtime under the Fair Labor Standards Act (“**FLSA**”). The first of these cases, *Wallace et al v. City of San José*, was conditionally certified as a class action involving approximately 516 firefighters, but subsequently, the federal district court decertified the class leaving three plaintiffs. The City prevailed on a summary judgment motion and judgment was entered in favor of the City. The plaintiffs have filed a notice of appeal in the Ninth Circuit Court of Appeal. Briefing in this case has concluded.



Subsequent to the decertification of the *Wallace* case, eight separate actions involving approximately 350 firefighter plaintiffs were filed against the City, with allegations similar to those made in the *Wallace* case. The City has filed motions to dismiss in each of these actions. These cases are consolidated before a single district court judge and are stayed pending the results of the appeal in the *Wallace* case.

In addition to the FLSA cases described above, there is another action, *Haag, et al., v. City of San José*, filed in federal district court by firefighters that is likely to involve approximately 150 plaintiffs. The allegations in the Haag case are that the City failed to include certain payments in its calculation of regular rate in accordance with the FLSA based on the Ninth Circuit Court of Appeals' decision in *Flores v. City of San Gabriel*. In *Flores*, the Ninth Circuit held that health care in lieu cash payments must be factored into the regular rate of pay for purposes of calculating overtime under the FLSA. The U.S. Supreme Court declined to review this case. Health in lieu payments are cash payments made to employees who provide proof of health coverage from another source, typically through a spouse's coverage. The City began factoring health care in lieu payments in calculating overtime in June 2017. Plaintiffs seek backpay, liquidated damages, and attorneys' fees. The City has paid back pay to the affected employees in the approximate amount of \$168,353 and the plaintiffs have agreed upon settlement terms under which the City would pay an additional amount of \$45,000 for plaintiffs' attorneys' fees to resolve the case. The parties will need to obtain the court's approval of the proposed settlement and anticipate that the request for approval will be heard by the court in July 2019.

There are also potential claims against the City by employees involving alleged violations of the calculation of overtime under the FLSA. The City is meeting with the bargaining units that represent the affected employees to resolve these potential claims. At this time, the City is unable to state the potential exposure for these claims.

- **Curb Ramp Claim.** The City and a civil rights organization have entered into a tolling agreement related to alleged violations of the federal American Disabilities Act (“**ADA**”) and other access statutes involving the City's sidewalk curb ramps. The tolling agreement does not have a specified expiration date, and instead is subject to termination upon 30 days written notice by either party. Currently, the City and the civil rights organization are in settlement discussions that could result in a consent decree under which the City would agree to install ADA compliant curb ramps to replace all non-ADA compliant curb ramps throughout the City. The estimated number of curb ramps subject to retrofit is approximately 28,000. The funding for the retrofit work is anticipated to be limited to general obligation bonds authorized under Measure T, State gas tax funds and VTA sales tax funds and would not include funding from the City's General Fund. The resolution of this matter is also anticipated to require the City's payment of the civil rights organization's attorneys' fees and a service award. The City is unable to predict if or when the settlement discussions will result in a consent decree on the terms described above or the amount of attorneys' fees and service award payable to the civil rights organization.



- ***Police civil rights cases.*** The City is defending several cases involving claims of police excessive force, wrongful arrest and/or other civil rights and state law violations. The cases are in various civil procedure stages with one case set for trial in June 2019 and others with trial dates in the next couple of years or in discovery and subject to motion practice. At this time, there is one excessive force case that involves a significant bodily injury (paraplegia) and others that involve wrongful death claims. The serious injury case poses potentially significant damages exposure if liability is assessed against the involved officers and/or the City. The other cases, collectively, pose significant damages exposure if the City and/or officers are found liable in those actions. Additionally, the City has exposure to the payment of the plaintiffs' attorneys fees and costs in each of these cases in the event the plaintiffs were to prevail.
- ***Constitutional and Preemption challenges.*** The City is currently defending several lawsuits in which the City has a potential exposure to the payment of the attorneys' fee and costs of the plaintiff or petitioner if the City does not prevail. These include a lawsuit challenging the City's sign ordinance and multiple lawsuits challenging City's rental property ordinances on various Constitutional grounds, and a lawsuit alleging that the City's policy governing disposition of surplus City property is preempted under State statute. Currently, these cases are at various stages. The lawsuit involving the City's sign ordinance is in federal district court with no decision rendered. The lawsuit challenging the 'City's surplus property policy is on appeal in the California Court of Appeal, Sixth Appellate District with the City prevailing in the trial court. Two of the lawsuits concerning the City's rental property ordinances are stayed in federal district court while a third lawsuit also involving the City's rental property ordinances, in which the City prevailed, is on appeal in the Ninth Circuit Court of Appeal. Collectively, the City's exposure to attorneys' fees and costs could be significant should the City ultimately not prevail in the various cases.
- ***Claims for Additional Attorneys' Fees Related to Measure B.*** In 2015 and 2016, the City and its bargaining units resolved litigation concerning Measure B by entering into settlement agreements referred to as settlement frameworks. For a more detailed discussion of the terms of these settlement frameworks, see APPENDIX B – "THE CITY OF SAN JOSE: RETIREMENT PLANS – RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS – Measure B – Settlements – *Settlement Frameworks.*" Under the Settlement Frameworks, the City agreed to pay the litigants attorneys' fees: \$1,500,000 to POA and IAFF, Local 230, and \$1,257,000 for the non-sworn litigants. The City has made these payments. Further, the City agreed to binding arbitration to resolve any additional claims for attorneys' fees of the POA and IAFF, OE#3 and the bargaining units represented by the International Federation of Professional and Technical Engineers, Local 21 ("**IFPTE, Local 21**") (the Association of Engineers and Architects, the Association of Maintenance Supervisory Personnel and the City Association of Management Personnel) related to the Measure B litigation and administrative proceedings. The bargaining unit represented by the Municipal Employees Federation does not have this right under the settlement framework with the non-sworn litigants. Counsel for the POA has demanded binding arbitration pursuant to the terms of the settlement framework entered into with the POA and IAFF, Local 230 and seeks additional attorneys' fees in the amount of \$1,050,000. In addition, the City has been advised by counsel for



IAFF, Local 230, OE #3, and IFPTE, Local 21 that he intends to formally demand binding arbitration on behalf of those bargaining units as well. The City cannot predict the outcome of the arbitration proceedings and the amount of attorneys' fees, if any, that an arbitrator may award.

- ***Dangerous condition of public property cases.*** The City is defending several cases in which serious bodily injuries are claimed as a result of alleged defective conditions in public roadways. Collectively, should the City be found liable for dangerous condition of public property, the exposure for personal injury damages, including future medical expenses and wage loss, as well as pain and suffering, could be significant.

### **Other Significant Proceedings**

***Overpayment of Pensions.*** Overpayment of pensions has been a matter considered by the Boards of both the Police and Fire Department Retirement Plan (the "**Police and Fire Plan**") and the Federated City Employees Retirement System (the "**Federated Plan**"). For the Police and Fire Plan, the overpayments involved non-pensionable FLSA pay issues related to the incorrect inclusion of non-pensionable earnings as pensionable for Fire members from 1998 to 2008 due to the City's payroll system programming; and non-FLSA pay issues such as Holiday-in-Lieu corrections, Higher Class Pay being erroneously counted as pensionable pay, disability pays which should have been pensionable, and lump sum retroactive pay not being spread to the correct pay periods.

With regard to the FLSA issues, the Police and Fire Board approved correcting the ongoing benefit payments in the February 2017 benefit payment. In June 2017, the Police and Fire Board approved the process to collect past over-payments to begin with the August 2017 benefit payments. In September 2017, the Police and Fire Board voted to send the City a letter seeking the balance of the monies owed but not recovered from the retirees for overpayments related to the FLSA. In November 2017, the Police and Fire Board voted to send a single letter to the City seeking the balance of monies owed but not recovered from the retirees arising from the FLSA issue and the other issues. In a letter sent to the City Manager, dated November 30, 2017, the Office of Retirement Services demanded that the City make payment to the Police and Fire Plan prior to December 31, 2017 in the amount of \$2,215,000 (including interest calculated at the rate of 7% per annum through December 31, 2017) for the overpayments related to the FLSA issue (\$1,214,000) and the other pensionable pay issues (\$1,000,000). This matter has not been resolved.

With respect to the Federated Plan, there have been pensionable pay corrections involving members of Federated Plan Tier 1 plan. According to a Memorandum dated August 8, 2018 to the Federated Plan Board, there has been overpayment of retirement benefits paid to certain retirees, due to errors in the City's reporting of pensionable pay that was then used in the members' benefit calculation. The total number of overpaid beneficiaries and members is 351.

At the August 16, 2018 Federated Plan Board meeting, the Board members voted, to the extent possible, to stop the overpayments made to members immediately and also voted to not seek repayment from the impacted retirees, but to instead have the overpayment added to the unfunded liability of Federated Plan Tier 1 plan, which is repaid from the City's contributions. Office of Retirement Services staff projected that overpayment amount would total



approximately \$1,783,000 as of August 31, 2018. See APPENDIX B – “THE CITY OF SAN JOSE: RETIREMENT PLANS.”

**FAA Audit of Use of Revenues.** Federal law requires all airport owners that receive federal assistance, such as the City, to use airport revenues for the capital or operating costs of the Airport. As a general rule, any use of airport revenues by an airport owner for costs that cannot properly be considered airport capital or operating costs is deemed to be improper revenue diversion. On June 2, 2010, auditors from the Federal Aviation Administration (the “FAA”) provided the City with a draft of its audit findings alleging improper use of Airport revenues by the City in three areas of expenditure. On August 14, 2015, as the result of discussions and correspondence with City staff, the FAA notified the City that it has closed two of the three audit issues. The remaining audit issue is described below.

**Cost Allocations.** The City uses both direct and indirect methodologies to allocate costs to the Airport. The FAA auditors found the direct cost allocations to be acceptable. The FAA contends that the City’s indirect methodology does not correlate to the cost of services actually provided by the City to the Airport. Consequently, the auditors have recommended that the City re-allocate its costs charged to the Airport for fiscal years 2005 through 2010 using an allocation methodology that reflects services actually provided to the Airport and repay any overcharges to the Airport, with interest. The City believes the allocation methodology used to allocate costs to the Airport is in compliance with federal cost allocation guidance. In an effort to resolve the issue, the City proposed and implemented a cap on the indirect cost allocations for certain City departments at 10%, which was the approximate rate charged to the Airport in pre-capital intensive years. This resulted in a total credit of \$5,600,000 that would be applied equally to the Airport cost allocation plan over a seven year period beginning in FY 2013 and ending in FY 2019. The City also has adjusted its indirect cost allocation methodology in an effort to address FAA concerns, including removal of debt expenditures from the relative expenditures base started in FY 2016, continuing with the 10% cap, and monitoring a rolling five-year average of the relative expenditure base to smooth out expenditure fluctuations.

On August 14, 2015, the FAA accepted the corrective actions that the City has already taken, however, the FAA, disagrees with the City’s inclusion of capital expenditures in the allocation of indirect costs. The City will continue discussions with the FAA, but cannot predict the final outcome of the audit.

On May 3, 2018, the City received a letter from the FAA in which the FAA requested a copy of the City’s fiscal year 2016-2017 indirect cost allocation plan to substantiate indirect charges to the Airport in order to finalize the FAA’s financial compliance review. The City responded to the FAA on July 20, 2018 with copies of the requested information and clarified actions taken by the City to date to implement the FAA’s recommendations. The FAA has not responded to the City’s July 2018 correspondence and the audit remains pending. The City cannot predict the final outcome of the audit.

**Potential Claim from FAA Regarding Reuse of Guadalupe Gardens.** In early 2002, the City Council approved a Master Plan for Guadalupe Gardens, consisting of approximately 120 acres of mostly vacant, City-owned property located south of the Airport, much of which falls within an FAA-established safety zone. The City acquired the Guadalupe Gardens properties using FAA grants for airport approach protection and noise compatibility, and the FAA grant agreements consequently required FAA approval of any planned City-use of the properties acquired with grant proceeds. By letter dated August 9, 2002, addressed to the City’s Director of Aviation, the FAA San Francisco Airport District Office (“ADO”) approved the City’s



Master Plan for reuse of Guadalupe Gardens for runway and approach protection, and the City finalized the Master Plan in reliance upon the FAA approval.

During discussions regarding proposals to develop certain portions of the Guadalupe Gardens, the FAA has taken the position that the City must dispose of any portion of the Guadalupe Gardens that is no longer needed for noise compatibility purposes. Citing provisions of federal law that require recipients of FAA grants for acquisition of land for noise compatibility purposes to dispose of any such acquired land when no longer needed by the airport owner for noise compatibility purposes, the FAA contends that the FAA ADO erred in its 2002 approval of the Guadalupe Gardens Master Plan and that the City is obligated to prepare an inventory of the Guadalupe Gardens to identify those parcels that were acquired by the City with noise compatibility grant proceeds. This inventory would then be used to prepare for FAA review and approval of a disposition plan for those parcels no longer needed by the City for noise compatibility. Proceeds of the sale of the parcels proportionate to the FAA grant share of the original purchase price would be required to be used for other approved noise compatibility projects at the Airport or returned to the FAA.

The City believes that it has viable defenses to any potential claim by the FAA with regard to Guadalupe Gardens. The FAA ADO's 2002 approval of the Guadalupe Gardens Master Plan constituted an official FAA approval of the City's reuse of the parcels acquired with proceeds from FAA noise compatibility grants, and the approval expressly provides that the entire Guadalupe Gardens is necessary for the continuing aeronautical purpose of runway and approach protection. Having received official FAA approval of its reuse of the parcels, the City believes it is under no obligation to take any further action to secure further FAA approval of its continuing use of the Guadalupe Gardens. However, the City cannot predict the final outcome of any such potential claim by the FAA.

***San José Clean Energy – CPUC Citation.*** The California Public Utilities Commission (“CPUC”) adopted a Resource Adequacy (“RA”) policy framework in 2004 in an effort to ensure the reliability of electric service in the State. In particular, the RA policy framework is designed to ensure that CPUC jurisdictional Load Serving Entities, such as SJCE, have sufficient capacity to meet their peak load with a 15% reserve margin.

In February 2019, the City received a notice of citation (the “**CPUC Citation**”) from the CPUC relating to the RA Reporting Requirements for 2019 (the “**2019 RA Requirements**”). The CPUC Citation assessed the City a penalty of approximately \$6.8 million (the “**CPUC Penalty**”) for failing to procure RA in amounts sufficient to satisfy the 2019 RA Requirements. On March 29, 2019, the City filed a notice of appeal with the CPUC to challenge the CPUC Citation on the basis that the penalty was excessive and unconstitutional because the City, among other things, undertook all reasonable steps to comply with the 2019 RA Requirements, but was unable to procure sufficient RA despite its diligence. The appeal is still pending, and the City is unable to predict the final resolution of the CPUC Citation.

SJCE budgeted approximately \$37.2 million to comply with its 2019 RA Requirements. SJCE was able to execute contracts for the purchase of RA totaling approximately \$32 million. Therefore, SJCE budgeted approximately \$5 million more than it spent for compliance with its 2019 RA Requirements. As a result, in the event the City's appeal of the CPUC Penalty is unsuccessful, SJCE's actual costs of purchasing power in 2019 are anticipated to be approximately \$1.7 million higher than budgeted.



## Consent Decrees

**Overview.** San Francisco Baykeeper (“**Baykeeper**”) filed a lawsuit in federal district court against the City in February 2015, and served its complaint on the City in April 2015. Baykeeper’s complaint alleged violations of the federal Clean Water Act. Specifically, the complaint alleged that the City was not in compliance with trash reduction requirements under its Municipal Separate Storm Sewer System (the “**MS4**”) Stormwater Permit (the “**Stormwater Permit**”) issued by the San Francisco Bay Regional Water Quality Control Board (“Regional Water Board”), and that there were discharge violations of sewage from the City’s Sanitary Sewer System that infiltrated into the MS4.

In order to settle the lawsuit, the City and Baykeeper agreed to a consent decree that was approved by the U.S. District Court in August 2016 (the “**Consent Decree**”). The Consent Decree has a 10 year term expiring in August 2026 and will require the City to:

- Comply with trash provisions of the current Stormwater Permit including installing full trash capture devices, supporting additional creek cleanup efforts, and monitoring of trash in receiving waters;
- Rehabilitate, replace, or repair 65 miles of high risk sanitary sewer system pipes at an average of 6.5 miles per year, based on the City’s existing program with some changes in the priority of segments of this work;
- Monitor and report fecal indicator bacteria (“**FIB**”) in receiving waters for a five-year period;
- Comply with green infrastructure planning as required in the Stormwater Permit, adding FIB as a pollutant for planning purposes;
- Bring forward new revenue measure options for Council consideration by December 31, 2017;
- Appropriate, contingent upon the receipt of sufficient new revenues, \$100,000,000 over a ten-year period for various green infrastructure projects with the goal of reducing pollutants and/or flows from the City’s urban areas into receiving waters, with expenditures anticipated to occur as follows:
  - Identify and design \$25,000,000 in total projects by September 2024;
  - Award \$25,000,000 in total projects by September 2025;
  - Identify and design an additional \$10,000,000 (\$35,000,000 in the aggregate) in total projects by September 2025;
  - Award an additional \$10,000,000 (\$35,000,000 in the aggregate) in total projects by the termination date of the consent decree;
  - Identify and design an additional \$15,000,000 (\$50,000,000 aggregate) in total projects by the termination date of the consent decree.

In the event that the City does not identify sufficient revenues by December 31, 2020 to make the appropriations identified above and meet the FIB Load Reduction Standard, then Baykeeper may terminate the Consent Decree and resume litigation against the City. The Consent Decree also provides for ongoing oversight by Baykeeper and a dispute resolution



process. The Consent Decree specifies limits on Baykeeper's ability to pursue additional litigation against the City during the Consent Decree's term and litigation fees that can be claimed by Baykeeper for dispute resolution are capped at \$200,000.

In addition to the expenditures outlined above, the City has incurred or will incur the following expenditures during the Consent Decree's term: (1) lump sum payment of attorney's fees and costs to Baykeeper in the amount of \$425,000, which payment has been made; (2) ongoing oversight costs payable to Baykeeper in the amount of \$10,000 per year for a total of \$100,000; and (3) \$200,000 per year for five years (a total of \$1,000,000) for supplemental environmental mitigation to be administered by the San José Parks Foundation for trash clean up grants, habitat restoration, or projects that generally improve the water quality in the Guadalupe and Coyote creeks and associated watershed areas.

The City and Baykeeper have entered into two amendments to the Consent Decree. In May 2017, Baykeeper and the City entered into a First Amendment to the Consent Decree that was subsequently approved by the U.S. District Court in August 2017 ("**First Amendment**"). The First Amendment modified the City's maintenance obligations related to trash capture devices, extended the deadline for one of the City's obligations under the Consent Decree related to contracting with a consultant and specified that the City will make payments of the annual funding of \$200,000 during years two through five for the supplemental mitigation projects directly to two organizations instead of to the San José Parks Foundation. In April 2019, the City and Baykeeper entered into the Second Amendment to the Consent Decree ("**Second Amendment**"), in order to make technical changes to the specifications related to FIB and the timing of City's annual monitoring payment to Baykeeper. The Second Amendment was approved by the U.S. District Court judge on April 30, 2019.

**Identification of Funds.** On December 19, 2017, the City Council considered a report from City staff concerning potential new revenue sources to fund the green infrastructure requirements specified in the Baykeeper Consent Decree described above. The potential revenues sources identified by City staff include general obligation bonds and a parcel tax, both of which would require voter approval by a two-thirds margin.

On August 10, 2018, the City Council approved placement of a measure on the November 2018 ballot, designated as Measure T, seeking voter authorization of up to \$650 million of general obligation bonds for various public improvements, including those that would prevent flooding and water contamination. The voters approved Measure T by more than the required two-thirds margin in November 2018. Some of the green infrastructure improvements required by the Baykeeper Consent Decree are eligible for funding under Measure T. However, there are a number of different types of improvements that are eligible for funding under Measure T, including an allocation of at least \$300 million for street improvements. The City Council approved \$25 million of the potential Measure T funds to be allocated for clean water projects, including green infrastructure improvements. The City is unable to predict the amount of funding that will be appropriated to the green infrastructure improvements required by the Baykeeper Consent Decree under Measure T. In any event, there are obligations under the Baykeeper Consent Decree that would be ineligible for funding from general obligation bond proceeds and staff continues to assess additional funding mechanisms to fund its obligations under the Consent Decree.



**Status of Green Infrastructure Projects.** The City prepared a draft Green Infrastructure Plan (“**GIP**”) outlining green infrastructure projects, including regional and green street projects, to meet the obligations under the Consent Decree as well as the City’s Stormwater Permit. The draft GIP, which has not been submitted to the City Council for approval, forecasts projects and goals through 2050. Potential projects identified in the GIP require further review and approval. The draft GIP contains a \$1.491 billion estimate for illustrative purposes to demonstrate the proportional costs among project types. Total cost of the implementation of the GIP through 2050 is difficult to estimate, and will be dependent upon several factors including, among others, future costs of construction, whether the project will be on City-owned property or required as part of a future private development.

Per the terms of the Consent Decree, the City provided Baykeeper with the draft GIP for review and comment and received Baykeeper’s comments on June 10, 2019. The City has the obligation under the Consent to consider Baykeeper’s comments in good faith and either incorporate Baykeeper’s comments into the GIP or explain to Baykeeper in writing why its comments were not accepted by July 10, 2019. The City is in the process of reviewing Baykeeper’s comments and expects to respond to Baykeeper by July 10, 2019.

Some components of the GIP are required by the City’s current Stormwater Permit, so City staff anticipates that the draft GIP in some form will ultimately be approved by the City Council. However, the City is unable to predict which projects will ultimately be approved or whether funding for the GIP will be available.

## **Affirmative Litigation**

**Monsanto Litigation.** As discussed above in Consent Decrees, the City operates a MS4 which collects runoff and discharges it into the San Francisco Bay (“**Bay**”) pursuant to a Stormwater Permit issued by the Regional Water Board. In 2015, the Regional Water Board imposed a stricter limit on the amount of polychlorinated biphenyls (“**PCBs**”) that can be discharged into the Bay through stormwater.

In September 2016, the City sued Monsanto Company, Solutia Inc., and Pharmacia LLC (“**Monsanto**”) in federal court alleging public nuisance arising from Monsanto’s production of PCBs, and claimed that it has and will spend money to reduce the PCB discharge from its municipal stormwater and dry weather runoff systems in order to comply with state and federal regulations. San Jose is seeking monetary tort damages from Monsanto. The cities of Oakland and Berkeley, California subsequently filed similar lawsuits which were joined with the San Jose lawsuit. Other cities in California, Oregon and Washington have filed lawsuits in different federal district courts; but these cases have not been coordinated in one court.

Separately, the City of Alameda filed a test claim in 2010 with the State Commission on Unfunded Mandates (the “**Commission**”), contending that its permit obligations constituted an unfunded state mandate for which the City of Alameda was entitled to reimbursement from the State. The City filed a similar claim. The claims of several cities, including San José, were consolidated in 2016 and are currently pending before the Commission.

While the City’s federal case against Monsanto is currently stayed pending a decision by the Commission, cases against Monsanto in other district courts are proceeding, and decisions made in those courts could have implications for the San José case. At this time, the City is not able to evaluate the total exposure for the containment of PCBs in the storm system nor the potential for recovery from Monsanto or the State.



**[Census Litigation.** In April 2018, the City and Black Alliance for Just Immigration sued the U.S. Commerce Secretary, Wilbur Ross, the U.S. Commerce Department, the Census Bureau, and the Director of the Census Bureau to enjoin the Secretary's decision to include a citizenship question on the 2020 Census. The City's case was joined with a separate case brought by the State of California and other public entities in the U.S. District Court for the Northern District of California. The City alleged that the inclusion of the citizenship question violated the Administrative Procedures Act ("**APA**") and the Enumeration Clause of the U.S. Constitution. The U.S. Census Department staff had concluded that the question would result in a significant undercount of certain residents, primarily immigrants and persons with Hispanic background. The City has large immigrant, and particularly Hispanic, communities and it is expected that the citizenship question will negatively affect the census count of persons residing in the City and in turn federal funding based on population, such as funding through the Workforce Innovation and Opportunity Act and Community Development Block Grants.

A trial was held in the case in January 2019, and in March 2019, Judge Richard Seeborg issued his decision finding that the Secretary had violated the APA and the Enumeration Clause in deciding to include the question, and enjoined the Commerce Department from using the question on the 2020 Census.

Prior to the trial before Judge Seeborg, a U.S. District Court judge in New York ("**New York Census Case**") issued a decision holding that the inclusion of the citizenship question on the 2020 Census violated the APA and ordered the Commerce Department to remove a citizenship question from the 2020 Census. The federal government subsequently filed an appeal directly to the U.S. Supreme Court, which the Court granted. Oral argument in the New York Census Case was heard in April 2019 and a decision is anticipated to be issued before June 30, 2019.

In the event that the U.S. Supreme Court reverses the decision in the New York Census Case and allows the citizenship question to be included in the 2020 Census, the City cannot estimate the potential loss of federal funds.]

## **RETIREMENT PLANS**

For a detailed discussion of the City's Retirement Plans, service retirement formulas, contributions and their calculation, funding status, other post-employment benefits, and other related matters, see APPENDIX B – "THE CITY OF SAN JOSE: RETIREMENT PLANS."

## **INVESTMENT POLICY AND PRACTICES**

The City and its related entities are required to invest all funds under the Director of Finance's control in accordance with principles of sound treasury management and in accordance with the provisions of the California Government Code, the Charter, the City Municipal Code and the City Investment Policy (the "**Investment Policy**").

The Investment Policy was originally adopted by the City Council on April 2, 1985, and is reviewed annually by the City Council. The Investment Policy specifically prohibits trading securities for the sole purpose of speculating or taking an un-hedged position on the future direction of interest rates. Per the Investment Policy, the investments conform to Sections



53600 et seq. of the California Government Code and the applicable limitations contained within the Investment Policy.

On March 19, 2019, the City Council approved various updates to the Investment Policy. All changes are consistent with the California Government Code. The primary objectives of the Investment Policy, in their order of priority, are to (1) provide for the safe preservation of principal, (2) ensure that there is sufficient liquidity for operating needs, and (3) attain the maximum yield possible as long as investment practices are consistent with the first two stated objectives. The City has not entered into any interest rate or commodity swap or hedging agreements and does not currently expect to enter into any such agreements.

## **INVESTMENT PORTFOLIO**

As of March 31, 2019, the book value of the City's pooled investment fund was \$1,704,612,867 while the market value was \$1,701,134,468. The fund is classified by different types of investment securities. The composition of this fund, including the weighted average days to maturity and yield, is provided in the table on the following page. The General Fund portion of the pool was approximately 15.5% as of March 31, 2019.

To prevent potential loss of principal on any of the City's investments, the Investment Policy strictly limits the composition of the holdings within the Investment Portfolio. The Finance Department's investment staff continues to focus investment decisions in accordance with the Investment Policy's primary investment objectives as described above in "INVESTMENT POLICY AND PRACTICES."



**Table 30**  
**City of San José**  
**Pooled Investment Fund – General Pool Investments<sup>(1)</sup>**  
**As of March 31, 2019**

	<b>Book Value</b>	<b>Percent of Portfolio</b>	<b>Market Value</b>	<b>Weighted Average Days to Maturity</b>	<b>Weighted Average Yield</b>
U.S. Treasury Bills and Notes	\$ 92,225,882	5.41%	\$ 91,938,514	595	1.955
Federal Agency Securities <sup>(2)</sup>	566,705,208	33.25	565,116,775	736	2.208
Supranational Securities <sup>(3)</sup>	175,489,602	10.29	174,804,945	747	2.225
Negotiable Certificate of Deposit	140,000,000	8.21	140,141,650	152	2.801
Commercial Paper	19,693,503	1.16	19,745,400	179	2.618
Corporate Notes	421,638,414	24.74	421,679,367	482	2.407
Municipal Bonds	208,484,027	12.23	207,331,586	738	2.073
Money Market Mutual Fund	25,015,742	1.47	25,015,742	1	1.583
State of California Local Agency Investment Fund <sup>(4)</sup>	55,360,489	3.25	55,360,489	1	2.400
Total <sup>(4)</sup> .....	<u>1,704,612,867</u>		<u>1,701,134,468</u>	579	2.281

(1) Excludes funds invested in separate, segregated accounts as part of City held invested funds; excludes bond proceeds held by fiscal agents/trustees.

(2) Composed of securities issued by Federal Home Loan Bank, Federal National Mortgage Association, Federal Home Loan Mortgage Corporation, Federal Farm Credit Bank, and Federal Agricultural Mortgage Corporation.

(3) Composed of securities issued by International Bank for Reconstruction and Development, International Finance Corporation, and Inter-American Development Bank.

(4) Estimated based upon City's participation in the Local Agency Investment Fund ("LAIF"). Weighted average yield for LAIF is based upon the most recently reported quarterly earnings rate.

Source: City of San José, Finance Department.

## DEBT MANAGEMENT POLICY

The City Council adopted a Debt Management Policy for the City on May 21, 2002, and is reviewed periodically by the City Council and was last amended on March 6, 2018. The policy allocates responsibility for debt management activities to the Finance Department, describes the purposes for which debt may be issued, establishes overall parameters for issuing and administering the City's debt, including initial and continuing disclosure as required under the City's undertakings entered into pursuant to Securities and Exchange Commission Rule 15c2-12.



## BONDED AND OTHER INDEBTEDNESS

**General Obligation and General Fund Debt.** The City may issue general obligation bonds for the acquisition and improvement of real property subject to the approval of the voters voting on the bond proposition. The Charter limits bonded indebtedness for General Obligation bonds to 15% of the total assessed valuation of all real and personal property within the City. The total assessed value of taxable property on the City's 2018-2019 tax roll was approximately \$182 billion, which results in a total debt limit of approximately \$27.3 billion.

In accordance with all relevant provisions of law, the City is obligated to levy ad valorem taxes upon all property within the City subject to taxation by the City, without limitation of rate or amount (except with respect to certain personal property that is taxed at limited rates), for the payment of all outstanding general obligation bonds and the interest thereon. Amounts levied for the payment of debt service on the City's outstanding general obligation bonds may not be used except to pay debt service on those bonds. The City is obligated to direct the County of Santa Clara to collect such ad valorem taxes in such amounts and at such times as is necessary to ensure the timely payment of debt service on the general obligation bonds (See "MAJOR GENERAL FUND REVENUE SOURCES – Property Taxes" herein).

Table 31 summarizes the various voter authorizations for general obligation bonds.

<b>Table 31</b> <b>City of San José</b> <b>General Obligation Bonds</b> <b>As of June 30, 2019</b>				
<b>Date of Election</b>	<b>Projects</b>	<b>Amount Authorized</b>	<b>Amount Issued</b>	<b>Amount Authorized but Unissued</b>
11/07/2000	San José Neighborhood Libraries Bonds	\$211,790,000	\$205,885,000	\$ 5,905,000 <sup>(1)</sup>
11/07/2000	San José Neighborhood Parks and Recreation Bonds	228,030,000	228,030,000	--
03/05/2002	San José 911, Fire, Police and Paramedic Neighborhood Security Act	159,000,000	155,675,000	3,325,000 <sup>(1)</sup>
11/06/2018	San José Disaster Preparedness, Public Safety and Infrastructure	650,000,000	--	650,000,000 <sup>(2)</sup>
<b>Total</b>		<b>\$1,248,820,000</b>	<b>\$589,590,000</b>	<b>\$659,230,000</b>

<sup>(1)</sup> The City anticipates issuing a portion of the Series 2019C Bonds pursuant to these voter authorizations. After the issuance of such bonds, no authorized but unissued amounts will remain under these voter authorizations.

<sup>(2)</sup> The City anticipates issuing the Series 2019A-1 Bonds, Taxable Series 2019A-2 Bonds and the Taxable Series 2019B Bonds pursuant to this authorization. After the issuance of such bonds, a principal amount of \$410,100,000\* will remain authorized but unissued pursuant to the authorization under Measure T.

\* Preliminary; subject to change.

Source: City of San José, Finance Department.

The City has the authority to issue a TRAN that is to be repaid within the same fiscal year for cash management purposes without first obtaining voter approval. On July 2, 2018, the City issued the 2018 TRAN in the principal amount of \$150,000,000 to facilitate the prefunding



of employer retirement contributions. Security for repayment of the 2018 TRAN is a pledge of the City's fiscal year 2018-2019 secured property tax and sales tax revenues plus all other legally available General Fund revenues of the City, if required. The 2018 TRAN has a stated maturity of June 28, 2019, and was repaid on April 1, 2019.

The City has authority to enter into long-term lease obligations without first obtaining voter approval. The City has entered into various lease arrangements under which the City must make annual payments to occupy public buildings or use equipment necessary for City operations. Securities have been issued which certificate these lease arrangements. As of June 30, 2018, the City had approximately \$469 million in non-voter approved bonded or certificated lease obligations outstanding.

Table 32 summarizes the bonded and certificated General Fund lease obligations payable out of the revenues and general funds of the City as of June 30, 2019. The City has never failed to pay principal of or interest on any debt or any lease obligation when due.

**Table 32**  
**City of San José**  
**Bonded and Certificated General Fund Lease Obligations**  
**As of June 30, 2019**  
**(In thousands)**

<b>Issuer/Issue</b>	<b>Amount Issued</b>	<b>Issue Date</b>	<b>Purpose</b>	<b>Final Maturity</b>	<b>Amount Outstanding</b>
<b><u>City of San José General Obligation Bonds</u></b>					
Series 2001 (Libraries and Parks)	\$71,000	06/06/2001	Community Facilities	09/01/2031	\$30,745
Series 2002 (Libraries, Parks, Public Safety)	116,090	07/18/2002	Community Facilities	09/01/2032	54,170
Series 2004 (Libraries, Parks, Public Safety)	118,700	07/14/2004	Community Facilities	09/01/2034	63,310
Series 2005 (Libraries and Public Safety)	46,300	06/23/2005	Community Facilities	09/01/2035	26,265
Series 2006 (Libraries and Parks)	105,400	06/29/2006	Community Facilities	09/01/2036	63,270
Series 2007 (Parks and Public Safety)	90,000	06/20/2007	Community Facilities	09/01/2037	57,000
Series 2008 (Libraries and Parks)	33,100	06/25/2008	Community Facilities	09/01/2038	22,050
Series 2009 (Public Safety)	9,000	06/25/2009	Community Facilities	09/01/2039	6,300
	<b>\$589,590</b>				<b>\$323,100</b>
<b><u>City of San José General Fund Debt</u></b>					
Lease-Purchase Agreement (Taxable) ESCO	<b>\$19,286</b>	5/29/2014	Equipment Lease	06/01/2034	<b>\$13,891</b>
<b><u>City of San José Financing Authority-Lease Revenue Bonds:</u></b>					
Series 2003A (Central Service Yard)	\$22,625	09/18/2003	Refunding	10/15/2023	\$7,400
Series 2006A (Civic Center Project)	57,440	06/01/2006	Refunding	06/01/2039	51,670
Series 2007A (Recreational Facilities)	36,555	06/28/2007	Refunding	08/15/2030	18,550
Series 2008E-1 (Taxable) (Ice Centre)	13,015	07/03/2008	Refunding	06/01/2025	6,550
Series 2008E-2 (Taxable) (Ice Centre)	13,010	07/03/2008	Refunding	06/01/2025	6,540
Series 2011A (Convention Center)	30,985	04/12/2011	Convention Center	05/01/2042	28,705
Series 2013A (Civic Center Project)	305,535	05/28/2013	Refunding	06/01/2039	277,975
Series 2013B (Civic Center Garage Project)	30,445	06/19/2013	Refunding	06/01/2039	26,555
	<b>\$509,610</b>				<b>\$423,945</b>
<b><u>City of San José Financing Authority Short-Term Debt:</u></b>					
Lease Revenue Commercial Paper Notes <sup>(2)</sup>	<b>\$125,000</b>	Various	Various	Various	<b>\$78,020</b>
<b>Grand Total</b>	<b>\$1,243,486</b>				<b>\$838,966</b>

<sup>(1)</sup> Amount issued for the Commercial Paper notes represents the authorized amount and Amount Outstanding represents the drawn amount.

Source: City of San José, Finance Department, Debt Management.



**Other Non-General Fund Debt.** In addition, the City has issued bonds or entered into installment purchase contracts secured by and payable out of loans and installment sale contracts, in order to provide conduit financing for multi-family housing. Such bonds, loans and certificates of participation are not secured by any City general funds or revenues. See “Appendix C - Basic Financial Statements of the City of San José for the Fiscal Year ended June 30, 2018, Note III.F” for a description of such debt as of June 30, 2018.

**San José Clean Energy Debt.** With respect to SJCE, in August 2017, the City Council approved the Financing Authority’s issuance of lease revenue commercial paper notes for the purpose of financing start-up costs relating to SJCE, including capitalization and related costs, in the principal amount of \$10 million. Such commercial paper notes are payable from lease payments from the City’s General Fund. SJCE launched services to the City in September 2018 and to City residents and businesses in February 2019, and its operating costs, including repayment of financing costs are anticipated to be borne by SJCE customers/ratepayers; however, ultimately the City’s General Fund is the source of repayment in the event that SJCE revenues are insufficient.

In November 2018, Barclays Bank PLC (“**Barclays**”) and the City entered into a Revolving Credit Agreement, dated as of November 1, 2018 (the “**Revolving Credit Agreement**”). The Revolving Credit Agreement was subsequently amended in May 2019. Under the terms of the Revolving Credit Agreement, as amended, Barclays has committed to issue revolving loans to the City under in an aggregate principal amount not to exceed \$30,000,000 and standby letters of credit for the account of the City in an aggregate principal amount not to exceed \$65,000,000, provided, however, that the aggregate principal amount outstanding under such facilities shall not to exceed \$80,000,000 at any one time. The City’s obligations under the Revolving Credit Agreement are secured solely by a pledge and lien on revenues of SJCE, including revenues deposited in an operating reserve account held by the City pursuant to the Revolving Credit Agreement.



## OVERLAPPING BONDED DEBT

Contained within the City are overlapping local agencies providing public services. These local agencies have outstanding bonds issued in the form of general obligation, lease revenue, and special assessment bonds. A statement of the overlapping debt of the City, prepared by California Municipal Statistics, Inc., as of [June 30, 2019], is shown in Table 33 below. The City makes no representations as to the completeness or accuracy of such statement.

**Table 33**  
**City of San José**  
**Statement of Direct and Overlapping Debt**

	<u>% Applicable</u>	<u>[Debt 3/01/19]</u>
<b><u>Direct and Overlapping Tax and Assessment Debt:</u></b>		
Santa Clara County .....	37.677%	\$356,884,079
Foothill-DeAnza Community College District.....	3.992	24,756,144
Gavilan Joint Community College District .....	5.149	4,568,965
San Jose-Evergreen Community College District.....	85.376	398,420,422
West Valley Community College District.....	31.729	153,984,010
Morgan Hill Unified School District.....	11.933	16,173,988
San Jose Unified School District.....	98.415	491,311,324
Santa Clara Unified School District.....	22.141	147,090,412
Campbell Union High School District.....	59.384	231,208,635
East Side Union High School District.....	96.189	762,340,408
Fremont Union High School District.....	8.820	36,356,930
Los Gatos-Saratoga Joint Union High School District.....	0.886	848,434
Alum Rock Union School District.....	77.230	77,801,502
Berryessa Union School District.....	95.919	78,416,690
Cambrian School District.....	64.304	31,840,090
Campbell Union School District.....	46.639	90,841,223
Cupertino Union School District.....	15.720	40,751,475
Evergreen School District.....	99.403	137,143,524
Franklin-McKinley School District .....	99.466	123,421,309
Los Gatos Union School District.....	1.818	1,472,126
Luther Burbank School District.....	19.790	1,698,396
Moreland School District.....	74.923	77,726,807
Mount Pleasant School District.....	88.104	16,481,784
Oak Grove School District.....	99.914	205,121,003
Orchard School District.....	100.000	37,510,982
Union School District .....	72.469	74,826,524
<b>City of San Jose.....</b>	<b>100.000</b>	<b>323,110,000<sup>(1)</sup></b>
City of San Jose Community Facilities Districts.....	100.000	18,265,000
City of San Jose Special Assessment Bonds.....	100.000	9,135,000
Midpeninsula Regional Open Space District .....	0.012	11,095
Santa Clara Valley Water District Benefit Assessment District.....	37.677	27,718,969
<b>Total Direct and Overlapping Tax and Assessment Debt</b>		<b>\$3,997,237,250</b>

**(continued)**



**Table 33 (Cont'd.)**  
**City of San José**  
**Statement of Direct and Overlapping Debt**

	<b>% Applicable</b>	<b>Debt 3/01/19</b>
<b>Direct and Overlapping General Fund Debt:</b>		
Santa Clara County General Fund Obligations .....	37.677%	\$ 273,417,890
Santa Clara County Pension Obligation Bonds.....	37.677	132,765,791
Santa Clara County Board of Education Certificates of Participation .....	37.677	1,878,198
Foothill-DeAnza Community College District General Fund Obligations .....	3.992	1,105,505
Gavilan Joint Community College District General Fund Obligations .....	5.149	711,618
San Jose-Evergreen Community College District Benefit Obligations.....	85.376	40,510,912
West Valley-Mission Community College District General Fund Obligations .....	31.729	19,735,438
Morgan Hill Unified School District Certificates of Participation .....	11.933	1,611,552
San Jose Unified School District Certificates of Participation .....	98.415	10,633,741
Santa Clara Unified School District Certificates of Participation.....	22.141	3,025,568
East Side Union High School District Post Employment Obligations.....	96.189	27,760,145
Los Gatos-Saratoga Joint Union High School District Certificates of Participation.....	0.886	34,226
Campbell Union High School District General Fund Obligations .....	59.384	5,938,400
Alum Rock Union School District Certificates of Participation .....	77.230	15,801,258
Berryessa Union School District Certificates of Participation .....	95.919	4,191,712
Campbell Union School District General Fund Obligations.....	46.639	1,301,228
Franklin-McKinley School District Certificates of Participation .....	99.466	3,322,164
<b>City of San Jose General Fund Obligations .....</b>	<b>100.000</b>	<b>500,990,000</b>
Midpeninsula Regional Open Space Park District General Fund Obligations .....	0.012	14,094
Santa Clara County Vector Control District Certificates of Participation .....	37.677	930,622
<b>TOTAL GROSS DIRECT AND OVERLAPPING GENERAL FUND DEBT</b>		<b>\$1,045,680,062</b>
Less: Santa Clara County supported obligations		<u>124,814,067</u>
<b>Total Direct and Overlapping General Fund Debt</b>		<b>\$ 920,865,995</b>
 <b>OVERLAPPING TAX INCREMENT DEBT (Successor Agency)</b>	 <b>100.000%</b>	 <b>\$1,567,580,000</b>
Gross Combined Total Debt		\$6,610,497,312 <sup>(2)</sup>
Net Combined Total Debt		\$6,485,683,245
<b>Ratios to 2018-19 Assessed Valuation:</b>		
<b>Direct Debt (\$323,110,000) .....</b>	<b>0.18%</b>	
Total Direct and Overlapping Tax and Assessment Debt .....	2.20%	
<b>Combined Direct Debt (\$824,100,000).....</b>	<b>0.45%</b>	
Gross Combined Total Debt .....	3.63%	
Net Combined Total Debt.....	3.57%	
 <b>Ratios to Redevelopment Valuation (\$30,623,181,537):</b>		
Total Overlapping Tax Increment Debt.....	5.12%	

<sup>(1)</sup> Excludes Bonds to be sold.

<sup>(2)</sup> Excludes tax and revenue anticipation notes, enterprise revenue, mortgage revenue and tax allocation bonds and non-bonded capital lease obligations.

Source: California Municipal Statistics, Inc.



**APPENDIX B**  
**THE CITY OF SAN JOSE**  
**RETIREMENT PLANS**



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## INTRODUCTION TO APPENDIX B

This Appendix B provides investors with information concerning the Retirement Plans (as defined below) for the City of San José (the “**City**”). Investors are advised to read the entire Official Statement, including this Appendix B, to obtain information essential to making an informed investment decision.

The Retirement Plans have required that the following statements in this paragraph be included in this Official Statement: The information contained in this Official Statement concerning the Federated City Employees Retirement System (the “**Federated Plan**”) and Police and Fire Department Retirement Plan (“**Police and Fire Plan**”) and together with the Federated Plan, the “**Retirement Plans**”) is derived in part from, among other sources, public information provided by the Retirement Plans and its independent accountants, actuaries and investment advisors. The Retirement Plans have not reviewed this Official Statement or approved its issuance, and no inference is intended or should be drawn that the Retirement Plans have reviewed or approved the issuance of this Official Statement or the Bonds. The statements made in this Official Statement are solely the responsibility of the City.

When used in this Appendix B and in any continuing disclosure made by the City, the words or phrases “will likely result,” “are expected to,” “will continue,” “is anticipated,” “estimate,” “project,” “forecast,” “expect,” and “intend,” and similar expressions identify “forward looking statements.” Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements. Any forecast is also subject to such risks and uncertainties. Inevitably, some assumptions used to develop the forecasts will not be realized and unanticipated events and circumstances may occur. Therefore, there are likely to be differences between forecasts and actual results, and those differences may be material. This Appendix B speaks only as of its date, and the information and expressions of opinion contained in this Official Statement are subject to change without notice.

This Appendix B summarizes portions of the City’s Basic Financial Statements for the Fiscal Year Ended June 30, 2018 included in the City’s Comprehensive Annual Financial Report (“**City of San José Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2018**”), the most recent Actuarial Valuation Report for the City’s Federated City Employees’ Retirement System (the “**Federated 2018 Pension Plan Actuarial Report**”) for the Fiscal Year ended June 30, 2018, the most recent Actuarial Valuation Report for the City’s Police and Fire Department Retirement Plan (the “**Police and Fire 2018 Pension Plan Actuarial Report**”) for the Fiscal Year ended June 30, 2018, as well as the Federated City Employees’ Retirement System Comprehensive Annual Financial Report (“**Federated 2018 CAFR**”) for the Fiscal Years ended June 30, 2018 and June 30, 2017, and the Police and Fire Department Retirement Plan Comprehensive Annual Financial Report for the Fiscal Years ended June 30, 2018 and June 30, 2017 (“**Police and Fire 2018 CAFR**”). In addition, other documents relevant to the Retirement Plans are referenced or discussed in this Appendix B, including the experience studies and investment policies for both Retirement Plans.

Copies of documents referred to in this Appendix B are available from the Finance Department – Debt Management, City of San José City Hall, 200 East Santa Clara Street, San José, CA 95113; Phone (408) 535-7010; email: [debt.management@sanjoseca.gov](mailto:debt.management@sanjoseca.gov).



The City maintains a number of websites, including a website for both Retirement Plans. However, the information presented on the City's websites is not part of this Official Statement and should not be relied upon in making an investment decision with respect to the Bonds.

## RETIREMENT PLANS IN GENERAL

### Overview

All regular full-time employees of the City and certain part-time employees, with the exception of certain unrepresented employees, participate in one of two Retirement Plans established pursuant to the City Charter: the Federated Plan for non-sworn employees and the Police and Fire Plan for sworn employees. The City does not participate in the Federal Social Security System.

Both Retirement Plans consist of a single-employer tax-qualified defined benefit pension plan and a post employment healthcare plan. The single-employer tax-qualified defined benefit pension plan offered under the Federated Plan and the Police and Fire Pension Plan are referred to in this Appendix B as, the "**Federated Pension Plan**" and the "**Police and Fire Pension Plan**," respectively; and collectively, the "**Pension Plans**." The postemployment healthcare plan offered under the Federated Plan and the Police and Fire Pension Plan are referred to in this Appendix B as the "**Federated Healthcare Plan**" and the "**Police and Fire Healthcare Plan**," respectively; and collectively, the "**Healthcare Plans**."

Each Retirement Plan is administered by its own Board of Administration (each, a "**Board**" and collectively, the "**Boards**"), and day-to-day operations are carried out by the City's Office of Retirement Services staff under the oversight by the Boards.

Both Retirement Plans are structured as tax-qualified defined benefit plans. The Pension Plans offer a monthly pension benefit based on salary and length of service and, depending on the tier, provide either fixed or index-based cost of living increases. The Healthcare Plans consist of accounts established under Section 401(h) of the Internal Revenue Code (the "**Code**") within the respective Pension Plan and Code Section 115 Trusts formed to supplement the Section 401(h) accounts. The Healthcare Plans pay all, or a portion of, health and dental insurance premiums for eligible retirees and their survivors and dependents. Participation by covered employees in the applicable Retirement Plans is mandatory, except for executive management and professional staff hired after February 2013 who can make an irrevocable election into a 401(a) retirement plan in lieu of the defined benefit retirement plans.

To fund such healthcare and retirement benefits, the objective of the Retirement Plans is to meet their respective obligations through investment income and contributions. The City and its employees make regular contributions to the Retirement Plans. Contributions to the Pension Plans are actuarially determined. The Municipal Code specifies the portion of the actuarially determined contribution paid by employees and the remaining portion is paid by the City. Contributions to the Healthcare Plans made by the City are actuarially determined and contributions by employees are made at rates established by the Municipal Code and the Settlement Frameworks (as hereinafter defined). Prior to the change in pension contribution calculations under Governmental Accounting Standards Board ("**GASB**") Statement No. 68, implemented by the City for financial statements beginning in fiscal year 2013-2014, the City generally paid the Annual Required Contribution (as hereinafter defined) for the pension benefit as presented by the actuaries for the Pension Plans. Subsequent to the adoption of the GASB



Statement No. 68, the City has contributed the Actuarially Determined Contribution (as hereinafter defined). For historical City contributions, please see “SUMMARY OF RETIREMENT PLANS – Summary of Retirement Plans Historic and Projected Contributions” and for historical investment returns, please see “PENSION PLANS – Investments” and “HEALTHCARE PLANS – Investments.” The City implemented GASB Statement No. 68 one fiscal year after implementation of GASB Statement No. 67 by the Retirement Plans.

Each Retirement Plan separately retains Cheiron, Inc. as actuary (the “**Plan Actuary**”) to calculate and value current and future benefits, contribution rates, assets, liabilities, and other necessary information. The Plan Actuary provides annual valuation reports for each Retirement Plan and contributes to each Retirement Plan’s Comprehensive Annual Financial Report.

### **Retirement Plans’ Governance**

Each Retirement Plan is governed by its own independent Board. The Retirement Plans are administered as entities separate from the City and for the benefit of the members of the Retirement Plans and their beneficiaries. The City Charter provides that the City Council shall establish by ordinance one or more retirement boards to administer the Retirement Plans in accordance with the fiduciary duties and obligations established by law, the City Charter, and as further prescribed by the San José Municipal Code (the “**Municipal Code**”). Additionally, the City Charter specifies that the term of membership, qualifications of the members and the size of each retirement board shall be prescribed by ordinance and that the members of each retirement board shall be appointed and removed by the City Council in a manner prescribed by ordinance.

The Police and Fire Plan is governed by a nine-member Board of Administration (the “**Police and Fire Board**”) appointed by the City Council. The Police and Fire Board’s membership is composed of: two City employees, one employed in the Police Department and one employed in the Fire Department, each recommended through an election of the employees of the respective departments who are members of the Police and Fire Plan; two retired Police and Fire Plan members, one retired from the Police Department and one retired from the Fire Department; and five public members, who are not connected with the City and have significant knowledge and experience relevant to the administration of a public pension system. The appointment of one of the five public members is subject to interview and the recommendation of the Police and Fire Board.

The appointment of the retired Police and Fire Plan members includes an interview process. If the appointment is to fill the unexpired term of a retired Police and Fire Plan member, then the Association of Retired San José Police Officers and Firefighters makes a recommendation of up to three candidates to be interviewed by the Police and Fire Board, after which the Police and Fire Board recommends one or more candidates for appointment by the City Council. If the appointment is for a complete term, then the retired members of the Police and Fire Plan, through an election of its membership, recommends up to three candidates to be interviewed by a panel comprised of the Police bargaining unit representative, the Fire bargaining unit representative and a representative of the City Manager’s Office. The interview process is for the purpose of ascertaining whether the recommended candidates are viable in that they will be able to attend meetings of the Police and Fire Board and fulfill the time commitment of Police and Fire Board members. Per the Municipal Code, the City Council may reject a recommended City employee Police and Fire Plan member or retired Police and Fire Plan member for cause, including without limitation, the City Council finding that the recommended candidate will not be able to attend meetings of the Police and Fire Board and fulfill the time commitment of a member



of the Police and Fire Board, or to act in accordance with fiduciary duties or carry out the requirements of governing legislation.

The Board of the Federated Plan (the “**Federated Board**,”) consists of seven members appointed by the City Council. The Federated Board’s membership is composed of: two City employees recommended through an election of the members; a retired Federated Plan member; and four public members, who are not connected with the City and have significant knowledge and experience relevant to the administration of a public pension system. The appointment of one of the four public members is subject to the recommendation of the Federated Board.

Appointment of the retired Federated Plan member for a complete term is through nomination by the retired members of the Federated Plan if there are four or more applicants with three nominees forwarded to the interview panel. If there are three or fewer applicants, then all of the applicants are interviewed by an interview panel. The interview panel process is similar to the process established for appointment of retired members to the Police and Fire Board except that the interview panel consists of different bargaining unit representatives, two San José Retired Employees Association (the “**Retirees’ Association**”) members and one City Manager representative.

To fill a vacancy of the Federated retired member seat to complete the remaining portion of the unexpired term, the Retirees’ Association proposes up to three retired Federated Plan members to the Federated Board who will then interview the candidates and make its recommendation to the City Council for appointment to complete the remainder of the unexpired term. Appointment to fill a vacancy of a City employee seat differs depending on whether the appointment is for a full term or to fill an unexpired term. In case of a vacancy of a City employee seat for full term, the employees who are members of the Federated Plan recommend a City employee through an election, for appointment by the City Council. For an appointment to fill the remaining portion of an unexpired term of a City employee seat, the City Council appoints a City employee in accordance with rules prepared by the City Clerk.

As is the case with the appointment of City employee and retired members to the Police and Fire Board, the City Council may only reject the recommended City employee and retiree members for cause as described above with respect to Police and Fire Board appointments.

Members of both Boards serve four-year terms and may only be removed for cause as defined under the Municipal Code. Retired members on both Boards may not serve more than two consecutive terms unless no other retired member is recommended.

Each Board is authorized to perform the functions necessary to carry out the operation of the Retirement Plans, consistent with their fiduciary duties to the respective Retirement Plan. Under the California Constitution and the City’s Municipal Code, Retirement Plan assets may only be used to provide benefits to plan participants and their beneficiaries and defraying reasonable costs of administration. The Boards are empowered to make certain decisions regarding investment of funds, management of assets, disbursement of benefits, hiring of legal counsel and financial advisors. Under the City Charter, each Board is required to adopt a budget approved by the City Council covering the entire aggregate expense of administration of the respective Retirement Plan.

The Office of Retirement Services is administered by its Chief Executive Officer. Both the Chief Executive Officer and Chief Investment Officer for the Retirement Plans are employees of the City who are appointed by and serve at the pleasure of the Boards. The Chief Executive



Officer has appointing authority over the other staff in the Office of Retirement Services. The Charter excludes the Chief Executive Officer, Chief Investment Officer and the other investment professional staff within the Office of Retirement Services from participating in the City's Retirement Plans.

### **Internal Revenue Code Limitations on Pension Payments**

Both Retirement Plans are tax qualified plans and are subject to the Code requirements. The Code places limits on the amount of compensation on which a pension may be calculated (\$280,000 for 2019) for employees who are members of the Retirement Plans. Additionally, the Code caps the annual maximum pension payment that is subject to periodic adjustment based on a consumer price index. For 2019, the maximum annual payment is \$225,000; however, the maximum amount is adjusted downward for non-public safety employees who retire before the age of 62, depending on the employee's age at retirement.

The Office of Retirement Services became aware of pension overpayments to certain retirees in the Federated Plan. The Office of Retirement Services conformed benefit payments to these retirees to the applicable Code limits as of July 1, 2015. The Federated Plan submitted an invoice to the City during fiscal year 2015-2016 for \$882,007, being the total prior pension overpayments plus interest, and subsequently filed a lawsuit against the City for the amounts claimed in the invoice. The City and the Federated Plan entered into a settlement under which the overpayment amount of \$866,000 as of June 2016 will be included as an actuarial loss in the calculation of the plan's unfunded actuarial accrued liability and will be paid by the City through its employer contributions and earnings on contributions over the amortization period set by the Federated Board in the ordinary course of the Board's determination of the City's required employer contribution.

Exceeding the maximum benefit payment limits places a pension plan at risk of receiving unfavorable tax treatment, which in turn, could subject the pension plan's income to the payment of income taxes that would reduce the amount available for retirement benefits. The Federated Plan took steps to voluntarily correct the overpayment errors under Internal Revenue Service ("IRS") guidance and preserve the tax-qualified status of the Federated Plan. However, the City has not independently verified whether the Federated Plan's corrective actions are sufficient under the Code or current IRS guidance.

On November 30, 2016, certain retired members and beneficiaries of the Federated Plan as well as an association representing a group of retired or to be retired Federated Plan members and beneficiaries (the "**Claimants**"), filed a claim against the City relating to limitations imposed by the Code on pension benefits payable by tax-qualified retirement plans. The claim alleges that the City has failed to provide the Claimants with their fully-earned vested retirement pension benefits as a result of the the Code's benefit payment limits ("**Excess Benefits**"). The claim further alleges that the City should have established a separate retirement plan for the Excess Benefits permitted under the Code or taken other lawful action as appropriate to pay the Excess Benefits. The claim sets forth a number of legal theories on which the Claimants base their claim against the City. The City has denied the claim.

Following a motion for judgment on the pleadings brought by the City, the Claimants amended their original claims. The amended complaint contains five causes of action. A judge subsequently found that specific California statutes apply to and bar most of the causes of action against the City except for two. Certain causes of action remain for two plaintiffs who have a "grandfathered" option under an earlier plan, and the City Manager remains a defendant with



respect to estoppel and fiduciary duty claims. The City continues to challenge the claims in court. The City cannot predict the outcome of these matters. For additional information and discussion regarding litigation by the Claimants related to Excess Benefits, please refer to “SIGNIFICANT LITIGATION, CLAIMS AND PROCEEDINGS AND COURT DECREES– Other Significant Proceedings – Overpayment of Pensions” in Appendix A.

### **Audit of Retirement Plans**

On February 14, 2017, the City Council approved the Mayor’s recommendation to direct the City Auditor to conduct an audit of the Retirement Plans with respect to the Retirement Plans’ “administrative expenses and investment performance relative to industry and policy benchmarks within the context of each of the Board’s sound direction to reduce volatility and risk.” The Mayor, in making this recommendation, noted that the Retirement Plans have underperformed their respective investment benchmarks over the past five fiscal years while their staffing and administrative expenses have increased substantially. In October 2017, the City Auditor issued report 17-06, Audit of Retirement Services: Greater Transparency Needed in the Budgeting Process, Interactions Among Stakeholders, Investment Policies, and Plan Administration. The report was published with five separate findings which are covered in 25 different recommendations. Five of the 25 recommendations are addressed to the City either solely or jointly to both the City and the Office of Retirement Services and the remaining 20 recommendations are addressed only to the Office of Retirement Services.

The City Auditor prepares a bi-annual report as of June 30 and December 31 on the implementation of audit recommendations. As of the December 2018 status report, 10 recommendations in report 17-06 were fully implemented. The two recommendations specific to the annual budget for each Retirement Plan are expected to be fully implemented with the City Council’s approval of the Operating Budget for fiscal year 2019-2020. These recommendations encompassed the approval process by the City Council and the respective Retirement Boards and that the budget for both Retirement Plans should cover the proposed personnel budget and staffing plan and the entire aggregate expense of administering each Retirement Plan, including the compensation paid to investment consultants and managers for investment consulting services.

Other recommendations in report 17-06 that have not been fully implemented but are in the process of being implemented include the adoption of a formal set of performance measures to be included in the Retirement Plans’ budgets for Plan administration and the investment programs, website upgrades to promote transparency and ease of navigation for stakeholders and the Plans’ members, and expansion of the Plans’ current newsletter to include more information about the Plans, upcoming events, and information about retirement. In addition to this audit, the City Auditor conducted a pensionable earnings audit in 2017 and found that contributions to the Pension Plans were being calculated correctly. Recommendations were provided to support City pension contribution calculation and processing practices.

### **APPENDIX B DEFINITIONS**

The following terms are used in this Appendix B:

**Actuarial Accrued Liability (“AAL”):** That portion of the present value of future benefits not provided for by future Normal Costs (defined below). The AAL can be thought of as the present value of benefits attributed to employees’ past service. It is used in the actuarial valuation as a



funding target. This measure is not appropriate for assessing the sufficiency of plan assets to settle the plan's benefit obligations on a risk free basis because actual events and plan experience may deviate from the assumptions used in the actuarial liability calculations.

**Actuarial Value of Assets:** The value of cash, investments, and other property belonging to the applicable plan as used by the actuary for the purpose of an actuarial valuation. The purpose of an actuarial value of assets is to smooth out fluctuations in market value of assets to dampen the impact on contributions.

**Actuarially Determined Contribution ("ADC"):** The payment to a pension plan as determined by the actuary using a contribution allocation procedure. It may or may not be the actual amount contributed to a pension plan. A contribution allocation procedure typically uses an actuarial cost method, an asset valuation method, and an amortization method to develop the Actuarially Determined Contribution. Under the contribution allocation procedure employed by the San José retirement plans, there are two components to the contribution: the Normal Cost (including administrative expenses) and an amortization payment on the Unfunded Actuarial Liability (defined below).

**Amortization Payment:** The portion of the pension plan or OPEB (defined below) contribution that is designed to pay interest and principal on the UAL in a given number of years.

**Annual Required Contribution ("ARC"):** Under GASB Statements No. 43 and 45, the employer's annual contribution to an OPEB plan that is calculated in accordance with the parameters established by GASB. Typically, the Annual Required Contribution includes the Normal Cost plus an amortization of the UAL where the amortization schedule is over a period no longer than 30 years. Whether or not the Annual Required Contribution is the amount actually contributed by the employer, it serves as the basis for calculating the annual expense reported in the City's financial statements. Prior to the implementation of GASB Statements No. 67 and 68, the Annual Required Contribution served a similar purpose for pension plans. Because GASB Statements No. 74 and 75 have been implemented, the Annual Required Contribution is no longer applicable to OPEB plans.

**Entry Age Normal Actuarial Cost Method:** A method under which the actuarial present value of the projected benefits of each individual included in an actuarial valuation is allocated as a level percentage of pay from the individual's date of entry into the plan to the individual's assumed cessation of employment.

**Fiduciary Net Position:** The fair or market value of assets in the pension plan trust.

**Funded Ratio:** Either the Market Value of Assets or Actuarial Value of Assets divided by the AAL. This ratio is not appropriate for assessing the sufficiency of plan assets to cover the costs of settling the plan's benefit obligations on a risk free basis because actual events and plan experience may deviate from the assumptions used in the actuarial calculations.

**Market Value of Assets:** The market value of assets is the estimated amount for which an asset should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently, and without compulsion. The market value of assets is adjusted for accruals at the end of each fiscal year and is reported in the Comprehensive Annual Financial Report of the plan.



**Net OPEB Liability:** The liability reported by the City for a Healthcare Plan on its statement of net position. It is calculated as the Total OPEB Liability (defined below) less the Fiduciary Net Position.

**Net Pension Liability:** The liability reported by the City for the pension plan on its statement of net position. It is calculated as the Total Pension Liability (defined below) less the Fiduciary Net Position.

**Normal Cost:** Normal Cost is the portion of the contribution that is expected to cover the present value of benefits that are attributable to current service by covered employees under the actuarial cost method adopted by the applicable plan.

**Other Postemployment Benefits (“OPEB”):** Certain benefits provided after the employees’ services have ended. OPEB includes postemployment healthcare benefits—including medical, dental, vision, hearing, and other health-related benefits—whether provided separately or provided through a defined benefit pension plan. OPEB arises from an exchange of salaries and benefits for employee services, and it is part of the compensation that employers offer for services received.

**Smoothing:** When measuring assets for determining contributions, many pension plans, including each of the Pension Plans, “smooth” gains and losses to reduce the volatility of contribution rates. See “PENSION PLANS – Pension Plans’ Actuarial Valuations – Smoothing Methodology” for a description of the smoothing methodology employed by the Pension Plans.

**Total OPEB Liability:** The portion of the actuarial present value of projected benefit payments that is attributed to past periods of employee service in conformity with the requirements of GASB Statements No. 74 and 75 for plans providing OPEB to more than 100 employees. The Total OPEB Liability is the AAL calculated under the entry age actuarial cost method using the discount rate determined for financial reporting purposes.

**Total Pension Liability:** The portion of the actuarial present value of projected benefit payments that is attributed to past periods of employee service in conformity with the requirements of GASB Statements No. 67 and 68. The Total Pension Liability is the AAL calculated under the entry age actuarial cost method using the discount rate determined for financial reporting purposes.

**Unfunded Actuarial Liability (“UAL”):** The UAL is the excess of the AAL over the Actuarial Value of Assets. The UAL typically results from investment losses and gains and changes in actuarial assumptions, benefit improvements and other experiences that differ from those anticipated by the actuarial assumptions. The purpose of the UAL calculation is to determine, as of the date of the calculation, the sufficiency of the assets in the Retirement Plans compared to the funding target (the AAL) and the additional contributions needed to achieve the funding target. The funding status is typically expressed as the ratio of the Actuarial Value of Assets to the AAL. If the actuarially calculated funding level of a plan is less than 100%, the plan has a UAL.

For a description of assumptions relating to the actuarial valuations of the Pension Plans and Healthcare Plans, please see “PENSION PLANS – Pension Plans’ Actuarial Valuations” and “HEALTHCARE PLANS – Healthcare Plans’ Actuarial Valuations and Funding Status” below.



## RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS

### Overview

On June 5, 2012, San José voters adopted Measure B, which enacted the Sustainable Retirement Benefits and Compensation Act (“**Measure B**”). Among other changes, Measure B amended the City Charter to: (1) increase pension contribution requirements for then current employees effective June 23, 2013; (2) require the City to establish an alternative voluntary plan with reduced benefits for then current employees (the “**Voluntary Election Plan**” or “**VEP**”) subject to IRS approval; (3) place limitations on disability retirements; (4) authorize the City Council to temporarily suspend the cost of living adjustments if the City Council adopts a resolution declaring a fiscal and service level emergency; (5) require the elimination of the Supplemental Retirement Reserve within each Retirement Plan that had provided supplemental pension benefits to retirees under certain circumstances; (6) codify in the City Charter contribution requirements for then current employees for the retiree health and dental benefits and provide for a reservation of rights for the City Council to terminate or modify any retiree healthcare plan; (7) require the establishment of Tier 2 plans for new employees within each Retirement Plan; and (8) reserve to the voters the right to approve future changes to retirement benefits.

Measure B was subsequently the subject of various legal challenges. In November 2016, the voters approved the Alternative Pension Reform Act (“**Measure F**”) that the City Council placed on the ballot as a result of settlement frameworks entered into with the City’s bargaining groups related to Measure B. The City Council adopted ordinances to implement the terms of the settlement frameworks and Measure F in February and May 2017. The City also approved a settlement in November 2017 in connection with a lawsuit brought by individual retirees and a retiree association. The legal challenges to Measure B have been resolved as described below.

### Measure B - Settlements

Settlement of the legal challenges brought in connection with Measure B are discussed below.

**Settlement Frameworks.** In August 2015, the City Council formally approved an Alternative Pension Reform Settlement Framework agreement (“**Public Safety Settlement Framework**”) with the San José Police Officers Association and San José Fire Fighters, International Association of Firefighters, Local 230. On December 15, 2015 and January 12, 2016, the City and the bargaining units representing employees in the Federated Plan agreed to a Federated Alternative Pension Reform Settlement Framework related to Measure B (the “**Federated Settlement Framework**”). The terms of the Federated Settlement Framework also applied to unrepresented employees, including unrepresented management and executive employees.

The Public Safety Settlement Framework and the Federated Settlement Framework (together, the “**Settlement Frameworks**”) include, among other things, revised Tier 2 pension benefits that include increased pension benefits for Tier 2 employees while preserving the 50/50 cost sharing between the City and Tier 2 employees; closing the defined benefit retiree healthcare benefit to new employees, as well as agreement on a new lowest cost medical plan associated with retiree healthcare; allowing Tier 1 and some Tier 2 employees to opt out of the applicable Healthcare Plan to a Voluntary Employee Benefit Association (“**VEBA**”) for retiree healthcare subject to legal and IRS approval (since received); allowing Tier 1 employees who terminated employment with the City and either subsequently returned or who return in the future to return as Tier 1 employees; and continuing the elimination of the Supplemental Retiree Benefit Reserve



(“SRBR”). In the Settlement Frameworks, the City also agreed that a ballot measure would be placed on the November 2016, election. The City complied with such agreement and placed Measure F on the November 2016 election, as described below.

**Measure F – Passage.** The City and its eleven bargaining units reached agreement on the provisions of Measure F to amend the City Charter to supersede the provisions implemented by Measure B consistent with the provisions agreed to in the Settlement Frameworks. On November 8, 2016, the voters approved Measure F. Measure F included, among other things: a prohibition on any enhancements to defined retirement benefits without voter approval; codifying the Tier 2 pension benefit; closure of the defined benefit retiree healthcare plan; and a prohibition on retroactive defined retirement benefit enhancements.

**San José Retired Employees Association Litigation Settlement.** In July 2014, the Retirees’ Association, along with four individually named retirees, filed, and subsequently served, a verified complaint against the City in the Santa Clara County Superior Court. The complaint alleged that the City changed the basic retiree healthcare benefit to a new plan that “fundamentally alters” the nature and quality of the benefit provided to retirees, because the plan has increased co-pays and deductibles. The complaint further alleged that the affected retirees had a vested right to the plan in existence when they were employed by the City, and to the premium amount paid by the City for their healthcare benefit. The action sought monetary damages for the increase in co-pays, deductibles and premium payments made by the affected retirees, as well as injunctive and writ relief prohibiting the City from continuing to provide the new health benefit to retirees.

On November 7, 2017, the City Council approved a settlement agreement (the “**Retirees’ Association Settlement Agreement**”) with the Retirees’ Association and the individual plaintiffs. The Retirees’ Association Settlement Agreement provides for the dismissal of the respective appeals in the Measure B litigation by the Retirees’ Association and the City, the dismissal by the Retirees’ Association of its stayed lawsuit with prejudice and the dismissal of the stayed lawsuit by the individual plaintiffs without prejudice.

The Retirees’ Association Settlement Agreement also included the following terms, among others:

- provides for the implementation of a new lowest cost healthcare plan for retirees who are members of the Healthcare Plans and additionally provides that the lowest cost plan for current and future retirees will be permanently set such that it is neither higher nor lower than the “Silver” level as specified in the Patient Protection and Affordable Care Act (“**ACA**”) in effect as of July 2015;
- specifies that the healthcare plan must provide at least 70% but no more than 79% of the current ACA “Silver” definition;
- continues the elimination of the SRBR and, in lieu of the SRBR, establishes a “Guaranteed Purchasing Power” provision, to apply prospectively, in order to maintain the monthly allowance for current and future Tier 1 retirees at 75% of the purchasing power in effect as of the date of retirement;
- creates a health-in-lieu premium credit option so that retirees can choose to receive twenty-five percent of the monthly premium of the lowest priced healthcare and dental plan (that cannot be taken in cash) in lieu of receiving healthcare coverage; and



- reimburses specific retirees (i.e., those earning a pension of \$54,000 or less in 2016, and who were enrolled in pre-Medicare health plan between January 1, 2013 and December 31, 2016) for a portion of their additional contributions towards retiree medical premiums up to a maximum total amount of \$1.25 million.

The Retirees' Association Settlement Agreement excludes the settlement of claims related to the payment of pensions in excess of limits established under the Code. For more information regarding such limits, please see "RETIREMENT PLANS IN GENERAL – Internal Revenue Code Limitations on Pension Payments."

### **Implementation of Measure F and Settlement Frameworks**

The City Council adopted Ordinance No. 29879 on February 14, 2017, amending the Municipal Code to reflect the terms of Measure F and the Public Safety Settlement Framework. Such changes to the Municipal Code became effective thirty days after February 14, 2017. The City Council adopted Ordinance No. 29904 on May 16, 2017, amending the Municipal Code to reflect the terms of Measure F and the Federated Settlement Framework. Such changes to the Municipal Code became effective thirty days after May 16, 2017. Most of the terms of Measure F and the Settlement Frameworks were implemented on June 18, 2017, being the first pay period of fiscal year 2017-2018.

Subsequent ordinances amending the Municipal Code to implement the terms of Measure F and the Settlement Frameworks have since been adopted by the City Council. As implementation issues arise, minor modifications to the Retirement Plans in the Municipal Code have been made to address these issues. In October 2017, to address various implementation issues, the City Council and the bargaining units entered into side letters amending the terms of the Settlement Agreements and the City Council approved ordinances further amending the terms of both retirement plans and the VEBA provisions. The City and the bargaining units also agreed to the terms and methodology for the amortization costs associated with reclassifying Tier 2 employees with previous Tier 1 service. Previously, employees who separated from City service as Tier 1 employees, but were rehired or reinstated after the implementation of Tier 2, would be placed into Tier 2. The Settlement Frameworks included a provision that these employees would be reclassified as Tier 1, however, they would split the costs of the reclassification on a 1:1 basis with the City. The side letter agreements with the bargaining units were agreed to in June 2018, and the Municipal Code amendments were approved by City Council in December 2018.

The terms of the Retirement Plans as of June 30, 2018 are described below and in APPENDIX C – "BASIC FINANCIAL STATEMENTS FOR THE FISCAL YEAR ENDED JUNE 30, 2018," Notes to Basic Financial Statements, Section IV Other Information.



**VEBA Establishment.** Measure F provides for the closure of the Healthcare Plans to Tier 2 employees of the Retirement Plans and Tier 1 Classic members of the Federated Plan. The Settlement Frameworks allowed Tier 1, with the exception of Tier 1 Classic members hired after September 27, 2013, and Tier 2A members of the Federated Plan and Tier 1 members of the Police and Fire Plan a one-time irrevocable election to remain in the defined benefit postemployment Healthcare Plan or opt into a defined contribution VEBA for employees of the respective Retirement Plan. Unrepresented Tier 1 and Tier 2 members of the Healthcare Plans were eligible to opt into a VEBA but are not eligible to make ongoing contributions to the applicable VEBA. The City will also not make contributions into the VEBAs and the VEBAs established for members of the Retirement Plans are not subject to the jurisdiction of the Boards. The VEBAs are administered by a five-member advisory committee, of which one member is appointed by the City Manager and four members are appointed by the City Council.

The Settlement Frameworks also provided that an amount estimated to be equal to the members' retiree healthcare contributions without interest would be transferred from the applicable 115 Trust to their VEBA accounts. For members who opted out of the applicable Healthcare Plan into a VEBA, an amount estimated to be equal to the member's prior contributions to the Healthcare Plan, without interest, would be contributed to the member's VEBA account from the applicable 115 Trust. Subject to certain eligibility requirements, a VEBA member who receives a service-connected disability retirement will be eligible to receive 100% of the single premium cost for the lowest cost plan provided through the applicable Healthcare Plan until the member is eligible for Medicare or obtains alternative employment with healthcare coverage after exhausting all funds in their individual VEBA account. A VEBA member with at least five years of service may be eligible to purchase into the Healthcare Plans but may only do so at the retiree only rate and not the blended rate with active employees. No amounts attributable to City contributions to the Healthcare Plans would be transferred to the VEBA.

**VEBA Election and Postretirement Healthcare Contribution Transfer.** At the time the Settlement Frameworks were executed, the City contemplated seeking IRS approval of the establishment of the VEBA, the opt-in by employees who are members of the Healthcare Plans and the transfer of the 115 Trust funds to the applicable VEBA. The IRS reviewed the issues related to the VEBA establishment, employee opt-in and transfer of funds under separate administrative processes. Consistent with the terms of the Settlement Frameworks, as more fully described in "RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS - Implementation of Measure F and Settlement Frameworks - VEBA Establishment," the City established the Federated VEBA Health Savings Plan (the "**Federated VEBA**") for eligible members of the Federated Healthcare Plan and Police and Fire VEBA Health Savings Plan (the "**Police and Fire VEBA**" and together with the Federated VEBA, the "**VEBAs**") for eligible members of the Police and Fire Healthcare Plan in fiscal year 2017-2018.

With the implementation of Measure F and establishment of the Police and Fire VEBA, Tier 2 members of the Police and Fire Plan were automatically placed into the Police and Fire VEBA. The City Manager on August 2, 2017, exercised discretion provided under the Municipal Code to terminate the Police and Fire Plan Tier 2 members' participation in the Police and Fire Healthcare Plan. On August 3, 2017, the Police and Fire Board took action to terminate the Police and Fire Healthcare Plan for Tier 2 Police and Fire members effective July 30, 2017. After July 30, 2017, the City's contribution rate to the Police and Fire Healthcare Plan continued to include the payroll of both Police and Fire Plan Tier 1 and Tier 2 members; however, the Police and Fire Plan Tier 2 members no longer made contributions to the Police and Fire Healthcare Plan.

In November 2017, the IRS and City entered into a Closing Agreement whereby Tier 1 members of both the Police and Fire Healthcare Plan and the Federated Healthcare Plan, and



Tier 2A members of Federated Healthcare Plan, were eligible for an irrevocable opt-out of the applicable Healthcare Plan into the VEBAs. The transfer of their retiree healthcare contributions (medical and dental) from the applicable Healthcare Plan to their individual VEBA accounts remained subject to further IRS approval. The VEBA opt-in election period commenced on October 18, 2017, and ended on December 15, 2017. In February 2018, the IRS issued favorable private letter rulings with respect to the transfer of retiree healthcare contributions from both the Healthcare Plans for those employees of the Healthcare Plans opting into the VEBAs and in March 2018, the retiree healthcare contributions of members of the Healthcare Plan who opted into the VEBAs were transferred from the applicable Healthcare Plan into their individual VEBA accounts. For the number of Healthcare Plan members who opted into the VEBAs and the amounts transferred from the Healthcare Plans to the VEBAs, please see “HEALTHCARE PLANS - General.” The IRS also approved allowing eligible employees who are rehired by the City during calendar years 2018 through 2022 to opt into the applicable VEBA and transfer the retiree healthcare contributions from the applicable Healthcare Plan to their individual VEBA accounts.

### **Retirement Plan Tiers**

As a result of the Settlement Frameworks and implementation of Measure F, members of each Retirement Plan are now categorized into membership categories based on when the member entered the respective Retirement Plan and whether certain prior service requirements are met.

Following the passage of Measure B, but prior to the Settlement Frameworks, the Federated Plan included Tier 1, Tier 2, Tier 2B, and Tier 2C. Tier 2, Tier 2B and Tier 2C had the same reduced pension benefits as compared to Tier 1. Tier 2 had the same retiree healthcare (medical and dental) benefits as Tier 1. Tier 2B originally consisted of employees who were newly hired or rehired on or after September 27, 2013, and they were not eligible for the defined benefit retiree health care benefits; however, the City was responsible for the contributions that both the City and the Tier 2B members would have otherwise paid had those employees been eligible. Tier 2C had retiree dental benefits but no retiree medical benefits. Tier 2C included employees who were previously Tier 1 members that separated from City service and returned on or after September 30, 2012, but on or before June 18, 2018. The Settlement Frameworks provided that all previous Tier 1 employees who were placed in Tier 2 would be classified as Tier 1. As a result, employees in Tier 2C have subsequently been moved to Tier 1.

The Police and Fire Plan had Tier 1 and Tier 2 for both Police and Fire Plan members with reduced pension benefits for the Tier 2 Police and Fire Plan members as compared to the Tier 1 members, and until July 30, 2017, Tier 1 and Tier 2 members of Police and Fire Plan had the same retiree healthcare (medical and dental benefits).



The effective membership categories for the Retirements Plans are described below in Table B-1a and Table B-1b.

<b>Table B-1a</b> <b>Federated Plan Membership Tiers</b>			
<b>Tier</b>	<b>Hire Date</b>	<b>Pension</b>	<b>Defined Benefit Retiree Healthcare (Medical/Dental)</b>
<b>Tier 1</b>	<ul style="list-style-type: none"> <li>On or before September 29, 2012</li> </ul>	Tier 1	Medical/Dental <sup>(2)(4)</sup>
<b>Tier 1 Rehire</b>	<ul style="list-style-type: none"> <li>Former Tier 1 rehired on or after June 18, 2017 who did not take a return of contributions <sup>(1)</sup></li> <li>Former Tier 1 rehired on or after September 30, 2012 through June 17, 2018 <sup>(1)</sup></li> </ul>	Tier 1	Medical/Dental <sup>(2)(4)(5)</sup>
<b>Tier 1 Classic</b>	<ul style="list-style-type: none"> <li>"Classic" membership with California Public Employees' Retirement System ("CalPERS")/reciprocal agency hired on or after September 30, 2012, but before September 27, 2013<sup>(6)</sup></li> <li>"Classic" membership with CalPERS/reciprocal agency hired on or after September 27, 2013<sup>(6)</sup></li> </ul>	Tier 1	Medical/Dental
<b>Tier 2 (or Tier 2A)</b>	<ul style="list-style-type: none"> <li>Hired/rehired/reinstated on or after September 30, 2012</li> </ul>	Tier 2	Medical/Dental <sup>(2)(4)</sup>
<b>Tier 2B</b>	<ul style="list-style-type: none"> <li>Hired/rehired/reinstated after September 27, 2013 and have not met City's eligibility for retiree healthcare</li> </ul>	Tier 2	Not eligible <sup>(3)(4)</sup>

<sup>(1)</sup> Employees in these tiers are responsible for 50% of the amortization costs for having any prior years of service in Tier 2 changed to Tier 1.

<sup>(2)</sup> Employees in these tiers were provided a one-time irrevocable election to remain in the Federated Healthcare Plan or opt into the Federated VEBA. Employees that opted into the Federated VEBA are not eligible for Federated Healthcare Plan. The Federated VEBA was implemented on March 25, 2018.

<sup>(3)</sup> Employees in these tiers were mandatorily placed into the Federated VEBA.

<sup>(4)</sup> Unrepresented employees were eligible to opt into the Federated VEBA but are not eligible to make ongoing contributions to the Federated VEBA.

<sup>(5)</sup> All Tier 1 rehires formerly in Tier 2B and Tier 2C who opted to remain in the Federated Healthcare Plan began contributing to the Federated Healthcare Plan on March 25, 2018.

<sup>(6)</sup> Employees in these tiers are responsible for 50% of the amortization costs for any prior years of service in Tier 2 changed to Tier 1 for all employees in the "Classic" tier regardless of start date.

Source: City of San José Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2018.



**Table B-1b**  
**Police and Fire Plan Membership Tiers**

<b>Tier</b>	<b>Hire Date</b>	<b>Pension</b>	<b>Defined Benefit Retiree Healthcare (Medical/Dental)</b>
<b>Police Tier 1</b>	<ul style="list-style-type: none"> <li>Before August 4, 2013</li> <li>Former Tier 1 rehired on or after June 18, 2017 who did not take a return of contributions <sup>(1)</sup></li> </ul>	Tier 1	Medical/Dental <sup>(2)(4)</sup>
<b>Police Tier 1 Rehire</b>	<ul style="list-style-type: none"> <li>Tier 1 employee rehired between August 4, 2013 through June 17, 2017</li> </ul>	Tier 1	Medical/Dental <sup>(2)(4)</sup>
<b>Fire Tier 1</b>	<ul style="list-style-type: none"> <li>Before January 2, 2015</li> <li>Former Tier 1 rehired on or after June 18, 2017 who did not take a return of contributions<sup>(1)</sup></li> </ul>	Tier 1	Medical/Dental <sup>(2)(4)</sup>
<b>Fire Tier 1 Rehire</b>	<ul style="list-style-type: none"> <li>Tier 1 employee rehired between January 2, 2015 through June 17, 2017</li> </ul>	Tier 1	Medical/Dental <sup>(2)(4)</sup>
<b>Tier 1 Classic</b>	<ul style="list-style-type: none"> <li>"Classic" membership with CalPERS/reciprocal agency hired on or after August 4, 2013 for Police and January 2, 2015 for Fire <sup>(5)</sup></li> </ul>	Tier 1	Not eligible
<b>Police Tier 2</b>	<ul style="list-style-type: none"> <li>On or after August 4, 2013</li> </ul>	Tier 2	Not Eligible <sup>(3)(4)</sup>
<b>Fire Tier 2</b>	<ul style="list-style-type: none"> <li>On or after January 2, 2015</li> </ul>	Tier 2	Not Eligible <sup>(3)(4)</sup>

<sup>(1)</sup> Employees in these tiers are responsible for 50% of the amortization costs for having any prior years of service in Tier 2 changed to Tier 1.

<sup>(2)</sup> Employees in these Tiers were provided a one-time irrevocable election to remain in the Police and Fire Healthcare Plan or opt into the Police and Fire VEBA. Employees that opted into the Police and Fire VEBA are not eligible for the Police and Fire Healthcare Plan. The Police and Fire VEBA was implemented on March 25, 2018.

<sup>(3)</sup> Employees in these tiers were mandatorily placed into the Police and Fire VEBA.

<sup>(4)</sup> Unrepresented employees were eligible to opt into a Police and Fire VEBA but are not eligible to make ongoing contributions to the Police and Fire VEBA.

<sup>(5)</sup> Employees in these tiers are responsible for 50% of the amortization costs for any prior years of service in Tier 2 changed to Tier 1 for all employees in the "Classic" tier regardless of start date.

Source: City of San José Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2018.



## **SUMMARY OF RETIREMENT PLANS**

### **Retirement Plans Membership**

As shown in Table B-2 on the following page, total membership in the Federated Plan increased by 336 members from 2017 to 2018. For the Police and Fire Plan, total membership increased by 143 members from 2017 to 2018. However, as of June 30, 2018, both Retirement Plans had total active member populations below the combined populations of retirees and terminated vested members. The ratio of retired and vested terminated members to active members is approximately 1.59 to 1 in the Federated Plan and 1.57 to 1 in the Police and Fire Plan. The proportion of active members contributing to the Retirement Plans to retired members or terminated vested members no longer paying into the Retirement Plans has generally decreased since June 30, 2013, potentially causing future contributions to vary more significantly year to year due in part to increased sensitivity to investment gains and losses.

With respect to distribution of Tier 1 and Tier 2 membership, the Federated 2018 CAFR and Police and Fire 2018 CAFR indicate that over 80% of the Retirement Plans' membership is in Tier 1. As of June 30, 2018, the division of membership between Tiers 1 and 2 within the Retirement Plans is as follows:

- 77.1% Tier 1 and 22.9% Tier 2 in the Federated Pension Plan;
- 98.4% Tier 1 and 1.6% Tier 2 in the Federated Healthcare Plan;
- 90.1% Tier 1 and 9.9% Tier 2 in the Police and Fire Pension Plan; and
- 100% Tier 1 in the Police and Fire Healthcare Plan.



**Table B-2**  
**Retirement Plans' Membership**

	<u>June 30, 2017</u>	<u>June 30, 2018</u>	<u>% Change</u>
<b>Pension Plan Membership</b>			
Federated Plan			
Retirees & beneficiaries receiving benefits <sup>(1)</sup>	4,115	4,225	2.7%
Terminated vested members not yet receiving benefits	1,352	1,434	6.1%
Active members	<u>3,410</u>	<u>3,554</u>	<u>4.2%</u>
<b>Total</b>	<b>8,877</b>	<b>9,213</b>	<b>3.8%</b>
Police and Fire Plan			
Retirees & beneficiaries receiving benefits <sup>(1)</sup>	2,192	2,250	2.6%
Terminated vested members not yet receiving benefits	333	323	(3.0%)
Active members	<u>1,544</u>	<u>1,639</u>	<u>6.2%</u>
<b>Total</b>	<b>4,069</b>	<b>4,212</b>	<b>3.5%</b>
<b>Healthcare Plan Membership</b>			
Federated Plan			
Retirees & beneficiaries receiving benefits <sup>(1)</sup>	3,535	3,627	2.6%
Terminated vested members not yet receiving benefits	158	164	3.8%
Active members	<u>2,155</u>	<u>1,751<sup>(2)</sup></u>	<u>(18.7%)</u>
<b>Total</b>	<b>5,848</b>	<b>5,542</b>	<b>(5.2%)</b>
Police and Fire Plan			
Retirees & beneficiaries receiving benefits <sup>(1)</sup>	2,061	2,102	2.0%
Terminated vested members not yet receiving benefits	13	16	23.1%
Active members	<u>1,544</u>	<u>1,218<sup>(2)</sup></u>	<u>(21.1%)</u>
<b>Total</b>	<b>3,618</b>	<b>3,336</b>	<b>(7.8%)</b>

<sup>(1)</sup> The combined domestic relations orders are not included in the count above as their benefit is included in the member count.

<sup>(2)</sup> Amount does not include members only eligible for catastrophic disability benefits.

Source: Federated 2018 CAFR; Police and Fire 2018 CAFR.

## Summary of Retirement Plans Historic and Projected Contributions

Investors are cautioned that the amount of the UAL, the Funded Ratio, and the calculations of Normal Cost as reported by the Retirement Plans and the resulting pension and healthcare contributions are “forward looking” information prepared by the Retirement Plans for their own purposes. Such “forward looking” information reflects the judgment of the Boards of the respective Retirement Plans and their Plan Actuary as to the amount of assets which the Retirement Plans will be required to accumulate to fund future benefits over the lives of the currently active employees, vested terminated employees, existing retired employees, and their beneficiaries. These judgments are based upon a variety of assumptions, one or more of which may prove to be inaccurate or that may change with the future experience of the Retirement Plans. The actuarial methods and assumptions could be changed by the Boards of the respective Retirement Plans at any time. Such changes could cause the City’s obligations to the Retirement Plans to be higher or lower in any particular year.



In its most recent valuation reports for the Federated Pension Plan and the Police and Fire Pension Plan, the Plan Actuary noted that future contributions may fluctuate higher than projected based on various risks, including investment risk, interest rate risk, longevity and other demographic risk, and assumption change risk. See the Federated 2018 Pension Plan Actuarial Report and the Police and Fire 2018 Pension Plan Actuarial Report regarding the identification and assessment of risks provided by the Plan Actuary.

Contributions to the Pension Plans are actuarially determined. The Municipal Code specifies the portion of the actuarially determined contribution paid by employees and the remaining portion is paid by the City. Contributions to the Healthcare Plans made by the City are actuarially determined and contributions by employees are made at rates established by the Municipal Code and the Settlement Frameworks. For the Pension Plan and Healthcare Plan contribution information, please see “PENSION PLAN – Pension Plan Contributions” and “HEALTHCARE PLANS – Funding Policy and Healthcare Plan Contributions.”

The City's contributions to the Pension Plans and Healthcare Plans are shown in Table B-3a. As shown in Table B-3a, the City's annual dollar contribution to the Pension Plans and Healthcare Plans has increased significantly since 2010, primarily due to investment losses, assumption changes and reductions in payroll.

**Table B-3a**  
**Federated and Police and Fire Retirement Plans**  
**Pension and Healthcare Contributions**

<b>Fiscal Year Ended June 30</b>	<b>Federated Plan</b>	<b>Police and Fire Plan</b>	<b>Total</b>
2009	\$ 73,388,000	\$ 62,991,000	\$ 136,379,000
2010	71,593,000	63,599,000	135,192,000
2011	76,326,000	94,919,000	171,245,000
2012	112,916,000	142,214,000	255,130,000
2013	124,360,000	121,046,000	245,406,000
2014	126,842,000	140,850,000	267,692,000
2015	141,710,000	150,189,000	291,899,000
2016	159,921,000	153,545,000	313,446,000
2017	170,388,000	157,624,000	328,012,000
2018	189,167,000	183,094,000	372,261,000

*Source: City of San José Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2018; Office of Retirement Services.*

In January and February 2019, as directed by the Retirement Plans, the Plan Actuary provided five-year budget projections for the City's contributions for the Pension Plans and Healthcare Plans based on the June 30, 2018 actuarial valuations. The projections assume that all valuation assumptions were exactly met and are exactly met each and every year for the projection period. In addition, the projections assume that the active population remains level and plan provisions remain unchanged. In reality, actual experience will deviate from the assumptions. Importantly, if all assumptions are met, contributions equal to the Normal Cost plus interest on the UAL are needed to prevent UAL from growing as a dollar amount.



The actuarially determined projections of the City's contributions to Retirement Plans for fiscal years 2019-2020 through 2023-2024 are shown in Table B-3b and Table B-3c. With respect to the Police and Fire Healthcare Plan, the City contribution rate is projected to exceed the City's optional contribution limit of 11.0% by 2022. The City's actual contribution will depend on various factors, including the actual returns of the Pension Plans over the course of this five-year time period covered in Table B-3b and Table B-3c.

**Table B-3b**  
**Federated Plan**  
**Projected City Contributions – Pension and Healthcare**  
**(in millions)**

<b>Fiscal Year Ended June 30</b>	<b>Federated Payroll</b>	<b>Pension Contribution</b>	<b>Pension Rate</b>	<b>Healthcare Contribution</b>	<b>Healthcare Rate</b>	<b>Total Contribution</b>	<b>Total Rate</b>
2020	\$ 308.7	\$ 179.6	58.17%	\$ 21.8	7.06%	\$ 201.3	65.22%
2021	318.7	188.6	59.19	22.1	6.94	210.8	66.13
2022	329.1	195.4	59.37	22.5	6.83	217.9	66.21
2023	339.8	199.7	58.78	22.8	6.70	222.5	65.48
2024	350.8	204.6	58.31	22.9	6.54	227.5	64.85

*Source: Cheiron 5-Year Budget Projections for Federated Plan, January 9, 2019.*

**Table B-3c**  
**Police and Fire Plan**  
**Projected City Contributions – Pension and Healthcare**  
**(in millions)**

<b>Fiscal Year Ended June 30</b>	<b>Police and Fire Payroll</b>	<b>Pension Contribution</b>	<b>Pension Rate</b>	<b>Healthcare Contribution</b>	<b>Healthcare Rate</b>	<b>Total Contribution</b>	<b>Total Rate</b>
2020	\$ 225.5	\$ 186.2	82.59%	\$ 24.0	10.64%	\$ 210.2	93.22%
2021	232.9	198.8	85.40	25.4	10.91	224.2	96.26
2022	240.4	206.2	85.75	27.0	11.23	233.2	97.00
2023	248.3	195.2	78.67	28.2	11.36	223.4	89.97
2024	256.3	199.3	77.76	29.4	11.48	228.7	89.27

*Source: Cheiron 5-Year Budget Projections for Police and Fire Pension Plan, January 30, 2019; Cheiron 5-Year Budget Projections for Police and Fire Healthcare Plan, February 27, 2019.*

For the Plan Actuary's twenty-year projection of contributions to the Federated Pension Plan and the Police and Fire Pension Plan, please see Table B-11 in "PENSION PLAN – Pension Plan Contributions.". For projected City contributions to the Healthcare Plans, please see "THE HEALTHCARE PLANS – Funding Policy and Healthcare Plan Contributions."

For additional information and discussion regarding the contribution policy of both Pension Plans and both Healthcare Plans, please refer to "PENSION PLAN – Pension Plans' Actuarial Valuations" and "HEALTHCARE PLANS – Healthcare Plans' Actuarial Valuations and Funding Status.". In addition, for both Healthcare Plans, the Plan Actuary's projections include changes to the healthcare plans offered to active employees as described in "RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS."



## **PENSION PLANS**

The Federated Pension Plan and the Police and Fire Pension Plan offer service retirement, disability retirement, survivor, and death benefits for members and their beneficiaries. The benefits available under the Pension Plans accrue throughout the time an employee engages in covered work for the City. Even though the benefits accrue during employment, certain age and service requirements must be attained to generate a retirement or other benefit upon retirement or termination of City employment. If met, an employee may elect to receive a monthly pension benefit, calculated by taking into account years of service, final compensation, and in certain instances, age at retirement.

The terms of the final benefit calculation and subsequent cost of living increases, if any, during retirement depends on the employee's Pension Plan tier. The pension benefits for employees in Tier 2 of each Pension Plan differ substantially from the Tier 1 pension benefits, as shown in Tables B-4a and B-4b. In addition, the contribution rates for Tier 2 members are calculated based on a 50/50 split of all costs, including UAL. Members in Tier 1 of each Pension Plan share a portion of the Normal Cost, but generally do not contribute towards UAL costs. As more fully explained below, the Plan Actuary expects that as more employees join Tier 2 and contributions are made to pay down the UAL, Pension Plan funding levels will generally increase and the City contribution rates will decrease over time.

Table B-4a and Table B-4b below provide a general description of service retirement pension benefit formulas (excluding early retirement) for each Tier in each Pension Plan. For more specific information about the current Pension Plan member tier service retirement and other benefit formulas, please see in APPENDIX C –“ BASIC FINANCIAL STATEMENTS FOR THE FISCAL YEAR ENDED JUNE 30, 2018,” Notes to Basic Financial Statements, Section IV Other Information and Title 3 of the Municipal Code.



As more fully described in “RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS,” the benefit formulas for Tier 2 changed significantly upon implementation of Measure F and necessary amendments to the Municipal Code.

The benefit formulas as of June 30, 2018, are described in Table B-4a and Table B-4b.

**Table B-4a**  
**Federated Plan Service Pension Formulas**

	<b>Normal Retirement Age</b>	<b>Minimum Vesting Service<sup>(1)</sup></b>	<b>Pension Allowance</b>	<b>Final Compensation</b>
<b>Tier 1</b>	<ul style="list-style-type: none"> <li>• 55 with 5 years service</li> <li>• 30 years service at any age</li> </ul>	5 years of service	<ul style="list-style-type: none"> <li>• 2.5% x years of service x final compensation (75% max).</li> </ul>	Average monthly base pay in highest one year compensation
<b>Tier 2</b>	<ul style="list-style-type: none"> <li>• 62 with 5 years of Federated Plan covered service</li> <li>• 55 with 5 years of Federated Plan covered service with reduction by a factor of 5% per year prior to age 62 as set forth in the Municipal Code</li> </ul>	5 years of Federated Plan covered City service	<ul style="list-style-type: none"> <li>• 2.0% x years of service x final compensation (70% max).</li> </ul>	Average monthly (or biweekly) base pay in highest consecutive three year compensation <sup>(2)</sup>

<sup>(1)</sup> Terminated employees with less than minimum vesting service who are not employed by a reciprocal agency must withdraw all contributions from the plan.

<sup>(2)</sup> Excludes premium pay or additional compensation.

Source: Federated 2018 CAFR.



**Table B-4b**  
**Police and Fire Plan Service Pension Formulas**

	<b>Normal Retirement Age</b>	<b>Minimum Vesting Service<sup>(1)</sup></b>	<b>Pension Allowance</b>	<b>Final Compensation</b>
<b>Police Tier 1</b>	<ul style="list-style-type: none"> <li>• 50 with 25 years service</li> <li>• 55 with 20 years service</li> <li>• 30 years service at any age (with reciprocity must be 50 years of age)</li> <li>• Mandatory retirement at 70 years of age</li> </ul>	10 years of service	<ul style="list-style-type: none"> <li>• First 20 years of Service: 50% of final compensation (2.5% per year)</li> <li>• 21-30 years service: 4% per year of service x final compensation (90% max)</li> </ul>	Highest one year average compensation
<b>Fire Tier 1</b>	<ul style="list-style-type: none"> <li>• 50 with 25 years service</li> <li>• 55 with 20 years service</li> <li>• 30 years service at any age (with reciprocity must be 50 years of age)</li> <li>• Mandatory retirement at 70 years of age</li> </ul>	10 years of service	<ul style="list-style-type: none"> <li>• First 20 years of service: 50% of final compensation (2.5% per year)</li> <li>• Beginning 21st year of service: 3% x years of service x final compensation (90% max).</li> <li>• All years convert to 3% after 20 years.</li> </ul>	Highest one year average compensation
<b>Police and Fire Tier 2</b>	<ul style="list-style-type: none"> <li>• 57 with 5 years of Police and Fire Department Plan covered service</li> <li>• 50 with 5 years of Police and Fire Department Plan covered service with reduction by a factor of 7% per year prior to age 57 as set forth in the Municipal Code</li> </ul>	5 years of Police and Fire Department Plan covered service	<ul style="list-style-type: none"> <li>• First 20 years of service: 2.4% per year of service x final compensation.</li> <li>• Beginning of 21st year: 3.0% per year of service x final compensation.</li> <li>• Beginning of 26th year: 3.4% per year of service x final compensation.</li> <li>• Maximum benefit is 80% of final compensation.</li> </ul>	Average annual base pay plus any premium pays authorized by ordinance for the highest 3 consecutive years of service.

<sup>(1)</sup> Terminated employees with less than minimum vesting service who are not employed by a reciprocal agency must withdraw all contributions from plan.

Source: Police and Fire 2018 CAFR.



## Pension Plan's Funding Status

The funding objective for the Pension Plans is to meet long-term benefit obligations through contributions and investment income. To determine on-going funding requirements for pension benefits, most pension plans utilize an actuarial value of pension assets that differs from the market value of those assets. For a description of each Retirement Plan's methodology for valuing pension plan assets, please see "PENSION PLANS – Pension Plans' Actuarial Valuations." The actuarial value of pension assets is based on smoothing year-to-year market value returns for purposes of reducing the resulting volatility on contributions. The market value represents the value of the pension assets if they were liquidated on the valuation date.

Table B-5a, Table B-5b, and Table B-5c show the market value of the pension assets of each Pension Plan and the applicable actuarial value for purposes of comparison. Table B-5a separately compares the market value and actuarial value with the actuarially determined value of all current and future benefits to be paid by the respective Pension Plan ("**Total Actuarial Liability**"). Because the market value of assets is smaller than the actuarial value in the Pension Plans, if assumptions are met in the future, the Plan Actuary expects an increase in contribution rates as the deferred asset losses are recognized in the Actuarial Value of Assets. These measures are intended to be used to assess contribution amounts for an ongoing pension plan. They are not appropriate for the assessment of the sufficiency of plan assets to settle the Pension Plans' obligations on a risk free basis because actual events and plan experience may deviate from the assumptions used in the actuarial calculations.

<b>Table B-5a</b> <b>Pension Assets &amp; Liabilities</b> <i>(in millions)</i>			
	<b>June 30, 2017</b>	<b>June 30, 2018</b>	<b>% Change</b>
<b>Federated Pension Plan</b>			
Total Actuarial Liability	\$ 3,924	\$ 4,101	4.5%
Market Value Assets	1,973	2,069	4.9%
Actuarial Value Assets	2,101	2,179	3.7%
Unfunded Actuarial Liability <sup>(1)</sup>	1,951	2,031	4.1%
Unfunded Actuarial Liability <sup>(2)</sup>	1,823	1,921	5.4%
Funded Ratio – Market Value	50.3%	50.5%	0.4%
Funded Ratio – Actuarial Value	53.6%	53.1%	(0.8%)
<b>Police and Fire Pension Plan</b>			
Total Actuarial Liability	\$ 4,464	\$ 4,696	5.2%
Market Value Assets	3,293	3,496	6.2%
Actuarial Value Assets	3,440	3,597	4.6%
Unfunded Actuarial Liability <sup>(1)</sup>	1,171	1,200	2.5%
Unfunded Actuarial Liability <sup>(2)</sup>	1,024	1,100	7.4%
Funded Ratio – Market Value	73.8%	74.4%	0.7%
Funded Ratio – Actuarial Value	77.1%	76.6%	(0.5%)

<sup>(1)</sup> UAL amount based on Market Value of Assets.

<sup>(2)</sup> UAL amount based on Actuarial Value of Assets.

Source: Federated 2018 Pension Plan Actuarial Report; Police and Fire 2018 Pension Plan Actuarial Report.



**Table B-5b**  
**Federated Pension Plan -**  
**Market and Actuarial Value of Pension Assets**  
*(in thousands)*

	<b>June 30, 2017</b>	<b>June 30, 2018</b>
Market Value, Beginning of Year	\$ 1,858,880	\$ 1,972,792
Contributions		
Member	17,228	20,501
City	138,484	156,770
Total	\$ 155,712	\$ 177,271
Net Investment Earnings <sup>(1)</sup>	146,009	117,493
Benefit Payments	(183,431)	(193,400)
Administrative Expenses	(4,379)	(4,823)
<b>Market Value, End of Year</b>	<b>\$ 1,972,791</b>	<b>\$ 2,069,333</b>
Actuarial Value of Assets	\$ 2,101,435	\$ 2,179,488

<sup>(1)</sup> Gross investment earnings less investment expenses.  
Source: Federated 2018 CAFR.

**Table B-5c**  
**Police and Fire Pension Plan -**  
**Market and Actuarial Value of Pension Assets**  
*(in thousands)*

	<b>June 30, 2017</b>	<b>June 30, 2018</b>
Market Value, Beginning of Year	\$ 3,043,653	\$ 3,293,257
Contributions		
Member	20,580	23,841
City	136,957	157,712
Total	\$ 157,537	\$ 181,553
Net Investment Earnings <sup>(1)</sup>	292,734	233,474
Benefit Payments	(196,032)	(206,630)
Administrative Expenses	(4,635)	(5,464)
<b>Market Value, End of Year</b>	<b>\$ 3,293,257</b>	<b>\$ 3,496,190</b>
Actuarial Value of Assets	\$ 3,439,922	\$ 3,596,590

<sup>(1)</sup> Gross investment earnings less investment expenses.  
Source: Police and Fire 2018 CAFR.



## Actuarial Funding Progress

The most recent determinations of funding status on an actuarial basis of both Pension Plans are summarized in Table B-6a and Table B-6b. The Funded Ratio in the following tables does not take into account the assets and liabilities related to retiree healthcare benefits. The most recent determination of actuarial funding status of the Healthcare Plans is summarized in "HEALTHCARE PLANS." The schedules of the funding progress for both Pension Plans are set forth in Pension Plan Actuarial Reports provided to the Retirement Plans by the Plan Actuary and are both as of June 30, 2018, representing the current data available for the funding progress for both Pension Plans as shown below in Tables B-6a and B-6b.

Table B-6a and Table B-6b on the following page show the historical dollar amount of the UAL and the Funded Ratio as of the last ten valuation dates calculated using the actuarial (smoothed) value of assets for both Pension Plans. Specific smoothing methodologies for the respective plans are discussed in "PENSION PLANS – Pension Plans' Actuarial Valuations – Smoothing Methodology." Over the past several years, both Pension Plans have experienced steady increases in the UAL, primarily attributable to actuarial assumption changes, including lowering of the discount rate, and recognition of prior unfavorable investment returns. The Plan Actuary has indicated that the UAL for both Pension Plans for fiscal year 2017-2018 increased primarily due to the recognition of investment losses and assumption changes. For a description of actuarial changes that can affect the calculation of the UAL, please see "PENSION PLANS – Pension Plans' Actuarial Valuations." The Plan Actuary provides the fiscal impact of assumption, investment, and demographic changes on the Federated Pension Plan and Police and Fire Pension Plan valuations in years covered by Tables B-6a and B-6b in "Section VI – Actuarial section of the CAFR" of each of the Federated 2018 Pension Plan Actuarial Report and the Police and Fire 2018 Pension Plan Actuarial Report.

The UAL as a percentage of covered payroll is a measure of the relative magnitude of the UAL. As illustrated in Table B-6a on the following page, the Federated Pension Plan's UAL was 643% of total covered annual payroll in 2018. It would require contributing nearly six and a half times the 2018-covered payroll to fund all of the Federated Pension Plan's Actuarial Accrued Liability.

Historically, the Federated Pension Plan contribution has been less than normal cost plus annual interest calculated on accrued UAL due to the length of the amortization period (30 years in 2009). As the remaining amortization period has become shorter, the Plan Actuary has noted that the Federated Pension Plan contribution is closer to the amount necessary to keep the UAL amount level, and expects the Federated Pension Plan contribution to be above that level in the future.



**Table B-6a**  
**Federated Pension Plan - Schedule of Pension Funding Progress**  
*(in thousands)*

<b>Valuation Date (June 30)</b>	<b>Actuarial Value of Assets</b>	<b>Actuarial Liability</b>	<b>UAL</b>	<b>Funded Ratio</b>	<b>Covered Payroll</b>	<b>UAL as % of Covered Payroll</b>
2009	\$ 1,756,558	\$ 2,486,155	\$ 729,597	71%	\$ 323,020	226%
2010	1,729,413	2,510,358	780,945	69	300,811	260
2011	1,788,660	2,770,227	981,567	65	228,936	429
2012	1,762,973	2,841,000	1,078,027	62	225,859	477
2013	1,783,270	3,013,763	1,230,493	59	225,779	545
2014	1,911,773	3,235,065	1,323,292	59	234,677	564
2015	2,004,481	3,569,898	1,565,417	56	251,430	623
2016	2,034,741	3,786,730	1,751,989	54	266,823	657
2017	2,101,435	3,923,966	1,822,531	54	287,339	634
2018	2,179,488	4,100,821	1,921,333	53	298,985	643

*Source: Federated 2018 Pension Plan Actuarial Report.*

As illustrated below for the Police and Fire Pension Plan, the UAL was 503.5% of total covered annual payroll in fiscal year 2017-2018. It would require contributing approximately five times the 2018-covered payroll to fund all of the Police and Fire Pension Plan's Actuarial Accrued Liability.

**Table B-6b**  
**Police and Fire Pension Plan - Schedule of Pension Funding Progress**  
*(in thousands)*

<b>Valuation Date (June 30)</b>	<b>Actuarial Value of Assets</b>	<b>Actuarial Liability</b>	<b>UAL</b>	<b>Funded Ratio</b>	<b>Covered Payroll</b>	<b>UAL as % of Covered Payroll</b>
2009	\$ 2,569,569	\$ 2,963,482	\$ 393,913	86.7%	\$ 255,223	154.3%
2010	2,576,705	3,230,456	653,751	79.8	251,058	260.4
2011	2,685,721	3,196,007	510,286	84.0	190,726	267.5
2012	2,703,539	3,397,792	694,253	79.6	187,959	369.4
2013	2,771,924	3,578,031	806,107	77.5	184,645	436.6
2014	3,025,101	3,813,825	788,724	79.3	188,189	419.1
2015	3,212,776	4,058,410	845,634	79.2	184,733	457.8
2016	3,303,550	4,355,990	1,052,440	75.8	194,072	542.3
2017	3,439,922	4,464,402	1,024,480	77.1	203,816	502.6
2018	3,596,590	4,696,428	1,099,838	76.6	218,429	503.5

*Source: Police and Fire 2018 Pension Plan Actuarial Report.*



## Funding Progress - Net Pension Liability

GASB Statement No. 68 requires calculation and disclosure of a pension plan's "Net Pension Liability," which is the difference between the actuarial present value of projected benefit payments that is attributed to past periods of employee service calculated using methods and assumptions known as the "Total Pension Liability" and the fair market value of the pension plan's assets known as the "Fiduciary Net Position." In fiscal year 2013-2014, the Retirement Plans implemented GASB Statement No. 67 for financial statements. The City implemented GASB Statement No. 68 for financial statements in fiscal year 2014-2015. The City financial statements calculate Net Pension Liability using a measurement date that is one fiscal year prior to the Net Pension Liability measurement date used for the Plans' financial statements.

Table B-7 provides the funded status of the Pension Plans calculated according to the assumptions and methodology provided by GASB Statement No. 68 as of the June 30, 2017 and the June 30, 2018 measurement dates. The Total Pension Liability for the Pension Plans as of June 30, 2017 and 2018 shown in Table B-7 is based on results of an actuarial valuation date of June 30, 2016 and 2017, respectively, and rolled-forward to June 30, 2017 and 2018 using standard roll forward procedures. Note that for purposes of financial reporting by the City pursuant to GASB Statement No. 68, the Net Pension Liability as of June 30 of a given fiscal year is measured as of the end of the previous fiscal year.

<b>Table B-7</b> <b>Components of Net Pension Liability</b> <i>(in thousands)</i>			
	<b>June 30, 2017</b>	<b>June 30, 2018</b>	<b>% Change</b>
<b>Federated Pension Plan</b>			
Total pension liability	\$ 3,923,210	\$ 4,057,348	3.4%
Plan fiduciary net position	1,972,792	2,069,333	4.9%
Net pension liability	\$ 1,950,418	\$ 1,988,015	1.9%
Plan fiduciary net position as a percentage of the total pension liability	50.3%	51.0%	1.4%
<b>Police and Fire Pension Plan</b>			
Total pension liability	\$ 4,533,776	\$ 4,635,937	2.3%
Plan fiduciary net position	3,293,257	3,496,191	6.2%
Net pension liability	\$ 1,240,519	\$ 1,139,746	(8.1%)
Plan fiduciary net position as a percentage of the total pension liability	72.6%	75.4%	3.9%
<i>Source: Federated 2018 CAFR; Police and Fire 2018 CAFR.</i>			

## Pension Plans' Actuarial Valuations

With respect to the Pension Plans, the actuarial valuations measure the financial position of each Pension Plan and determine the amount to be contributed by current employees and the City. The Plan Actuary employs a variety of actuarial methods and assumptions in these calculations, which are discussed in the following section. To produce these actuarial valuations, the Plan Actuary uses demographic data (including employee age, salary and service credits),



economic assumptions (including estimated future salary increases and interest rates), and decrement assumptions (including employee turnover, mortality and retirement rates) to produce the necessary information.

To calculate each Pension Plan's actuarial value of assets, the Plan Actuary uses a five-year smoothing method for investment gains and losses. This means that, for actuarial valuation purposes, the annual gains or losses, as calculated at year end, are smoothed (amortized) with the net gains and losses resulting from the prior four years. The Pension Plans utilize an individual Entry Age Normal Actuarial Cost Method, whereby the Normal Cost is computed as the level annual percentage of pay required to fund the retirement benefits between each member's date of hire and assumed termination of employment. The Actuarial Accrued Liability is the difference between the present value of future benefits and the present value of future Normal Costs. See "– Smoothing Methodology" for a description of the smoothing methodology employed by the Pension Plans.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality and investment return. Experience studies are performed by the Plan Actuary to determine appropriate revision to each Pension Plan's actuarial assumptions. Actual results are compared with past expectations and new estimates are made about the future. In 2015, the Plan Actuary performed experience studies for each Pension Plan and as a result of these studies the assumptions used by the Pension Plans were revised. The actuarial assumptions may be adjusted where the respective Board determines that current assumptions will not provide the most accurate expectation of future events.

The Federated Board adopted certain demographic changes based on an experience study covering a period from 2010 to 2015 performed by the Plan Actuary. The Plan Actuary determined that the assumption changes caused a 5.7% increase in Actuarial Accrued Liability of the Federated Plan. Further, the amortization payments for the UAL calculated under the 2015 assumptions were phased in over a three-year period. As of the date of the June 30, 2018 valuation, the phase-in period was complete. The Federated Board also adopted wage inflation, amortization growth rate, mortality improvement and discount rate changes in 2017 and adopted a lower discount rate of 6.750% and updated mortality improvement for the June 30, 2018 valuation.

The Police and Fire Board adopted a number of assumption changes, including merit salary increases, retirement rates and mortality improvement, recommended by the Plan Actuary based on an experience study covering Police and Fire Pension Plan experience from 2009 to 2017. The Plan Actuary determined that the assumption changes caused a 2.9% decrease in Actuarial Accrued Liability of the Police and Fire Pension Plan. The Police and Fire Board also adopted a lower discount rate of 6.750% for the June 30, 2018 valuation.

Below are highlights of several of the Pension Plans' actuarial methods and assumptions for the June 30, 2018 valuations:

***Actuarially Assumed Investment Rates of Return.*** The net rate of return assumed by each Pension Plan represents the long-term expected rate of return on the applicable Pension Plan's investments net of investment expenses. The Federated Board decided to further reduce the assumed investment rate for the Federated Plan to 6.75% effective for the June 30, 2018 valuation and for future year valuations. The reduction of the assumed investment rate and an update to the most recent mortality improvement projection scale increased the UAL for the June



30, 2018 valuation by \$54 million for the Federated Pension Plan. The Police and Fire Board also decided to reduce the assumed investment return rate for the Police and Fire Pension Plan to 6.75% effective for the June 30, 2018 valuation and for future year valuations. The assumed investment rate of return reduction for the June 30, 2018 valuation resulted in an increase in liability of \$76 million for the Police and Fire Pension Plan. The Boards for the Pension Plans have incrementally reduced their respective assumed rates of return from 8.25% beginning July 1, 2009 for the Federated Pension Plan, and from 8.0% beginning July 1, 2010 for the Police and Fire Pension Plan.

Table B-8 shows the historical discount rates for the Pension Plans from fiscal year 2008-2009 through fiscal year 2017-2018.

Table B-8 Historical Discount Rates									
<u>Federated Pension Plan</u>									
<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
7.75%	7.95%	7.50%	7.50%	7.25%	7.00%	7.00%	6.875%	6.875%	6.750%
<u>Police and Fire Pension Plan</u>									
<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>
8.00%	7.75%	7.50%	7.25%	7.125%	7.00%	7.00%	6.875%	6.875%	6.750%

Source: Federated 2018 Pension Plan Actuarial Report; Police and Fire 2018 Pension Plan Actuarial Report.

**Smoothing Methodology.** When measuring assets, many pension plans, including each of the Pension Plans, “smooth” gains and losses to reduce the volatility of contribution rates. Both Pension Plans utilize a smoothing or spreading of that shortfall or excess over a five-year period. If in the one-year period prior to the annual actuarial valuation, the actual net investment return on the Pension Plan’s market value of assets is lower or higher than the actuarial assumed net rate of return, then 20% of the shortfall or excess is recognized each year when determining the recommended contribution rates for that actuarial valuation. The impact of this will result in smoothed assets that are lower or higher than the market value of assets depending upon whether the remaining amount to be smoothed is either a net gain or a net loss. The Police and Fire Pension Plan has, in past practice, limited the smoothing of assets to no greater than 120% and no less than 80% of the market value of assets. Under this practice, any investment gains or losses that would cause smoothed assets to fall outside of this 80%-120% market value corridor would be recognized immediately rather than smoothed over five years.

**Amortization Method and Period.** The Tier 1 UAL for the Federated Pension Plan as of June 30, 2009 is amortized over a 30-year closed period, and changes in the Tier 1 UAL are amortized over a 20-year closed period, beginning with the valuation period in which they arise, with a separate amortization schedule set up for each change in UAL in each year for pension benefits. Tier 1 assumption changes are amortized over 25-year periods beginning with the valuation date in which they first arise. Effective June 30, 2017, all prior assumption amortization base periods were increased by 5 years so they have the same remaining period as if they had originally been amortized over 25 years.



The Tier 2 UAL for the Federated Pension Plan as of June 30, 2017, is amortized over a closed 10-year period. Future Tier 2 actuarial gains and losses, assumption changes, and plan changes will be amortized over 10-year periods beginning with the valuation date in which they first arise. Amortization payments are scheduled to increase 3.00% each year while aggregate payroll is expected to grow 3.25% each year.

With respect to the Police and Fire Pension Plan, actuarial gains and losses and plan changes are amortized as a level percentage of pay assuming 3.25% annual growth in payroll over a 15-year period (16 years for gains and losses prior to June 30, 2016) beginning with the valuation date in which they first arise. Changes in methods and assumptions are amortized as a level percentage of pay assuming 3.25% annual growth in payroll over a 20-year period (16 years for changes prior to June 30, 2011) beginning with the valuation date on which they are effective.

Tables B-9 and B-10 summarize actuarial assumptions including future rates of return used by both Pension Plans for the 2018 valuations.

<b>Table B-9</b> <b>Federated Pension Plan – Pension Actuarial Assumptions</b>	
Valuation Date	June 30, 2018
Actuarial funding method	Entry Age Normal
Amortization method	Level percent of pay, closed, layered
Amortization payment growth rate	3.00%
Asset valuation method	5-year smoothing of return
Actuarial Assumptions:	
Discount Rate	6.75%
Wage inflation <sup>(1)</sup>	3.25% compounded annually
Cost-of-Living Adjustments <sup>(2)</sup>	Tier 1-3.0% per year; Tier 2-1.25% - 2.0% per year depending on years of service
<sup>(1)</sup> Additional merit salary increases of 0.25% to 4.50% based on a participant's years of service are also assumed. <sup>(2)</sup> Cost-of-living adjustments are fixed at 3% by the plan provisions for Tier 1 and do not fluctuate with actual inflation. For Tier 2, adjustments fluctuate with actual inflation and are capped at 1.25% to 2.0% depending on service. Source: Federated 2018 Pension Plan Actuarial Report.	



**Table B-10**  
**Police and Fire Pension Plan – Pension Actuarial Assumptions**

Valuation Date	June 30, 2018
Actuarial funding method	Entry Age Normal
Amortization method	Level percent of pay, closed, layered
Amortization payment growth rate	3.25%
Asset valuation method	5 year smoothing of return Minimum of 80% and maximum of 120% of market value
Actuarial Assumptions:	
Discount Rate	6.75%
Wage inflation <sup>(1)</sup>	3.25% compounded annually
Cost-of-Living Adjustments <sup>(2)</sup>	Tier 1-3.0% per year; Tier 2-2.0% per year

<sup>(1)</sup> Additional merit salary increases of 0.5% to 6.0% based on a participant's years of service are also assumed.

<sup>(2)</sup> Cost-of-living adjustments are fixed at 3% by the plan provisions for Tier 1 and do not fluctuate with actual inflation.

For Tier 2, adjustments fluctuate with actual inflation and are capped at 2.0%.

Source: Police and Fire 2018 Pension Plan Actuarial Report.

**Federated Pension Plan 2018 Valuation Summary.** The most recent actuarial valuation of the Federated Pension Plan was performed by the Plan Actuary and summarized in its report entitled, "Federated City Employees' Retirement System June 30, 2018 Actuarial Valuation Report," and included both Tier 1 and Tier 2. The Federated Pension Plan's Actuarial Value of Assets is calculated by recognizing the deviation of actual investment returns compared to the expected return for the period ending on the valuation date (6.875% for fiscal year 2017-2018 and fiscal year 2016-2017, 7.00% for fiscal year 2015-2016 and fiscal year 2014-2015) over a five-year period. The dollar amount of the expected return on the Market Value of Assets is determined using actual contributions, benefit payments and administrative expenses during the year. Any difference between this amount and the actual net investment earnings is considered a gain or loss.

In the Federated 2018 Pension Plan Actuarial Report, the Plan Actuary concluded that as of June 30, 2018:

- The Funded Ratio based on the Actuarial Value of Assets for the Federated Pension Plan was 53.1%, down from 53.6% as of June 30, 2017.
- The Funded Ratio based on the Market Value of Assets for the Federated Pension Plan increased from 50.3% as of June 30, 2017 to 50.5%.
- The UAL using the Actuarial Value of Assets was approximately \$1.921 billion as compared to a UAL of approximately \$1.823 billion as of June 30, 2017. The UAL using the Market Value of Assets increased from \$1.951 billion as of June 30, 2017 to \$2.031 billion.



- The Actuarial Value of Assets was approximately \$2.179 billion and the Actuarial Accrued Liability was approximately \$4.101 billion. The Federated Pension Plan's Total Actuarial Liability increased by 4.5% and the Market Value of Assets increased by 4.9% when compared to the June 30, 2017 valuation.
- The UAL using the Actuarial Value of Assets increased approximately \$99 million since the June 30, 2017 valuation. For fiscal year 2017-2018, the UAL increased as a result of investment losses and assumption changes, contributions less than Normal Cost plus interest on the prior UAL and plan benefit changes as a result of Measure F implementation. These increases were only partially offset by decreases from aggregate plan liability experience, such as member salary and retirement experience.

***Police and Fire Pension Plan 2018 Valuation Summary.*** The most recent actuarial valuation of the Police and Fire Pension Plan, was performed by the Plan Actuary and summarized in its report entitled: "City of San José Police and Fire Department Retirement Plan June 30, 2018 Actuarial Valuation Report" as of June 30, 2018. The Police and Fire Pension Plan's Actuarial Value of Assets is calculated by recognizing the deviation of actual investment returns compared to the expected return (6.875% for fiscal year 2017-2018 and fiscal year 2016-2017, 7.00% for fiscal year 2015-2016 and fiscal year 2014-2015, and 7.125% for fiscal year 2013-2014) over a five-year period. The dollar amount of the expected return on the Market Value of Assets is determined using the actual contributions and benefit payments during the year. Any difference between this amount and the actual net investment earnings is considered a gain or a loss.

In the Police and Fire 2018 Pension Plan Actuarial Report, the Plan Actuary concluded that as of June 30, 2018:

- The Funded Ratio based on the Actuarial Value of Assets was 76.6%, down from 77.1% as of June 30, 2017.
- The Funded Ratio based on the Market Value of Assets was 74.4%, up from 73.8% as of June 30, 2017.
- The UAL using the Actuarial Value of Assets was approximately \$1.100 million as compared to the UAL of approximately \$1.024 million reported as of June 30, 2017.
- The Actuarial Value of Assets was approximately \$3.597 billion and Actuarial Accrued Liabilities were approximately \$4.696 billion. For the Police and Fire Pension Plan, the Total Actuarial Liability increased by 5.2% and the market value of assets increased by 6.2% compared to the prior valuation.
- The UAL using the Actuarial Value of Assets increased approximately \$75 million since the June 30, 2017 valuation. As a result of assumption changes and investment losses, the UAL increased, but the increase was offset in part by decreases attributable to plan liability experience, such as member salary and retirement experience and contributions in excess of aggregate Normal Cost and interest accruing on the prior UAL.



## Pension Plan Contributions

**General.** Annual contributions to the Pension Plans for both the City and employees are actuarially determined amounts sufficient to provide adequate assets to pay benefits when due. When the respective Boards of the Pension Plans approve contribution rates and amounts, these become the City's and the employees' legally required contribution rates and amounts for the fiscal year beginning one year after the valuation date. Currently, the Plan Actuary employs the Entry Age Normal actuarial cost method. There are two components to the annual City and employee contribution: the Normal Cost (including administrative expenses) and the UAL contribution. The annual contributions are based upon actuarial calculations that take into consideration a number of economic and demographic assumptions, including assumed investment earnings on the assets of the Pension Plans that are used to pay benefits. For a description of assumptions relating to the actuarial valuations to determine Plan contributions, please see "PENSION PLANS – Pension Plans Actuarial Valuations."

The required contributions determined by the Plan Actuary anticipate that the City will make contributions on a bi-weekly basis throughout the fiscal year. The City may elect to prefund all or part of its total required contributions to the Pension Plans at the beginning of each fiscal year, in which case the Plan Actuary applies an interest discount to the required contributions to account for the fact that contributions are made at the beginning of the year instead of throughout the year. The "prefunded" annual contributions are made on the basis of estimated bi-weekly payroll in the actuarial valuation for the fiscal year and may be increased at the end of the fiscal year based on actual bi-weekly payroll. To the extent contributions are made after the beginning of the fiscal year, the amounts are adjusted for interest.

The Pension Plans employ a "split funding method" for payment of contributions for Tier 1 whereby the UAL portion of the City's contribution is a dollar amount as recommended by the Plan Actuary in the annual valuation report and approved by the Boards (adjusted for interest based on time of contribution), and the Normal Cost (including administrative expense) portion of the City's contribution is the greater of: (1) the dollar amount recommended by the Plan Actuary in the annual valuation report and approved by the Boards (adjusted for time of contribution) or, (2) the dollar amount determined by applying the Normal Cost as a percent of payroll reported in the actuarial valuation to the actual payroll for the fiscal year if actual payroll exceeds the actuarial payroll. The City's Federated Pension Plan Tier 2 contribution is based on the contribution rate determined by the Plan Actuary and approved by the Federated Board multiplied by the actual Tier 2 member payroll. The Police Tier 2 and Fire Tier 2 contribution is based on the contribution rate approved by the Police and Fire Board multiplied by the actual Tier 2 member payroll. For City and member contribution rates, please see "PENSION PLANS – Pension Plan Contributions – Federated Plan Pension Contribution" and "PENSION PLANS – Pension Plan Contributions – Police and Fire Plan Pension Contribution."

Table B-11 provides a comparison of the actuarially determined annual contribution to the Pension Plans by the City and the actual contribution to the Pension Plans by the City from fiscal year 2012-2013 to fiscal year 2017-2018.



**Table B-11**  
**Schedule of City Pension Plan Contributions**  
*(in thousands)*

	<b>2012- 2013</b>	<b>2013- 2014<sup>(1)</sup></b>	<b>2014- 2015</b>	<b>2015- 2016<sup>(1)</sup></b>	<b>2016- 2017</b>	<b>2017- 2018</b>
<b>Federated Pension Plan</b>						
Actuarially Determined Contribution	\$ 103,109	\$102,811	\$ 114,751	\$ 129,456	\$ 138,483	\$ 156,770
Actual Contribution	103,109	107,544	114,751	124,723	138,483	156,770
<b>Contribution Deficiency (excess)</b>	<b>\$ 0</b>	<b>(\$ 4,733)</b>	<b>\$ 0</b>	<b>\$ 4,733</b>	<b>\$ 0</b>	<b>\$ 0</b>
<b>Police and Fire Pension Plan</b>						
Actuarially Determined Contribution	\$ 105,234	\$ 123,583	\$ 129,279	\$ 132,480	\$ 136,957	\$ 157,712
Actual Contribution	105,234	123,583	129,279	132,480	136,957	157,712
<b>Contribution Deficiency (excess)</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>	<b>\$ 0</b>

<sup>(1)</sup> Contributions for fiscal year 2014 included \$4.7 million that should have been credited to the Healthcare Plan, and such error was corrected in fiscal year 2016.

Source: City of San José Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2018.

Table B-12 provides 20-year projections of City contributions calculated by the Plan Actuary for the Pension Plans assuming such contributions are made by the City mid-year .

For the Federated Pension Plan, the 20-year projections show contribution rates increasing for the next few years due to recognition of recent investment losses. Thereafter, the City's contribution rate is projected to gradually reduce through 2033. The projections show a further reduction in the City's contribution rate to 40.0% of projected payroll in 2039. The dollar amount of the UAL is expected by the Plan Actuary to increase in fiscal year 2019-2020 as a result of recent lower than expected investment returns recognized in the actuarial value of assets but is expected to decrease thereafter if all assumptions are met. The Plan Actuary indicated in the 2018 Actuarial Report that, if all assumptions are met, the Federated Pension Plan will reach a funded status of 80% by 2033.

For the Police and Fire Pension Plan, the 20-year projections show contribution rates staying relatively flat until 2026 then declining substantially from 80.7% of total projected payroll in 2026 to 19.1% of total projected payroll in 2039 when portions of the UAL are fully amortized. The Plan Actuary indicates in the most recent Police and Fire 2018 Pension Plan Actuarial Report that there may be significant volatility in future City contribution rates to the Police and Fire Pension Plan due to investment return volatility, the plan asset to payroll ratio, and the standard deviation of the current investment portfolio. The volatility in contribution rates could be limited by extending amortization periods, but such extension would only control short term volatility. However, the Plan Actuary noted the risk of very high contribution rates would need to be addressed through the Police and Fire Pension Plan's investments.



**Table B-12**  
**20-Year Projections of Pension Contributions**  
*(in thousands)*  
*(middle of the year)*

<b>Fiscal Year Ended June 30</b>	<b>Federated Pension Plan</b>		<b>Police and Fire Pension Plan</b>	
	<b>Projected City Contribution Amount</b>	<b>Projected Total Contribution Rate (% of Payroll)</b>	<b>Projected City Contribution Amount</b>	<b>Projected Total Contribution Rate (% of Payroll)</b>
2020	\$ 179,558	58.2%	\$ 186,259	82.6%
2021	188,649	59.2	198,871	85.4
2022	195,393	59.4	206,168	85.8
2023	199,740	58.8	195,301	78.7
2024	204,582	58.3	199,295	77.8
2025	209,336	57.8	215,252	81.3
2026	214,329	57.3	220,373	80.7
2027	219,563	56.9	166,967	59.2
2028	225,073	56.5	131,306	45.1
2029	230,164	55.9	170,928	56.8
2030	236,186	55.6	160,233	51.6
2031	242,375	55.2	152,186	47.5
2032	241,726	53.4	165,189	49.9
2033	248,719	53.2	138,703	40.6
2034	245,491	50.8	109,719	31.1
2035	242,407	48.6	101,806	27.9
2036	252,843	49.1	81,945	21.8
2037	260,978	49.1	65,769	16.9
2038	229,234	41.8	61,972	15.5
2039	226,804	40.0	79,147	19.1

*Source: Cheiron 5-Year Budget Projections for Federated Plan, January 9, 2019; Cheiron 5-Year Budget Projections for Police and Fire Pension Plan, January 30, 2019.*

It is certain that not all assumptions will be exactly met each and every year. The Plan Actuary indicated in the Federated 2018 Pension Plan Actuarial Report and the Police and Fire 2018 Pension Plan Actuarial Report that there is a significant level of uncertainty in projections of the future, the largest source of which is the projection of investment returns. Actual investment returns that vary from the assumed rate of investment return can result in significantly different contribution rates.

The next two sections provide, for both Pension Plans, information on the contribution rates and dollar amounts for fiscal year 2018-2019 and the contribution rates and dollar amounts for fiscal year 2019-2020. The Boards have approved the contribution rates and dollar amounts for the City and the members for fiscal year 2019-2020. The City has chosen not to prefund its contribution for fiscal year 2019-2020.

**Federated Plan Pension Contribution.** The employee member pension contribution rate for Federated Pension Plan Tier 1 is a proportion (3/11ths) of the Normal Cost (including administrative expenses, but excluding reciprocity) with the remaining 8/11ths of the Normal Cost allocated to the City. In addition to the 8/11ths of the Normal Cost (including administrative expenses), the City is allocated all of the Reciprocity Normal Cost (the cost of funding reciprocity



with other California pension plans) plus an amortization payment on the UAL. Tier 1 members who were rehired into Tier 2 and then returned to Tier 1 under Measure F also pay half of the increased cost attributable to their Tier 2 service. For Tier 2, the members and the City each pay half of the total contribution rate. However, the member's UAL contribution rate cannot increase by more than 0.33% of pay each year. The City contributes any amounts in excess of this cap that would otherwise be contributed by the member.

The increase in the City's Tier 1 contribution rate for fiscal year 2019-2020 is primarily due to the reduction in the discount rate and investment losses. Payroll for Tier 1 is expected to decrease over time as members leave the system and new entrants join Tier 2. The increase in the Tier 2 contribution rates for the City and the members is primarily due to the reduction in the discount rate.

Table B-13a below summarizes the pension contribution rates for employee members of the Federated Plan for fiscal years 2018-2019 and 2019-2020. The Normal Cost/Admin rate is determined by dividing the total Normal Cost plus assumed administrative expenses determined by the Plan Actuary by the payroll expected for members active on the valuation date. The UAL rate is determined by dividing the UAL payment calculated by the Actuary by the total expected payroll for the year (including members active on the valuation date and new entrants expected to replace active members who are expected to leave employment). The Federated Board approved method for communicating the contribution amounts changed for the 2019-2020 Estimated City contributions for Police and Fire Tier 1. The Tier 1 UAL contribution is now shown as a dollar amount, whereas the Tier 1 Normal Cost and Administrative Expense is shown as both a dollar amount and a contribution amount.

**Table B-13a  
Federated Pension Plan Member Contribution Rates**

	2018-2019			2019-2020		
	<u>Basic</u>	<u>COLA</u>	<u>Total</u>	<u>Basic</u>	<u>COLA</u>	<u>Total</u>
<b><u>Tier 1</u></b>						
Total Member Normal Cost/Admin Rate <sup>(1)</sup>	4.93%	1.88%	6.81%	5.08%	1.98%	7.06%
<b><u>Tier 2</u></b>						
Member Normal Cost/Admin Rate	6.75%	1.18%	7.93%	6.92%	1.14%	8.06%
Member UAL Rate	0.22	0.13	0.35	0.18	0.09	0.27
<b>Total Member Rate</b>	<b>6.97%</b>	<b>1.31%</b>	<b>8.28%</b>	<b>7.10%</b>	<b>1.23%</b>	<b>8.33%</b>

<sup>(1)</sup> Excludes additional reclassified rate (UAL) for Classic and Reclassified Tier 1 Members

Source: Resolution No. 8686 of the Federated Board, approved by the Federated Board on May 17, 2018; Resolution No. 8687 of the Federated Board, approved by the Federated Board on May 17, 2018; Resolution No. 8943 of the Federated Board, approved by the Federated Board on May 16, 2019; Resolution No. 8944 of the Federated Board, approved by the Federated Board on May 16, 2019.



Table B-13b illustrates the City's contribution dollar amounts for the Federated Pension Plan for fiscal years 2018-2019 and 2019-2020 assuming the City contribution is made periodically throughout the year.

**Table B-13b**  
**Federated Pension Plan Employer Contribution Amounts For Pension Benefit**  
*(in thousands)*  
*(throughout the year)*

	2018-2019			2019-2020		
	<u>Basic</u>	<u>COLA</u>	<u>Total</u>	<u>Basic</u>	<u>COLA</u>	<u>Total</u>
<b><u>Tier 1</u></b>						
City Normal Cost/Admin <sup>(1)</sup>	\$ 21,355	\$ 8,193	\$ 29,548	\$ 20,747	\$ 8,120	\$ 28,867
City UAL Cost <sup>(2) (3)</sup>	64,495	63,399	127,894	70,032	67,377	137,409
<b>Total City Contribution</b>	<b>\$ 85,850</b>	<b>\$ 71,592</b>	<b>\$ 157,442</b>	<b>\$ 90,779</b>	<b>\$ 75,497</b>	<b>\$ 166,276</b>
<b><u>Tier 2<sup>l</sup></u></b>						
City Normal Cost/Admin	\$ 9,309	\$ 1,627	\$ 10,936	\$ 11,034	\$ 1,817	\$ 12,851
City UAL Cost	303	179	482	287	144	431
<b>Total City Contribution</b>	<b>\$ 9,612</b>	<b>\$ 1,806</b>	<b>\$ 11,418</b>	<b>\$ 11,321</b>	<b>\$ 1,961</b>	<b>\$ 13,282</b>

<sup>(1)</sup> Includes the reciprocity rate for the prefunding of the liability for reciprocal benefits with certain other California public pension plans.

<sup>(2)</sup> Includes the deficiency rate for the amortization of the funding deficiency.

<sup>(3)</sup> Includes the golden handshake rate for the cost for funding additional benefits granted in the past to certain retiring employees.

Source: Resolution No. 8686 of the Federated Board, approved by the Federated Board on May 17, 2018; Resolution No. 8687 of the Federated Board, approved by the Federated Board on May 17, 2018; Resolution No. 8943 of the Federated Board, approved by the Federated Board on May 16, 2019; Resolution No. 8944 of the Federated Board, approved by the Federated Board on May 16, 2019.

**Police and Fire Plan Pension Contribution.** For Tier 1 members of the Police and Fire Plan, the employee member contribution rate is a proportion (3/11ths) of the Normal Cost (excluding reciprocity) plus the employee member's historic share of assumed administrative expenses. In addition, employee members pay a portion of the UAL attributable to certain benefit improvements. The remaining 8/11ths of the Normal Cost is allocated to the City. In addition to the 8/11ths of the Normal Cost (including administrative expenses), the City is allocated all of the Reciprocity Rate (the cost of funding reciprocity with other California pension plans) and the remaining portion of the UAL rate. For Tier 2 members of the Police and Fire Plan, members and the City share the total contribution rate equally.

Table B-14a and Table B-14b summarize the pension contribution rates for the employee members of the Police and Fire Pension Plan. Table B-14c summarizes the City contribution amounts for fiscal years 2018-2019 and 2019-2020. Tier 1 rates increase from 2018-2019 to 2019-2020, due to assumption changes and investment losses only partially offset by plan liability experience. Tier 2 rates increase slightly primarily due to the assumption changes. The Board approved method for communicating the contribution amounts changed for the 2019-2020 Estimated City contributions for Police and Fire Tier 1. The Tier 1 UAL contribution is now shown as a dollar amount, whereas the Tier 1 Normal Cost and Administrative Expense is shown as both a dollar amount and a contribution amount.



**Table B-14a**  
**Police and Fire Pension Plan Tier 1 Member Pension Contribution Rates**  
**(% of Payroll)**

	2018-2019			2019-2020		
	<u>Basic</u>	<u>COLA</u>	<u>Total</u>	<u>Basic</u>	<u>COLA</u>	<u>Total</u>
<b><u>Fire Tier 1</u></b>						
Member Normal Cost/AdminRate	7.64%	3.45%	11.09%	7.88%	3.58%	11.46%
Member UAL Rate <sup>(1)</sup>	0.00	0.00	0.00	0.00	0.00	0.00
<b>Total Member Rate</b>	<b>7.64%</b>	<b>3.45%</b>	<b>11.09%</b>	<b>7.88%</b>	<b>3.58%</b>	<b>11.46%</b>
<b><u>Police Tier 1</u></b>						
Member Normal Cost/Admin Rate	7.08%	3.14%	10.22%	7.32%	3.30%	10.62%
Member UAL Rate <sup>(1)</sup>	0.04	0.02	0.06	0.05	0.03	0.08
<b>Total Member Rate</b>	<b>7.12%</b>	<b>3.16%</b>	<b>10.28%</b>	<b>7.37%</b>	<b>3.33%</b>	<b>10.70%</b>

<sup>(1)</sup> Excludes additional reclassified rate (UAL) for Classic and Reclassified Tier 1 Members

Source: Resolution No. 4608 of the Police and Fire Board, approved by the Police and Fire Board on June 7, 2018; Resolution No. 4609 of the Police and Fire Board, approved by the Police and Fire Board on June 7, 2018; Resolution No. 4770 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4771 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4772 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4773 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4774 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019.

**Table B-14b**  
**Police and Fire Plan Tier 2 Member Pension Contribution Rates**  
**(% of Payroll)**

	2018-2019			2019-2020		
	<u>Basic</u>	<u>COLA</u>	<u>Total</u>	<u>Basic</u>	<u>COLA</u>	<u>Total</u>
<b><u>Fire Tier 2</u></b>						
Member Normal Cost/Admin Rate	11.81%	3.09%	14.90%	12.11%	3.23%	15.34%
Member UAL Rate	0.12	0.11	0.23	(0.01)	0.06	0.05
<b>Total Member Rate</b>	<b>11.93%</b>	<b>3.20%</b>	<b>15.13%</b>	<b>12.10%</b>	<b>3.29%</b>	<b>15.39%</b>
<b><u>Police Tier 2</u></b>						
Member Normal Cost/Admin Rate	10.80%	2.76%	13.56%	11.13%	2.89%	14.02%
Member UAL Rate	0.06	0.09	0.15	(0.03)	0.07	0.04
<b>Total Member Rate</b>	<b>10.86%</b>	<b>2.85%</b>	<b>13.71%</b>	<b>11.10%</b>	<b>2.96%</b>	<b>14.06%</b>

Source: Resolution No. 4610 of the Police and Fire Board, approved by the Police and Fire Board on June 7, 2018; Resolution No. 4611 of the Police and Fire Board, approved by the Police and Fire Board on June 7, 2018; Resolution No. 4770 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4771 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4772 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4773 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4774 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019.



Table B-14c below shows the estimated dollar amounts of the City's contributions for 2018-2019 and 2019-2020 for the Police and Fire Pension Plan assuming contributions are made throughout the fiscal year.

**Table B-14c**  
**Police and Fire Plan Employer Contribution Amounts For Pension Benefit**  
*(in thousands)*  
*(throughout the year)*

	2018-2019			2019-2020		
<b>Police</b>	<b>Basic</b>	<b>COLA</b>	<b>Total</b>	<b>Basic</b>	<b>COLA</b>	<b>Total</b>
<b><u>Tier 1</u></b>						
City Normal Cost/Admin	\$ 19,516	\$ 8,524	\$ 28,040	\$ 20,140	\$ 8,910	\$ 29,050
City UAL Cost	26,554	35,751	62,305	30,376	39,648	70,024
<b>Total City Contribution</b>	<b>\$ 46,070</b>	<b>\$ 44,275</b>	<b>\$ 90,345</b>	<b>\$ 50,516</b>	<b>\$ 48,558</b>	<b>\$ 99,074</b>
<b><u>Tier 2</u></b>						
City Normal Cost/Admin	\$ 3,411	\$ 872	\$ 4,283	\$ 4,869	\$ 1,264	\$ 6,133
City UAL Cost	19	28	47	(13)	31	18
<b>Total City Contribution</b>	<b>\$ 3,430</b>	<b>\$ 900</b>	<b>\$ 4,330</b>	<b>\$ 4,856</b>	<b>\$ 1,295</b>	<b>\$ 6,151</b>
<b>Fire</b>						
<b><u>Tier 1</u></b>						
City Normal Cost/Admin	\$ 16,106	\$ 7,240	\$ 23,346	\$ 16,146	\$ 7,291	\$ 23,437
City UAL Cost	21,487	28,878	50,365	23,917	31,114	55,031
<b>Total City Contribution</b>	<b>\$ 37,593</b>	<b>\$ 36,118</b>	<b>\$ 73,711</b>	<b>\$ 40,063</b>	<b>\$ 38,405</b>	<b>\$ 78,468</b>
<b><u>Tier 2</u></b>						
City Normal Cost/Admin	\$ 1,345	\$ 352	\$ 1,697	\$ 2,020	\$ 539	\$ 2,559
City UAL Cost	14	12	26	(2)	10	8
<b>Total City Contribution</b>	<b>\$ 1,359</b>	<b>\$ 364</b>	<b>\$ 1,723</b>	<b>\$ 2,018</b>	<b>\$ 549</b>	<b>\$ 2,567</b>

*Source: Resolution No. 4608 of the Police and Fire Board, approved by the Police and Fire Board on June 7, 2018; Resolution No. 4609 of the Police and Fire Board, approved by the Police and Fire Board on June 7, 2018; Resolution No. 4610 of the Police and Fire Board, approved by the Police and Fire Board on June 7, 2018; Resolution No. 4611 of the Police and Fire Board, approved by the Police and Fire Board on June 7, 2018; Resolution No. 4770 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4771 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4772 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4773 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019; Resolution No. 4774 of the Police and Fire Board, approved by the Police and Fire Board on May 2, 2019.*

## Investments

The State Constitution and the Municipal Code provide that the Board of each Retirement Plan has exclusive control over the investment of the assets of the respective Pension Plans. As discussed above in "RETIREMENT PLANS IN GENERAL," assets within the 401(h) account in each Pension Plan are designated for the payment of the applicable Healthcare Plan benefits. The Municipal Code also specifies that each Board is to manage the investments for the purpose of providing benefits to its members and beneficiaries, maintaining the actuarial soundness of the Pension Plan, and defraying reasonable expenses of administering the Pension Plan. The Boards for both Retirement Plans have retained investment consultants to advise them.



Table B-15 below illustrates the historic annual returns for both Pension Plans at the identified interval as reported by the Pension Plans' respective investment consultants in their respective quarterly reports for the period ending December 31, 2018.

<b>Table B-15</b> <b>Historical Investment Performance For Pension Plans</b> <b>(As of December 31, 2018)</b>		
<b>Measurement Period</b>	<b>Federated Pension Plan<sup>(1)</sup></b>	<b>Police and Fire Pension Plan<sup>(2)</sup></b>
Since Inception	6.4% <sup>(3)</sup>	8.2% <sup>(4)</sup>
10 Years	6.0	6.8
5 Years	2.7	3.2
3 Years	4.2	5.0
1 Year	(3.9)	(2.9)

<sup>(1)</sup> The returns for certain investments (fixed income, private debt and real assets) are gross of fees through June 2015 and net of fees thereafter.  
<sup>(2)</sup> Net of fees.  
<sup>(3)</sup> Measurement Period Beginning January 1994.  
<sup>(4)</sup> Measurement Period Beginning March 1971.  
*Source: Meketa Investment Group Federated Pension Plan Quarterly Review December 31, 2018; Meketa Investment Group Police and Fire Pension Plan Quarterly Review December 31, 2018.*

Annually, the Boards for both Pension Plans receive projections from their respective investment consultants for the expected net rates of return based on the respective approved target asset allocations. Potential investment returns and the subsequent risk associated with those returns are partially a function of the underlying assets of the respective Pension Plan. Each Board, as part of its fiduciary responsibilities, adopts asset allocation targets commensurate with the applicable Board's diversification goals and risk tolerance.

Table B-16 illustrates each Pension Plan's most current approved asset allocation targets. It is important to note that the stated asset allocation targets for both Pension Plans represent the ultimate allocation goal of the Pension Plans; however, during periods of allocation transition, asset allocation target objectives may not be achieved. For detailed asset class holdings and for further information on plan assets to the Investment Policy Statement of the Federated Pension Plan adopted on April 18, 2019, Investment Policy Statement of the Police and Fire Pension Plan adopted on April 4, 2019, the Police and Fire 2018 CAFR, and the Federated 2018 CAFR.



**Table B-16**  
**Target Asset Allocations for Pension Plans**

<b>Asset Class</b>	<b>Federated Target %</b>	<b>Police and Fire Target %</b>
<b>Growth</b>	<b>58</b>	<b>56</b>
Public Equity	30	31
Private Markets	25	22
Private Equity	10	8
Venture/Growth Capital	5	4
Private Debt	4	4
Growth Real Estate	3	3
Private Real Assets	3	3
Emerging Markets Bonds	3	3
<b>Zero Beta</b>	<b>32</b>	<b>32</b>
Cash	0	0
Short-Term Investment-Grade Bonds	20	20
Investment Grade Bonds	0	0
Market Neutral Strategies	7	7
Bonds (Immunized Cash Flows)	5	5
<b>Other</b>	<b>10</b>	<b>12</b>
Core Real Estate	5	5
Sovereign Bonds ex-U.S.	0	3
Commodities	3	2
TIPS	2	2
10-Year Expected Return <sup>(1)</sup>	7.3	7.0
20-Year Expected Return <sup>(1)</sup>	7.8	7.5
Standard Deviation <sup>(1)</sup>	11.6	11.0

<sup>(1)</sup> Neither the City nor the Purchaser can provide any assurance that actual returns will not be less than those expected by the respective Board.

Source: Meketa Investment Group presentation to the Federated Board, Police and Fire Board and San José City Council at a joint meeting on April 30, 2019; Police and Fire Department Retirement Plan Investment Policy Statement, Approved by the Police and Fire Board on April 4, 2019; Federated City Employees' Retirement System Investment Policy Statement, Approved by the Federated Board on April 18, 2019.

For a description of the types of investments in each asset class identified in Table B-16, please see the Federated City Employees' Retirement System Investment Policy Statement, Approved by the Federated Board on April 18, 2019, and the Police and Fire Department Plan Investment Policy Statement, Approved by the Police and Fire Board on April 4, 2019, which may be found at <https://sjrs.legistar.com/MeetingDetail.aspx?ID=687980&GUID=C9713B0A-A68F-4035-A4EF-2DF78A9B363C&Search=> and <https://sjrs.legistar.com/MeetingDetail.aspx?ID=685165&GUID=B895D44B-1CEB-41B2-841F-7926B4EAE97&Options=info&Search=>, respectively. None of the foregoing websites or webpages are incorporated into this Appendix B. They are referenced for informational purposes only. The City and the Purchasers make no representation whatsoever as to the accuracy or completeness of any of the information on such websites or webpages.



## HEALTHCARE PLANS

### General

As discussed above in “RETIREMENT PLANS IN GENERAL,” each Retirement Plan includes a Healthcare Plan, which provides eligible retirees, their dependents, and survivors with health and dental benefits. For health benefits, both Healthcare Plans pay that portion of the premium that is equivalent to the premium for the lowest-priced medical plan with which the City contracts for medical benefits for active City employees. If the retiree elects a medical plan that is not the lowest priced plan, the eligible retiree or survivor pays the difference between the portion paid by the applicable Healthcare Plan and that charged by the medical care provider. In the case of dental benefits, both Healthcare Plans pay the entire premium. Retired members of the Healthcare Plans eligible for medical and/or dental benefits may elect annually not to receive Healthcare Plan benefits for the plan year and participate in the in-lieu credit program, providing a credit equal to 25% of the lowest cost plan for that year which may be applied to Member premiums in future years.

As more fully described in “RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS,” the Healthcare Plans are closed to new members. Generally, members of the Retirement Plans hired before July 2013 that did not elect to opt into the applicable VEBA are eligible for defined benefit retiree healthcare benefits from the Healthcare Plans. Subject to certain eligibility requirements, a VEBA member who receives a service-connected disability retirement will be eligible to receive 100% of the single premium cost for the lowest cost plan provided through the applicable Healthcare Plan until the member is eligible for Medicare after exhausting all funds in their individual VEBA account.

Table B-17a sets forth the number of members of the Healthcare Plans and associated member contributions transferred to the respective VEBA as of June 30, 2018:

<b>Table B-17a</b>		
<b>Healthcare Plans VEBA Transfers</b>		
<b>(as of June 30, 2018)</b>		
	<b>Members</b>	<b>Transferred Amounts</b>
Federated Healthcare Plan	240	\$13,497
Police and Fire Healthcare Plan <sup>(1)</sup>	273	7,897
<b>Total</b>	<b>513</b>	<b>\$ 21,394</b>

<sup>(1)</sup> Includes members who elected or who were required to participate in the Police and Fire VEBA and all associated employee contributions.  
Source: City of San José Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2018; Office of Retirement Services.

The contributions for the members who opted into the VEBAs and opted out of the Healthcare Plans were transferred to the individual VEBA accounts in March 2018.

The financial reporting, disclosure, and accounting for costs and obligations related to the Healthcare Plans are consistent with the requirements of GASB Statement No. 74 and GASB Statement No. 75. Both Healthcare Plans provide financial reporting according to the requirements of GASB Statement No. 74. The City provides financial reporting, disclosure, and accounting for costs and obligations related to the Healthcare Plans according to the requirements of GASB Statement No. 75. The changes implemented by GASB Statement No. 74 and GASB



Statement No. 75 related to healthcare plan reporting are similar in concept to those requirements imposed by GASB Statement No. 67 and GASB Statement No. 68 on pension plan reporting. GASB Statement No. 74 and GASB Statement No. 75 require the liability for OPEB obligations, known as the Net OPEB Liability, and an OPEB expense to be recognized in the financial statements of the Healthcare Plans and the City. The OPEB expense in GASB Statement No. 74 and GASB Statement No. 75 is no longer equal to the Annual Required Contribution and has shorter recognition periods than under prior GASB Statements No. 43 and 45. OPEB expense under GASB Statement No. 74 and GASB Statement No. 75 recognizes deferred outflows of resources and deferred inflows of resources related to OPEB over a defined, closed period, rather than a choice between an open or closed period.

### **Establishment of 115 Trusts for Healthcare Plans; Tax Limitations**

The Code Section 401(h) permits a pension plan to provide retiree healthcare benefits under certain conditions, including: (1) a separate account (the “**401(h) account**”) maintained for the healthcare benefits and (2) the healthcare benefits are subordinate to the pension benefits. Under IRS regulations, subordination means that the contributions for healthcare benefits do not exceed 25% of the aggregate contributions excluding contributions to fund past service credits. Exceeding the subordination limit puts a pension plan at risk of losing its tax-exempt status, which in turn, would subject the pension plan’s income to the payment of income tax and reduce the assets available for the payment of benefits.

To avoid exceeding the subordination limit for the 401(h) accounts held in both Pension Plans, the City Council enacted an ordinance to establish a separate trust under Code Section 115 for the Federated Plan effective June 2011 (the “**Federated 115 Trust**”). For the Police and Fire Plan, the City Council enacted an ordinance, effective June 2012 to establish separate trusts under Code Section 115 for the Police members (the “**Police 115 Trust**”) and the Fire members (the “**Fire 115 Trust**”) and together with the Police 115 Trust, the “**Police and Fire 115 Trusts**”). The Board for each Retirement Plan also serves as the board of trustees for the corresponding 115 Trust. On June 11, 2013, the City Council adopted amendments to the City’s Municipal Code provisions applicable to the Police and Fire 115 Trusts for the Police 115 Trust and the Fire 115 Trust to allow two wholly separate sub-trusts of a single trust.

Both the Federated Board and the Police and Fire Board have sought and received private letter rulings from the IRS on the tax-exempt status of the respective 115 Trusts. Additionally, on August 6, 2013, in response to the City’s request, the IRS issued a private letter ruling indicating that employee contributions into the Federated 115 Trust and the Police and Fire 115 Trusts may be made as employer contributions and therefore are excludable from the employee’s gross income and are not subject to income or other employment taxes. For the Federated Plan, employee contributions to the Federated 115 Trust commenced on December 22, 2013. For the Police and Fire Plan, it has not been determined if or when employee contributions will begin to be deposited in the Police and Fire 115 Trusts.

Both Boards have been advised that the contributions made to the 115 Trust must be treated as non-refundable in order to maintain the 115 Trust’s tax exempt status. Both Retirement Plans permit return of employee pension and retiree healthcare contributions held in the 401(h) accounts, although the retiree healthcare contributions have been refunded from each Pension’s Plan’s pension fund and not the 401(h) account within each pension fund.



## **Funding Policy and Healthcare Plan Contributions**

Historically, member and City contributions to the Healthcare Plans were negotiated through collective bargaining and were not actuarially determined. Until the City entered into agreements with various bargaining groups in 2009 and prior to implementation of Measure F, contributions for the health and dental benefits for both the City and the participating employees of both Healthcare Plans were based upon an actuarially determined percentage of employees' base salary sufficient to provide adequate assets to pay benefits when due over the next 10 years for the Police and Fire Plan and the next 15 years for the Federated Plan. From 2009 until the implementation of Measure F, the City had been in the process of phasing in payment of the ARC for the retiree health and dental benefits provided by both Healthcare Plans as calculated pursuant to GASB Statement No. 43 and GASB Statement No. 45 then in effect. However, the contribution rates for the City and members of the Healthcare Plans were capped before the full ARC was reached.

The annual contribution costs for the Healthcare Plans' benefits are allocated to both the City and the active employee members. Contributions to the Healthcare Plans for both the City and the participating members are based upon agreements between the City and the bargaining units. With the implementation of Measure F, member contributions are fixed as a percentage of pay and the City's contribution toward the explicit subsidy (premium subsidy) is an Actuarially Determined Contribution determined by the Healthcare Plans. The Actuarially Determined Contribution for the Healthcare Plans is the Normal Cost plus the Amortization Payment on the UAL, less expected member contributions. The City has an option to limit its Actuarially Determined Contribution for each Healthcare Plan to a fixed percentage of the payroll of all active members of the respective Retirement Plan. The Actuarially Determined Contribution for each Healthcare Plan is calculated beginning with the 2018-2019 fiscal year. See "RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS" for a discussion of Measure F.

The Plan Actuary in the Federated 2018 Postemployment Healthcare Actuarial Report and the Police and Fire 2018 Postemployment Healthcare Actuarial Report has indicated that because the Healthcare Plans are closed to new entrants, member contributions are expected to decline as current active members retire or otherwise leave active employment with the City. Because member contributions pay all of the Normal Cost plus a portion of the UAL, the City's Actuarially Determined Contribution is expected to increase as the member contributions decrease over the coming years.

The City will pay the implicit subsidy on a pay-as-you go basis as part of active health premiums. An implicit subsidy for retiree health benefits exists because the medical experience for retirees under age 65 are pooled with the experience for active employees thereby resulting in a lowering of the premium paid for retirees under age 65. The liabilities for the implicit subsidy have been included in the GASB Statement No. 74 and GASB Statement No. 75 disclosure calculations reported in the financial statements of both Healthcare Plans and the City. The implicit subsidy is included in the actuarial valuations of both the Federated Healthcare Plan and the Police and Fire Healthcare Plan. The implicit subsidy is shown as both a contribution and payment from the Healthcare Plans. However, the implicit subsidy is not actually contributed to or paid from the Healthcare Plan. Rather, it is paid directly by the City on a pay-as-you-go basis as a part of active member health plan premiums. The Plan Actuary separately calculates the total UAL, being the aggregate UAL for both implicit and explicit subsidies, and the UAL for only the explicit subsidy. The UAL for the explicit subsidy is used to calculate the City's Actuarially Determined Contribution.



Table B-17b below summarizes the estimated OPEB payroll and Actuarially Determined Contribution amounts for the next five years. The estimated full benefit payroll is for the closed group of members entitled to full OPEB benefits. The total payroll also includes members only eligible for catastrophic disability benefits. The Plan Actuary has indicated that the City contributions for the Healthcare Plans are payments toward the Unfunded Actuarial Liability, as member contributions are sufficient to cover Normal Costs during this period.

The projections in Table B-17 show that the City contributions to the Federated Healthcare Plan rise gradually over the next five years but remain significantly below the City's contribution cap of 14% of the pay of the active members of the Federated Plan. The Plan Actuary's January 17, 2019 presentation to the Federated Board related to final valuation results for the fiscal year ended June 30, 2018, indicated that the explicit subsidy is expected to be fully funded in the next twenty years. The City's contributions to the Police and Fire Healthcare Plan are projected to increase over the next five years and exceed the City's contribution cap by 2022. The City can elect at such time to limit its contribution, if the Actuarially Determined Contribution exceeds the contribution cap, to 11% of the pay of the active members of the Police and Fire Retirement Plan.

**Table B-17b**  
**5-Year Projections of Healthcare Plans Contributions**  
**(in thousands)**  
**(Throughout the Year)**

<b>Federated Healthcare Plan</b>				
<b>Fiscal Year Ended June 30</b>	<b>Full Benefit Payroll</b>	<b>Total Payroll</b>	<b>Estimated City Contribution Cap</b>	<b>Actuarially Determined Contribution</b>
2020	\$ 131.9	\$ 308.7	\$ 43.2	\$ 21.8
2021	121.7	318.7	44.6	22.1
2022	111.5	329.1	46.1	22.5
2023	102.1	339.8	47.6	22.8
2024	93.6	350.8	49.1	23.0

  

<b>Police and Fire Healthcare Plan</b>				
<b>Fiscal Year Ended June 30</b>	<b>Full Benefit Payroll</b>	<b>Total Payroll</b>	<b>Estimated City Contribution Cap</b>	<b>Actuarially Determined Contribution</b>
2020	\$ 154.4	\$ 225.5	\$ 24.8	\$ 24.0
2021	144.9	232.9	25.6	25.4
2022	134.1	240.4	26.4	27.0
2023	121.8	248.2	27.3	28.2
2024	110.7	256.3	28.1	29.4

*Source: Cheiron 5-Year Budget Projections for Federated Plan, January 9, 2019; Cheiron 5-Year Budget Projections for Police and Fire Department Healthcare Plan, February 27, 2019.*



**Federated Healthcare Plan Funding Policy.** Effective March 25, 2018, the Tier 1 and Tier 2 members in the Federated Healthcare Plan who opted to remain in the Federated Healthcare Plan contribute 7.5% of pay. The City continued to pay the phased-in contribution rate until the beginning of fiscal year 2018-2019. Currently, the City makes the Actuarially Determined Contribution determined by the Federated Board subject to a cap of 14% of payroll of all active members of the Federated Plan, not just active members of the Federated Healthcare Plan. For purposes of calculating the City's contribution for the explicit subsidy UAL, the UAL as of June 30, 2017, is amortized as a level dollar amount over a closed 20-year period. All future UAL amortization bases will be amortized over 20-year periods with a 3-year phase-in and phase-out.

Table B-18 below provides the components of the Actuarially Determined Contribution for the Federated Healthcare Plan for fiscal years 2018-2019 and 2019-2020.

<b>Table B-18</b> <b>Federated Healthcare Plan Actuarially Determined Contribution</b> <b>Explicit Subsidy Only</b> <b>(in thousands)</b>			
	<b>2018-2019</b>	<b>2019-2020</b>	<b>% Change</b>
Normal Cost	\$ 6,238	\$ 6,108	(2.10)
UAL Payment	25,787	25,572	(0.80)
Total Contribution	\$32,025	\$ 31,680	(1.10)
Projected Member Contributions	10,778	9,890	(8.20)
City ADC Amount	\$ 21,247	\$ 21,790	2.60
Projected Total Payroll	\$ 296,678	\$ 308,702	4.10
City ADC Percentage	7.20%	7.10%	(0.10)
<i>Source: Federated 2018 Postemployment Healthcare Actuarial Report; Police and Fire 2018 Postemployment Healthcare Actuarial Report.</i>			



**Police and Fire Healthcare Plan Funding Policy.** Members remaining in the Police and Fire Healthcare Plan make contributions fixed at 8.0% of pay effective March 25, 2018. In fiscal year 2018-2019, the City's contribution toward the explicit subsidy will be actuarially determined separately for Police and Fire, and the City will also pay the implicit subsidy on a pay-as-you-go basis as a part of the active health premiums. For purposes of calculating the City's contribution for the explicit subsidy UAL, the UAL as of June 30, 2017, was amortized as a level percent of payroll over a closed 25-year period. All future UAL amortization bases will be amortized over 25-year periods with a 3-year phase-in and phase-out. In addition, the City has an option to limit its contribution for the explicit subsidy to 11% of Police and Fire Retirement Plan payroll.

Table B-19 below provides the components of the Actuarially Determined Contribution for the Police and Fire Healthcare Plan for fiscal years 2018-2019 and 2019-2020

<b>Table B-19</b> <b>Police and Fire Healthcare Plan Actuarially Determined Contribution</b> <b>(Explicit Subsidy Only)</b> <i>(in thousands)</i>			
	<b>2018-2019</b>	<b>2019-2020</b>	<b>% Change</b>
<b>Police</b>			
Normal Cost	\$ 5,095	\$ 5,728	12.4%
Administrative Expense	0	106	
UAL Payment	15,518	15,632	0.7%
Total Contribution	20,614	21,466	4.1%
Projected Member Contributions	6,891	6,871	(0.3)%
City ADC Amount	\$ 13,723	\$ 14,595	6.4%
Projected Payroll	\$124,209	\$136,175	9.6%
City ADC Percentage	11.0%	10.70%	(3.0%)
<b>Fire</b>			
Normal Cost	\$ 4,571	\$ 4,989	9.2%
Administrative Expense		73	
UAL Payment	9,699	9,822	1.3%
Total Contribution	14,271	14,885	4.3%
Projected Member Contributions	5,519	5,477	(0.8%)
City ADC Amount	\$ 8,752	\$ 9,408	7.5%
Projected Payroll	\$86,231	\$89,354	3.6%
City ADC Percentage	10.1%	10.5%	3.7%
<b>Total</b>			
City ADC Amount	\$ 22,475	\$ 24,003	6.8%
Projected Total Payroll	210,440	225,528	7.2%
City ADC Percentage	10.7%	10.6%	(0.3%)
<i>Source: Police and Fire 2018 Postemployment Healthcare Actuarial Report.</i>			



## Healthcare Plans' Actuarial Valuations and Funding Status

Actuarial valuations of a plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about claim costs, health care trend rates and dependent coverage elections. These measures are intended to be used to assess contribution amounts for an ongoing other post employee benefits plan. They are not appropriate for the assessment of the sufficiency of plan assets to settle the Healthcare Plans' obligations on a risk-free basis because actual events and plan experience may deviate from the assumptions used in the actuarial calculations.

Table B-20a provides the changes in valuations for the prior two fiscal years.

<b>Table B-20a</b> <b>Healthcare Plans' Assets and Liabilities</b> <b>(in thousands)</b>			
	<b>June 30, 2017</b>	<b>June 30, 2018</b>	<b>% Change</b>
<b>Federated Plan</b>			
Total Actuarial Liability	\$ 630,452	\$ 650,114	3.1%
Market Value Assets	248,583	277,256	11.5%
Explicit Subsidy Unfunded Actuarial Liability	299,588	286,450	(4.4%)
Explicit Subsidy Funded Percentage	45.3%	49.2%	8.5%
Total Unfunded Actuarial Liability	381,868	372,858	(2.4%)
Total Funded Percentage	39.4%	42.6%	8.2%
<b>Police and Fire Plan</b>			
Total Actuarial Liability	\$ 680,246	\$ 747,274	9.9%
Market Value Assets	142,517	162,519	14.0%
Explicit Subsidy Unfunded Actuarial Liability	411,382	436,407	6.1%
Explicit Subsidy Funded Percentage	25.7%	27.1%	1.4%
Total Unfunded Actuarial Liability	537,729	584,754	8.7%
Total Funded Percentage	21.0%	21.7%	0.8%
<i>Source: Federated 2018 Postemployment Healthcare Actuarial Report; Police and Fire 2018 Postemployment Healthcare Actuarial Report.</i>			

Table B-20b and Table B-20c provide a comparison of the changes to market value for the prior fiscal years. For the 2017 actuarial valuations for the Healthcare Plans that set the City's contribution for fiscal year 2018-2019 for the respective plan, the Plan Actuary removed the members who elected to transfer to the VEBAs and adjusted the respective Healthcare Plan's assets for an estimated VEBA transfer amount. The actual transfers did not occur until after the 2017 actuarial valuation date, but the Plan Actuary was aware of the VEBA transfers at the time of these valuations. With the 2018 actuarial valuation, the Plan Actuary adjusted the previously estimated VEBA transfer amounts to reflect the actual final VEBA transfer amounts.



**Table B-20b**  
**Federated Healthcare Plan - Market Value of Plan Assets**  
*(in thousands)*

	<b>2016-2017</b>	<b>2017-2018</b>
Market Value, Beginning of Year	\$ 225,845	\$ 260,370
Contributions		
Member	16,827	15,545
City	27,328	28,579
Implicit Subsidy	4,577	3,818
Total	<u>\$ 48,732</u>	<u>\$ 47,942</u>
Net Investment Earnings <sup>(1)</sup>	17,041	12,336
Benefit Payments <sup>(2)</sup>	(31,007)	(29,724)
Admin Expense	(242)	(170)
VEBA Transfer	(0)	(13,497)
<b>Market Value, End of Year</b>	<u><b>\$ 260,370<sup>(3)</sup></b></u>	<u><b>\$ 277,257</b></u>

<sup>(1)</sup> Gross investment earnings less investment expenses.

<sup>(2)</sup> Includes both explicit and implicit subsidies. The implicit subsidy is shown as both a contribution and a payment from the plan, but it is not actually contributed to the trust or paid from the trust. It is paid by the City as a part of active health plan premiums.

<sup>(3)</sup> Total does not sum due to rounding.

Source: Federated 2018 CAFR.

**Table B-20c**  
**Police and Fire Healthcare Plan - Market Value of Plan Assets**  
*(in thousands)*

	<b>2016-2017</b>	<b>2017-2018</b>
Market Value, Beginning of Year	\$ 123,427	\$ 149,682
Contributions		
Member	18,116	16,127
City	19,068	19,666
Implicit Subsidy	1,599	5,716
Total	<u>\$ 38,783</u>	<u>\$ 41,509</u>
Net Investment Earnings <sup>(1)</sup>	12,453	7,071
Benefit Payments <sup>(2)</sup>	(24,799)	(27,686)
Administrative Expenses	(182)	(159)
VEBA Transfer	(0)	(7,897)
<b>Market Value, End of Year</b>	<u><b>\$ 149,682</b></u>	<u><b>\$ 162,520</b></u>

<sup>(1)</sup> Gross investment earnings less investment expenses.

<sup>(2)</sup> Includes both explicit and implicit subsidies. The implicit subsidy is shown as both a contribution and a payment from the plan, but it is not actually contributed to the trust or paid from the trust. It is paid by the City as a part of active health plan premiums.

Source: Police and Fire 2018 CAFR.



**2018 Federated Healthcare Plan Valuation.** As with the Federated Pension Plan, the Plan Actuary performed an actuarial valuation of the Federated Healthcare Plan as of June 30, 2018. The Actuarial Accrued Liability of the Federated Healthcare Plan as of June 30, 2018, is approximately \$650.1 million with approximately \$277.3 million in assets, resulting in a UAL of approximately \$372.9 million (a decrease of approximately \$9.1 million from the prior year). The Actuarial Accrued Liability of the Federated Healthcare Plan, including both the explicit and implicit subsidies, increased by 3%. The Plan Actuary explained that the primary sources of the reduction in the UAL were contributions and plan experience including lower than expected increases in the Medicare eligible premium rates. These UAL reductions were partially offset by aggregate assumption changes, including the discount rate reduction and health trend changes, investment experience and additional transfers to the Federated VEBA. As a result, the UAL decreased by about 2.4% and the funded percentage improved from 39.4% to 42.6%. The Plan Actuary has indicated that if all assumptions are met in the future, including an expected return of 6.75% each year, the funded percentage for the explicit subsidy is expected to exceed 100% by 2038. Because Federated Healthcare Plan contributions are only being made to the Federated 115 Trust and benefits are being paid only from the Federated Healthcare Plan 401(h) accounts, the Plan Actuary has noted that the assets held in the Federated Healthcare Plan 401(h) accounts will be exhausted soon. As such, the Plan Actuary indicated that the expected rate of return for the Federated Healthcare plan should be based primarily on the expected investment return of the Federated 115 Trust reflecting the investment policy of the trust chosen by the Federated Board.

Table B-21 shows the UAL, Funded Ratio and discount rates of the Federated Healthcare Plan from fiscal year 2009-2010 through fiscal year 2017-2018.

<b>Table B-21</b> <b>Federated Healthcare Plan</b> <b>Historical UAL, Funded Ratios and Discount Rates</b> <b>(UAL in millions)</b> <b>(Implicit and Explicit Subsidies)</b>									
	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>	<b>2014</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>
Funded Ratio	13.7%	14.5%	18.6%	23.9%	30.0%	29.1%	30.7%	39.4%	42.6%
UAL	\$ 681.5	\$ 800.5	\$ 604.7	\$ 501.3	\$ 465.2	\$ 511.9	\$ 510.9	\$ 381.9	\$ 372.9
Discount Rate	7.95%	7.50%	7.50%	7.25%	7.00%	7.00%	6.875%	6.875%	6.75%

*Source: Federated Postemployment Healthcare Plan 2018 Actuarial Valuation Report.*

**2018 Police and Fire Healthcare Plan Valuations.** The Plan Actuary performed an actuarial valuation as of June 30, 2018, of the Police and Fire Healthcare Plan, which was presented to the Police and Fire Plan Board at its March, 2019 meeting. The Actuarial Accrued Liability, as of June 30, 2018, was approximately \$747.3 million with approximately \$162.5 million in the actuarial value of assets resulting in a UAL of approximately \$584.8 million (an increase of approximately \$47.0 million from the prior valuation). The Plan Actuary indicated that the primary source of the UAL increase was changes in assumptions, including discount rate and health trend changes. Further, the UAL increased because of investment experience and explicit subsidy contributions less than the Normal Cost and interest on prior UAL. These increases were only offset in part by Police and Fire Healthcare Plan experience. However, the Funded Ratio



increased slightly to 21.7% from 21.0% in the prior valuation. The Plan Actuary has indicated that if all assumptions are met in the future including an expected return of 6.50% each year, the funded percentage for the explicit subsidy is expected to reach 100% by 2044.

Table B-22 shows the UAL, Funded Ratio and discount rates of the Police and Fire Healthcare Plan from fiscal year 2009-2010 through fiscal year 2017-2018.

**Table B-22**  
**Police and Fire Healthcare Plan**  
**Historical UAL, Funded Ratios and Discount Rates**  
*(UAL in millions)*  
*(Implicit and Explicit Subsidies)*

	2010	2011	2012	2013	2014	2015	2016	2017	2018
Funded Ratio	6.2%	6.0%	6.7%	10.7%	13.2%	15.5%	17.4%	21.0%	21.7%
UAL	\$ 887.7	\$ 943.1	\$ 930.9	\$ 625.5	\$ 613.1	\$ 625.2	\$ 643.7	\$ 537.7	\$ 584.8
Discount Rate	7.75%	7.50%	7.25%	7.125%	7.00%	7.00%	6.875%	6.875%	6.50%

*Source: Police and Fire Healthcare Plan 2018 Actuarial Valuation Report; Cheiron Inc.*

### **Funding Progress - Net OPEB Liability**

In fiscal year 2016-2017, the Retirement Plans implemented GASB Statement No. 74. The City implemented GASB Statement No. 75 in fiscal year 2017-2018. GASB Statements No. 74 and 75 require the Retirement Plans and the City respectively to report Net OPEB Liability in their respective financial statements. Net OPEB Liability is measured as the Total OPEB Liability less the OPEB plan fiduciary net position. The City financial statements calculate Net OPEB Liability using a measurement date that is one year prior to the measurement date used for the Plans financial statements. As a result, the Plans financial statements show Net OPEB Liability one year later in date.

The Total OPEB Liability as of June 30, 2018 and 2017 shown in Table B-23 is based on results of an actuarial valuation date of June 30, 2017 and 2016, rolled-forward to June 30, 2018 and 2017, using generally accepted actuarial procedures. Using a measurement date of June 30, 2018, Net OPEB Liability was \$374.0 million for the Federated Healthcare Plan and approximately \$549.3 million for the Police and Fire Healthcare Plan.

The Plan Actuary in its most recent valuations of the Healthcare Plans indicated that following the implementation of GASB Statement No. 75, the annual OPEB expense may be very volatile; however, the changes required by GASB Statement No. 75 do not necessarily alter City contribution policy. OPEB expense recognizes deferred outflows of resources and deferred inflows of resources related to OPEB over a defined, closed period, rather than a choice between an open or closed period. As a result of the implementation of GASB Statement No. 75, the fiscal year 2016-2017 net OPEB obligation under GASB Statement No. 45 was replaced with the Net OPEB Liability in the City's BASIC FINANCIAL STATEMENTS FOR THE FISCAL YEAR ENDED JUNE 30, 2018 attached as Appendix A. Note that for purposes of financial reporting by the City pursuant to GASB Statement No. 75, the Net OPEB Liability as of June 30 of a given fiscal year is measured as of the end of the previous fiscal year.



**Table B-23**  
**Components of Net OPEB Liability**  
**(in thousands)**

	<u>June 30, 2017</u>	<u>June 30, 2018</u>	<u>% Change</u>
<b>Federated Healthcare Plan</b>			
Total OPEB Liability	\$ 766,801	\$ 651,222	15.1%
Plan fiduciary net position	(260,370)	(277,257)	6.5%
Net OPEB Liability	\$ 506,431	\$ 373,965	(26.2%)
Plan fiduciary net position as a percentage of the Total OPEB Liability	34.0%	42.6%	25.3%
<b>Police and Fire Healthcare Plan</b>			
Total OPEB Liability	\$ 714,517	\$ 711,832	(0.4%)
Plan fiduciary net position	(149,682)	(162,520)	8.6%
Net OPEB Liability	\$ 564,835	\$ 549,312	(2.8%)
Plan fiduciary net position as a percentage of the Total OPEB Liability	21.0%	22.8%	8.6%

*Source: Federated 2018 CAFR; Police and Fire 2018 CAFR.*

### Actuarial Funding Progress

The actuarial determinations of funding status for the last ten years for the Healthcare Plans are summarized in Table B-24a. The schedule of funding progress compares the assets used for funding purposes to the comparable liabilities to determine how well the Healthcare Plans are funded and how this status has changed over the past several years. The Actuarial Accrued Liability is compared to the Actuarial Value of Assets to determine the Funded Ratio. The schedule of funding progress for the Federated Healthcare Plan is set forth in Table B-24b and for the Police and Fire Healthcare Plan is set forth in Table B-24c.

As shown in Table B-24a, the Healthcare Plans have shown a steady increase in Funded Ratio since 2009, but both Healthcare Plans remain substantially underfunded. Please note that prior to fiscal year 2015-2016, the UAL of the Police and Fire Healthcare Plan shown in Tables B-24a and B-24c was calculated based on the actuarial value of assets of such plan. The UAL of the Federated Healthcare Plan shown in Tables B-24a and B-24b for each year was calculated based on the market value of assets of the plan. As a result, the UAL and Funded Ratio for the respective Healthcare Plan reflect differing actuarial calculation methodologies. These ratios are not appropriate for measuring or assessing the solvency of the Healthcare Plans or the sufficiency of Healthcare Plan assets to cover the estimated cost of settling the Healthcare Plans' benefit obligations on a risk free basis because actual events and plan experience may deviate from the assumptions used in the actuarial calculations.



**Table B-24a**  
**Healthcare Plans Schedule of Funding Progress**  
*(in thousands)*

Fiscal Year Ended June 30	Federated Healthcare Plan		Police and Fire Healthcare Plan		Total
	UAL	Funded Ratio	UAL	Funded Ratio	UAL
2009	\$ 710,884	11%	\$ 705,986	7.3%	\$ 1,416,870
2010	818,360	12	887,722	6.2	1,706,082
2011	1,009,906	12	943,087	6.0	1,952,993
2012	958,822	13	930,936	6.7	1,889,758
2013	713,177	18	625,490	10.7	1,338,667
2014	529,630	27	613,105	13.2	1,142,735
2015	607,912	26	625,188	15.5	1,233,100
2016	538,416	30	643,664	17.4	1,182,080
2017	381,869	39	537,729	21.0	919,598
2018	372,858	43	584,755	21.7	957,613

Source: 2018 Federated Postemployment Healthcare Plan Actuarial Report; Police and Fire Healthcare Plan 2018 Actuarial Report.

**Federated 2018 Funding Progress.** Table B-24b shows an overall decrease in Actuarial Accrued Liability and UAL for the Federated Healthcare Plan from Fiscal year 2009-2010 through fiscal year 2017-2018. The Funded Ratio of the Federated Healthcare Plan has as a result substantially increased during this period from 12% to 43%.

**Table B-24b**  
**Federated Healthcare Plan - Schedule of OPEB Funding Progress**  
*(in thousands)*

Valuation Date (June 30)	Market Value of Assets	Actuarial Liability	UAL	Funded Ratio	Covered Payroll	UAL as % of Covered Payroll
2010	\$ 108,011	\$ 926,371	\$818,360	12%	\$ 300,069	273%
2011	135,454	1,145,360	1,009,906	12	228,936	441
2012	137,798	1,096,620	958,822	13	225,859	425
2013	157,695	870,872	713,177	18	226,098	315
2014	199,776	729,406	529,630	27	234,677	226
2015	209,761	817,673	607,912	26	251,430	242
2016	225,845	764,261	538,416	30	266,823	202
2017	248,583	630,452	381,869	39	287,339	133
2018	277,256	650,114	372,858	43	298,985	125

Source: Federated 2018 Postemployment Healthcare Plan Actuarial Report.



**Police and Fire Funding Progress.** Although the Actuarial Accrued Liability and UAL for the Police and Fire Healthcare Plan increased in fiscal year 2017-2018, the Actuarial Accrued Liability and UAL have substantially decreased since the June 30, 2010 valuation date. The Funded Ratio has seen a gradual increase during this period, but still shows significant underfunding.

**Table B-24c**  
**Police and Fire Healthcare Plan - Schedule of OPEB Funding Progress**  
*(in thousands)*

<b>Valuation Date (June 30)</b>	<b>Market Value of Assets<sup>(1)</sup></b>	<b>Actuarial Liability</b>	<b>UAL</b>	<b>Funded Ratio</b>	<b>Covered Payroll</b>	<b>UAL as % of Covered Payroll</b>
2010	\$ 58,586	\$ 946,308	\$ 887,722	6.2%	\$ 222,699	399%
2011	60,709	1,003,795	943,086	6.0	190,726	494
2012	66,385	997,321	930,936	6.7	172,626	539
2013	75,035	700,525	625,490	10.7	184,645	339
2014	93,605	706,710	613,105	13.2	188,189	326
2015	114,565	739,753	625,188	15.5	184,733	338
2016	135,207	778,871	643,664	17.4	194,072	332
2017	142,517	680,246	537,729	21.0	203,816	264
2018	162,519	747,274	584,755	21.7	218,429	268

<sup>(1)</sup> Actuarial value of assets prior to fiscal year 2015-2016 and earlier.

Source: Police and Fire 2018 Postemployment Healthcare Plan Actuarial Report.

## Healthcare Plans' Actuarial Assumptions

Actuarial assumptions used for the valuations for the health and dental benefits provided by the Federated Healthcare Plan and the Police and Fire Healthcare Plan are generally the same as are used for the valuations of the Pension Plans, but also include assumptions with respect to future healthcare utilization and inflation. Tables B-25a and B-25b set forth the significant actuarial valuation methods and assumptions used for the June 30, 2018 valuations of the Federated Healthcare Plan and Police and Fire Healthcare Plan. The valuations reflect the changes to the Healthcare Plans, such as membership and contributions implemented as part of Measure F and the Settlement Frameworks.



**Table B-25a**  
**Federated Healthcare Plan – Healthcare Actuarial Assumptions**

Valuation Date	June 30, 2018
Actuarial cost method	Entry Age Normal
Amortization method	Level dollar, closed, layers
Amortization period	20 Years -3 year phase in and out
Asset valuation method <sup>(1)</sup>	Market Value
Actuarial Assumptions:	
Payroll Growth Rate	3.25%
Discount Rate	6.75%

<sup>(1)</sup> The market value of assets means the actual value of assets, and not the smoothed value, is used.  
Source: Federated 2018 Postemployment Healthcare Actuarial Report.

**Table B-25b**  
**Police and Fire Plan – Healthcare Actuarial Assumptions**

Valuation Date	June 30, 2018
Actuarial cost method	Entry Age Normal
Amortization method	Level percent of pay, closed, layers
Amortization period	25 Years -3 year phase in and out
Asset valuation method <sup>(1)</sup>	Market Value
Actuarial Assumptions:	
Payroll Growth Rate	3.25%
Discount Rate	6.50%

<sup>(1)</sup> The market value of assets means the actual value of assets, and not the smoothed value, is used.  
Source: Police and Fire 2018 Postemployment Healthcare Actuarial Report.



## Investments

The Boards of both Healthcare Plans currently utilize the investment policies and asset allocations of the respective Pension Plans for the 401(h) portion of the Healthcare Plans. In addition, the City has established Code Section 115 Trusts as a supplement to the 401(h) accounts, both of which are funded as described above in “Establishment of 115 Trusts For Healthcare Plans; Tax Limitations.” Table B-26a below illustrates the historic annual returns net of fees for both Healthcare Plans at the identified interval as reported by the Healthcare Plans’ respective investment consultants in their respective quarterly reports for the period ending December 31, 2018.

<b>Table B-26a</b> <b>Historical Investment Performance For Healthcare Plans</b> <b>(As December 31, 2018)</b>		
<b>Measurement Period</b>	<b>Federated Healthcare Plan</b>	<b>Police and Fire Healthcare Plan</b>
Since Inception	3.7% <sup>(1)</sup>	3.4% <sup>(2)</sup>
10 Years	-	-
5 Years	1.7	2.1
3 Years	3.8	3.0
1 Year	(5.1)	(6.5)

<sup>(1)</sup> Measurement Period Beginning July 2011.  
<sup>(2)</sup> Measurement Period Beginning July 2012.  
Source: Meketa Investment Group Federated Retiree Healthcare 115 Trust Quarterly Review December 31, 2018; Meketa Investment Group Police and Fire Retiree Healthcare 115 Trust Quarterly Review December 31, 2018.

Due to the smaller asset size of the 115 trusts, as compared to the Pension Plans, the Investment Managers of the respective Boards advised the use of asset allocations different from the allocations applicable to the Pension Plans’ investments, including the 401(h) accounts. The Healthcare Plans most recent target allocations for the 115 Trust only are shown in Tables B-26b and B-26c.

<b>Table B-26b</b> <b>Federated Healthcare Plan 115 Trust Target Asset Allocation</b>			
<b>Asset Class</b>	<b>Minimum %</b>	<b>Target %</b>	<b>Maximum %</b>
Global Equity	40	55	54
Fixed Income	20	28	40
Real Assets	15	17	30
Total		100	

Source: Federated 2018 CAFR.



**Table B-26c**  
**Police and Fire Healthcare Plan 115 Trust Target Asset Allocation**

<b>Asset Class</b>	<b>Minimum %</b>	<b>Target %</b>	<b>Maximum %</b>
Equity	25	43	50
Fixed Income	5	15	25
Inflation Linked Absolute Return/Global Tactical Asset	12	22	25
Allocation	0	20	25
Cash	0	0	5
Total		100	

*Source: Police and Fire 2018 CAFR.*



## **APPENDIX C**

### **BASIC FINANCIAL STATEMENTS FOR THE FISCAL YEAR ENDED JUNE 30, 2018**



## APPENDIX E

## FORM OF CONTINUING DISCLOSURE CERTIFICATE

\$ \_\_\_\_\_  
 GENERAL OBLIGATION BONDS,  
 SERIES 2019A-1  
 (DISASTER PREPAREDNESS, PUBLIC  
 SAFETY, AND INFRASTRUCTURE)

\$ \_\_\_\_\_  
 TAXABLE GENERAL OBLIGATION BONDS,  
 SERIES 2019A-2  
 (DISASTER PREPAREDNESS, PUBLIC  
 SAFETY, AND INFRASTRUCTURE)

\$ \_\_\_\_\_  
 TAXABLE GENERAL OBLIGATION BONDS,  
 SERIES 2019B  
 (DISASTER PREPAREDNESS, PUBLIC SAFETY, AND INFRASTRUCTURE)

\$ \_\_\_\_\_  
 GENERAL OBLIGATION BONDS,  
 SERIES 2019C  
 (REFUNDING, LIBRARIES, PARKS, AND  
 PUBLIC SAFETY PROJECTS)

\$ \_\_\_\_\_  
 TAXABLE GENERAL OBLIGATION BONDS,  
 SERIES 2019D  
 (REFUNDING, LIBRARIES, PARKS, AND  
 PUBLIC SAFETY PROJECTS)

This Continuing Disclosure Certificate (the "Disclosure Certificate") is executed and delivered by the City of San José (the "City") in connection with the issuance by the City of the bonds captioned-above (collectively, the "Bonds"). The Bonds are being issued pursuant to a resolution adopted by the City Council of the City on June [25], 2019 and a Fiscal Agent Agreement (the "Fiscal Agent Agreement"), dated as of July 1, 2019, by and between the City and Wilmington Trust, National Association, as fiscal agent (the "Fiscal Agent").

The City hereby covenants and agrees as follows:

**Section 1. Purpose of the Disclosure Certificate.** This Disclosure Certificate is being executed and delivered by the City for the benefit of the holders and beneficial owners of the Bonds and in order to assist the Participating Underwriter in complying with S.E.C. Rule 15c2-12(b)(5).

**Section 2. Definitions.** In addition to the definitions set forth above and in the Fiscal Agent Agreement, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section 2, the following capitalized terms have the following meanings:

*"Annual Report"* means any Annual Report provided by the City pursuant to, and as described in, Sections 3 and 4.

*"Annual Report Date"* means the date not later than April 1 after the end of each fiscal year of the City (currently June 30<sup>th</sup>).

*"Current Fiscal Year"* means the then current fiscal year as of an Annual Report Date. For example, with respect to the Annual Report Date of April 1, 2020, the Current Fiscal Year means the 2019-20 fiscal year.



*“Dissemination Agent”* means the City or any other Dissemination Agent designated in writing by the City and which has filed with the City a written acceptance of such designation. As of the date of this Disclosure Certificate, the City is acting as Dissemination Agent.

*“Listed Events”* means any of the events listed in Section 5(a).

*“MSRB”* means the Municipal Securities Rulemaking Board, which has been designated by the Securities and Exchange Commission as the sole repository of disclosure information for purposes of the Rule.

*“Official Statement”* means the final official statement executed by the City in connection with the issuance of the Bonds.

*“Participating Underwriter”* means any of the original purchasers of the Bonds required to comply with the Rule in connection with offering of the Bonds.

*“Preceding Fiscal Year”* means the most recently ended fiscal year preceding an Annual Report Date. For example, with respect to the Annual Report Date of April 1, 2020, the Preceding Fiscal Year means the 2018-19 fiscal year.

*“Rule”* means Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

### **Section 3. Provision of Annual Reports.**

(a) The City shall, or shall cause the Dissemination Agent to, not later than the Annual Report Date, commencing April 1, 2020 with the report for the 2018-19 fiscal year, provide to the MSRB in an electronic format as prescribed by the MSRB, an Annual Report that is consistent with the requirements of Section 4 of this Disclosure Certificate. Not later than 15 Business Days prior to the Annual Report Date, the City shall provide the Annual Report to the Dissemination Agent (if other than the City). If by 15 Business Days prior to the Annual Report Date the Dissemination Agent (if other than the City) has not received a copy of the Annual Report, the Dissemination Agent shall contact the City to determine if the City is in compliance with the previous sentence. The Annual Report may be submitted as a single document or as separate documents comprising a package, and may include by reference other information as provided in Section 4 of this Disclosure Certificate; provided that the audited financial statements of the City may be submitted separately from the balance of the Annual Report, and later than the Annual Report Date, if not available by that date. If the City’s fiscal year changes, it shall give notice of such change in the same manner as for a Listed Event under Section 5(b). The City shall provide a written certification with each Annual Report furnished to the Dissemination Agent to the effect that such Annual Report constitutes the Annual Report required to be furnished by the City hereunder.

(b) If the City does not provide (or cause the Dissemination Agent to provide) an Annual Report by the Annual Report Date, the City shall provide (or cause the Dissemination Agent to provide) to the MSRB, in an electronic format as prescribed by the MSRB, a notice in substantially the form attached as Exhibit A.



- (c) With respect to each Annual Report, the Dissemination Agent shall:
  - (i) determine each year prior to the Annual Report Date the then-applicable rules and electronic format prescribed by the MSRB for the filing of annual continuing disclosure reports; and
  - (ii) if the Dissemination Agent is other than the City, file a report with the City certifying that the Annual Report has been provided pursuant to this Disclosure Certificate, and stating the date it was provided.

**Section 4. Content of Annual Reports.** The City's Annual Report shall contain or incorporate by reference the following:

(a) The City's audited financial statements prepared in accordance with generally accepted accounting principles as promulgated to apply to governmental entities from time to time by the Governmental Accounting Standards Board for the Preceding Fiscal Year. If the City's audited financial statements are not available by the Annual Report Date, the Annual Report shall contain unaudited financial statements in a format similar to the financial statements contained in the final Official Statement, and the audited financial statements shall be filed in the same manner as the Annual Report when they become available.

(b) Unless otherwise provided in the audited financial statements filed on or before the Annual Report Date, financial information and operating data with respect to the City for the Preceding Fiscal Year or Current Fiscal Year, as specified below, substantially similar to that provided in the Official Statement:

- (i) The budget transmittal letter of the City for the Current Fiscal Year, together with summary information relating to the City's operating budget for the Current Fiscal Year, historical and trend information relating to the City's operating budgets, and budget policies and practices relating to the City's operating budgets, but only to the extent such material is prepared by the City in connection with the Current Fiscal Year's operating budget;
- (ii) Changes, if any, in the operation of the County of Santa Clara's Teeter Plan affecting the City;
- (iii) Assessed value of taxable property within the jurisdiction of the City for the Current Fiscal Year;
- (iv) Property tax collection delinquencies for the Preceding Fiscal Year for the City if the City is no longer a participant in the County of Santa Clara's Teeter Plan;
- (v) Amount of all general obligation debt of the City outstanding, and total scheduled debt service on such general obligation debt as of the preceding June 30; and
- (vii) The top ten real property tax assesses of the City for the Current Fiscal Year, the total taxable value for the Current Fiscal Year, and the percentage of total assessed value for each of the top ten real property assesses for the Current Fiscal Year.



(c) In addition to any of the information expressly required to be provided under this Disclosure Certificate, the City shall provide such further material information, if any, as may be necessary to make the specifically required statements, in the light of the circumstances under which they are made, not misleading.

(d) Any or all of the items listed above may be included by specific reference to other documents, including official statements of debt issues of the City or related public entities, which are available to the public on the MSRB's internet web site or filed with the Securities and Exchange Commission. The City shall clearly identify each such other document so included by reference.

#### **Section 5. Reporting of Significant Events.**

(a) The City shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds:

- (1) Principal and interest payment delinquencies.
- (2) Non-payment related defaults, if material.
- (3) Unscheduled draws on debt service reserves reflecting financial difficulties.
- (4) Unscheduled draws on credit enhancements reflecting financial difficulties.
- (5) Substitution of credit or liquidity providers, or their failure to perform.
- (6) Adverse tax opinions, the issuance by the Internal Revenue Service of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB) or other material notices or determinations with respect to the tax status of the security, or other material events affecting the tax status of the security.
- (7) Modifications to rights of security holders, if material.
- (8) Bond calls, if material, and tender offers.
- (9) Defeasances.
- (10) Release, substitution, or sale of property securing repayment of the securities, if material.
- (11) Rating changes.
- (12) Bankruptcy, insolvency, receivership or similar event of the City or other obligated person.
- (13) The consummation of a merger, consolidation, or acquisition involving the City or an obligated person, or the sale of all or substantially all of the assets of the City or an obligated person (other than in the ordinary course of business), the entry into a definitive agreement to undertake such an action, or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material.
- (14) Appointment of a successor or additional trustee or the change of name of a trustee, if material.



- (15) Incurrence of a financial obligation of the City, if material, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the City or an obligated person, any of which affect security holders, if material.
- (16) Default, event of acceleration, termination event, modification of terms, or other similar events under the terms of a financial obligation of the City, any of which reflect financial difficulties.

(b) Whenever the City obtains knowledge of the occurrence of a Listed Event, the City shall, or shall cause the Dissemination Agent (if not the City) to, file a notice of such occurrence with the MSRB, in an electronic format as prescribed by the MSRB, in a timely manner not in excess of 10 business days after the occurrence of the Listed Event. Notwithstanding the foregoing, notice of Listed Events described in subsections (a)(8) and (9) above need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to holders of affected Bonds under the Fiscal Agent Agreement.

(c) The City acknowledges that the events described in subparagraphs (a)(2), (a)(7), (a)(8) (if the event is a bond call), (a)(10), (a)(13), (a)(14) and (a)(15) of this Section 5 contain the qualifier “if material.” The City shall cause a notice to be filed as set forth in paragraph (b) above with respect to any such event only to the extent that the City determines the event’s occurrence is material for purposes of U.S. federal securities law.

(d) For purposes of this Disclosure Certificate, any event described in paragraph (a)(12) above is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent, or similar officer for the City in a proceeding under the United States Bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the City, or if such jurisdiction has been assumed by leaving the existing governing body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement, or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the City.

(e) For purposes of Section 5(a)(15) and (16), “financial obligation” means a (i) debt obligation; (ii) derivative instrument entered into in connection with, or pledged as security or a source of payment for, an existing or planned debt obligation; or (iii) guarantee of (i) or (ii). The term financial obligation shall not include municipal securities as to which a final official statement has been provided to the Municipal Securities Rulemaking Board consistent with the Rule.

**Section 6. Identifying Information for Filings with the MSRB.** All documents provided to the MSRB under the Disclosure Certificate shall be accompanied by identifying information as prescribed by the MSRB.

**Section 7. Termination of Reporting Obligation.** The City’s obligations under this Disclosure Certificate shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Bonds. If such termination occurs prior to the final maturity of the Bonds, the City shall give notice of such termination in the same manner as for a Listed Event under Section 5(b).

**Section 8. Dissemination Agent.** The City may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out its obligations under this Disclosure Certificate,



and may discharge any Dissemination Agent, with or without appointing a successor Dissemination Agent. Any Dissemination Agent may resign by providing 30 days' written notice to the City.

**Section 9. Amendment; Waiver.** Notwithstanding any other provision of this Disclosure Certificate, the City may amend this Disclosure Certificate, and any provision of this Disclosure Certificate may be waived, provided that the following conditions are satisfied:

- (a) if the amendment or waiver relates to the provisions of Sections 3(a), 4 or 5(a), it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature, or status of an obligated person with respect to the Bonds, or type of business conducted;
- (b) the undertakings herein, as proposed to be amended or waived, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the primary offering of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and
- (c) the proposed amendment or waiver either (i) is approved by holders of the Bonds in the manner provided in the Fiscal Agent Agreement for amendments to the Fiscal Agent Agreement with the consent of holders, or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the holders or beneficial owners of the Bonds.

If the annual financial information or operating data to be provided in the Annual Report is amended pursuant to the provisions hereof, the first annual financial information filed pursuant hereto containing the amended operating data or financial information shall explain, in narrative form, the reasons for the amendment and the impact of the change in the type of operating data or financial information being provided.

If an amendment is made to the undertaking specifying the accounting principles to be followed in preparing financial statements, the annual financial information for the year in which the change is made shall present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles. The comparison shall include a qualitative discussion of the differences in the accounting principles and the impact of the change in the accounting principles on the presentation of the financial information, in order to provide information to investors to enable them to evaluate the ability of the City to meet its obligations. To the extent reasonably feasible, the comparison shall be quantitative. A notice of the change in the accounting principles shall be filed in the same manner as for a Listed Event under Section 5(b).

**Section 10. Additional Information.** Nothing in this Disclosure Certificate shall be deemed to prevent the City from disseminating any other information, using the means of dissemination set forth in this Disclosure Certificate or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Certificate. If the City chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Certificate, the City shall have no obligation under this



Disclosure Certificate to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event.

**Section 11. Default.** If the City fails to comply with any provision of this Disclosure Certificate, the Participating Underwriter or any holder or beneficial owner of the Bonds may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the City to comply with its obligations under this Disclosure Certificate. A default under this Disclosure Certificate shall not be deemed an Event of Default under the Fiscal Agent Agreement, and the sole remedy under this Disclosure Certificate in the event of any failure of the City to comply with this Disclosure Certificate shall be an action to compel performance.

**Section 12. Duties, Immunities and Liabilities of Dissemination Agent.**

(a) The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Certificate, and the City agrees to indemnify and save the Dissemination Agent, its officers, directors, employees and agents, harmless against any loss, expense and liabilities which they may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's negligence or willful misconduct. The Dissemination Agent shall have no duty or obligation to review any information provided to it by the City hereunder, and shall not be deemed to be acting in any fiduciary capacity for the City, the Bond holders or any other party. The obligations of the City under this Section shall survive resignation or removal of the Dissemination Agent and payment of the Bonds.

(b) The Dissemination Agent shall be paid compensation by the City for its services provided hereunder in accordance with its schedule of fees as amended from time to time, and shall be reimbursed for all expenses, legal fees and advances made or incurred by the Dissemination Agent in the performance of its duties hereunder.

**Section 13. Notices.** Any notice or communications to be among any of the parties to this Disclosure Certificate may be given as follows:

To the City:

City of San José - Finance  
Debt Management  
200 East Santa Clara Street, 13<sup>th</sup> Floor Tower  
San José, California 95113-1905  
Debt.Management@sanjoseca.gov

Any person may, by written notice to the other persons listed above, designate a different address or telephone number(s) to which subsequent notices or communications should be sent.

**Section 14. Beneficiaries.** This Disclosure Certificate shall inure solely to the benefit of the City, the Dissemination Agent, the Participating Underwriter and holders and beneficial owners from time to time of the Bonds, and shall create no rights in any other person or entity.



**Section 15. Counterparts.** This Disclosure Certificate may be executed in several counterparts, each of which shall be regarded as an original, and all of which shall constitute one and the same instrument.

Date: \_\_\_\_\_, 2019

**CITY OF SAN JOSE**

By: \_\_\_\_\_  
Julia H. Cooper  
Director of Finance

**APPROVED AS TO FORM:**  
Richard Doyle, City Attorney

By: \_\_\_\_\_  
Danielle Kenealey  
Chief Deputy City Attorney



## EXHIBIT A

### NOTICE OF FAILURE TO FILE ANNUAL REPORT

Name of Issuer: City of San José (the "City")

Name of Bond Issue: City of San José General Obligation Bonds, Series 2019A-1  
(Disaster Preparedness, Public Safety, and Infrastructure)

City of San José Taxable General Obligation Bonds, Series  
2019A-2 (Disaster Preparedness, Public Safety, and  
Infrastructure)

City of San José Taxable General Obligation Bonds, Series  
2019B (Disaster Preparedness, Public Safety, and  
Infrastructure)

City of San José General Obligation Bonds, Series 2019C  
(Refunding, Libraries, Parks, and Public Safety Projects)

City of San José Taxable General Obligation Bonds, Series 2019D  
(Refunding, Libraries, Parks, and Public Safety Projects)

Date of Issuance: \_\_\_\_\_, 2019

NOTICE IS HEREBY GIVEN that the City has not provided an Annual Report with respect to the above-named Bonds as required by the Continuing Disclosure Certificate, dated \_\_\_\_\_, 2019. The City anticipates that the Annual Report will be filed by \_\_\_\_\_.

Date: [DISSEMINATION AGENT]

By: \_\_\_\_\_

Name:

Title:



## **APPENDIX F DTC AND THE BOOK-ENTRY-ONLY SYSTEM**

*The following description of the Depository Trust Company (“DTC”), the procedures and record keeping with respect to beneficial ownership interests in the Bonds, payment of principal, interest and other payments on the Bonds to DTC Participants or Beneficial Owners, confirmation and transfer of beneficial ownership interest in the Bonds and other related transactions by and between DTC, the DTC Participants and the Beneficial Owners is based solely on information provided by DTC. Accordingly, no representations can be made concerning these matters and neither the DTC Participants nor the Beneficial Owners should rely on the foregoing information with respect to such matters, but should instead confirm the same with DTC or the DTC Participants, as the case may be.*

*Neither the issuer of the Bonds (the “Issuer”) nor the trustee, fiscal agent or paying agent appointed with respect to the Bonds (the “Agent”) take any responsibility for the information contained in this Appendix.*

*No assurances can be given that DTC, DTC Participants or Indirect Participants will distribute to the Beneficial Owners (a) payments of interest, principal or premium, if any, with respect to the Bonds, (b) certificates representing ownership interest in or other confirmation or ownership interest in the Bonds, or (c) redemption or other notices sent to DTC or Cede & Co., its nominee, as the registered owner of the Bonds, or that they will so do on a timely basis, or that DTC, DTC Participants or DTC Indirect Participants will act in the manner described in this Appendix. The current “Rules” applicable to DTC are on file with the Securities and Exchange Commission and the current “Procedures” of DTC to be followed in dealing with DTC Participants are on file with DTC.*

1. The Depository Trust Company (“DTC”), will act as securities depository for the securities (the “Securities”). The Securities will be issued as fully-registered securities registered in the name of Cede & Co. (DTC’s partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Security certificate will be issued for each issue of the Securities, each in the aggregate principal amount of such issue, and will be deposited with DTC. If, however, the aggregate principal amount of any issue exceeds \$500 million, one certificate will be issued with respect to each \$500 million of principal amount, and an additional certificate will be issued with respect to any remaining principal amount of such issue.

2. DTC, the world’s largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC’s participants (“Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and



dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has a Standard & Poor's rating of AA+. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found on its website. The information contained on this Internet site is not incorporated herein by reference.

3. Purchases of Securities under the DTC system must be made by or through Direct Participants, which will receive a credit for the Securities on DTC's records. The ownership interest of each actual purchaser of each Security ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Securities are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Securities, except in the event that use of the book-entry system for the Securities is discontinued.

4. To facilitate subsequent transfers, all Securities deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Securities with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Securities; DTC's records reflect only the identity of the Direct Participants to whose accounts such Securities are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

5. Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of Securities may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Securities, such as redemptions, tenders, defaults, and proposed amendments to the Security documents. For example, Beneficial Owners of Securities may wish to ascertain that the nominee holding the Securities for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.



6. Redemption notices will be sent to DTC. If less than all of the Securities within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

7. Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Securities unless authorized by a Direct Participant in accordance with DTC's MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to Issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Securities are credited on the record date (identified in a listing attached to the Omnibus Proxy).

8. Redemption proceeds, distributions, and dividend payments on the Securities will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from Issuer or Agent, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, Agent, or Issuer, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of Issuer or Agent, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

9. DTC may discontinue providing its services as depository with respect to the Securities at any time by giving reasonable notice to Issuer or Agent. Under such circumstances, in the event that a successor depository is not obtained, Security certificates are required to be printed and delivered.

10. Issuer may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, Security certificates will be printed and delivered to DTC.

11. The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that Issuer believes to be reliable, but Issuer takes no responsibility for the accuracy thereof.