

PRELIMINARY OFFICIAL STATEMENT DATED _____, 2020

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, interest on the Bonds is exempt from State of California personal income taxes. Bond counsel observes that interest on the Bonds is not excluded from gross income for federal income tax purposes. Bond Counsel expresses no opinion regarding any other tax consequences caused by the ownership or disposition of, or the accrual or receipt of interest on, the Bonds. See "TAX MATTERS" herein."



\$ _____ *

CITY OF SAN JOSE FINANCING AUTHORITY
TAXABLE LEASE REVENUE BONDS, SERIES 2020B
(ICE CENTRE PROJECT)

Dated: Date of Delivery

Due: June 1, as shown on inside cover

Authority for Issuance. The bonds captioned above (the "Bonds") are being issued by the City of San José Financing Authority (the "Authority") under a resolution adopted by the Board of Directors of the Authority on August 25, 2020, and an Indenture of Trust dated as of October 1, 2020 (the "Indenture"), by and between the Authority and Wilmington Trust, National Association, as trustee (the "Trustee"). See "THE BONDS – Authority for Issuance."

Purpose. The Bonds are being issued primarily to (i) refinance on a current basis the outstanding Taxable Lease Revenue Bonds, Series 2008E-1 (Ice Centre Refunding Project) and Taxable Lease Revenue Bonds, Series 2008E-2 (Ice Centre Refunding Project) of the Authority and the related lease payment obligation of the City of San José (the "City"), (ii) finance the acquisition and construction of public improvements, (iii) fund a deposit to a debt service reserve account for the Bonds, (iv) fund capitalized interest on the Bonds, and (v) pay the costs of issuing the Bonds. See "FINANCING PLAN."

Security. Under the Indenture, the Bonds are payable from and secured by a first pledge of and lien on "Revenues" (as defined in this Official Statement) received by the Authority under the Lease Agreement, dated as of October 1, 2020, by and between the Authority, as lessor, and the City, as lessee (the "Lease"), consisting primarily of lease payments (the "Lease Payments") made by the City under the Lease with respect to the lease of certain real property, as further described in this Official Statement. The Bonds are also secured by certain funds on deposit under the Indenture, including a debt service reserve account for the Bonds. See "SECURITY FOR 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 ("DTC"). The Bonds are issuable as fully registered securities in denominations of \$5,000 or any integral multiple of \$5,000. Purchasers of the Bonds (the "Beneficial Owners") will not receive physical certificates representing their interest in the Bonds. See "THE BONDS" and APPENDIX G.

Payments. Interest on the Bonds accrues from the date of delivery and is payable semiannually on June 1 and December 1 of each year, commencing [June 1, 2021]. Payments of principal and interest on the Bonds will be paid by the Trustee to DTC for subsequent disbursement to DTC Participants, which will remit such payments to the Beneficial Owners of the Bonds. See "THE BONDS – General Provisions."

Redemption. The Bonds are subject to optional redemption, mandatory sinking fund payment redemption and special mandatory redemption from insurance or condemnation proceeds prior to maturity. See "THE BONDS – Redemption."

NONE OF THE BONDS, THE OBLIGATION OF THE AUTHORITY TO PAY PRINCIPAL OF OR INTEREST THEREON, OR THE OBLIGATION OF THE CITY TO MAKE THE LEASE PAYMENTS CONSTITUTE A DEBT OR A LIABILITY OF THE AUTHORITY, THE CITY, THE STATE OF CALIFORNIA OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL LIMITATION ON INDEBTEDNESS, OR A PLEDGE OF THE FULL FAITH AND CREDIT OF THE CITY. THE BONDS ARE SECURED SOLELY BY THE PLEDGE OF REVENUES AND CERTAIN FUNDS HELD UNDER THE INDENTURE. THE BONDS ARE NOT SECURED BY A PLEDGE OF THE TAXING POWER OF THE CITY.

MATURITY SCHEDULE
(see inside cover)

THIS COVER PAGE CONTAINS CERTAIN INFORMATION FOR GENERAL REFERENCE ONLY. IT IS NOT A SUMMARY OF THIS ISSUE OF BONDS. INVESTORS MUST READ THE ENTIRE OFFICIAL STATEMENT TO OBTAIN INFORMATION ESSENTIAL TO THE MAKING OF AN INFORMED INVESTMENT DECISION WITH RESPECT TO THE PURCHASE OF THE BONDS.

The Bonds are offered when, as and if issued and received by the Underwriters and subject to the approval as to their legality by Jones Hall, A Professional Law Corporation, San Francisco, California, Bond Counsel. Certain legal matters will also be passed upon for the Authority and the City by Jones Hall, A Professional Law Corporation, as Disclosure Counsel. Certain legal matters will be passed upon for the Authority and the City by the City Attorney. Certain legal matters will be passed upon for the Underwriters by its counsel, Nixon Peabody LLP. It is anticipated that the Bonds will be delivered in book-entry form through the facilities of DTC on or about _____, 2020.

BofA SECURITIES
J.P. MORGAN US BANCORP

The date of this Official Statement is: _____, 2020

* Preliminary; subject to change.

CITY OF SAN JOSE FINANCING AUTHORITY
Taxable Lease Revenue Bonds, Series 2020B
(Ice Centre Project)

MATURITY SCHEDULE*
(Base CUSIP:† _____)

\$ _____ Serial Bonds

<u>Maturity Date</u> <u>(June 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 maturing June 1, 20__; Yield: __%; Price: ____;
CUSIP†: ____

* Preliminary; subject to change.

† CUSIP Copyright 2020, 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. None of the City or the Underwriters takes any responsibility for the accuracy of the CUSIP data.

**CITY OF SAN JOSE FINANCING AUTHORITY
CITY OF SAN JOSE, CALIFORNIA**

AUTHORITY BOARD MEMBERS AND CITY COUNCIL

Sam Liccardo, Mayor, Chair

District 1: Charles "Chappie" Jones, Vice
Mayor, Member

District 2: Sergio Jimenez, Member

District 3: Raul Perez Member

District 4: Lan Diep, Member

District 5: Magdalena Carrasco, Member

District 6: Devora "Dev" Davis, Member

District 7: Maya Esparza, Member

District 8: Sylvia Arenas, Member

District 9: Pam Foley, Member

District 10: Johnny Khamis, Member

AUTHORITY AND CITY OFFICIALS

David Sykes, Executive Director and City Manager

Toni Taber, Secretary and City Clerk

Julia H. Cooper, Treasurer and Director of Finance

Nora Frimann, Acting City Attorney

PROFESSIONAL SERVICES

BOND AND DISCLOSURE COUNSEL

Jones Hall, A Professional Law Corporation
San Francisco, California

MUNICIPAL ADVISOR

Public Resources Advisory Group
Oakland, California

TRUSTEE

Wilmington Trust, National Association
Costa Mesa, California

VERIFICATION AGENT

Causey Demgen & Moore P.C.
Denver, Colorado

GENERAL INFORMATION ABOUT THIS OFFICIAL STATEMENT

Use of Official Statement. This Official Statement is submitted in connection with the sale of the Bonds referred to herein and may not be reproduced or used, in whole or in part, for any other purpose. This Official Statement is not a contract between any bond owner and the Authority or the Underwriters.

No Offering Except by This Official Statement. No dealer, broker, salesperson or other person has been authorized by the Authority, the City or the Underwriters to give any information or to make any representations other than those contained in this Official Statement and, if given or made, such other information or representation must not be relied upon as having been authorized by the Authority, the City or the Underwriters.

No Unlawful Offers or Solicitations. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy nor may there be any sale of the Bonds by a person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale.

Information in Official Statement. The information set forth in this Official Statement has been furnished by the Authority and other sources which are believed to be reliable, but it is not guaranteed as to accuracy or completeness.

Estimates and Forecasts. When used in this Official Statement and in any continuing disclosure by the Authority in any press release and in any oral statement made with the approval of an authorized officer of the City or the Authority or any other entity described or referenced herein, 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. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, give rise to any implication that there has been no change in the affairs of the City, Authority or any other entity described or referenced herein since the date hereof.

Involvement of Underwriters. The following statement has been included in this Official Statement on behalf of the Underwriters: The Underwriters have reviewed the information in this Official Statement in accordance with, and as a part of, its responsibilities to investors under the Federal Securities Laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

Stabilization of and Changes to Offering Prices. The Underwriters may overallocate or take other steps that stabilize or maintain the market prices of the Bonds at levels above that which might otherwise prevail in the open market. If commenced, the Underwriters may discontinue such market stabilization at any time. The Underwriters may offer and sell the Bonds to certain securities dealers, dealer banks and banks acting as agent at prices lower than the public offering prices stated on the inside cover page of this Official Statement, and those public offering prices may be changed from time to time by the Underwriters.

Document Summaries. All summaries of the Indenture or other documents referred to in this Official Statement are made subject to the provisions of such documents and qualified in their entirety to reference to such documents, and do not purport to be complete statements of any or all of such provisions.

No Securities Laws Registration. The Bonds have not been registered under the Securities Act of 1933, as amended, in reliance upon exceptions therein for the issuance and sale of municipal securities. The Bonds have not been registered or qualified under the securities laws of any state.

Effective Date. 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, give rise to any implication that there has been no change in the affairs of the City, the Authority, the other parties described in this Official Statement, or the condition of the property within the City since the date of this Official Statement.

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



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OFFICIAL STATEMENT

\$ _____ *

CITY OF SAN JOSE FINANCING AUTHORITY
Taxable Lease Revenue Bonds, Series 2020B
(Ice Centre Project)

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 the bonds captioned above (the “**Bonds**”) by the City of San José Financing Authority (the “**Authority**”). All capitalized terms used in this Official Statement, unless noted otherwise, have the meanings set forth in the Indenture (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 and the documents summarized or described herein. A full review should be made of the entire Official Statement. The offering of the Bonds to potential investors is made only by means of the entire Official Statement.

Authority for Issuance. The Authority is issuing the Bonds under the following:

- (a) Article 4 of Chapter 5, Division 7, Title 1 of the California Government Code, as amended, commencing with Section 6584 (the “**Law**”);
- (b) resolutions adopted by the Board of Directors (the “**Board**”) of the Authority on August 25, 2020 (the “**Authority Resolution**”), and by the City Council (the “**City Council**”) of the City of San José (the “**City**”) on August 25, 2020 (the “**City Resolution**”); and
- (c) an Indenture of Trust (the “**Indenture**”) dated as of October 1, 2020, by and between the Authority and Wilmington Trust, National Association, as trustee (the “**Trustee**”).

The City. The City, with an estimated population as of January 1, 2020 of approximately 1,049,187 (as reported by the California Department of Finance), is the third most populous city in the State of California (the “**State**”) and the tenth most populous 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**”).

* Preliminary; subject to change.

The Authority. The Authority was formed pursuant to a Joint Exercise of Powers Agreement dated December 8, 1992, by and between the City and the former Redevelopment Agency of the City of San José (the “**Former Agency**”), and is qualified to issue the Bonds under the Law. As a result of changes to the California Community Redevelopment Law, the Former Agency has been dissolved and the Successor Agency to the Redevelopment Agency of the City of San José (the “**Successor Agency**”) has become the successor agency to the Former Agency. The Authority, the Successor Agency and the City are each separate and distinct legal entities, and the debts and obligations of one such entity are not the debts or obligations of the other entities. See “THE AUTHORITY.”

COVID-19 Statement. The COVID-19 pandemic has resulted in a public health crisis that is fluid and unpredictable, with financial and economic impacts that cannot be predicted. As such, investors are cautioned that the City cannot at this time predict the impacts that the COVID-19 pandemic may have on its operations and finances, property values in the City, and economic activity in the City. For more disclosure regarding the COVID-19 emergency, see “BONDOWNERS’ RISKS – COVID-19 Pandemic,” and “APPENDIX A – THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MAJOR GENERAL FUND REVENUE SOURCES - COVID-19 Pandemic.”

Purpose of the Bonds. The Bonds are being issued to:

- Refinance, on a current basis, all of the Authority’s outstanding lease revenue bonds captioned Taxable Lease Revenue Bonds, Series 2008E-1 (Ice Centre Refunding Project) (the “**Series 2008E-1 Bonds**”) and Taxable Lease Revenue Bonds, Series 2008E-2 (Ice Centre Refunding Project) (the “**Series 2008E-2 Bonds**”) and together with the Series 2008E-1 Bonds, the “**2008E Bonds**”) and the City’s related lease payment obligations;
- Finance the acquisition and construction of public improvements benefitting the City, including two additional ice rinks and related facilities at the Ice Centre (as defined in this Official Statement);
- Fund a deposit to a debt service reserve account for the Bonds;
- Fund capitalized interest on the Bonds; and
- Pay the costs of issuing the Bonds.

See “FINANCING PLAN.”

Security for the Bonds and Pledge of Revenues. Under the Indenture, the Bonds are payable from and secured by a first pledge of and lien on “**Revenues**” (as defined in this Official Statement) received by the Authority under the Lease Agreement dated as of October 1, 2020, between the Authority, as lessor, and the City, as lessee (the “**Lease**”), consisting primarily of lease payments (the “**Lease Payments**”) made by the City under the Lease. The Bonds are also secured by certain funds on deposit under the Indenture (as defined in this Official Statement). See “SECURITY FOR THE BONDS.”

Under the Indenture, a Reserve Account is established for the Bonds (the “**Reserve Account**”). Amounts on deposit in the Reserve Account are to be used only to make payments with respect to the Bonds. Proceeds of the Bonds, in the amount of \$_____, being the initial

Reserve Requirement, will be deposited into the Reserve Account on the date of issue of the Bonds. See “SECURITY FOR THE BONDS – Reserve Account.”

The City and the Authority will enter into a Site Lease dated as of October 1, 2020 (the “**Site Lease**”). Under the Site Lease, the City will lease certain real property to the Authority, consisting of an ice skating facility (as described herein, the “**Leased Property**”). Concurrently, the City and the Authority will enter into the Lease, under which the Authority will lease the Leased Property back to the City. See “THE LEASED PROPERTY.”

Form of Bonds; Book-Entry Only. The Bonds will be issued in fully registered form, registered in the name of The Depository Trust Company, New York, New York (“**DTC**”), or its nominee, which will act as securities depository for the Bonds. Purchasers of the Bonds will not receive certificates representing the Bonds that are purchased. See “THE BONDS – Book-Entry Only System” and “APPENDIX G – DTC AND THE BOOK-ENTRY ONLY SYSTEM.”

Redemption. The Bonds are subject to optional redemption, mandatory sinking fund payment redemption, and special mandatory redemption from the proceeds of insurance or condemnation proceeds prior to their stated maturity dates. See “THE BONDS – Redemption.”

Abatement. The Lease Payments are subject to complete or partial abatement in the event and to the extent that there is substantial interference with the City’s use and possession of the Leased Property or any portion thereof. If the Lease Payments are abated under the Lease, the Bond Owners would receive less than the full amount of principal of and interest on the Bonds. To the extent proceeds of rental interruption insurance are available (as described below), Lease Payments (or a portion thereof) may be made from those proceeds during periods of abatement. See “SECURITY FOR THE BONDS – Abatement” and “BOND OWNERS’ RISKS.”

Legal Opinion. Upon delivery of the Bonds, Jones Hall, A Professional Law Corporation, San Francisco, California, Bond Counsel (“**Bond Counsel**”), will release its final approving legal opinion with respect to the Bonds, regarding the validity and the exemption of interest on the Bonds from State of California personal income taxes, in the form attached hereto as APPENDIX E.

Tax Matters. In the opinion of Bond Counsel, subject, however, to certain qualifications described herein, under existing law, the interest on the Bonds is exempt from State of California personal income taxes. Bond Counsel observes that interest on the Bonds is not excluded from gross income for federal income tax purposes. Bond Counsel expresses no opinion regarding any other tax consequences caused by the ownership or disposition of, or the accrual or receipt of interest on, the Bonds. See “TAX MATTERS” and APPENDIX E for the form of Bond Counsel’s opinion to be delivered concurrently with the Bonds.

Risks of Investment. Debt service on the Bonds is payable only from Lease Payments and other amounts payable by the City to the Authority under the Lease, and certain funds on deposit under the Indenture, including the Reserve Account. For a discussion of some of the risks associated with the purchase of the Bonds, see “BOND OWNERS’ RISKS.”

NONE OF THE BONDS, THE OBLIGATION OF THE AUTHORITY TO PAY PRINCIPAL OF OR INTEREST THEREON, OR THE OBLIGATION OF THE CITY TO MAKE THE LEASE PAYMENTS CONSTITUTE A DEBT OR A LIABILITY OF THE AUTHORITY, THE CITY, THE STATE OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL LIMITATION ON INDEBTEDNESS, OR A PLEDGE OF THE FULL FAITH

AND CREDIT OF THE CITY. THE BONDS ARE SECURED SOLELY BY THE PLEDGE OF REVENUES AND CERTAIN FUNDS HELD UNDER THE INDENTURE. THE BONDS ARE NOT SECURED BY A PLEDGE OF THE TAXING POWER OF THE CITY.

Continuing Disclosure. The City has covenanted and agreed that it will comply with and carry out all of the provisions of the Continuing Disclosure Certificate, dated the date of issuance of the Bonds and executed by the City (the “**Continuing Disclosure Certificate**”). The form of the Continuing Disclosure Certificate is included in Appendix F hereto. See “CONTINUING DISCLOSURE.”

Concurrent Financing. On September __, 2020, the Authority issued its Taxable Lease Revenue Bonds, Series 2020A (Civic Center Refunding Project) (the “**2020A Bonds**”) in order to (i) refinance (a) the Authority’s Lease Revenue Refunding Bonds, Series 2006A (Civic Center Project), (b) the Authority’s Lease Revenue Bonds, Series 2007A (Recreational Facilities Refunding Project) (c) the Authority’s Lease Revenue Refunding Bonds, Series 2013A (Civic Center Project), and (ii) prepay the City’s rental obligations under a Master Equipment Lease/Purchase Agreement, and (iii) fund the acquisition and construction of public improvements benefitting the City, including the build-out of existing space within the 4th and San Fernando Garage for office space to be occupied by the San José Clean Energy Department (“**SJCE**”) and other city operations. The 2020A Bonds will evidence fractional interests in certain lease payments to be made by the City, as lessee under a lease agreement for the City’s Civic Center. See “APPENDIX A – “THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – BONDED AND OTHER INDEBTEDNESS” for additional information.”

Other Information. This Official Statement speaks only as of its date, and the information contained in this Official Statement is subject to change.

FINANCING PLAN

Refinancing of 2008E Bonds

Authority and Purpose of 2008E Bonds. On July 3, 2008, the Authority issued its Taxable Lease Revenue Bonds, Series 2008E (Ice Centre Refunding Project) (the “**Original 2008E Bonds**”), as publicly-marketed variable rate “demand” bonds supported by credit facilities, for the purpose of refinancing the City’s acquisition and construction of an ice skating facility, consisting of four ice skating rinks and related facilities, which is currently commonly known as the Ice Centre at San José.

On October 14, 2010, the Authority re-designated the Original 2008E Bonds as Taxable Lease Revenue Bonds, Series 2008E-1 (Ice Centre Refunding Project) (the “**Series 2008E-1 Bonds**”) and its Taxable Lease Revenue Bonds, Series 2008E-2 (Ice Centre Refunding Project) (the “**Series 2008E-2 Bonds**” and together with the Series 2008E-1 Bonds, the “**2008E Bonds**”).

On December 18, 2013, the Authority directly placed the 2008E Bonds with U.S. Bank National Association, the credit facilities were terminated and the 2008E Bonds ceased to be remarketed on the open market.

The refinancing plan calls for the outstanding 2008E Bonds to be redeemed in full on _____, 2020 (the “**Redemption Date**”), at a redemption price equal to the principal amount thereof, together with interest coming due and payable on the Redemption Date.

Irrevocable Escrow Fund Deposit. In order to accomplish the refinancing plan, a portion of the proceeds of the Bonds will be sent to Wells Fargo Bank, National Association, acting as the trustee for the 2008E Bonds (the “**Prior Trustee**”), for deposit into an escrow fund (the “**Escrow Fund**”) to be established under irrevocable refunding instructions (the “**Refunding Instructions**”) to be given by the City to the Prior Trustee. The Prior Trustee will hold the amounts on deposit in the Escrow Fund as cash. These funds will be sufficient to defease the outstanding 2008E Bonds as of the date of issuance of the Bonds and redeem the 2008E Bonds in full on the Redemption Date.

The moneys held by the Prior Trustee in the Escrow Fund are pledged to the payment and redemption of the 2008E Bonds and will not be available for payment of the Bonds.

Public Improvements. Proceeds of the Bonds will also finance the acquisition and construction of public improvements benefitting the City, including two additional ice rinks and related facilities at the Ice Centre at San José. See “THE PROJECT.”

THE PROJECT

Proceeds of the Bonds will also finance the acquisition and construction of public improvements benefitting the City, including two additional ice rinks and related facilities at the City-owned Ice Centre at San José, formerly the Ice Centre of San José (the “**Project**” or the “**Ice Centre**”). The Ice Centre opened in April 1994 and is located at the corner of South 10th Street and Alma Avenue. The facility is open daily for public ice skating sessions. In addition to general admission figure skating, the facility provides private and group skating lessons, curling, and hosts hockey leagues for various age groups, serves as the official training center of the National Hockey League’s San José Sharks (the “**Sharks**”) and the American Hockey League’s San José Barracuda (the “**Barracuda**”), a professional ice hockey team affiliated with the Sharks, and is the home venue for the San José State University hockey team and the San José Sharks junior teams.

The Ice Centre is managed by Sharks Ice, LLC (the “**Manager**”). The Manager is a wholly-owned subsidiary of Sharks Sports & Entertainment, LLC, as is San Jose Arena Management, the operator of the SAP Center at San Jose, the home of the San Jose Sharks. See “*Management of the Ice Centre*” below..

Existing Facilities. The existing Ice Centre facilities were built between 1994 and 2005. Each phase was constructed in accordance with applicable codes.

Original Facility. The original facility, including the mezzanine, was approximately 80,000 square feet and was comprised of two NHL-sized ice skating rinks; spectator seating; changing/locker rooms; a pro shop; a snack bar/grill; an arcade area; offices; and a meeting area.

First Expansion. With proceeds of bonds previously issued by the Authority, the City undertook the following improvements, which were necessary for the Ice Centre to become the official training facility for the Sharks:

- Added approximately 58,300 square feet of new improvements including a third rink, associated dressing rooms, the Sharks training center, and a new arcade area.
- Remodeled the existing mezzanine area between the two original rinks to provide an enhanced skater exercise and dance area and increased meeting rooms and storage space.
- Added new bathrooms, expanded and improved existing dressing rooms, and upgraded electronics and fire safety systems.
- Remodeled and expanded the current entry area to enhance food and beverage service, enhanced and expanded the pro-shop and created a ceremonial display of awards/honors for community ice users.

Second Expansion. In response to usage of the Ice Centre’s three ice rinks, the City and SJAM decided to install an approximately 33,034 square foot addition to the Ice Centre, and to finance it with proceeds of lease revenue bonds issued by the Authority. The improvements included the following first-floor “expansion” and second-floor “renovation” elements:

Expansion. The City and SJAM added the following facilities on the first floor:

- Fourth ice rink and bench areas (20,635 square feet).
- Dressing rooms/locker areas (3,700 square feet).
- Zamboni room, bleachers, restrooms, equipment room (2,500 square feet).

Renovation. The City and SJAM made the following renovations on the second floor:

- Addition of 1,100 square feet to the existing mezzanine to include a 5,580-square foot restaurant and a 285-square foot banquet room.
- Addition of mechanical room (770 square feet) and bathrooms (500 square feet).

Third Expansion. The construction of a two-story expansion to the Ice Centre by approximately 6,800 square feet for a private locker room and related facilities for the Barracuda. The third expansion was funded by the Sharks and included the expansion of:

- A locker room for use by 25 players.
- Weight training room.
- Medical and physiotherapy area.
- Offices for coaching staff.
- Storage and laundry facilities.
- New public entrance.

The existing facilities were designed and built to include the following elements:

Sustainable Building. All four phases of the existing facilities were constructed to incorporate energy efficiency (cooling, heating and lighting), water conservation and overall environmental quality. These features are not only intended to benefit the environment but also to reduce operating costs.

Seismic Considerations. All phases of the existing facilities were designed in accordance with the California Building Code and are made of pre-engineered steel. A site soils report was prepared for each phase of the project by a geotechnical consulting firm. All findings were provided to the Engineer of Record and were used to design building foundations.

Fire Suppression Systems. The existing facilities are protected by a fire sprinkler system designed in accordance with the applicable Uniform Fire Code and National Fire Prevention Association section 13 requirements.

Security. The Ice Centre's security system includes closed circuit televisions with remote monitoring capabilities.

The Project. In order to meet an increase in regional demand and to provide an alternate home arena for the Barracuda, the City expects to use proceeds of the Bonds to undertake the fourth expansion of the Ice Centre (the “**Future Expansion**”). The proposed expansion is anticipated to add approximately 204,193 square feet of space to the Ice Centre with the construction of two new buildings adjacent to the Ice Centre’s existing third ice rink, on City-owned property. Construction of the proposed expansion is anticipated to commence in the Fall of 2020 with completion expected in August of 2022, at a total estimated cost of approximately \$120 million, to be funded entirely with proceeds of the Bonds.

To accommodate the Future Expansion, the site will need to be reconfigured resulting in a loss of parking. Pursuant to the City’s land use requirements, Sharks Ice is required to provide 2185 off-street parking spaces. The Project will accommodate 667 on-site parking spaces with the remaining 1586 spaces to be provided through a Memorandum of Understanding between Sharks Ice and San Jose State University (“**SJSU**”) for use of a SJSU parking facility with a term that commences upon completion of the Future Expansion and continues for approximately 28 years which is expected to be coterminous with the term of the lease of the Ice Centre between the City and Sharks Ice. See “- *Management of the Ice Centre*” below.

The Project also includes the demolition of the San Jose Municipal Firing Range (“Firing Range”) and removing asbestos and lead containing components and materials located in the Firing Range building and surrounding environs

The improvements to be constructed as part of the Future Expansion consist of the following:

Third Ice Rink. The third ice rink is expected to be retrofitted in order to improve outdated piping and technology system, as described below. The third ice rink will also include construction of a ticketing area which is approximately 545 square feet.

In April of 2018, the two rinks from the original facility were taken out of service in order to remediate a broken pipe which caused the subsurface to freeze and heave. These rinks, which were 24 years old, utilized a design that is no longer acceptable in the industry. The City has determined that the pipe failure was due to an outdated design flaw. With these improvements, rinks 1, 2, and 4 are updated with the latest design and technology to meet industry standard. The fifth and sixth rinks expected to be constructed as part of the Project will also utilize the latest design to meet and exceed industry standard piping system and improved technology with no known failure risks. However, the third rink has several major components that are at the end of their useful life and need to be replaced (such as the compressor and pumps). Also, the third rink has a sand base that needs to be brought up to current industry standards by upgrading the subfloor piping system and encasing it in concrete. This retrofit work is planned to be completed as part of the Project.

Fourth Ice Rink. The fourth ice rink will include the construction of a bridge connector located at the second floor to the fifth ice rink totaling 259 square feet.

Fifth Ice Rink. The fifth ice rink is anticipated to be housed in a new two-story building totaling approximately 49,376 square feet, to be located adjacent to the existing third ice rink. The fifth ice rink will serve as an additional community rink to be used by the public. The fifth ice rink expansion is anticipated to include the following:

- On the first floor, 12 public locker rooms and arena support spaces, including a security office, main electrical room, ice making equipment for rinks 3, 5 and 6, boiler room, water entry room and fire pump room (approximately total square footage of 36,389).
- On the second floor, a homework/study room, a bar restaurant, seats for 100 spectators and training space for patrons (approximately total square footage of 12,987).

Sixth Ice Rink. The sixth ice rink is anticipated to be housed in a new three-story building totaling approximately 154,013 square feet, to be located south and adjacent to the existing third ice rink on City-owned property. The sixth ice rink will serve as the home ice competition and practice rink for the Barracuda. When not in use by the Barracuda, the sixth rink will be available as a public rink for the community. The sixth rink is expected to seat approximately 4,213 spectators and include the following:

- An oval-shaped seating bowl with general and premium seating.
- An arena level with a total of 3,523 fixed and moveable spectator seats, locker rooms, restrooms, a ticket lobby, concessions/commissary, merchandise location, lounge and loading docks (approximately total square footage of 75,209).
- A club level with up to 690 seats in suites, a theatre box and loge boxes, along with a press area, locker room and team training space, club seating and suites pantry. The club level would also include a shell space designed to be improved in the future for offices, physical therapy or other compatible uses (approximately 4,370 square feet).
- A suite level that includes suite concourse, private suites, upper seating bowl, administrative office, support facilities, office space, restrooms, and concession (approximately 57,346 square feet).
- A third level with shell space designed to be improved in the future for medical or other office uses (approximately 17,088 square feet). The shell spaces are anticipated to be leased to a third-party medical provider specializing in sports medicine and related services, or other compatible uses.

Exterior Site Work. Replacement of sidewalk (10 feet wide), driveways, curb & gutter, wheelchair ramp; underground utility connection; landscape improvement which will include installation of 31 tree wells and irrigation supply line; on-site bio retention; 22 ADA designated and 17 electric vehicle designated parking stalls.

Sustainability and Other Considerations. The facilities to be constructed as part of the expansion of the fifth and sixth rinks are anticipated to be certified LEED Silver (or higher). In addition, the City anticipates that all such facilities will be designed in accordance with the California Building Code and made of pre-engineered steel.

Seismic Considerations. A site soils report was prepared for the expansion of the fifth and sixth rinks by a geotechnical consulting firm. There are six active faults within 16 miles of the Ice Centre. The site soils report considered fault rupture, ground shaking and liquefaction potential. All findings were provided to the Engineer of Record and will be used to design building foundations.

City's Review and Approval of the Project.

The City's Debt Management Policy requires a two-thirds City Council approval prior to embarking on a lease revenue financing in which project revenues are identified as the repayment source. In these situations, the Policy requires a preparation of a feasibility study to determine the volatility of the revenue and provide a sensitivity analysis on project revenue projections including worse/best case scenarios. On December 10, 2019 the City Council accepted the Finance Feasibility Report (the "**Study**"), prepared by an independent feasibility consultant, selected by the City, on the feasibility of financing the proposed expansion of the Ice Centre. The Study evaluated the sustainability of the Ice Centre operation after expansion and the feasibility consultant presented three operating projection scenarios: (1) conservative; (2); expected and (3) aggressive. Projections in the Study assumed smooth growth over time, but recognized that business can be affected by unpredictable local and national economic factors; and, demand is often cyclical and based on market conditions. The Study also provided an economic sensitivity analysis for the Expected Scenario for the first year of expected stabilized operations in FY 2025-2026 that presented a range of possible outcomes for Ice Centre operations under typical, cyclical market conditions and the impact of a significant economic downturn or recession. The sensitivity analysis included a 10%, 20%, and 30% reduction of operating and non-operating revenues in the Expected Scenario. The Study did not contemplate a pandemic which forced a prolonged closure of the facility and a reopening under strict operating guidelines for social distancing and regular/frequent cleaning.

As part of the Study, the base rent payments from the Manager were set to be sufficient to cover the debt service payments on the Bonds. City Council directed staff to (1) develop a bond financing structure and prepare the necessary documents for consideration by the Authority Board and City Council; and (2) negotiate the Amended Management Agreement (as defined below). At the onset of the shelter-in-place order related to the COVID-19 pandemic, staff was anticipating Council approval of the Bond financing in April 2020, with closing expected to occur in May 2020.

City staff provided a written update on the Ice Centre expansion project on June 30, 2020, which included an independent report from the Sharks updating the City Council on the current operations at the Ice Centre and the impact of COVID-19, status of the public works project and the status of the Bond financing. The Ice Centre was closed for three months (March 13 to June 14, 2020) in response to the Santa Clara County public health orders. On June 15, the Ice Centre reopened with youth camps as approved by the County with required public health protocols in place and since June 15, all programs that have been offered have filled to capacity. Additional programming at the Ice Centre will occur after the County provides public health guidelines for expanded programming for indoor sports facilities.

The economic sensitivity analysis included in City staff's update used current market analysis of the proposed bonds to fund the Ice Centre expansion and a 30% reduction of operating and non-operating revenues in the Expected Scenario in the Study along with potential longer capitalized interest period, updated debt service using market rates as of June 22, 2020 and increased project costs from assumptions used in December 2019. This analysis demonstrated that net income from Ice Centre operations would be sufficient to cover the estimated Sharks base rent payments to the City by more than 1.0x. [This economic sensitivity analysis was updated and presented to the Council in the staff report presented at the August 25, 2020 City Council meeting approving the issuance of the Bonds. The updated analysis continued to demonstrate that net income from Ice Centre operations would be sufficient to cover estimated Sharks base rent payments to the City by more than 1.0x.]

Management of the Ice Centre. On May 25, 2004, Sharks Ice, LLC (the “**Manager**”) and the City entered into the Amended and Restated Lease and Management Agreement, which amended and restated the Original Management Agreement. Concurrently with the delivery of the Bonds, the Manager and the City expect to enter into the Second Amended and Restated Ice Centre Lease and Management Agreement (the “**Amended Lease and Management Agreement**”).

Pursuant to the Amended Lease and Management Agreement, the Manager will operate the Ice Centre as a community recreation facility for use by all members of the public, and will make base rental payments to the City to finance the costs of the Project through the final maturity date of the Bonds. The base rental payments to the City are also secured by a Letter of Credit covering two years of debt service, the corporate guarantee by Sharks Ice’s parent company, and the requirement that the Sharks make lease payments regardless of *force majeure* events (except those which result in abatement of City payments due under the bond documents due to physical damage to the property). In the event the Sharks relocate to another facility, the Manager is obligated to continue making payments to the City until a substitute tenant is found.

The Manager will make additional rental payments to the City to reimburse the City for property insurance expenses and certain expenses related to oversight of the Ice Centre. During the term of the Amended Lease and Management Agreement, the Manager is required to maintain a letter of credit in an amount sufficient to pay two years of base rental payments. However, the letter of credit is not pledged to the Bonds, and the City and the Manager may elect at any time to amend the provisions of the Amended Management Agreement to eliminate the requirement for a letter of credit.

IT IS ANTICIPATED THE SHARKS WILL MAKE BASE RENT PAYMENTS TO THE CITY FOR THE USE OF THE ICE CENTRE THAT WILL BE SUFFICIENT TO PAY DEBT SERVICE ON THE BONDS, THE OBLIGATION TO REPAY THE BONDS RESTS WITH THE CITY. NEITHER THE PAYMENTS FROM THE SHARKS OR THE LETTER OF CREDIT PLEDGED TO BONDHOLDERS. THE BONDS ARE SECURED SOLELY BY REVENUES AND OTHER FUNDS PLEDGED UNDER THE INDENTURE. SEE “SECURITY FOR THE BONDS.”

Estimated Sources and Uses of Funds

The estimated sources and uses of funds relating to the Bonds are as follows:

Sources of Funds:

Principal Amount of Bonds	\$
Plus: Funds Available with Respect to 2008E Bonds	
<i>TOTAL SOURCES</i>	<hr/> \$

Uses of Funds:

Deposit to Escrow Fund ⁽¹⁾	\$
Deposit to Project Fund ⁽²⁾	
Deposit to Interest Account ⁽³⁾	
Deposit to Reserve Account	
Deposit to Costs of Issuance Fund ⁽⁴⁾	
Underwriters' Discount	
<i>TOTAL USES</i>	<hr/> \$

(1) Represents funds to be used to defease and redeem the 2008E Bonds. See "– Refinancing of 2008E Bonds" above.

(2) Represents funds to be used to finance the acquisition and construction of the Project.

(3) Represents capitalized interest on the Bonds through approximately _____.

(4) Represents funds to be used to pay costs of issuance, which include legal fees, printing costs, rating agency fees and other costs of issuing the Bonds.

THE LEASED PROPERTY

Description and Location

Lease Payments will be made by the City under the Lease for the use and occupancy of the Ice Centre, including the Future Expansion (the “**Leased Property**”). See “THE FINANCING PLAN – Public Improvements – *Existing Facilities*” for a detailed description of the Leased Property.

Impact of COVID-19

The outbreak of COVID-19, a respiratory disease caused by a new strain of coronavirus (“**COVID-19**”), has halted sporting events, including professional hockey. The Ice Centre was closed for three months due to COVID-19, but re-opened for youth camps on June 15, 2020. The Sharks have retained experts to ensure that applicable public health guidelines will be followed as the Ice Centre continues to reopen to the public. No changes are anticipated to the timing of the Project as a result of COVID-19, and it is currently expected that the Project will be complete prior to the 2022-2023 hockey season.

The City cannot guarantee that the COVID-19 pandemic, future shelter-in-place directives, interruptions in construction or social distancing efforts may have on the Project or the Leased Property.

Modification of Leased Property

Under the Lease, the City has the right, at its own expense, to make additions, modifications and improvements to the Leased Property or any portion thereof. All additions, modifications and improvements to the Leased Property will thereafter comprise part of the Leased Property and become subject to the provisions of the Lease.

Such additions, modifications and improvements may not in any way damage the Leased Property, or cause the Leased Property to be used for purposes other than those authorized under the provisions of state and federal law; and the Leased Property, upon completion of any additions, modifications and improvements made thereto under this provision of the Lease, must be of a value which is not substantially less than the value thereof immediately prior to the making of such additions, modifications and improvements.

The City will not permit any mechanic’s or other lien to be established or remain against the Leased Property for labor or materials furnished in connection with any remodeling, additions, modifications, improvements, repairs, renewals or replacements made by the City under this provision of the Lease; except that if any such lien is established and the City first notifies or causes to be notified the Authority of the City’s intention to do so, the City may in good faith contest any lien filed or established against the Leased Property, and in such event may permit the items so contested to remain undischarged and unsatisfied during the period of such contest and any appeal therefrom and will provide the Authority with full security against any loss or forfeiture which might arise from the nonpayment of any such item, in form satisfactory to the Authority. The Authority will cooperate fully in any such contest, upon the request and at the expense of the City.

Substitution

Under the Lease, the City has the option at any time and from time to time, to substitute other real property (the “**Substitute Property**”) for the Leased Property or any portion thereof (the “**Former Property**”), upon satisfaction of all of the requirements set forth in the Lease, which includes (among others) the following:

- The City has filed with the Authority and the Trustee, and caused to be recorded in the office of the County Recorder, sufficient memorialization of an amendment of the Lease, the Site Lease and the Assignment Agreement that adds the legal description of the Substitute Property and deletes therefrom the legal description of the Former Property, and has filed and caused to be recorded corresponding amendments to the Site Lease and Assignment Agreement.
- The City has obtained a CLTA policy of title insurance insuring the City’s leasehold estate under the Lease in the Substitute Property, subject only to Permitted Encumbrances (as defined in the Lease), in an amount at least equal to the estimated value thereof.
- The City has certified in writing to the Authority and the Trustee that the Substitute Property serves the municipal purposes of the City and constitutes property which the City is permitted to lease under the laws of the State of California.
- The City has filed with the Authority and the Trustee a written certificate of the City or other written evidencing stating that the useful life of the Substitute Property at least extends to the final maturity date of the Bonds, that the estimated value of the Leased Property, after substitution of the Substitute Property and release of the Former Property, is at least equal to the aggregate Outstanding principal amount of the Bonds, and the fair rental value of the Leased Property, after substitution of the Substitute Property and release of the Former Property, is at least equal to the Lease Payments thereafter coming due and payable under the Lease.

See “APPENDIX D – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS.”

Upon the satisfaction of all such conditions precedent, the Term of the Lease will thereupon end as to the Former Property and commence as to the Substitute Property, and all references to the Former Property will apply with full force and effect to the Substitute Property. The City is not entitled to any reduction, diminution, extension or other modification of the Lease Payments whatsoever as a result of any substitution of property under this provision of the Lease.

Release of Leased Property

Under the Lease, the City has the option at any time and from time to time to release any portion of the Leased Property from the Lease (the “**Released Property**”) provided that the City has satisfied all of the requirements under the Lease that are conditions precedent to such release, which include (among others) the following:

- The City has filed with the Authority and the Trustee, and caused to be recorded in the office of the County Recorder, sufficient memorialization of an amendment of the Lease, the Site Lease and the Assignment Agreement which removes the Released Property from the Lease, the Site Lease and the Assignment Agreement.

- The City has certified in writing to the Authority and the Trustee that the value of the property which remains subject to the Lease following such release is at least equal to the aggregate Outstanding principal amount of the Bonds, and the fair rental value of the property which remains subject to the Lease following such release is at least equal to the Lease Payments thereafter coming due and payable thereunder.

See “APPENDIX D – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS.”

Amendments to the Lease

Under the Lease, the Authority and the City may at any time amend or modify any of the provisions of this Lease, but only: (a) with the prior written consents of the Owners of a majority in aggregate principal amount of the Outstanding Bonds; or (b) without the consent of the Trustee or any of the Bond Owners, but only if such amendment or modification is for any one or more of the purposes described in the Lease. Amendments or modifications that do not require the consent of the Trustee or any of the Bond Owners include amendments or modifications to obligate the City to pay additional amounts of rental for the use and occupancy of the Leased Property, but only if (A) such additional amounts of rental are pledged or assigned for the payment of any bonds, notes, leases or other obligations the proceeds of which are applied to finance or refinance the acquisition or construction of any real or personal property for which the City is authorized to expend funds subject to its control, (B) the City has certified in writing to the Trustee that the estimated fair market value of the Leased Property is at least equal to the aggregate principal amount of the Outstanding Bonds and all such other bonds, notes, leases or other obligations, and (C) the City has filed with the Trustee written evidence that the amendments will not of themselves cause a reduction or withdrawal of any rating then assigned to the Bonds.

See “APPENDIX D – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS.”

THE BONDS

This section provides summaries of the Bonds and certain provisions of the Indenture. See APPENDIX D for a more complete summary of the Indenture. Capitalized terms used but not defined in this section have the meanings given in APPENDIX D.

Authority for Issuance

The Bonds are being issued under the Law, the Authority Resolution and the Indenture. Under the Authority Resolution and City Resolution, the Bonds may be issued in a principal amount not to exceed \$155,000,000.

General Provisions

Bond Terms. The Bonds will be dated their date of delivery and issued in fully registered form without coupons in integral multiples of \$5,000, so long as no Bond has more than one maturity date.

Interest on the Bonds will be payable on June 1 and December 1 in each year, commencing [June 1, 2021] (each an “**Interest Payment Date**”). The Bonds will mature in the

amounts and on the dates, and bear interest at the annual rates, set forth on the inside cover page of this Official Statement.

Calculation of Interest. Interest on the Bonds is payable from the Interest Payment Date next preceding the date of authentication thereof unless:

- (a) a Bond is authenticated on or before an Interest Payment Date and after the close of business on the preceding Record Date, in which event it will bear interest from such Interest Payment Date;
- (b) a Bond is authenticated on or before the first Record Date, in which event interest thereon will be payable from the Closing Date; or
- (c) interest on any Bond is in default as of the date of authentication thereof, in which event interest thereon will be payable from the date to which interest has been paid in full, payable on each Interest Payment Date.

Interest with respect to the Bonds will be computed on the basis of a 360-day year composed of 12 months of 30 days each.

Record Date. Under the Indenture, “Record Date” means, with respect to any Interest Payment Date, the 15th calendar day of the month preceding such Interest Payment Date, whether or not such day is a Business Day.

Payments of Principal and Interest. Interest is payable on each Interest Payment Date to the persons in whose names the ownership of the Bonds is registered on the Registration Books at the close of business on the immediately preceding Record Date, except as provided below. Interest on any Bond which is not punctually paid or duly provided for on any Interest Payment Date is payable to the person in whose name the ownership of such Bond is registered on the Registration Books at the close of business on a special record date for the payment of such defaulted interest to be fixed by the Trustee, notice of which is given to such Owner by first-class mail not less than 10 days prior to such special record date.

The Trustee will pay interest on the Bonds by check of the Trustee mailed by first class mail, postage prepaid, on each Interest Payment Date to the Owners of the Bonds at their respective addresses shown on the Registration Books as of the close of business on the preceding Record Date. At the written request of the Owner of Bonds in an aggregate principal amount of at least \$1,000,000, which written request is on file with the Trustee as of any Record Date, the Trustee will pay interest on such Bonds on each succeeding Interest Payment Date by wire transfer in immediately available funds to such account of a financial institution within the United States of America as specified in such written request, which will remain in effect until rescinded in writing by the Owner.

The Trustee will pay principal and premium, if any, of the Bonds in lawful money of the United States of America by check of the Trustee upon presentation and surrender of such Bonds at the Office of the Trustee.

While the Bonds are subject to the book-entry system, the principal, interest and any redemption premium with respect to the Bonds will be paid by the Trustee to DTC for subsequent disbursement to beneficial owners of the Bonds. See “– Book-Entry Only System” below.

Redemption*

Optional Redemption. The Bonds maturing on or after June 1, 20__, are subject to redemption, as a whole or in part, at the option of the Authority, on June 1, 20__, and on any date thereafter, at a redemption price equal to 100% of the principal amount of Bonds to be redeemed, together with accrued interest thereon to the date fixed for redemption, without premium.

Make-Whole Call Redemption. The Bonds maturing on or before June 1, 20__ may be redeemed in whole or in part at the election of the Authority on any date before June 1, 20__, from any moneys that may be provided for such purpose, at a redemption price for such Bonds to be redeemed (the “**Make-Whole Redemption Price of Bonds**”) determined by the Designated Investment Banker equal to the greater of (i) 100% of the principal amount of such 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 such Bonds to be redeemed, not including any portion of those payments of interest accrued and unpaid as of the date on which the Bonds are to be redeemed, discounted to the date on which such 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 __ basis points, plus accrued and unpaid interest on the Bonds to be redeemed on the redemption date.

“Comparable Treasury Issue” means, with respect to any redemption date for a particular 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 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 Bonds to be redeemed.

“Comparable Treasury Price” means, with respect to any redemption date for a particular Bond, the average of five Reference Treasury Dealer Quotations for that redemption date, after excluding the highest 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 Authority and the City.

“Reference Treasury Dealer” means each of five firms, specified by the Authority and the City from time to time, that are primary U.S. Treasury 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 Authority 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 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 Authority, the City and the Trustee 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 particular Bonds, the rate per annum, expressed as a percentage of the principal amount, equal to the actual or

* Preliminary; subject to change.

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.

“U.S. Treasury” means any direct general obligations of the United States of America (including obligations issued or held in book entry form on the books of the Department of the Treasury of the United States of America), for which the full faith and credit of the United States of America are pledged.

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

Special Mandatory Redemption From Insurance or Condemnation Proceeds. The Bonds are subject to redemption as a whole, or in part on a pro rata basis among maturities, on any date, from any Net Proceeds required to be used for such purpose as provided in the Indenture, at a redemption price equal to 100% of the principal amount thereof plus interest accrued thereon to the date fixed for redemption, without premium.

Mandatory Sinking Fund Redemption. The Bonds maturing on June 1, 20__, June 1, 20__ and June 1, 20__ (collectively, the ***“Term Bonds”***) are subject to mandatory sinking fund redemption in part prior to their stated maturity date, on each September 1 in accordance with the tables set forth below, respectively, at a redemption price equal to 100% of the principal amount thereof called for redemption, plus accrued interest to the redemption date, without premium:

Term Bonds Maturing June 1, 20__

Redemption Date (June 1)	Principal Amount of Bonds to be Redeemed
-----------------------------	---

(maturity)

Selection of Bonds for Redemption. If less than all of the Bonds are to be redeemed, the particular maturities of Bonds to be redeemed at the option of the Authority will be determined by the Authority in its sole discretion.

If the Bonds are registered in book-entry only form and so long as DTC or a successor securities depository is the sole registered owner of such Bonds, if less than all of the Bonds of a maturity are called for prior redemption, the particular Bonds or portions thereof to be redeemed shall be allocated on a pro rata pass-through distribution of principal basis in accordance with DTC procedures, provided that, so long as the Bonds are held in book-entry form, the selection for redemption of such Bonds shall be made in accordance with the operational arrangements of DTC then in effect, and, if the DTC operational arrangements do not allow for redemption on a

pro rata pass-through distribution of principal basis, the Bonds will be selected for redemption, in accordance with DTC procedures, by lot.

The Authority intends that redemption allocations made by DTC be made on a pro rata pass-through distribution of principal basis as described above. However, neither the Authority nor the Underwriters can provide any assurance that DTC, DTC's direct and indirect participants or any other intermediary will allocate the redemption of Bonds on such basis.

In connection with any repayment of principal, including payments of scheduled mandatory sinking fund payments, the Trustee will direct DTC to make a pass-through distribution of principal to the holders of the Bonds.

For purposes of calculation of the "pro rata pass-through distribution of principal," "pro rata" means, for any amount of principal to be paid, the application of a fraction to each denomination of the respective Bonds where (a) the numerator of which is equal to the amount due to the respective bondholders on a payment date, and (b) the denominator of which is equal to the total original par amount of the respective Bonds.

If the Bonds are no longer registered in book-entry-only form, each owner will receive an amount of Bonds equal to the original face amount then beneficially held by that owner, registered in such investor's name. Thereafter, any redemption of less than all of the Bonds of any maturity will continue to be paid to the registered owners of such Bonds on a pro-rata basis, based on the portion of the original face amount of any such Bonds to be redeemed..

Notice of Redemption. The Trustee shall mail notice of redemption of the Bonds by first class mail, postage prepaid, not less than 20 nor more than 60 days before any redemption date, to the respective Owners of any Bonds designated for redemption at their addresses appearing on the Registration Books and to one or more Securities Depositories and to the Municipal Securities Rulemaking Board as provided in the Continuing Disclosure Certificate.

Neither the failure to receive any notice nor any defect therein will affect the sufficiency of the proceedings for such redemption or the cessation of accrual of interest from and after the redemption date.

Rescission of Redemption. The Authority has the right to rescind any notice of optional redemption of the Bonds by written notice to the Trustee on or prior to the date fixed for redemption.

Any notice of redemption will 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 will not constitute an Event of Default under the Indenture.

The Authority and the Trustee have no liability to the Bond Owners or any other party related to or arising from such rescission of redemption. The Trustee will mail notice of such rescission of redemption in the same manner as the original notice of redemption was sent under the Indenture.

Effect of Redemption. If notice of redemption has been duly given as provided in the Indenture, and moneys for payment of the redemption price of, together with interest accrued to the date fixed for redemption on, including any applicable premium, the Bonds (or portions

thereof) so called for redemption being held by the Trustee, on the redemption date designated in such notice, the Bonds (or portions thereof) so called for redemption will become due and payable, interest on the Bonds so called for redemption will cease to accrue, said Bonds (or portions thereof) will cease to be entitled to any benefit or security under the Indenture, and the Owners of said Bonds will have no rights in respect thereof except to receive payment of the redemption price thereof.

Book-Entry Only System

The Bonds will be issued as fully registered bonds in book-entry only form, registered in the name of Cede & Co. as nominee of DTC, and will be available to ultimate purchasers in the denomination of \$5,000 or any integral multiple of \$5,000, under the book-entry system maintained by DTC. While the Bonds are subject to the book-entry system, the principal, interest and any redemption premium with respect to a Bond will be paid by the Trustee to DTC, which in turn is obligated to remit such payment to its DTC Participants for subsequent disbursement to Beneficial Owners of the Bonds. Purchasers of the Bonds will not receive certificates representing their interests therein, which will be held at DTC.

See APPENDIX G for further information regarding DTC and the book-entry system.

Transfer, Registration and Exchange

The following provisions regarding the exchange and transfer of the Bonds apply only during any period in which the Bonds are not subject to DTC's book-entry system. While the Bonds are subject to DTC's book-entry system, their exchange and transfer will be effected through DTC and the Participants and will be subject to the procedures, rules and requirements established by DTC. See "APPENDIX G – DTC AND THE BOOK-ENTRY ONLY SYSTEM."

Bond Register. The Trustee will keep or cause to be kept, at the Office of the Trustee, sufficient records for the registration and transfer of ownership of the Bonds, which shall upon reasonable notice as agreed to by the Trustee, be open to inspection during regular business hours by the Authority; and, upon presentation for such purpose, the Trustee shall, under such reasonable regulations as it may prescribe, register or transfer or cause to be registered or transferred, on such records, the ownership of the Bonds as provided in the Indenture.

Transfer of Bonds. Any Bond may, in accordance with its terms, be transferred, upon the Registration Books, by the person in whose name it is registered, in person or by a duly authorized attorney of such person, upon surrender of such Bond to the Trustee at its Office for cancellation, accompanied by delivery of a written instrument of transfer in a form acceptable to the Trustee, duly executed. The Trustee will require the Owner requesting such transfer to pay any tax or other governmental charge required to be paid with respect to such transfer. Whenever any Bond or Bonds are surrendered for transfer, the Authority will execute and the Trustee will authenticate and deliver to the transferee a new Bond or Bonds of like series, interest rate, maturity and aggregate principal amount. The Authority will pay the cost of printing Bonds and any services rendered or expenses incurred by the Trustee in connection with any transfer of Bonds.

Exchange of Bonds. The Bonds may be exchanged at the Office of the Trustee for a like aggregate principal amount of Bonds of other authorized denominations and of the same series, interest rate and maturity. The Trustee will require the Owner requesting such exchange to pay any tax or other governmental charge required to be paid with respect to such exchange.

The Authority will pay the cost of printing Bonds and any services rendered or expenses incurred by the Trustee in connection with any exchange of Bonds.

Limitations on Transfer and Exchange. The Trustee may refuse to transfer or exchange, under these provisions of the Indenture, any Bonds selected by the Trustee for redemption under the Indenture, or any Bonds during the period established by the Trustee for the selection of Bonds for redemption.

DEBT SERVICE SCHEDULE

The table below shows scheduled annual debt service payments on the Bonds, assuming no early redemptions.

Year Ending June 1	Principal	Interest	Total Debt Service
2021			
2022			
2023			
2024			
2025			
2026			
2027			
2028			
2029			
2030			
2031			
2032			
2033			
2034			
2035			
2036			
2037			
2038			
2039			
2040			
2041			
2042			
2043			
2044			
2045			
2046			
2047			
2048			
2049			
2050			
2051			
Total:			

SECURITY FOR THE BONDS

The principal of and interest on the Bonds are not a debt of the Authority or the City, nor a legal or equitable pledge, charge, lien or encumbrance, upon any of their respective property, or upon any of their income, receipts, or revenues except the Revenues and other amounts pledged under the Indenture.

This section provides summaries of the security for the Bonds and certain provisions of the Indenture, the Lease and the Site Lease. See APPENDIX D for a more complete summary of the Indenture, the Lease and the Site Lease. Capitalized terms used but not defined in this section have the meanings given in APPENDIX D.

Revenues; Pledge of Revenues

Pledge of Revenues and Other Amounts. Subject only to the provisions of the Indenture permitting the application thereof for the purposes and on the terms and conditions set forth therein, all of the Revenues and all amounts (including proceeds of the sale of the Bonds) held in any fund or account established under the Indenture other than the Costs of Issuance Fund and the Project Fund are pledged to secure the payment of the principal of and interest and premium (if any) on the Bonds in accordance with their terms and the provisions of the Indenture. Said pledge constitutes a lien on and security interest in the Revenues and such amounts and will attach, be perfected and be valid and binding from and after the Closing Date, without the need for any physical delivery thereof or further act. The Project is not pledged to secure the payment of the principal of and interest and premium (if any) on the Bonds.

“**Revenues**” are defined in the Indenture to mean:

- (a) all amounts received by the Authority or the Trustee under or with respect to the Lease, including, without limiting the generality of the foregoing, all of the Lease Payments (including both timely and delinquent payments, any late charges, and whether paid from any source), but excluding (i) any amounts described in the provisions of the Lease relating to permitted amendments that provide for additional rental to be pledged or assigned for the payment of bonds issued to finance or refinance projects for which the City is authorized to expend its funds, and (ii) any Additional Rental Payments (consisting of certain administrative costs due to the Authority and the Trustee under the Lease), and
- (b) all interest, profits or other income derived from the investment of amounts in any fund or account established under the Indenture.

Assignment to Trustee. Under the Assignment Agreement, the Authority has transferred to the Trustee all of the rights of the Authority in the Lease (other than the rights of the Authority under the provisions of the Lease regarding Additional Rental Payments, advances, release and indemnification covenants, and agreement to pay attorneys’ fees).

The Trustee is entitled to collect and receive all of the Revenues, and any Revenues collected or received by the Authority will be deemed to be held, and to have been collected or received, by the Authority as the agent of the Trustee and will forthwith be paid by the Authority to the Trustee.

The Trustee is also entitled to and required to, subject to the provisions of the Indenture regarding rights of the Trustee, take all steps, actions and proceedings which the Trustee

determines to be reasonably necessary in its judgment to enforce, either jointly with the Authority or separately, all of the rights of the Authority and all of the obligations of the City under the Lease.

Allocation of Revenues by Trustee; Application of Funds

Deposit of Revenues in Bond Fund. All Revenues will be promptly deposited by the Trustee upon receipt thereof in a special fund designated as the “Bond Fund,” which the Trustee will establish, maintain and hold in trust; except that all moneys received by the Trustee and required under the Indenture or under the Lease to be deposited in the Redemption Fund or the Insurance and Condemnation Fund will be promptly deposited in such funds.

On the Closing Date, a portion of the proceeds of the Bonds in the amount of \$_____ will be deposited into the Capitalized Interest Subaccount of the Interest Account. See “– Application of Interest Account” below

All Revenues deposited with the Trustee will be held, disbursed, allocated and applied by the Trustee only as provided in the Indenture. Any surplus remaining in the Bond Fund, after payment in full of the principal of and interest on the Bonds or provision therefore under Indenture, and any applicable fees and expenses to the Trustee, will be withdrawn by the Trustee and remitted to the City.

Allocation of Revenues. On or before each Interest Payment Date, the Trustee will transfer from the Bond Fund and deposit into the following respective accounts and subaccounts (each of which the Trustee will establish and maintain within the Bond Fund), the following amounts in the following order of priority:

(a) Deposit to Interest Account. The Trustee will deposit in the Interest Account an amount required to cause the aggregate amount on deposit in the Interest Account to be at least equal to the amount of interest becoming due and payable on such Interest Payment Date on all Bonds then Outstanding.

(b) Deposit to Principal Account. The Trustee will deposit in the Principal Account an amount required to cause the aggregate amount on deposit in the Principal Account to equal the principal amount of the Bonds coming due and payable on such Interest Payment Date, including principal of any Term Bonds payable as a result of mandatory sinking fund redemption.

(c) Deposit to Reserve Account. The Trustee shall deposit in the Reserve Account an amount, if any, required to cause the amount on deposit in the Reserve Account to be equal to the Reserve Requirement. See “– Reserve Account” below.

Application of Interest Account

All amounts in the Interest Account shall be used and withdrawn by the Trustee solely for the purpose of paying interest on the Bonds as it comes due and payable (including accrued interest on any Bonds purchased or redeemed prior to maturity).

Moneys in the Capitalized Interest Subaccount shall be expended before moneys in the Interest Account. Amounts on deposit in the Capitalized Interest Subaccount shall be used and withdrawn by the Trustee solely for the payment of interest on the Bonds in the following amounts on the following dates:

Dates	Interest Amount to be Paid
	\$

The balance, if any, in the Capitalized Interest Subaccount on _____, 20__ shall be fully expended for the payment of interest, and the Capitalized Interest Subaccount shall be closed.

Application of Principal Account

All amounts in the Principal Account shall be used and withdrawn by the Trustee solely to pay the principal amount of the Bonds at their respective maturity dates.

Reserve Account

Under the Indenture, the Trustee is required to maintain and hold in trust a separate fund known as the “**Reserve Account.**” Amounts on deposit in the Reserve Account are to be used only to make payments with respect to the Bonds. The Reserve Account will be funded in an amount equal to the Reserve Requirement, which is defined in the Indenture to mean, as of any date of calculation, an amount equal to the lesser of (a) 10% of the initial principal amount of the Bonds, (b) the maximum annual debt service on the Bonds and (c) 125% of average annual debt service on the Bonds.

On the date of issuance of the Bonds, \$_____ of the proceeds of the Bonds will be deposited into the Reserve Account, constituting the initial Reserve Requirement, which amount is equal to the Reserve Requirement on such date.

While any Bonds are Outstanding, any moneys in excess of the Reserve Requirement will be transferred to the Bond Fund and will be allocated as set forth in the Indenture.

A Supplemental Indenture providing for the issuance of additional bonds of the Authority to facilitate the issuance of additional obligations of the City under the Lease Agreement as provided in the Lease may provide for the establishment of separate funds and accounts. Such Supplemental Indenture shall provide for (i) a deposit to the Reserve Account in an amount necessary such that the amount deposited therein shall equal the Reserve Requirement following issuance of such additional bonds, (ii) a deposit to a reserve account for such additional Bonds (and such other series of bonds identified by the City) in an amount defined in such Supplemental

Indenture, as long as such Supplemental Indenture expressly declares that the Owners of such additional bonds will have no interest in or claim to the Reserve Account and that the Owners of the additional bonds covered by the Reserve Account will have no interest in or claim to such other reserve account, or (iii) no deposit to either the Reserve Account or another reserve account as long as such Supplemental Indenture expressly declares that the Owners of such additional bonds will have no interest in or claim to the Reserve Account or any other reserve account. The Supplemental Indenture may provide that the Authority may satisfy the reserve requirement for a series of additional bonds by the deposit into the reserve account established pursuant to such Supplemental Indenture of an irrevocable standby or direct-pay letter of credit, insurance policy, or reserve policy issued by a commercial bank or insurance company as described in the Supplemental Indenture.

See “APPENDIX D – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS.”

Lease Payments; Covenant to Appropriate

Obligation to Pay. Under the Lease, subject to the provisions of Lease regarding abatement and prepayment, the City agrees to pay to the Authority, its successors and assigns, the Lease Payments in the respective amounts specified in the Lease, to be due and payable in immediately available funds on the Interest Payment Dates immediately following each of the respective Lease Payment Dates specified in the Lease, and to be deposited by the City with the Trustee on each of the Lease Payment Dates specified in the Lease.

Any amount held in the Bond Fund, the Interest Account (including the Capitalized Interest Subaccount) and the Principal Account on any Lease Payment Date (other than amounts on deposit in the Reserve Account, resulting from the prepayment of the Lease Payments in part but not in whole under the Lease, and amounts required for payment of past due principal or interest on any Bonds not presented for payment) will be credited towards the Lease Payment then required to be paid under the Lease. The City is not required to deposit any Lease Payment with the Trustee on any Lease Payment Date if the amounts then held in the Bond Fund, the Interest Account (including the Capitalized Interest Subaccount) and the Principal Account are at least equal to the Lease Payment then required to be deposited with the Trustee.

The Lease Payments payable in any Rental Period are for the use of the Leased Property during that Rental Period.

Fair Rental Value. The aggregate amount of the Lease Payments and Additional Rental Payments coming due and payable during each Rental Period constitute the total rental for the Leased Property for such Rental Period, and are payable by the City in each Rental Period for and in consideration of the right of the use and occupancy of, and the continued quiet use and enjoyment of the Leased Property during each Rental Period.

The City and the Authority have agreed and determined that the total Lease Payments represent the fair rental value of the Leased Property. In making that determination, consideration has been given to the estimated value of the Leased Property, other obligations of the City and the Authority under this Lease, the uses and purposes which may be served by the Leased Property and the benefits therefrom which will accrue to the City and the general public.

Source of Payments; Covenant to Budget and Appropriate. Under the Lease, the Lease Payments are payable from any source of legally available funds of the City, subject to the provisions of the Lease regarding abatement. See “ – Abatement” below.

Subject to the provisions of the Lease regarding abatement, the City covenants in the Lease to take all actions required to include the Lease Payments in each of its budgets during the Term of the Lease and to make the necessary appropriations for all Lease Payments and Additional Rental Payments. This covenant of the City constitutes a duty imposed by law and each and every public official of the City is required to take all actions required by law in the performance of the official duty of such officials to enable the City to carry out and perform the covenants and agreements agreed to be carried out and performed by the City under the Lease. Notwithstanding any other provision of the Lease, the City will in no event be obligated to pay any Lease Payments or Additional Rental Payments due hereunder in any Rental Period for any succeeding Rental Period.

Limited Obligation

THE OBLIGATION OF THE CITY TO MAKE THE LEASE PAYMENTS DOES NOT CONSTITUTE A DEBT OF THE CITY, THE AUTHORITY OR THE STATE OR OF ANY POLITICAL SUBDIVISION THEREOF WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMIT OR RESTRICTION, AND DOES NOT CONSTITUTE AN OBLIGATION FOR WHICH THE CITY IS OBLIGATED TO LEVY OR PLEDGE ANY FORM OF TAXATION OR FOR WHICH THE CITY HAS LEVIED OR PLEDGED ANY FORM OF TAXATION.

Abatement

Termination or Abatement Due to Eminent Domain. Under the Lease, if the Leased Property is taken permanently under the power of eminent domain or sold to a government threatening to exercise the power of eminent domain, the Term of the Lease thereupon ceases as of the day possession is taken. If less than all of the Leased Property is taken permanently, or if the Leased Property is taken temporarily, under the power of eminent domain, then:

(a) the Lease will continue in full force and effect with respect thereto and does not terminate by virtue of such taking, and the parties waive the benefit of any law to the contrary; and

(b) the Lease Payments are subject to abatement in an amount determined by the City such that the resulting Lease Payments represent fair consideration for the use and occupancy of the remaining usable portions of the Leased Property; *provided, however,* that the Lease Payments are not subject to abatement to the extent that amounts in the Reserve Account are available to pay Lease Payments which would otherwise be abated under the Lease, and such amounts will constitute special funds for the payment of the Lease Payments.

Abatement Due to Damage or Destruction. Under the Lease, the Lease Payments are subject to abatement during any period in which by reason of damage or destruction (other than by eminent domain as described above) there is substantial interference with the use and occupancy by the City of the Leased Property or any portion thereof.

The Lease Payments are subject to abatement in an amount determined by the City such that the resulting Lease Payments represent fair consideration for the use and occupancy of the remaining usable portions of the Leased Property not damaged or destroyed. Such abatement

will continue for the period commencing with such damage or destruction and ending with the substantial completion of the work of repair or reconstruction.

In the event of any such damage or destruction, this Lease continues in full force and effect and the City waives any right to terminate this Lease by virtue of any such damage and destruction. Notwithstanding the foregoing, the Lease Payments are not subject to abatement to the extent that amounts in the Reserve Account are available to pay Lease Payments which would otherwise be abated under the Lease, and such amounts will constitute special funds for the payment of the Lease Payments.

Abatement Due to Non-Completion of the Project. The Lease Payments are subject to abatement during any period prior to the issuance of a certificate of occupancy for the Project in which there is substantial interference with the use and occupancy by the City of the Leased Property or any portion thereof. The Lease Payments are subject to abatement in an amount determined by the City such that the resulting Lease Payments represent fair consideration for the use and occupancy of the usable portions of the Leased Property. Such abatement will continue for the period commencing with the substantial interference with the use and occupancy of the Leased Property and ending with the substantial completion of the Project.

Insurance

Liability and Property Damage Insurance. Under the Lease, the City is required to maintain or cause to be maintained throughout the Term of the Lease, but only if and to the extent available from reputable insurers at reasonable cost in the reasonable opinion of the City, a standard commercial general liability insurance policy or policies in protection of the Authority, the City, and their respective members, officers, agents, employees and assigns. Said policy or policies shall provide for indemnification of said parties against direct or contingent loss or liability for damages for bodily and personal injury, death or property damage occasioned by reason of the operation of the Leased Property.

Such policy or policies shall provide coverage in such liability limits and be subject to such deductibles as the City deems adequate and prudent. Such insurance may be maintained as part of or in conjunction with any other insurance coverage carried by the City, and may be maintained in whole or in part in the form of self-insurance by the City, subject to the provisions of the Lease, or in the form of the participation by the City in a joint powers agency or other program providing pooled insurance.

The proceeds of such liability insurance must be applied toward extinguishment or satisfaction of the liability with respect to which paid.

Casualty Insurance. Under the Lease, the City is required to procure and maintain, or cause to be procured and maintained, throughout the Term of the Lease, casualty insurance against loss or damage to all buildings situated on the Leased Property, in an amount at least equal to the lesser of (a) 100% of the replacement value of the insured buildings, or (b) 100% of the aggregate principal amount of the Outstanding Bonds.

Such insurance must, as nearly as practicable, cover loss or damage by explosion, windstorm, riot, aircraft, vehicle damage, smoke and such other hazards as are normally covered by such insurance, and must include flood and earthquake insurance, but only if available at reasonable cost from reputable insurers in the judgment of the City.

Such insurance may be subject to such deductibles as the City deems adequate and prudent. Such insurance may be maintained as part of or in conjunction with any other insurance coverage carried by the City, and may be maintained in whole or in part in the form of the participation by the City in a joint powers agency or other program providing pooled insurance. The Net Proceeds of such insurance must be applied as provided in the Lease and described below.

Rental Interruption Insurance. Under the Lease, the City is required to procure and maintain, or cause to be procured and maintained, throughout the Term of the Lease, rental interruption or use and occupancy insurance to cover loss, total or partial, of the use of any portion of the Leased Property constituting buildings or other improvements as a result of any of the hazards covered in the casualty insurance described above, in an amount at least equal to the maximum such Lease Payments coming due and payable during any consecutive two Fiscal Years.

Such insurance may be maintained as part of or in conjunction with any other insurance coverage carried by the City, and may be maintained in whole or in part in the form of the participation by the City in a joint powers agency or other program providing pooled insurance; provided that such insurance may not be maintained by the City in the form of self-insurance.

The Net Proceeds of such insurance, if any, must be paid to the Trustee and deposited in the Bond Fund, to be applied as a credit towards the payment of the Lease Payments allocable to the insured improvements as the same become due and payable.

Application of Net Proceeds. The Trustee, as assignee of the Authority under the Assignment Agreement, has the right to receive all Net Proceeds. As provided in the Indenture, the Trustee will deposit all Net Proceeds in the Insurance and Condemnation Fund to be applied to the redemption of Bonds as set forth in the Indenture. However, if the Leased Property is damaged or destroyed in full, the Net Proceeds of such insurance shall be used by the City to rebuild or replace the Leased Property if such proceeds are not sufficient to redeem Outstanding Bonds equal in aggregate principal amount to the unpaid Lease Payments allocable to the Leased Property.

Additional Risk Management Programs; Additional Insurance. Notwithstanding anything in the Lease Agreement to the contrary, the City has the right to adopt alternative risk management programs to insure against any of the risks required to be insured against under the terms of the Lease Agreement, including a program of self-insurance (except self-insurance for rental interruption and title insurance as required by the Lease Agreement), in whole or in part. In addition, the City Manager of the City may approve such other types of insurance, including any increases in the insurance coverage required by the Lease Agreement. The City self-insures for casualty insurance and rental interruption insurance, and does not carry earthquake insurance.

See "APPENDIX D – SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

THE AUTHORITY

Creation of the Authority. The Authority was created by a Joint Exercise of Powers Agreement, dated as of December 8, 1992 (the “**Agreement**”), between the City and the Former Agency. The Agreement was entered into pursuant to the Joint Exercise of Powers Act, Chapter 5 of Division 7 of Title 1 of the State Government Code. The Authority was created for the purpose of facilitating the financing of public improvements and facilities within the City.

The Former Agency was dissolved as of February 1, 2012, and the Successor Agency has become the successor agency of the Former Agency. The Agreement remains in effect.

Governing Board of the Authority. The Authority is governed by an eleven-member Governing Board that consists of the members of the City Council of the City.

Powers of the Authority. Pursuant to the Law, the Authority is authorized to issue bonds for the purpose of financing, refinancing or providing reimbursement for costs incurred in connection with the construction, expansion, remodeling, renovation, furnishing, equipping or acquisition of public capital improvements of public entities such as the City. The Law provides for the issuance of revenue bonds by joint exercise of powers authorities, such as the Authority, to be repaid from the proceeds of certain public obligations, such as the Lease. The intent of the California Legislature, as stated in the Law, is to assist in the reduction of local borrowing costs, help accelerate the construction, repair and maintenance of public capital improvements, and promote greater use of existing and new financial instruments and mechanisms such as bond pooling by local agencies.

The Bonds are limited obligations of the Authority payable solely from and secured solely by the Revenues pledged under the Indenture and certain funds held under the Indenture.

CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS

The constitutional and statutory provisions discussed in this section have the potential to affect the ability of the City to levy taxes and spend tax proceeds for operating and other purposes. 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.

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 XIIC 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 XIID."

Article XIIC. Article XIIC 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 XIIC 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 XIIC 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 XIID. Article XIID 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. 4th 637

(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. 4th 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. 4th 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 XIIC and XIID 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 term “sewer” for purposes of Article XIID. 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 XIID’s sewer fee requirements. Subsequent storm sewer fee increases have been adopted in accordance with Article XIID’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 XIID’s sewer fee requirements, the City’s storm sewer fee increases require voter

approval under Article XIID, 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 XIID, and went on to hold that charges for ongoing water delivery which are fees and charges within the meaning of Article XIID are also “fees” within the meaning of Article XIIC’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 XIIC 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 XIIC 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 XIID 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 2017-2018 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 2007-2008 the amount transferred was approximately \$4.6 million. For fiscal year 2008-2009 the amount transferred was reduced to approximately \$2.8 million. For fiscal years 2009-2010 through 2019-

2020, 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 2015-2016 remains pending in the trial court and in February, 2020 a lawsuit was filed against cities and water providers throughout California, including the City, that appears to allege violations of Article XIID with respect to water rates that were charged to customers. See APPENDIX A – “THE CITY OF SAN JOSE: GEOGRAPHIC, 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* (1995) 11 Cal. 4th 220 (“**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.* (2001) 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 \$85.1 million has been collected from July 1, 2016 through June 30, 2019 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 2004-2005 Budget, approved by the voters in November 2004 and generally effective in fiscal year 2006-2007, 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 2008-2009, 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 – “THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – REDEVELOPMENT DISSOLUTION.”

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.

BOND OWNERS' RISKS

The following describes certain special considerations and risk factors affecting the payment of and security for the Bonds. The following discussion is not meant to be an exhaustive list of the risks associated with the purchase of any Bonds and does not necessarily reflect the relative importance of the various risks. Potential investors in the Bonds are advised to consider the following special factors along with all other information in this Official Statement in evaluating the Bonds. There can be no assurance that other considerations will not materialize in the future.

COVID-19 Pandemic

The outbreak of COVID-19, has been declared a pandemic by the World Health Organization, a national emergency by the President of the United States and a state of emergency by the Governor of the State, the County Board of Supervisors, and the City Council. The COVID-19 outbreak has caused tremendous economic volatility in the United States and globally, producing significant declines and the onset of a national and global recession.

The State of California and several counties in the San Francisco Bay Area, including Santa Clara County, where the City is located, have issued mandatory orders for all people to shelter in place, except to meet essential needs or to work to provide essential services ("shelter-in-place directives or orders"). Santa Clara County's current shelter-in-place directive became effective on July 13, 2020, restricting activities that were previously re-opened following an increase in cases of COVID-19 in the County. The order will remain in effect until the County's health officer amends or rescinds it. The categories of businesses and activities no longer permitted include, but are not limited to, indoor dining at restaurants and other facilities, entertainment centers, places of worship, fitness centers and cardrooms,

The COVID-19 pandemic is ongoing, and its dynamic nature leads to uncertainties, including spread and severity of the virus, the duration of the outbreak, actions that may be taken by governmental authorities to contain or mitigate the outbreak, the development of medical treatments or vaccinations, and the impact of the outbreak on the local or global economy.

The ultimate impact of COVID-19 on the City's operations and finances is not fully known, and it may be some time before the full adverse impact of the COVID-19 outbreak is known. The City continues to monitor the spread of COVID-19 and is working with local, state, and national agencies to address the potential impact of the COVID-19 pandemic upon the City. Although the overall potential impact of COVID-19 on the City cannot be fully quantified at this time, actual revenues and expenses of the City are likely to be different than those currently projected by the City.

For additional information about the how the City expects to be impacted by the COVID-19 outbreak, see APPENDIX A – "THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – MAJOR GENERAL FUND REVENUE SOURCES."

Economic Condition in Local, State and National Economics

The financial condition of the City can be significantly affected by generally prevailing conditions in the local, State and national economies. Such conditions and factors may impact the funds available to the City to make the Lease Payments. A number of the City's revenue sources are collected by the State or allocated in accordance with State law (most significantly, property taxes). There can be no assurances that the current or future recessions or otherwise declining conditions in the local, State or national economies will not materially adversely affect the financial condition of the City in the future.

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.

Drought. As with much of the State of California, the City experiences recurring drought as a result of its climate conditions. Droughts impact public health and safety related to both water supply and wildfire risk. For additional information about the risks related to drought in the City, see "APPENDIX A – THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – GEOGRAPHIC INFORMATION - Drought."

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. For additional information about the risk of natural flooding in the City, see "APPENDIX A – THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – GEOGRAPHIC INFORMATION - Flood Hazards."

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 a number of dams. In a catastrophic event, damage to one or more of these dams could result in flooding within the City. For additional information about the risk of dam inundation in the City, see "APPENDIX A – THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION – GEOGRAPHIC INFORMATION - Flood Hazards."

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

Valley Water released water from the dam. 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 Valley Water 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 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 damage 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 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: GEOGRAPHIC, 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 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 magnify the wildfire threat and place substantially more people and property at risk than ever before.” For additional information about the wildfire areas in the City, and the City’s prevention measures, see “APPENDIX A – THE CITY OF SAN JOSE: GEOGRAPHIC,

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.

Clean Water Compliance

In 2015, it was alleged that the City violated the Clean Water Act and its stormwater permit by discharging sewage into the City’s municipal separate storm water systems. The City is subject to a related consent decree under which it is required to appropriate \$100,000,000 over a 10-year period. If the City is unable to prevent sewage infiltration in the future, or to comply with its existing consent decree, the City may be subject to significant costs or litigation. For additional information see APPENDIX A - “THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION - SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND COURT DECREES - Clean Water Compliance” and “- Consent Decrees.”

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.

Trees may pose a risk to underground gas pipelines. The City has been coordinating with PG&E on their Community Pipeline Safety Initiative (“**CPSI**”) regarding the removal of certain trees that are planted above PG&E gas transmission pipelines. The CPSI is nearing an end with only a few dozen trees remaining to be considered for removal.

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, including facilities owned by the City like the Leased Property, 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**"). On July 1, 2020, PG&E emerged from bankruptcy completing its restructuring process and implementing its Plan of Reorganization (the "Plan") that was confirmed by the United States Bankruptcy Court on June 20, 2020.

The Plan requires PG&E to pay all allowed claims. This includes all of the City's allowed pre-petition claims that arose before PG&E filed for bankruptcy protection on January 29, 2019. A pre-petition claim is considered allowed if PG&E has not objected to the claim on a timely basis or, following a timely objection, the claim has been adjudicated in a determined amount. The Plan requires PG&E to file objections to pre-petition claims within 180 days of the Plan's effective date. The Plan went into effect on July 1, 2020.

The City filed proofs of claims in the PG&E Bankruptcy Proceeding for pre-petition claims totaling \$30,660,000 and consisting of:

- unpaid permit fees and property damage in the amount of approximately \$60,000;
- assessments for unpaid utility users taxes on various surcharges in the amount of approximately \$9.9 million, for the period of April 1, 2014 through March 31, 2017 including interest and penalties calculated through December 31, 2020;
- estimated amounts for unpaid utility users taxes in the range of \$8.7 million, for the period of April 1, 2017 through January 28, 2019 including interest and penalties calculated through December 31, 2020;
- assessments for unpaid utility users taxes and franchise fees for under-reporting gross charges (by improperly deducting California climate credits from charges billed for electricity and gas) in the amount of approximately \$9.2 million and \$2.8 million, respectively, for the period of April 1, 2014 through October 31, 2018 including interest and penalties calculated through May 12, 2020.

In February 2020, PG&E contested the assessments for unpaid utility users taxes on various surcharges through a proceeding held before the Director of Finance on February 27, 2020 and in its letter in support of its arguments of the same date. In a subsequent letter dated May 27, 2020, PG&E also contested the assessments for unpaid utility users taxes for the under-reporting of gross charges. The decision of the Director of Finance on these assessments is pending.

[At this time, it is unknown whether PG&E will object to one or more of the City's claims.]

PG&E Power Shutoffs

PG&E adopted a Community Wildfire Safety Program in an effort to prevent wildfires in the State. In May, 2019, as part of its Community Wildfire Safety Program, PG&E notified customers, including the City, that PG&E implemented additional precautionary measures to help reduce the risk of wildfires. In particular, PG&E 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 “**PG&E Shutoff**”). Under regulations issued by the California Public Utilities Commission (“**CPUC**”), investor owned utilities, such as PG&E, are authorized to use power shutoffs as a measure of last resort under specified conditions. The impact of a PG&E Shutoff is not limited to customers in areas that are 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 of a PG&E 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: GEOGRAPHIC, 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.

In 2019, the City experienced two PG&E Shutoffs. The first PG&E Shutoff occurred on October 9, 2019 when PG&E de-energized transmission and distribution lines to several parts of the City, mostly in portions of the eastern and southern districts of the City. The power was shut off to approximately 23,000 customer accounts, with an estimated impact to over 100,000 City residents. PG&E reported that all customer accounts were restored on October 10, 2019.

The second PG&E Shutoff occurred on October 26, 2019 when PG&E de-energized transmission and distribution lines to several parts of the City, mostly in the Alum Rock and Almaden Valley areas, which are often referred to as the wildland-urban interface areas. In this second PG&E Shutoff, power was shut off to approximately 7,500 customer accounts, with an estimated impact to over 24,000 City residents. PG&E reported that all customer accounts were restored on October 29, 2019.

Following these two PG&E Shutoffs, the City contacted PG&E to set up a series of workshops to address concerns that the City has regarding future PG&E Shutoffs, including: Critical infrastructure inspections, data access, circuit maps, weather data interpretation, notification and communications protocols, and outreach to medical baseline customers. In addition, City staff met with Santa Clara County Office of Emergency Management staff to develop stronger lines of communication with County agencies providing services to City residents.

On March 17, 2020, the City Administration brought forward a Public Safety Power Shutoff After Action Report for City Council approval which presented three fundamental areas of focus: People, Processes, and Technology, resulting in a series of recommendations designed to improve the City’s resilience and capacity to respond to future PG&E Shutoffs.

The financial cost to the City for its response to the first and second PG&E Shutoffs was approximately \$746,000, and \$500,000, respectively, not including City staff time spent responding to the shutoffs. In January 2020, the City Council accepted a grant from Cal OES in the amount of \$500,000 to support the City's resiliency to power shutoffs, including funding for equipment and the development of plans for future shutoff events.

In addition to these costs, the City incurred costs as the operator of SJCE, which supplies the City and City residents and businesses with cleaner electricity options through PG&E's infrastructure. During the first 2019 outage, an estimated 23,000 customers lost power for approximately 48 hours, which cost SJCE approximately \$40,000 per day. During the second 2019 outage, an estimated 7,500 customers lost power for approximately 48-60 hours, which cost SJCE approximately \$15,000 per day.

Certain start-up costs of SJCE were financed with proceeds from commercial paper notes issued by the Authority. Although SJCE's operating costs, including repayment of financing costs (such as the commercial paper notes issued by the 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. The PG&E Shutoffs in 2019 did not significantly impact SJCE's operating costs. However, in the event of future PG&E Shutoffs, 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 Authority.

It is anticipated that there will be additional PG&E Shutoffs under current CPUC regulations. The impact that any PG&E 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: GEOGRAPHIC, 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 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 in a way that is compliant with the California Environmental Quality Act (CEQA) 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 Senate Bill No. 32 for emissions reductions through year 2030. Further, the Greenhouse Gas Reduction Strategy 2030, once adopted, would allow future development projects to demonstrate consistency with the Green House Gas Reduction Strategy 2030 to streamline the GHG emissions analysis for the environmental review process. The City anticipates that the City Council will consider adoption of the Green House Gas Reduction Strategy 2030 prior to the end of calendar year 2020.

In February 2018, City Council accepted the Climate Smart San José Plan (“**Climate Smart**”) which is intended to provide a policyframework 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 SJCE 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 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: GEOGRAPHIC, 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 Valley Water 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**"). As a result of the Levee project, the San Francisco Regional Water Quality Board is requiring the RWF to close inactive, legacy lagoons used until the 1970s for drying residual solids and remediate environmental contamination. Cost of remediation is preliminarily estimated to be approximately \$40 million, but it is anticipated that the City's portion of such costs would be borne by ratepayers, or may be partially 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 are subject to cyber threats, including, but not limited to: hacking, viruses/malware, social engineering, activist campaigns, and other attacks on City information and communications assets. 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 developed and disseminated an administrative policy entitled "Information and Systems Security Policy" to set forth policies and procedure governing the use and security of the City's information systems and an Information Security Standards Handbook that establishes the security baseline of the City's information systems. The Cybersecurity Office also worked with City departments to improve system and infrastructure changes by establishing a Citywide 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 across all impacted departments. Additionally, a Cybersecurity Advisory Board, with cybersecurity leaders from the public and private sectors, was established to validate and refine the City's cybersecurity strategies, policies approach, and roadmap.

The City has conducted training with City employees who handle credit card transactions. The Cybersecurity Office also provided cybersecurity training and testing for all City employees, including phishing email tests, social engineering tests, periodic cybersecurity newsletters, and workshops. These efforts have been coupled with the Cybersecurity Office's ongoing information technology security assessments to identify and remediate potential weaknesses in networks. In its 2019-20 Adopted Operating Budget, the City has also allocated additional funding totaling approximately \$1.2 million to support the City's Cybersecurity program.

Many municipalities were impacted with ransomware attacks in 2019. In response, the City has upgraded its servers and workstations to guard against various strains of cryptoware and has implemented a solution to address Business Email Compromise (the attack of the City's email system through which the attacker gains access to a City email account). In 2019, the City also focused on creating system contingency plans to test recovery of systems in the event of a major disaster.

To mitigate its risk, the City purchased specialized insurance coverage covering cyber risks but there is no assurance that such coverage will be maintained in the future or that the coverage amount will be sufficient to address the cost of any particular cyberattack.

In 2020, as a resolute of the COVID-19 pandemic, the City has adapted to allow for remote work, utilizing online cloud tools and a private network. Safeguards were enhanced to mitigate the mobile workforce while maintaining a balance between functionality and security, including secure cloud access as return to work plans and processes are put into place for COVID-19 recovery. The City continues to perform technical refresh projects with an aim to reduce risk of legacy systems by designing modern secure architectures that take advantage of hybrid cloud and on-premise infrastructures.

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.

Split Roll Initiative.

An initiative measure (the "**Split Roll Initiative**") to amend Article XIII A has qualified for the State's November 2020 ballot. If adopted, the Split Roll Initiative would base property taxes for commercial and industrial properties on market values beginning in tax year 2020-21. Such market values would be reassessed by the applicable county assessor's office at least once every three years. The Split Roll Initiative includes exceptions for businesses with a total market value of less than \$2 million (adjusted for inflation), which would continue to be subject to property taxes based on purchase price, and exempts from property tax assessments up to \$500,000 of the value of personal property, or all personal property for businesses with fewer than 50 employees. There can be no assurance that the Split Roll Initiative will be adopted. Moreover, if the Split Roll Initiative is adopted, the City is unable to predict how it would affect the level of commercial building activity within the City and the relationship of the assessed value between land use types (i.e. residential versus commercial) in the City.

Change in Law

No assurance can be given that the State, the County or the City electorate will not at some future time adopt initiatives, or that the State Legislature or the City Council will not enact legislation that will amend the laws of the State or the City's Municipal Code, respectively, in a manner that could result in a reduction of the City's General Fund revenues and therefore a reduction of the funds legally available to the City to make Lease Payments. See, for example, "CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS – Articles XIIC and XIID of the State Constitution."

Future Litigation

There can be no assurance that future lawsuits or governmental actions will not affect repayment of the Bonds. See the section entitled "LITIGATION AND SIGNIFICANT CLAIMS AND PROCEEDINGS" in APPENDIX A – "THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION."

Limited Obligations; Lease Not a Debt of the City

The Bonds are limited obligations of the Authority payable solely from and secured solely by the Revenues pledged therefor under the Indenture, together with amounts on deposit from time to time in certain funds and accounts held by the Trustee. Revenues consist primarily of Lease Payments. If for any of the reasons described below, or for any other reason, the Authority does not receive sufficient Lease Payments to pay debt service on the Bonds, the Authority will not be obligated to utilize any other of its funds, other than amounts on deposit in the Reserve Account and certain other amounts on deposit in the funds and accounts established under the Indenture, to pay debt service on the Bonds.

The Lease Payments are not secured by any pledge of or lien on taxes or other revenue of the City, but are payable from all funds lawfully available to the City. The City has the capacity to enter into other obligations that may constitute additional obligations against its revenues. In the event the City's revenue sources are less than its total obligations, the City could choose to fund other obligations before making Lease Payments; in that case, the failure to pay Lease Payments in full would constitute a default under the Lease. The same result could occur if, because of State constitutional limits on expenditures, the City is not permitted to appropriate and spend all of its available revenues; in that case, the failure to pay Lease Payments in full would constitute a default under the Lease. The City must adopt a balanced Budget each year, and has covenanted in the Lease to budget for, appropriate and make the Lease Payments in each year that it has possession and use of the Leased Property. For a general understanding of the City's budget process and budget forecasts, see APPENDIX A – "THE CITY OF SAN JOSE: GEOGRAPHIC, DEMOGRAPHIC, ECONOMIC AND FINANCIAL INFORMATION."

Abatement of Lease

Under California law, the obligation of the City to make Lease Payments is contingent upon the availability of the Leased Property for use and occupancy by the City. The Lease Payments will be abated proportionately during any period in which by reason of material damage or destruction, there is substantial interference with the use and occupancy of any portion of the Leased Property by the City, and such abatement will continue until substantial completion of the work of repair or replacement of the portion of the Leased Property damaged or destroyed; provided that, in determining the amount of abatement, the City shall consider the then-current

value of the Leased Property but only to reduce or eliminate the amount of the abatement. Any abatement of Lease Payments could affect the Authority's ability to pay debt service on the Bonds.

In the event Lease Payments are abated, no assurances can be given that moneys on deposit in the Revenue Fund and the Reserve Account, or the proceeds of rental interruption insurance (which is not expected to be available to cover earthquake damage) will be sufficient to pay the debt service on the Bonds during the period of such abatement. In addition, even if such amounts are sufficient to make such payments, moneys remaining in the Reserve Account after such payments may be less than the Reserve Requirement.

Notwithstanding the provisions of the Lease specifying the extent of abatement in the event of the City's failure to have full use and occupancy of the Leased Property, such provisions may be superseded by operation of law, and, in such event, the resulting Lease Payments of the City may not be sufficient to pay all of the remaining principal and interest with respect to the Bonds.

Limitation on Remedies

The enforcement of any remedies provided for in the Lease and in the Indenture could prove to be both expensive and time-consuming. Although the Lease provides that if there is a default by the City, the Trustee may take possession of and relet the Leased Property, no assurance can be given that the amounts received from such reletting would be sufficient to pay the principal of and interest with respect to the Bonds when due.

The Lease provides that upon the occurrence and during the continuance of the City's failure to deposit with the Trustee any Lease Payments when due, the bankruptcy of the City, or if the City breaches any other terms, covenants, conditions or agreements contained in the Lease (subject to a cure period as described in the Lease), the Trustee, as assignee of the Authority, has the following general remedies: (i) to reenter the Leased Property and relet the Leased Property; or (ii) to enforce its rights to recover Lease Payments as they become due. See APPENDIX D – "SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

In addition to the limitations on remedies contained in the Lease and the Indenture, the rights and remedies provided in those documents may be limited by and are subject to provisions of federal bankruptcy laws, as now or hereafter enacted, and to other laws or equitable principles that may affect creditors' rights generally. The various legal opinions to be delivered concurrently with the issuance of the Bonds will be qualified as to the enforceability of the various legal instruments by limitations imposed by State and federal laws, rulings and decisions affecting remedies, and by bankruptcy, reorganization or other laws of general application affecting the enforcement of creditors' rights, including equitable principles. See "- Bankruptcy Risks" below.

No Acceleration Upon Default

In the event of a default, there is no remedy of acceleration of the total Lease Payments for the term of the Lease. Any suit for money damages would be subject to the legal limitations on remedies against cities and counties in the State of California, including a limitation on enforcement of judgments against funds needed to serve the public welfare and interest. See APPENDIX D – "SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Bankruptcy Risks

The rights of the owners of the Bonds and the enforceability of the Authority's obligation to make payments on the Bonds may be subject to bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting creditors' rights under currently existing law or laws enacted in the future, and may also be subject to the exercise of judicial discretion under certain circumstances.

Under existing law, the City is eligible to file for bankruptcy. Should the City file for bankruptcy, there could be adverse effects on the holders of the Bonds. In a bankruptcy of the City, the Authority or the Trustee as its assignee and the owners of the Bonds may be prohibited from taking any action against the City, any official of the City, or any property of the City (including the Leased Property) to enforce the terms of the Lease, unless the consent of the bankruptcy court is first obtained. The bankruptcy court is not required to give its consent. This prohibition on action may even prohibit the Trustee from using funds in its possession to make payments on the Bonds. As a result, Owners may experience temporary or permanent delays in the payment of the Bonds.

In a bankruptcy case, a plan of adjustment for the City could be confirmed that would allow for enforcement of the Lease, but the priority, interest rate, payment terms, collateral, maturity dates, payment sources, covenants and other terms or provisions of the Lease and the Bonds may be altered by the bankruptcy court. Such a plan could be confirmed even over the objections of the Authority or the Trustee as its assignee and the owners of the Bonds, and without their consent. Additionally, the resulting plan could adjust some or all of the City's financial obligations, which include the City's lease payment obligations under the Lease and the City's obligation to fund certain retirement benefits. The adjustment of similar obligations is currently being litigated in federal court in connection with bankruptcy applications by the cities of San Bernardino and Stockton. The City can provide no assurances about the outcome of the bankruptcy cases of other California municipalities or the nature of any adjustment plan if it were to file for bankruptcy.

In addition, if the Lease is determined to constitute a "true lease" by the bankruptcy court (rather than a financing lease providing for the extension of credit), the City could choose not to perform under the Lease and the claim of the owners of the Bonds could be substantially limited. An allowable claim could be substantially less than the amount of the Bonds outstanding, resulting in the owners of the Bonds suffering a substantial loss.

State Law Limitations on Appropriations

Article XIIIB of the California Constitution limits the amount that local governments can appropriate annually. The ability of the City to make Lease Payments may be affected if the City should exceed its appropriations limit. The State may increase the appropriation limit of cities in the State by decreasing the State's own appropriation limit. The City does not anticipate exceeding its appropriations limit in the foreseeable future. See "CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS – Article XIIIB of the State Constitution."

z Limitation on Remedies

The enforcement of any remedies provided for in the Lease and in the Indenture could prove to be both expensive and time-consuming. Although the Lease provides that if there is a default by the City, the Trustee may take possession of and relet the Leased Property, no

assurance can be given that the amounts received from such reletting would be sufficient to pay the principal of and interest with respect to the Bonds when due.

The Lease provides that upon the occurrence and during the continuance of the City's failure to deposit with the Trustee any Lease Payments when due, the bankruptcy of the City, or if the City breaches any other terms, covenants, conditions or agreements contained in the Lease (subject to a cure period as described in the Lease), the Trustee, as assignee of the Authority, has the following general remedies: (i) to reenter the Leased Property and relet the Leased Property; or (ii) to enforce its rights to recover Lease Payments as they become due. See APPENDIX D – "SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

In addition to the limitations on remedies contained in the Lease and the Indenture, the rights and remedies provided in those documents may be limited by and are subject to provisions of federal bankruptcy laws, as now or hereafter enacted, and to other laws or equitable principles that may affect creditors' rights generally. The various legal opinions to be delivered concurrently with the issuance of the Bonds will be qualified as to the enforceability of the various legal instruments by limitations imposed by State and federal laws, rulings and decisions affecting remedies, and by bankruptcy, reorganization or other laws of general application affecting the enforcement of creditors' rights, including equitable principles. See "- Bankruptcy Risks" below.

No Acceleration Upon Default

In the event of a default, there is no remedy of acceleration of the total Lease Payments for the term of the Lease. Any suit for money damages would be subject to the legal limitations on remedies against cities and counties in the State of California, including a limitation on enforcement of judgments against funds needed to serve the public welfare and interest. See APPENDIX D – "SUMMARY OF PRINCIPAL LEGAL DOCUMENTS."

Bankruptcy Risks

The rights of the owners of the Bonds and the enforceability of the Authority's obligation to make payments on the Bonds may be subject to bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting creditors' rights under currently existing law or laws enacted in the future, and may also be subject to the exercise of judicial discretion under certain circumstances.

Under existing law, the City is eligible to file for bankruptcy. Should the City file for bankruptcy, there could be adverse effects on the holders of the Bonds. In a bankruptcy of the City, the Authority or the Trustee as its assignee and the owners of the Bonds may be prohibited from taking any action against the City, any official of the City, or any property of the City (including the Leased Property) to enforce the terms of the Lease, unless the consent of the bankruptcy court is first obtained. The bankruptcy court is not required to give its consent. This prohibition on action may even prohibit the Trustee from using funds in its possession to make payments on the Bonds. As a result, Owners may experience temporary or permanent delays in the payment of the Bonds.

In a bankruptcy case, a plan of adjustment for the City could be confirmed that would allow for enforcement of the Lease, but the priority, interest rate, payment terms, collateral, maturity dates, payment sources, covenants and other terms or provisions of the Lease and the Bonds may be altered by the bankruptcy court. Such a plan could be confirmed even over the objections of the Authority or the Trustee as its assignee and the owners of the Bonds, and without their

consent. Additionally, the resulting plan could adjust some or all of the City's financial obligations, which include the City's lease payment obligations under the Lease and the City's obligation to fund certain retirement benefits. The adjustment of similar obligations is currently being litigated in federal court in connection with bankruptcy applications by the cities of San Bernardino and Stockton. The City can provide no assurances about the outcome of the bankruptcy cases of other California municipalities or the nature of any adjustment plan if it were to file for bankruptcy.

In addition, if the Lease is determined to constitute a "true lease" by the bankruptcy court (rather than a financing lease providing for the extension of credit), the City could choose not to perform under the Lease and the claim of the owners of the Bonds could be substantially limited. An allowable claim could be substantially less than the amount of the Bonds outstanding, resulting in the owners of the Bonds suffering a substantial loss.

State Law Limitations on Appropriations

Article XIII B of the California Constitution limits the amount that local governments can appropriate annually. The ability of the City to make Lease Payments may be affected if the City should exceed its appropriations limit. The State may increase the appropriation limit of cities in the State by decreasing the State's own appropriation limit. The City does not anticipate exceeding its appropriations limit in the foreseeable future. See "CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS – Article XIII B of the State Constitution."

Secondary Market for Bonds

There can be no guarantee that there will be a secondary market for the Bonds or, if a secondary market exists, that any Bonds can be sold for any particular price. Occasionally, because of general market conditions or because of adverse history or economic prospects connected with a particular issue, secondary marketing practices in connection with a particular issue are suspended or terminated. Additionally, prices of issues for which a market is being made will depend upon then-prevailing circumstances. Such prices could be substantially different from the original purchase price.

TAX MATTERS

The interest on the Bonds is not intended by the Authority to be excluded from gross income for federal income tax purposes. However, in the opinion of Jones Hall, A Professional Law Corporation, Bond Counsel, San Francisco, California, interest on the Bonds is exempt from California personal income taxes. The proposed form of opinion of Bond Counsel with respect to the Bonds, which is to be delivered on the date of issuance of the Bonds, is set forth in APPENDIX E.

Owners of the Bonds should also be aware that the ownership or disposition of, or the accrual or receipt of interest on, the 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 Bonds, the ownership, sale or disposition of the Bonds, or the amount, accrual or receipt of interest on the Bonds.

CERTAIN LEGAL MATTERS

Jones Hall, A Professional Law Corporation, Bond Counsel, will render an opinion with respect to the validity of the Bonds, the form of which is set forth in APPENDIX E. Certain legal matters will also be passed upon for the City and the Authority by Jones Hall, as Disclosure Counsel. Certain legal matters will be passed upon for the City and the Authority by the City Attorney, and for the Underwriters by their counsel, Nixon Peabody LLP.

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.

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 hereto. See "APPENDIX A – THE CITY OF SAN JOSE: GEOGRAPHIC, 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.

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, 2021 with the report for the 2019-2020 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 Trustee 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 Indenture.

The City engaged third-party consultants to conduct an analysis of the historical compliance of the City and 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 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 2015-2016 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 fiscal years 2015-2016 through 2017-18 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 issues of general obligation bonds that were defeased in July 2019.

MUNICIPAL ADVISOR

The City has retained Public Resources Advisory Group, Oakland, California, as its municipal advisor (the “**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.

UNDERWRITING

The underwriters named on the cover page of this Official Statement (collectively, the “**Underwriters**”), have entered into a Bond Purchase Agreement with the Authority under which they will purchase the Bonds at a purchase price of \$_____ (which is equal to the par amount of the Bonds, less an Underwriters’ discount of \$_____, and plus (less) a net original issue premium (discount) of \$_____).

BofA Securities, Inc. has entered into a distribution agreement with its affiliate Merrill Lynch, Pierce, Fenner & Smith Incorporated (“**MLPF&S**”). As part of this arrangement, BofA Securities, Inc. may distribute securities to MLPF&S, which may in turn distribute such securities to investors through the financial network of MLPF&S. As part of this arrangement, BofA Securities, Inc. may compensate MLPF&S as a dealer for their selling efforts with respect to the Bonds.

J.P. Morgan Securities LLC (“**JPMS**”) has entered into negotiated dealer agreements (each, a “**Dealer Agreement**”) with each of Charles Schwab & CO., Inc. (“**CS&Co.**”) and LPL Financial LLC (“**LPL**”) for the retail distribution of certain securities offerings at the original issue prices. Pursuant to each Dealer Agreement, each of CS&Co. and LPL may purchase bonds from JPMS at the original issue price less a negotiated portion of the selling concession applicable to any Bonds that such firm sells.

“US Bancorp” is the marketing name of U.S. Bancorp and its subsidiaries, including U.S. Bancorp Investments, Inc., which is serving as an Underwriter of the Bonds. U.S. Bancorp and its affiliates are full-service financial institutions engaged in various activities, that may include securities trading, commercial and investment banking, brokerage, and asset management.

The Underwriters will be obligated to take and pay for all of the Bonds if any are taken. The Underwriters intend to offer the Bonds to the public at the offering prices set forth on the inside cover page of this Official Statement. After the initial public offering, the public offering price may be varied from time to time by the Underwriters.

PROFESSIONAL SERVICES

In connection with the issuance of the Bonds, fees payable to the following professionals involved in the offering are contingent upon the issuance and delivery of the Bonds: Jones Hall, A Professional Law Corporation, as Bond Counsel and Disclosure Counsel; the Municipal Advisor; the Trustee, and Underwriters’ counsel.

ADDITIONAL INFORMATION

Quotations from and summaries and explanations of the Bonds, the Indenture 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.

EXECUTION

The execution of this Official Statement and its delivery have been authorized by the Board of the Authority and the City Council of the City.

CITY OF SAN JOSE FINANCING AUTHORITY

By: _____
Treasurer

CITY OF SAN JOSE

By: _____
Director of Finance

APPENDIX A

THE CITY OF SAN JOSE: GEOGRAPHIC, 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, 2019 (included in this Official Statement as Appendix C);
- Comprehensive Annual Financial Report for the Fiscal Year ended June 30, 2019;
- Comprehensive Annual Debt Report for the Fiscal Year ended June 30, 2019;
- Adopted Operating Budget for the Fiscal Years ended June 30, 2019 and June 30, 2020;
- Annual Report for the Fiscal Years ended June 30, 2018 and June 30, 2019;
- 2019-2020 Mid-Year Budget Report;
- 2020-2021 City Manager’s Budget Request & 2021-2025 Five-Year Forecast and Revenue Projections;
- 2020-2021 Mayor’s March and June Budget Message;
2020-2021 Proposed Operating Budget adopted on June 16, 2020, as modified by the City Manager’s Budget Addendum #33 adopted by the City Council on June 23, 2020 in connection with the City Council’s adoption of the Annual Appropriation Ordinance and the Annual Funding Sources Resolution implementing the 2020-2021 Operating and Capital Budgets.

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.

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 2020 estimated population of approximately 1,049,187¹, 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 336,200 workers out of a total civilian employment level of 1.04 million². 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 OUTLOOK

Recent Developments

The outbreak of COVID-19, a respiratory disease caused by a new strain of coronavirus (“COVID-19”), has been declared a pandemic by the World Health Organization, a national emergency by the President of the United States and a state of emergency by the Governor of the State, the County Board of Supervisors, and the City Council. The COVID-19 outbreak has caused tremendous economic volatility in the United States and globally, producing significant declines and the onset of a national and global recession.

The COVID-19 pandemic is ongoing, and its dynamic nature leads to uncertainties, including spread and severity of the virus, the duration of the outbreak, actions that may be taken by governmental authorities to contain or mitigate the outbreak, the development of medical treatments or vaccinations, and the impact of the outbreak on the local or global economy. The ultimate impact of COVID-19 on the City’s operations and finances is not fully known, and it may be some time before the full adverse impact of the COVID-19 outbreak is known.

While the COVID-19 pandemic is ongoing, the City expects significant reductions in revenue, including sales taxes, transient occupancy taxes, business taxes, and licensing and permit fees. While the City originally forecasted a General Fund surplus for 2020-2021 of \$0.5 million, that number was revised to an overall shortfall of \$77.6 million due to the effects of COVID-19, largely driven by revenue shortfalls that, when compared to 2018-2019 actuals, exceeds revenue shortfalls experienced in either the “Great Recession” or “Dotcom Bust.” The City was

¹ State of California, Department of Finance, E-4 Population Estimates for Cities, Counties, and State (Released May 2020).

² State of California, Employment Development Department, Labor Market Information Division, June 2020.

able to balance its 2020-2021 Adopted Operating Budget through a mix of ongoing and one-time solutions, with approximately 67% of the shortfall solved on an ongoing basis. For additional information see “MAJOR GENERAL FUND REVENUE SOURCES” in this Appendix A.

The State Department of Public Health has instituted a monitoring list for all counties in the State (the “**Watch List**”), with activities in each county restricted based on status. [The County is currently on the Watch List, and will not be able to continue its reopening plan until it meets the requirement for removal from the Watch List].

2020 Ballot Measures

On August 4, 2020, the City Council approved placing two measures on the November 3, 2020 ballot: (1) a measure related to the City’s cardrooms (the “Cardroom Measure”); and (2) a measure to (a) amend the City Charter to expand the Independent Police Auditor’s oversight, (b) revise the size and composition of the Planning Commission from 7 to 11 members with one member representing each Council District and one “at-large” member, and (c) to allow the City Council to establish timelines for redistricting when the results of the federal census are delayed.

The Cardroom Measure would amend the City’s Municipal Code to: increase the number of tables permitted by 30, to increase the existing tax on gross revenues of the City’s two cardrooms from 15% to 16.5% and to impose a tax on the gross revenues of the entities that bank the card games played at the cardrooms, referred to as third party providers of proposition player services, at the following rates;

Total Annual Gross Revenues	Rate
Up to \$25,000,000	5%
\$25,000,001 - \$30,000,000	7.5%
Over \$30,000,000	10%

For example, annual gross revenues of \$35 million would be taxed at a rate of 10% on the entire \$35 million with the resulting tax of \$3.5 million. The annual estimated revenue from the Cardroom Measure is \$15 million, assuming that the cardrooms are operating normally. Currently, both cardrooms are closed due to the health orders imposed to mitigate the spread of COVID-19. The revenues of the taxes imposed under the Cardroom Measure would be available for any governmental purpose. For more information on the City’s existing cardroom tax, see “MAJOR GENERAL FUND REVENUE SOURCES – Business Taxes – *Cardroom Tax*,” below.

The provision of the Cardroom Measure to increase the number of tables is subject to the review and comment of the California Department of Justice. All of the measures placed on the November 2020 ballot require majority approval in order to pass. The City cannot predict the outcome of any of the ballot measures or the outcome of the California Department of Justice’s review and comment on the proposed increase to the number of tables in the event the voters approve the Cardroom Measure.

2009 to 2020

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 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, including four voter-approved tax measures. These actions, 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 then under construction. The City did not emerge from a decade of deficits until 2012-2013, and has never experienced a significant surplus during the recently ended economic expansion, despite years of implementing structural deficit elimination plans. Now at the start of a new recession, the City anticipated that difficult decisions will be necessary to ensure a structurally balanced budget in future years as the economic impact of COVID-19 becomes clearer.

MUNICIPAL GOVERNMENT

Current Structure

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. Revisions to the Charter require voter approval.

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 that 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, Ice Centre at San José, and the SAP Center at San José (the “**SAP Center**”), 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.

Consideration of Governance Changes – Charter Review Commission

At City Council meetings during June and July 2020, the City Council considered placing a measure on the November 3, 2020 ballot to amend the Charter to, among other revisions, change the form of City government from a “Council – Manager” to a “Mayor – Council” form of government, to change the cycle of the Mayoral election to align with the presidential election and to specify certain limitations regarding campaign contributions, acceptance of gifts and membership on City boards and commissions in the City Charter. Ultimately, the City Council did not place the proposed measure on the November ballot.

Instead, on July 28, 2020, the City Council voted to establish a Charter Review Commission to bring forward recommendations to the City Council on (1) the City’s governance structure including the “Mayor-Council” governance structure found in other cities in the United States in which the Mayor has executive authority and the Council has legislative authority, and (2) alignment of the Mayoral election with the presidential election and whether the term of office of the candidate elected to be Mayor in 2022 would serve a two year term or six year term. In addition, the City Council referred to the Charter Review Commission and the City’s Board of Fair Campaign Practices, the limitations on campaign contributions, acceptance of gifts and membership on City boards and commissions that had been considered by the City Council at its meetings in June and July 2020 for consideration and recommendation. Consistent with the direction given by the City Council at the July 28, 2020 meeting, it is anticipated that City staff will return to the City Council in Fall 2020 with the proposed appointment to the Charter Review Commission for the City Council’s consideration and approval.

REDEVELOPMENT DISSOLUTION

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**”) pursuant to certain legal provisions 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.

On December 21, 2017, the Successor Agency issued the following refunding tax allocation bonds (collectively, the “**2017 Tax Allocation Refunding Bonds**”): (i) \$79,825,000 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 were outstanding in the total amount of approximately \$46.5 million, as of June 30, 2019, but have since been repaid with tax increment revenues generated within the project areas established by the Former Agency.

See Note IV. C. 4 to the City’s Basic Financial Statements for the Fiscal Year ended June 30, 2019, 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.

GEOGRAPHIC INFORMATION

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. The Coyote and Guadalupe rivers run through the city. The City is located in the Santa Clara Valley at the southern tip of San Francisco Bay, 48 miles south of San Francisco and 40 miles south of Oakland. The area is known as the Southern Peninsula. San Jose is the seat of Santa Clara County and the center of a large and expanding metropolitan area bordered by the Santa Cruz Mountains on the west and the Diablo Mountain range on the east. The Coyote and Guadalupe rivers run through the city.

There are potential risks to the City associated with its location and geography. See also “BOND OWNERS’ RISKS” in the forepart of this Official Statement.

Seismic Hazards. The City is in a region of very high seismic activity. Seismic hazards include 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. According to the most recent published maps prepared by the California Division of Mines and Geology, City Hall is located in an area that has potential for liquefaction during a major earthquake. According to the most recent published maps prepared by the California Geological Survey, City Hall is located in an area that has potential for liquefaction during a major earthquake. City Hall is located within the State of California Seismic Hazard Zone of Required Investigation for Liquefaction.

Drought. The City averages 300 days of sunshine annually, with temperatures varying from an average of 50 degrees Fahrenheit in January to an average of 70 degrees in July with a mean precipitation of 15.08 inches. In addition to seasonal variation, the area’s climate is subject to periodic droughts that impact water supply. Most recently, the City experienced a 5-year drought event of 2012-2017. Other notable droughts include an extreme single-year drought in 1976, when annual rainfall amounted to about one-half of the average rainfall; and a severe, prolonged drought in the late 1980s and early 1990s; over a four-year period, where annual rainfall was only two-thirds of the annual average.

The City is served by three retail water suppliers, the City owned and operated San Jose Municipal Water System, Great Oaks Water Company Incorporated, and San Jose Water Company. City residents are served with water from different sources, including groundwater, local surface water supplies, and wholesale supply from the San Francisco Public Utilities Commission (“**SFPUC**”) and Valley Water.

Water suppliers prepare an Urban Water Management Plan (“**UWMP**”) for the California Department of Water Resources every five years. These plans must assess the reliability of the water sources over a 20-year planning time frame, describe demand management, report on progress toward meeting a targeted 20 percent reduction in water per capita by 2020; and discuss the planned use of recycled water.

The latest UWMP prepared by the City for the San José Municipal Water System was due to the DWR in 2016, and a 2020 Plan is anticipated in 2021. As stated in the UWMP, climate change could result water resource impacts, including impacts on the watersheds in the Bay Area: (i) reductions in the average annual snowpack due to a rise in the snowline and a shallower snowpack in the low and medium elevation zones, such as in the Tuolumne River basin, and a

shift in snowmelt runoff to earlier in the year; (ii) changes in the timing, intensity and variability of precipitation, and an increased amount of precipitation falling as rain instead of as snow; (iii) long-term changes in watershed vegetation and increased incidence of wildfires that could affect water quality and quantity; (iv) sea level rise and an increase in saltwater intrusion; (v) increased water temperatures with accompanying potential adverse effects on some fisheries and water quality; (vi) increases in evaporation and concomitant increased irrigation need; and (vii) changes in urban and agricultural water demand.

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

Natural Flooding. The City is situated within the two major watersheds in the South San Francisco Bay. The largest of these is the Coyote Watershed, which encompasses 322 square miles and drains a large area in the eastern foothills, including major portions of Henry Coe State Park in the upper watershed above Anderson and Coyote Reservoirs. Coyote Creek is the primary feature within this watershed and runs north through both Coyote and Anderson Reservoirs towards the City through the North Coyote Valley, entering south San José and passing through central and north San José, joining the South San Francisco Bay on the eastern side of Alviso. Numerous small streams are tributary to Coyote Creek, generally originating in the undeveloped eastern foothills of East San José.

The Guadalupe Watershed drains the southern and western portions of the South Bay and portions of the Santa Cruz Mountains through both the Guadalupe River and Los Gatos Creek and their respective tributaries. The watershed includes 170 square miles. Other developed communities within the Guadalupe watershed include Campbell, Los Gatos, Saratoga, Monte Sereno, and unincorporated areas of Santa Clara County.

The Santa Clara Valley Water District (“**Valley Water**”) is responsible for flood protection infrastructure in the County on streams and waterways. Valley Water operates 10 reservoirs and dams in Santa Clara County, including 7 of which are within the Coyote or Guadalupe watersheds. The reservoirs, which were constructed in the 1930’s and 1950’s for water conservation (not flood protection), capturing runoff that would otherwise flow into San Francisco Bay. Reservoir operations and storage capacities do provide incidental flood protection, serve recreational needs, and benefit the environment by storing water for habitat preservation and groundwater infiltration.

Valley Water 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. Valley Water staff also prepare and maintain reports of severe flood events. These reports dating back to 1955 can be found on Valley Water’s website under Flood Protection. *Such website is not incorporated into this Official Statement. It is referenced for informational purposes only. The City and the Underwriters make no representation whatsoever as to the accuracy or completeness of any of the information on such website.*

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 FIRMs 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 FIRMs 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, San José Municipal Code Chapter 17.08 Special Flood Hazard Area Regulations. The Leased Property is located in an area designated by FEMA as Zone D.

Dam Inundation. Parts of the City are in the dam inundation area for a number of dams including Guadalupe Dam, Lenihan Dam, Anderson Dam and Cherry Flat Dam. Valley Water is also responsible for these dams, with the exception of Cherry Flat Dam, which is owned by the City. In a catastrophic event, damage to one or more of these dams could result in flooding within the City as depicted on inundation maps originally prepared by Valley Water in the early 1970's and mid 1990's. Updated versions of these inundation maps are on file with the California Office of Emergency Services and with the City.

Cherry Flat Dam. The City currently is not in compliance with State law that requires dam owners to prepare an inundation map and emergency action plan. In July 2020, the Division of Safety of Dams (“**DSOD**”) notified the City that the inundation map and associated technical report must be submitted to DSOD by September 30, 2020, or DSOD will pursue an enforcement action. Under State law, DSOD has the ability to enforce dam requirements through both civil and criminal actions and has the authority to impose civil penalties up to \$1,000 per day of violation. Prior to receiving DSOD's July 2020 letter, the City had initiated a flood inundation study for Cherry Flat Dam that will result in an inundation map for submittal to DSOD. Upon approval of the DSOD, the inundation map will assist with the development of and Emergency Action Plan, which will be submitted to the California Office of Emergency Services (“**Cal OES**”). On July 28, 2020, the City responded to DSOD's letter, providing the current schedule for completion of the inundation map by December 18, 2020 with the expectation that depending on the time for review by DSOD and Cal OES, the inundation map, emergency action and associated technical report would be completed and approved by May 2021. On August 3, 2020, DSOD notified the City, acknowledging the City's schedule, requiring the City to provide DSOD with a status update by September 30, 2020 and informing the City that further delay could expose the City to enforcement action as described above.

Anderson Dam. Valley Water commenced seismic stability studies on nine of Valley Water's dams in 2007. On July 6, 2011, Valley Water 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 City believes 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 one of the 42 Jurisdictional Dams in the County regulated by DSOD, 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. Prior to February 20, 2020, these regulatory agencies 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, but after a large inflow event, the dam operator must use available measures to lower the water surface to the maximum height dictated by the DSOD operating restriction. Studies have shown a large earthquake could damage Anderson Dam, causing damage or failure and an uncontrolled release of water that could inundate cities and rural areas from San Francisco Bay south to Monterey Bay, including much of Silicon Valley.

In response to the seismic study, Valley Water 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 2031 at an estimated cost of approximately \$563 million. City staff has (and will continue to) meet with Valley Water 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, and Valley Water will utilize storage capacity in existing reservoirs to monitor and maintain low to moderate creek flows downstream to avoid flooding.

On February 20, 2020, the Federal Energy Regulatory Commission (“**FERC**”) notified Valley Water of new Dam Safety Directives requiring that Valley Water immediately take all appropriate measures to maintain and quickly lower the reservoir to elevation 565 feet if the reservoir rises in the event of significant inflow, and further lower the reservoir to elevation 488 feet by no later than October 1, 2020, and take all appropriate measures to maintain and quickly lower the reservoir to deadpool in the event of significant inflow once the elevation is reached. Valley Water has responded to the FERC directive by noting that emptying the Anderson Reservoir has the potential to damage the intake structure, which would result in a loss of control of water flows out of the reservoir, potentially impacting downstream communities.

Pursuant to the FERC directive, Valley Water immediately restricted the reservoir operating level to elevation 565 feet and began defining the interim risk reduction measures now referred to as the FERC Order Compliance Project “**FOCP**”).

The FOCP is a set of proposed interim risk reduction measures as set forth in the FERC Order during the interim time period, concluding with the completion of a seismic retrofit project at the Anderson Dam. FERC expects construction of certain physical

improvements of the FOCIP to commence no later than early 2021 and be completed within approximately three years.

Coyote Dam. Coyote Reservoir and Dam, also operated by Valley Water, 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 23,666 acre-feet, which is approximately 25% of the storage capacity of Anderson Reservoir, which can store a total of 90,300 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.

Calero and Guadalupe Dams. On October 26, 2011, Valley Water 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, Valley Water has further restricted reservoir levels at the Calero and Guadalupe dams. In 2012, Valley Water 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 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.

Almaden, Lenihan and Stevens Creek Dams. 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. Valley Water 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.

The County also has 42 jurisdictional dams, of various sizes, nine of which are within or may impact the City. Of those, four have condition assessment ratings of "fair" and have reservoir operating restrictions in place, and five have condition assessment ratings of "satisfactory," with no restrictions on reservoir operations.

Wildfires. 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.

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.

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.

Population

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 whom 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. 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.

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 1 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 through 2019. The population in the City was 1,049,187 as of January 2020.

Table 1
City, County and State Population Statistics

	City of San José	% Change	County of Santa Clara	% Change	State of California	% Change
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.....	1,037,952	9.73	1,931,565	8.41	39,131,307	5.04
2017.....	1,045,047	0.68	1,942,176	0.55	39,398,702	0.68
2018.....	1,048,875	0.37	1,951,088	0.46	39,586,646	0.48
2019.....	1,047,871	(0.10)	1,954,833	0.19	39,695,376	0.28
2020.....	1,049,187	0.13	1,961,969	0.37	39,782,870	0.22

Sources: U.S. Census Bureau (1960-2010), California Department of Finance (2017-2020).

Economic Overview

General. The Silicon Valley, including the City, experienced a long period of economic expansion from 2010 through 2019, fueled primarily by technology sectors. That run of economic growth came to a sudden end in the first quarter of 2020, as the region, like much of the United States and the world, was forced to abide by restrictive public health orders in order to combat the spread of the COVID-19. Santa Clara County was among the first counties in the nation to order the closure of most businesses, resulting in temporary business closures and heavy job losses, particularly in the hospitality and service sectors. It remains unclear how many of these business closures and job losses will become permanent. Future economic prospects will depend on the status of public health orders, public health conditions and consumer confidence, which remain uncertain.

Employment. The June 2020 employment level in the San José MSA was 1,064,100, which represents an 8.1% drop from the June 2019 employment level. Between June 2019 and June 2020, employment contracted by 93,900 jobs in the San José MSA, including 30,100 jobs in the leisure and and hospitality sector. Other sectors that decreased include trade, transportation, and utilities (down 15,400 jobs), professional and business services (down 10,700 jobs), manufacturing (down 8,200 jobs), information (down 6,900 jobs), and government (down 6,700 jobs). 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.

Unemployment. Prior to the shelter-in-place mandate that was issued in March 2020, the unemployment rate at the local level had not exceeded 3.0% since August 2017. In February 2020, the San José MSA unemployment rate totaled 2.7%, but then immediately rose to 3.5% in March 2020. After growing to 12.0% in April 2020, the local unemployment rate has steadily declined to 11.3% in May 2020 and 10.8% in June 2020. This compares with an unadjusted unemployment rate of 15.1% for the State, 11.2% for the nation and 10.7% for the County in June 2020.³

Construction. Local residential construction activity in calendar year 2019 decreased 8.29% from calendar year 2018. Local residential construction activity through June 2020 decreased 29% from calendar year 2018. In particular, residential permits for new dwelling units through June 2020 totaled 1,992 versus 2,985 in the prior year. Correspondingly, the valuation of new residential construction and alteration activity have also decreased to approximately \$353.4 million in 2020, down from \$567.5 million in 2019. However, overall construction valuation (new construction and additions/alterations) increased by 2.7% across residential, commercial and industrial projects between the 2019 and 2020 calendar years. That increase is driven by a combined commercial and industrial total valuation, which increased by 22.2% year to year (rising from \$1.74 billion in 2019 to \$1.79 billion in 2020). See “– Construction Activity” for a history of construction valuation and new dwelling units for the most recent five calendar years.

From March 2020 through early May 2020, much of the Bay Area construction industry was required to stop work to comply with public health orders enacted to slow the spread of COVID-19. Construction has since been allowed to resume, but with additional safety requirements. Certain requirements could have an impact on the industry’s efficiency, which could

³ State of California Employment Development Department Labor Market Information Division Press Release, July 17, 2020.

impact project completion times, and the City is unable to predict whether future public health orders will again halt construction projects.

Home Prices and Sales. From spring 2012 through fall 2018, the median sale price for homes had consistently experienced year-over-year growth. Beginning in October 2018, however, the local real estate market in the County experienced a slow down, which lasted for approximately 12 months, until fall 2019 when the market began to stabilize and grow again. Recently, however, the COVID-19 pandemic and the resulting shelter-in-place orders have impacted portions of the local real estate market. According to data from the Santa Clara County Association of Realtors, for the months March 2020 through June 2020 the number of property transfers (sales) decreased from 10% to 54% year-over-year (from the same time period in the prior year). However, the median single-family home price has continued to grow with year-over-year increases ranging from 3% to 14% from March 2020 through June 2020 when compared to the same time period in the prior year.

Table 2 shows the average monthly median price for a single-family home in the City for 2010-2011 through 2019-2020.

Fiscal Year	Average Median Price	Percentage Change
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.....	1,120,042	(1.0)
2019-2020.....	1,136,729	1.5

Source: Santa Clara County Association of Realtors.

Employment

The City is the largest city in the County and third largest in the State. 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 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 last recession, but decreased to 2.3% in December 2019. Due to the COVID-19 pandemic and resulting recession, the City's unemployment rate rose to 10.8% in June of 2020.

Table 3 Estimated Average Annual Employment and Unemployment of Resident Labor Force⁽¹⁾					
Civilian Labor Force <i>(in thousands)</i>	2016	2017	2018	2019	2020⁽³⁾
City of San José					
Employed	524	532	540	556	489
Unemployed	22	19	15	13	69
Total ⁽²⁾	546	551	555	569	558
County of Santa Clara					
Employed	990	1,007	1,021	1,051	929
Unemployed	39	33	27	23	111
Total ⁽²⁾	1,029	1,040	1,048	1,074	1,040
Unemployment Rates					
City	3.9%	3.3%	2.7%	2.3%	10.8%
County	3.8	3.2	2.6	2.2	10.7
State	5.5	4.8	4.2	3.9	15.1
United States	4.9	4.4	3.9	3.7	11.2

⁽¹⁾ Data is not seasonally adjusted.

⁽²⁾ Totals may not add due to independent rounding.

⁽³⁾ As of June 2020.

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

Table 4 shows the composition of employment in the San José MSA by general category as of June 2018, 2019 and 2020.

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

Industry	2018	Percent of Total	2019	Percent of Total	2020	Percent of Total
Farm.....	6,400	0.56%	6,000	0.52%	5,300	0.50%
Natural Resources & Mining	200	0.02%	200	0.02%	200	0.02%
Construction	49,900	4.37%	53,700	4.64%	51,100	4.80%
Manufacturing	173,300	15.19%	173,100	14.95%	164,900	15.50%
Wholesale Trade	32,500	2.85%	31,600	2.73%	28,300	2.66%
Retail Trade.....	85,100	7.46%	82,600	7.13%	70,600	6.63%
Transportation, Warehousing, Utilities ...	15,500	1.36%	15,700	1.36%	15,600	1.47%
Information	93,500	8.20%	101,700	8.78%	94,800	8.91%
Financial Activities.....	36,600	3.21%	37,400	3.23%	36,100	3.39%
Professional & Business Services.....	237,400	20.81%	244,500	21.11%	233,800	21.97%
Educational & Health Services	174,000	15.26%	175,500	15.16%	169,800	15.96%
Leisure & Hospitality	108,000	9.47%	108,100	9.34%	78,000	7.33%
Other Services	29,300	2.57%	29,500	2.55%	23,900	2.25%
Government	98,900	8.67%	98,400	8.50%	91,700	8.62%
Total ⁽¹⁾	1,140,600		1,158,000		1,064,100	

⁽¹⁾ 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 January 2020. 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 January 2020

	Company/Organization	Approximate Number of Employees	Percent of Total City Employment
1	County of Santa Clara	18,870	4.30%
2	Cisco Systems	9,390	2.14%
3	City of San Jose	6,620	1.51%
4	IBM	3,870	0.88%
5	San Jose State University	3,600	0.82%
6	PayPal, Inc.	3,600	0.82%
7	eBay	3,500	0.80%
8	Adobe Systems Inc.	3,400	0.77%
9	Kaiser Permanente	3,040	0.69%
10	Western Digital	2,710	0.62%
11	Good Samaritan Health System	2,240	0.51%
12	Super Micro Computer	2,220	0.51%
13	Cadence Design Systems	1,900	0.43%
14	Intel	1,800	0.41%
15	Regional Medical Center	1,630	0.37%

Source: City of San José, Office of Economic Development, San José business tax filings, and company surveys.

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 2018, the most recent American Community Survey available. The San José MSA had the highest median household income in 2018, which was well above the national median.

Table 6
United States
2018 Top Ten Median Household Income

1.	San José-Sunnyvale-Santa Clara, CA Metro Area	\$124,696
2.	San Francisco-Oakland-Fremont, CA Metro Area	107,898
3.	Washington-Arlington-Alexandria, DC-VA-MD-WV Metro Area	102,180
4.	California-Lexington Park, MD Metro Area	92,250
5.	Bridgeport-Stamford-Norwalk, CT Metro Area	91,079
6.	Boston-Cambridge-Newton, MA-NH Metro Area	88,711
7.	Seattle-Tacoma-Bellevue Metro Area	87,910
8.	Napa, CA Metro Area	87,025
9.	Santa Cruz-Watsonville, CA Metro Area	86,941
10.	Oxnard-Thousand Oaks-Ventura, CA Metro Area	84,566
	U.S. Median	\$61,937

Source: U.S. Census Bureau, American Community Survey 2018 1-Year Estimates.

Retail Sales

Table 7 sets forth a history of taxable sales for the City for calendar years 2016 to 2019, as reported by the California State Board of Equalization (the “**BOE**”) for 2016 and the California Department of Tax and Fee Administration (“**CDTFA**”) for years 2017 through 2019. Taxable sales are reported using the North American Industry Classification System codes.

For 2018-2019, sales tax receipts of the City totaled approximately \$263.5 million, an increase of approximately \$37.2 million over sales tax receipts of approximately \$226.3 million for 2017-2018. This increase is partially the result of processing issues by the CDTFA that resulted in approximately \$10 million of Sales Tax revenue being recognized in 2018-2019 that was attributed to 2017-2018 activity. 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 2015 to 2019 (in thousands)				
	2016	2017	2018	2019
Motor Vehicle and Parts Dealers	\$2,034,428	\$2,134,572	\$2,415,535	\$2,309,530
Home Furnishings and Appliance Stores	727,764	728,521	849,860	750,997
Bldg. Matrl. and Garden Equip. and Supplies.....	945,772	972,171	1,041,280	1,035,431
Food and Beverage Stores	559,060	577,938	587,734	612,820
Gasoline Stations.....	954,475	1,050,646	1,185,859	1,191,977
Clothing and Clothing Accessories Stores.....	998,722	971,102	1,000,629	1,004,646
General Merchandise Stores	1,071,528	1,110,193	1,328,693	1,359,652
Food Services and Drinking Places.....	1,940,194	2,045,134	2,127,153	2,248,265
Other Retail Group.....	1,014,199	968,095	1,007,301	1,803,334
Total Retail and Food Services.....	10,246,142	10,558,372	11,544,044	12,316,652
All Other Outlets	4,878,198	4,495,992	4,867,941	4,790,466
Total All Outlets	<u>\$15,124,340</u>	<u>\$15,054,364</u>	<u>\$16,411,985</u>	<u>\$17,107,118</u>
<i>Source: California State Board of Equalization. Taxable Sales in California (Sales & Use Tax) for 2016. State Department of Tax and Fee Administration for years 2017 through 2019.</i>				

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 <i>(in thousands)</i>					
	2015	2016	2017	2018	2019
Valuation:⁽¹⁾					
Residential	\$ 483,399	\$ 563,521	\$ 694,998	\$536,303	\$500,873
Non-Residential .	870,199	1,535,204	1,658,682	795,116	1,687,996
Total	\$ 1,353,598	\$ 2,098,725	\$2,353,680	\$1,331,419	\$2,188,869
New Dwelling Units:					
Single Family	160	226	201	315	568
Multi-Family.....	1,860	1,862	2,896	2,658	1,881
Total	2,020	2,088	3,097	2,973	2,449

⁽¹⁾ Valuation figures are adjusted to 2019 dollars (December, 2019 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 2019-2020 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, 67 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, 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**”), which the City owns and operates, 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 63,600 in 2019. Caltrain typically 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, the Milpitas Transit Center and the Berryessa Transit Center, that are part of two bigger, new transit centers that opened in June 2020. The Milpitas and Berryessa/North San José BART Stations are served by two lines providing direct and connecting service to the entire BART system.

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 2029-2030. 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. The final environmental impact report for the high-speed rail system project is expected to be released in May 2021.

In 2019, the City, in partnership with VTA, the County and neighboring cities, issued a request for information to develop transit options from Diridon Station to the Airport. Twenty-three responses were received, and City Council expects to discuss next steps in Fall of 2020.

Impacts of COVID-19. Currently, the historic Diridon Station, is served by Caltrain, VTA light rail, Altamont Corridor Express, and Amtrak/Capitol Corridor, and numerous bus lines. As of August 10, 2020, Bay Area transit and rail agencies, including VTA, Caltrain and BART, are running reduced schedules and/or service hours due to COVID-19 and related public health orders. [To be updated]]

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 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 2018, the most recent data available,, the Airport was the 40th busiest airport nationwide in terms of total passengers.

To accommodate the large increase in air traffic, the Airport recently built 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 during calendar year 2019.

On April 28, 2020, City Council in approved an amendment to the Airport Master Plan and approved a new Environmental Impact Report (“**EIR**”). The purpose of the amendments to the Airport Master Plan include:

- extending the planning horizon and update the aviation demand projections to year 2037;
- incorporating the airfield safety and reconfiguration projects recommended in the Runway Incursion Mitigation/Design Standards Analysis (“**RIM**”) Study;
- modifying various landside facility improvement projects to adequately serve demand projected to year 2037.

In addition, as a recipient of federal funds, the Airport will be required to update the environmental effects for the proposed new Airport Master Plan following the requirements of the National Environmental Policy Act by completing an Environmental Assessment (“**EA**”). The Airport expects to bring the EA before the City Council for approval in late 2020 or early 2021, although there are no plans to implement the Airport Master Plan by beginning construction while the COVID-19 pandemic is ongoing.

The Airport is experiencing and expects to continue to experience a significant decrease in aviation and non-aviation revenues as a result of the COVID-19 pandemic. Airport revenues

depend on the level of aviation activity and passenger traffic at the Airport. The ability of the Airport to derive revenues from operations depends upon the financial health of the airlines serving the Airport and the entire airline industry.

RECENT ECONOMIC DEVELOPMENT ACTIVITIES

Overview

The value of new industrial development and alterations in the City increased in 2019-2020 over 2018-2019, while new residential construction and alterations declined over the same time period, according to City permitting data that includes project valuations. Meanwhile, commercial development and alterations increased. After years of growth, recent trends suggested that development levels had plateaued, and the rate of new development may begin to slow. This trend was evident prior to the outbreak of COVID-19, which may further chill development momentum, but much remains unclear about the depth and length of the impacts of the pandemic and its economic effects. See “DEMOGRAPHIC AND ECONOMIC INFORMATION - Economic Overview - Construction for additional information about recent construction activity in the City.

Overall, according to the City’s five-year planning forecast, which was last updated in early 2020, prior to the outbreak of COVID-19, new residential units were forecasted to decline in 2020-2025 based on building permits issued in 2018- 2019 and the housing market, which has slowed due to increases in the costs associated with new construction. New commercial and retail construction may also decline as the market absorbs existing big-box vacancies, as consumer shopping habits shift online, and due to disruption and widespread retail bankruptcies expected as a result of the COVID-19 crisis.

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. The General Plan provided capacity for a large expansion of both jobs and residences, a critical component of which 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 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, of the sale of the Diridon SARA Properties was completed. 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 addition, discussions are currently underway between the City and Google with respect to an option agreement for the roughly 10.5-acre property north of Santa Clara Street and adjacent to the SAP Center that is operated by Sharks Sports and Entertainment (“**SSE**”) under a lease with the City. The option agreement specifies that Google and SSE must come to mutual agreement to effectuate the transfer of the property, and the City is unable to predict whether the parties will come to an agreement. Should the parties not agree, Google may complete the transaction at the conclusion of the term of SSE’s lease of the SAP Center, which ends in 2040.

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. While the current schedule targets an April 2021 date for City Council consideration of approval of the development agreement, the City cannot provide any assurance as to when such a development agreement will be entered into, if ever. In October of 2019, Google submitted its Downtown West Mixed-Use Plan to the City, initiating the City’s project review period.

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.

Google is not the only party interested in investing in the Downtown core. Approximately 3.6 million square feet of office space was under construction in the Downtown area and Diridon Station Area, as of July 2020. From 2017 through July 2020, investors spent over \$4.2 billion on land-development sites, existing office buildings, hotel properties, multifamily investments, and retail properties, according to CoStar, a real estate information service. As of July 2020, developers had received approved entitlements for roughly 4.4 million square feet of office space in the downtown area and Diridon Station Area that had not yet proceeded to construction, not including the Google proposal. The largest 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. The proposal was approved by the City Council in June, 2020. The City can provide no assurances on when the project will be built, if ever.

Most Downtown construction during the last several years has been residential in nature, but the office construction market has recently been increasing. As of July 2020, approximately 1,668 residential units, 67,582 square feet of retail, and 2,639,312 square feet of office space were under construction in the core downtown area. Expanding the area to include the Diridon Station Area yields another 1 million square feet of office space as well as 249 residential units under construction.

While Downtown is still a relatively small office market (it had a daytime employment of roughly 43,000 as of 2018), these under-construction and 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.

Adobe North Tower. On June 24, 2019, Adobe commenced 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. The fourth office tower is being constructed on a parcel across the street from the existing three-tower campus. The fourth tower 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 has provided to the City. Construction was halted during the initial phase of the shelter-in-place order to combat COVID-19, but construction resumed as of mid-May 2020, and construction sites were still active as of July 2020. It is currently expected that some companies will allow their employees to continue working remotely until the COVID-19 crisis is over, and perhaps on a permanent basis. The City cannot predict when construction of the North Tower will be completed, if ever, or whether it will be occupied upon completion.

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 in the North San José area has been boosted by recent 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. In November 2019, Apple announced its intention to commit \$2.5 billion toward helping to alleviate housing availability and affordability in the Bay Area. Of the total amount, Apple announced \$300 million would come from the Apple-owned land in North San José. It is not clear exactly what Apple will propose to do with the land. 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 additional 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. The third agreement is with the City of Milpitas and the City has satisfied its obligations under that agreement

Both settlement agreements with the City of Santa Clara and the County 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 Boulevard and Trade Zone Boulevard, including all portions of the Expressway, regardless of City boundaries, including interchange modifications at I-880 and the Trimble Road flyover (the “**Flyover**”) as part of Phase I of the NSJ ADP. Some of the work to widen Montague Expressway to eight lanes 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 this does not include funding for the Trimble Flyover, as detailed below. 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, so the Phase I obligations of these settlement agreements are not yet applicable.

The City has attempted unsuccessfully to negotiate changes to the settlement agreements with the City of Santa Clara, attempting primarily to amend the NSJ ADP phasing plan to provide more housing opportunities and to change the phasing of the transportation improvement to reflect where development has occurred. The City of Santa Clara requested advisory mediation in accordance with the provisions of the agreements alleging an anticipatory breach of its settlement agreement if the City were to carry out its intent to rephase the NSJ ADP. The City and the City of Santa Clara are currently engaged in the mediation process.

On July 1, 2020, the City advised the City of Santa Clara that it intends to reconsider its prior area plans for North San José. Instead, the City will transition to a project-by-project approach for development in the area consistent with the City's General Plan. Should that occur, the City would withdraw the North San Jose Development Policies, meaning the obligations set out in the 2006 settlement agreements would no longer be applicable to development in the area and would thereafter need to be re-negotiated.

If the City is unable to come to an agreement with the City of Santa Clara, the City may become engaged in litigation, which could be costly, and could delay development in the City, hindering growth in property tax receipts. In 2018, the time of the most recent estimate, the City preliminarily projected that it would be responsible for approximately \$47 million in costs if required to complete the Flyover modifications. The City has not set any funds aside for this purpose,

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 expanded the 1.5-million-square-foot mall by 650,000 square feet. It was substantially completed by mid-2020. The expansion included a new Bloomingdale's store, a new flagship Apple store, space for 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 to be located on the portion of Valley Fair within the City. The expansion's first phase, which included the Bloomingdale's department store, opened in February 2020, shortly before the public health orders closed most retail establishments throughout the City. Westfield and other malls in the City re-opened in June 2020, after the loosening of the shelter-in-place order. However, the State again ordered the closure of malls in mid-July 2020, and it is unclear when malls may reopen. The long-term outlook of many traditional mall tenants was uncertain due to the trend of consumers shifting to online shopping, and additional retailers have filed for bankruptcy protection following the outbreak of COVID-19.

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 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. Federal Realty Investment Trust has begun construction on the first building, totaling 350,000 square feet, on the site. Construction halted during the first phase of the shelter-in-place orders, but resumed in mid-May 2020.

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 Costco store that opened in 2017), and 386,000 square feet of data center space. Most of these projects are now either complete or under construction, with the final 700 residential units nearing completion. Western Digital has also expanded over the past few years, 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. Interest in the construction of data centers in the Edenvale area has remained strong, and there is a roughly 300,000-square-foot data center project for China Mobile currently under construction

Development Challenges

Future development within the City is expected to face a number of 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, even prior to the outbreak of COVID-19. These challenges, which are not unique to San José, were 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 (“**KMA**”) 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.

A nexus analysis was prepared July 2020 for the City by KMA, considering a potential commercial linkage fee to be imposed on new non-residential development to fund affordable housing, which explains that the COVID-19 pandemic has had widespread effects on business and society and caused a sharp economic downturn which, within Santa Clara and San Benito counties, resulting in the loss of approximately 133,000 jobs from February to May 2020. The recession created by the pandemic is expected to be a temporary condition from which the economy will eventually recover over the long term and will extend over the life of new commercial development. However, in addition to short-term economic damage, the pandemic is contemplated as a driver of possible long-term changes which need to be taken into consideration.

The coronavirus pandemic has resulted in a need for businesses to implement measures to protect the health and safety of workers. Among the changes being implemented or contemplated are modifications to office layouts that increase the distance and physical

separation between employees. This has led to speculation that the density of employment within office buildings could be reduced on a more permanent basis. Interviews with local developers conducted by KMA in June 2020 confirmed a reduced density of employment within office buildings is currently being imagined as a possible longer-term outcome of the pandemic, especially with respect to high-tech tenants which tend to have open floor plan offices and a high density of employment. The experience adapting to remote working during the pandemic has led some businesses to plan for remote work as a larger part of their operations post-pandemic. A trend toward remote work would be expected to reduce demand for new commercial buildings overall, but does not necessarily reduce employment density within the commercial buildings that are already built.

The COVID-19 crisis could further challenge development if an extended recession depresses the demand for real estate, depresses rents, or negatively impacts the capital markets and ability of lenders to finance projects. Consumer behavioral shifts could also contribute to changes in business operations that result in lower demand for real estate. For instance, as explained above, demand for office space may decline if companies allow more employees to work from home. Prolonged concern about the use of public transit could threaten the attractiveness of transit-oriented development projects. Accelerated adoption of e-commerce could diminish plans for future retail, commercial and entertainment development. Additionally, widespread disruption, bankruptcies and consolidation in the retail sector could depress future development of these types of shopping centers.

San Jose Municipal Water System's Water Supply: Through its San Jose Municipal Water System, the City provides water service to approximately 26,000 potable and recycled water customers combined, representing roughly 100,000 residents in the Evergreen, North San Jose/Alviso, Edenvale, and Coyote Valley areas.

San Jose Municipal Water relies on four sources of supply: surface water from SFPUC, local and imported surface water from Valley Water, groundwater from the Santa Clara groundwater basin, and the City's recycled water program. All water supplies may be impacted by the challenges related to drought as outlined above in the "**Drought**" above. For the SFPUC water supply, serving the North San Jose/Alviso area, the business relationship between the SFPUC and its wholesale customers is largely defined by the "Water Supply Agreement between the City and County of San Francisco and Wholesale Customers in Alameda County, San Mateo County and Santa Clara County (WSA)" as amended and restated in 2018. The 2018 action amended a 2009 25-year WSA without extending the term, which expires in June, 2034, with options through 2044. The WSA addresses the ratemaking methodology used by the SFPUC in setting wholesale water rates for its customers in addition to addressing water supply and water shortages. The WSA serves as the master agreement and it provides for a 184 million of gallons per day (MGD) Supply Assurance to all the permanent SFPUC wholesale customers on an annual average basis. The WSA is supplemented by an individual Water Sales Contract between SFPUC and each individual retailer, entered into in July 2009. The individual Water Sales Contract indicates any specific conditions between SFPUC and the retailer. The City's Water Sales Contract as amended in 2009 continues to be a temporary and interruptible supply contract. The City has no Individual Supply Guarantee but does have an Interim Supply Allocation of 4.5 MGD, which requires 10-year notice before interruption. For drought conditions, the WSA contains a Water Shortage Allocation Plan which first requires voluntary reductions, but then permits the SFPUC to implement mandatory reductions if necessary to respond to water shortages.

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 2020-2021 on June 16, 2020 and adopted the Annual Appropriation Ordinance and Funding Sources Resolution implementing the 2020-2021 Operating and Capital Budgets on June 23, 2020. See “FISCAL OUTLOOK” 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.

2019-2020 Adopted Operating Budget

The City Council adopted the 2019-2020 Adopted Operating Budget on June 11, 2019 (the "**2019-2020 Adopted Operating Budget**"), after a series of City Council Budget Study Sessions to consider the many proposals set forth in the 2019-2020 Proposed Operating Budget. The 2019-2020 Adopted Operating Budget was a balanced budget that continues efforts to address the highest priority community and organization needs while maintaining budget stability.

The 2019-2020 Adopted Operating Budget included investments across multiple City funds that supported the following major initiatives as identified in the Mayor's March and June Budget Messages and as approved by the City Council for Fiscal Year 2019-2020: Saving; Public Safety; Confronting the High Cost of Housing and Living; Homelessness; Combatting Blight; the Environment; Educational Opportunity and Enrichment for Youth; Inclusive, Age-Friendly, and Family-Friendly Services; Neighborhood Empowerment and Community Building; Economic and Cultural Vitality; and Innovation and Technological Implementation.

COVID-19 Impacts to the 2019-2020 Budget and the 2020-2021 Budget Development Process

The onset of the COVID-19 pandemic, and the economic impact of the necessary public health orders to limit the disease's spread, significantly altered revenue projections and the budget modification and development processes for 2019-2020 and 2020-2021. The 2019-2020 Mid-Year Budget Review released on January 31, 2020, and approved by the City Council on February 11, 2020, reported that City funds were generally performing within budgeted levels, and that General Fund revenues were on pace to exceed estimates by \$15 million to \$20 million.

The 2020-2021 City Manager's Budget Request & 2021-2025 Five-Year Forecast (the **"2021-2025 Forecast"**) released on March 2, 2020 anticipated moderately positive economic growth through 2020-2021 with a modest estimated General Fund surplus of \$0.5 million; however, the 2020-2021 Forecast stated that the impacts of the COVID-19 were just beginning to be felt and that the City would closely monitor the changing economic conditions as part of the 2020-2021 Proposed Budget Process. The Mayor's March Budget Message for Fiscal Year 2020-2021, released on March 6, 2020, and approved by the City Council on March 17, 2020, highlighted the recent outbreak of COVID-19 in the County and gave direction to focus budget development using a tiered approach, focusing first on fiscal resilience and generally limiting other General Fund investments unless economic conditions were to significantly improve.

As economic conditions continued to deteriorate, City staff presented a preliminary estimate of economically sensitive revenue categories to the City Council on April 7, 2020, estimating General Fund revenue shortfalls of \$45 million in 2019-2020 and \$65 million in 2020-2021. At its meeting on April 28, 2020, the City Council approved reductions to the 2019-2020 General Fund revenue estimate of \$45 million attributable to projected decreases in sales tax (\$27 million), transient occupancy taxes (\$6.5 million), fees, rates and charges (\$5.5 million), utility taxes (\$3 million), business taxes (\$2 million), and fines, forfeitures and penalties (\$1 million). The revenue reduction was offset by recognizing additional sales tax revenue generated from the Revenue Capture Agreement with eBay in the amount of \$18.0 million, recognizing additional net savings from the sale of the Hayes Mansion Property in February 2019 of \$2.6 million, as well as reducing a number of expenditures and liquidating reserves totaling \$24.4 million. See "MAJOR GENERAL FUND REVENUE SOURCES - Sales and Use Taxes" for additional discussion of the Revenue Capture Agreement.

Table 9 on the following page summarizes the City's actual General Fund performance for 2018-2019, the Modified Operating Budget for 2019-2020, and the Adopted Operating Budget for 2020-2021.

Table 9
City of San José
General Fund Budget Summaries⁽¹⁾
2018-2019 Actuals, 2019-2020 Modified Budget and 2020-21 Adopted Budget
(in thousands)

SOURCE OF FUNDS	2018-2019 Actuals	2019-2020 Modified Operating Budget⁽²⁾	2020-2021 Adopted Operating Budget
FUND BALANCE			
Encumbrance Reserve	\$38,467	\$46,555	\$46,555
Carryover	249,953	364,813	346,336
Total Fund Balance	\$288,420	\$411,368	\$392,891
GENERAL REVENUES			
Property Tax	\$330,199	\$364,000	\$370,500
Sales and Use Tax	263,530	249,300	242,500
Transient Occupancy Tax	20,536	13,500	9,000
Franchise Fees	48,397	48,641	45,921
Utility Taxes	99,253	96,645	95,800
Real Property Transfer Tax	--	--	30,000
Telephone Line Tax	21,593	20,000	20,000
Business Taxes	74,903	70,200	70,900
Licenses and Permits	65,295	62,009	20,023
Fines and Forfeitures	17,402	15,213	15,730
Revenue from Use of Money and Property	10,072	13,144	11,755
Revenue from Local Agencies	16,685	17,365	18,195
Revenue from the State Government	15,102	23,037	14,320
Revenue from the Federal Government	3,106	6,540	3,715
Fees, Rates and Charges	55,703	50,236	25,576
Other Revenue	247,368	37,796	48,512
Total General Revenue	\$1,289,145	\$1,087,662	\$1,042,446
Overhead Reimbursements	\$53,237	\$56,273	\$69,198
Transfers to the General Fund	35,295	40,758	27,409
Reimbursements for Services	17,200	17,275	15,746
Total Interfund Transfers Reimbursements	105,732	114,307	112,352
TOTAL SOURCE OF FUNDS	\$1,683,297	\$1,613,336	\$1,547,689
USE OF FUNDS			
DEPARTMENTAL			
General Government	\$103,173	\$126,880	\$121,657
Public Safety	632,699	647,244	698,912
Capital Maintenance	80,541	89,138	74,011
Community Services	164,648	190,470	139,919
Total Departmental	\$981,060	\$1,053,732	\$1,034,500
NON-DEPARTMENTAL			
Citywide	\$228,671	\$121,820	\$123,612
Capital Expenditures	14,366	73,627	54,442
Transfers to Other Funds	47,831	48,967	74,103
Earmarked Reserves	--	228,635	174,477
Encumbrance Reserve	46,555	46,555	46,555
Contingency Reserve	--	40,000	40,000
Total Non-Departmental and Reserves	\$337,424	\$559,604	\$513,190
TOTAL USE OF FUNDS	\$1,318,485	\$1,613,336	\$1,547,689

⁽¹⁾ Totals may not add due to independent rounding.

⁽²⁾ As of June 30, 2020.

Source: City of San José.

2020-2021 Proposed Operating Budget

On May 12, 2020, the City Manager released the 2020-2021 Proposed Operating Budget (the “**2020-2021 Proposed Operating Budget**”) that addresses an anticipated General Fund shortfall of \$71.6 million, with an estimated revenue decline of 9% from fiscal year 2018-2019 actual receipts. The revenue shortfall of \$65 million preliminary estimated in the April 7th City Council memorandum grew to \$78.6 million, partially offset by revised expenditure assumptions to arrive at the net shortfall of \$71.6 million. This magnitude is substantially higher than the decreases experienced during the Dotcom Bust (in 2001-2002 and 2002-2003) and Great Recession (in 2008-2009 and 2009-2010), during which General Fund revenues dropped 2.9% and 5.5%, respectively, over a two-year period. As described below, during the budget process in May and June 2020, the total shortfall grew from \$71.6 million to \$77.6 million.

In the 2020-2021 Proposed Budget, the total net funding is \$4.1 billion for all City funds, including capital funds, \$523.6 million (11.2%) below the 2019-2020 Adopted Budget. This decrease primarily reflects the loss of revenue anticipated across all City resources as a result of the COVID-19 pandemic and lower levels of financing proceeds. The Proposed Budget, however, does not include funds that will be re-budgeted and added to the 2020-2021 Adopted Budget to complete multi-year projects.

Led by deep year-over-year reductions in Sales Tax, Business Taxes, and Transient Occupancy Tax, combined with shortfalls in Utility Taxes and Franchise Fees, and reduced growth rates for Property Tax proceeds, General Fund revenues are forecasted to drop 9% compared to 2018-2019 actuals. Although the exact depth or length of this recession is not known, especially given that social distancing is likely to continue for an extended period of time, the City expects General Fund shortfalls over the next several years.

Of the \$71.6 million shortfall in the General Fund projected in the 2020-2021 Proposed Operating Budget, \$51.9 million (73%) was resolved on an ongoing basis. The remaining shortfall of \$19.7 million (27%) was solved using one-time funds. Though in a normal budgeting cycle the City would strive to keep estimated ongoing revenues and expenditures in balance, given the extraordinary and sudden nature of the economic decline and a compressed timeline for budget development, the prudent use of one-time bridge funding into 2021-2022 is the recommended approach in the 2020-2021 Proposed Operating Budget. Although the Proposed Operating Budget resulted in a net position reduction of 103 full-time equivalent positions, the City leveraged the elimination of vacant positions such that no employees were laid off due to actions included in the 2020-2021 Proposed Operating Budget.

To resolve the General Fund shortfall for 2020-2021, the 2020-2021 Proposed Operating Budget includes recommendations grouped in four categories: (1) COVID-19 Impacted Services; (2) Other Direct Service Impacts; (3) Strategic Support Impacts; and (4) Proposals with No Impact. “Proposals with No Impact” play a substantial role in resolving the then projected General Fund shortfall of \$71.6 million, which include the following:

Sales Tax – Revenue Capture Agreement Annualization. As described above, the proceeds from the Revenue Capture Agreement with eBay are anticipated to yield ongoing sales tax revenues for the City. The amount estimated in 2020-2021 is \$22 million.

Pre-Funding of City Retirement Contributions. Actions are included in the Proposed Budget to facilitate prepayment of the City’s retirement costs for both the

Tier 1 pension costs and the Tier 1 Unfunded Actuarial Liability in the Federated City Employees' Retirement System Plan and the Police and Fire Department Retirement Plan (collectively, the "**Retirement Plans**"). See APPENDIX B – "THE CITY OF SAN JOSE: RETIREMENT PLANS."

Annual prepayments by the City of its employer contributions to the Retirement Plans in lieu of biweekly contributions will generate approximately \$13.9 million in savings in all funds, \$11.4 million in the General Fund. In the General Fund, these savings will be offset by an estimated \$2.6 million loss in interest earnings and \$1.4 million in short-term borrowing costs (TRANs debt service), resulting in a total net savings of \$7.4 million. See "BONDED AND OTHER INDEBTEDNESS - Tax and Revenue Anticipation Notes."

Pay Down Debt. The City anticipates leveraging the refunding of existing indebtedness (the 2006A Bonds, the 2007A Bonds and the 2013A Bonds) to yield one-time funds of approximately \$26 million that will pay off the remaining debt associated with the LED streetlight conversion project (\$10.6 million) under the Equipment Lease and the Los Lagos Golf Course (\$7.9 million) financed by the 2007A Bonds. See "FINANCING PLAN" in the forepart of this Official Statement.

Fuel Savings. Fuel savings are recognized through an updated forecast of oil and fuel prices impacted by global and regional economic conditions, resulting in city-wide savings of \$1.24 million, of which \$940,000 is in the General Fund.

Contingency Package. The City has also considered the possibility that conditions may worsen further and that revenue shortfalls could be significantly greater than currently estimated. A contingency package of budget reduction proposals is included as an attachment to the City Manager's transmittal in the Proposed Budget. The contingency package provides for the reduction of General Fund expenditures of \$12.1 million through a series of additional actions that may be brought forward later, if necessary, to address an even larger shortfall. Such actions include the reduction of an additional 75 full-time equivalent employees. It is important to note that future City Council action would be necessary to enact these reductions.

It is important to note that of the \$32 million Budget Stabilization Reserve previously set aside by the City as a buffer against sudden revenue losses or unavoidable expenditure increases, the City used \$11 million to help balance the 2020-2021 budget, leaving \$21 million to provide additional buffering against any further impacts in 2020-2021, and to assist with an expected challenging budget development process for 2021-2022.

2020-2021 Mayor's June Budget Message

On June 8, 2020, the Mayor released the June Budget Message for 2020-2021 (the "**Mayor's June Budget Message**"), outlining his final recommendations and changes to the 2020-2021 Proposed Operating Budget. The public hearing on the Mayor's June Budget Message occurred on June 15, 2020, and the City Council completed the final review and approval of the message, with a number of revisions, on June 16, 2020.

2020-2021 Adopted Operating Budget

After a series of City Council Budget Study sessions and a public hearing, the City Council adopted the 2020-2021 Proposed Operating Budget on June 16, 2020, with certain modifications on June 23, 2020, in connection with the City Council's adoption of the Annual Appropriation Ordinance and the Annual Funding Sources Resolution implementing the 2020-2021 Operating and Capital Budgets. The 2020-2021 Proposed Operating Budget as modified by the City Manager's Budget Addendum #33 and adopted by the City Council on June 23, 2020 is referred to in this Official Statement as the "**2020-2021 Adopted Operating Budget.**" Such modifications include the changes to the 2020-2021 Proposed Operating Budget set forth in the Mayor's June Budget Message that were reviewed and revised by the City Council on June 16, 2020. The City anticipates publishing the 2020-2021 Adopted Operating Budget in the Fall of 2020.

The modifications to the 2020-2021 Proposed Operating Budget with the approval of the Mayor's June Budget Message included a number of changes impacting positions on a one-time basis. These changes included the delayed implementation of reduced branch library hours by one year, which deferred the elimination of 28 positions until 2021-2022; the reallocation of Police Department overtime funding to restore five Community Service Officer positions on a one-time basis; and the carry-over, or re-budgeting, of unspent funding from 2019-2020 into 2020-2021 to continue a number of positions in various departments for an additional year that were previously set to expire on Jun 30, 2020.

The 2020-2021 Adopted Operating Budget also includes the recognition of funding from an agreement with the Valley Transportation Authority to pay for seven sworn Police Department positions to provide police and security services for the Berryessa/North San José BART Station that began operation in June 2020. As a result of these and other miscellaneous actions included with the approval of the Mayor's June Budget Message, the change in full-time equivalent positions included in the 2020-2021 Adopted Operating Budget decreased by 55 positions when compared to the 2019-2020 Adopted Operating Budget (the 2020-2021 Proposed Operating Budget would have resulted in a net decrease of 103 positions). Finally, the revisions to the 2020-2021 Proposed Operating Budget also included a downward revision to the Transient Occupancy Tax in 2020-2021 by \$6 million in the General Fund (offset with a corresponding reduction to the Budget Stabilization Reserve), which increased the ongoing General Fund shortfall from \$71.6 million to \$77.6 million. Of the \$77.6 million shortfall, \$51.9 million (67%) was resolved on an ongoing basis and \$25.7 million (33%) was solved using one-time funds.

The 2020-2021 Adopted Operating Budget is a balanced budget that responds to the COVID-19 pandemic with the information available to City staff, limits impact to critical City services, and makes significant ongoing cost reductions to address what will likely be a challenging budgetary environment for the foreseeable future. The equitable allocation of resources was a consistent discussion point with City staff and the City Council, including direction from the City Council at its April 7, 2020 meeting to employ an equity lens in the development of the cost reductions for the 2020-2021 Proposed Operating Budget, the release of two Manager's Budget Addenda on the subject (MBA #2 – Equity Review of the 2020-2021 Proposed Operating Budget and MBA #31 – Equity Analysis and the Budget Process), and the establishment of the Office of Racial Equity as included with the approval of the Mayor's June Budget Message. Deliberately posing questions regarding the equitable allocation of resources will again be necessary during the development of the 2021-2022 budget, as resources will continue to be constrained.

The 2020-2021 Adopted Operating Budget includes the liquidation of various earmarked reserves, the sale of surplus properties, and the annualization of the Revenue Capture Agreement. See “MAJOR GENERAL FUND REVENUE SOURCES - Sales and Use Taxes” in this Appendix A.

State Budget

Fiscal Year 2020-21 State Budget. The Governor signed the fiscal year 2020-21 State Budget (the “**2020-21 State Budget**”) on June 29, 2020. The 2020-21 State Budget notes that the COVID-19 pandemic has impacted every sector of the State's economy and has caused record high unemployment, and further action from the federal government is needed as a result of the crisis. The Governor is pursuing \$1 trillion in flexible federal aid to state and local governments across the country, which support will be critical to mitigate the effects of the public health crisis, encourage recovery, and support persons in need.

At the time of the Governor's proposed 2020-21 State Budget in January, the State was projecting a surplus of \$5.6 billion. At the time of the May Revision with respect to the 2020-21 State Budget, the State had a budget deficit of \$54.3 billion. The 2020-21 State Budget includes measures to close the gap and bring the State's resources and spending into balance while preserving reserves for future years.

ERAF Legislation. In the early 1990s, the California Legislature permanently redirected a significant portion of property tax revenue from cities, counties, and special districts to schools and community colleges. The redirected revenue is deposited into a countywide account known as the “Educational Revenue Augmentation Fund” (“**ERAF**”). In the mid-1990s, the State Legislature enacted a law shifting the portion of ERAF not needed for schools and community colleges to other agencies. The revenue shifted through this process is known as “excess ERAF.”

In fiscal year 2019-20, the California Legislative Analyst Office issued a report on “**excess ERAF**” with a different interpretation of calculating excess ERAF performed in various counties, including the County. As a result, the City reduced its estimated ERAF refund in the 2020-2021 Proposed Operating Budget by 50%. The reduced budget, however, does not account for further State findings and/or potential State takeaways, including the potential repayment of prior year excess ERAF allocations. The funding that may be necessary to address any such reduced revenues or repayments of prior year proceeds would need to be identified, including use of the City's General Fund reserves.

Impact of State Budget on City. 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.

Additional Information. Information about the 2020-2021 State budget and other State budgets is available at www.ebudget.ca.gov. An impartial analysis of the budget is posted by the Legislative Analyst Office at www.lao.ca.gov. In addition, various State official statements, many of which contain a summary of the current and past State budgets, may be found at the website

of the State Treasurer, www.treasurer.ca.gov. *The information referred to in this paragraph is prepared by the respective State agency maintaining each website and not by the City or the Underwriters, and the City and the Underwriters take no responsibility for the continued accuracy of the Internet addresses or for the accuracy or timeliness of information posted there, and such information is not incorporated in this Official Statement by these references.*

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, including the ongoing and unknown impacts of COVID-19.

The table on the following page summarizes the actual revenues for 2018-2019, the Modified Operating Budget for 2019-2020 and the Adopted Operating Budget for 2020-2021. 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 10
City of San José
General Fund Revenues⁽¹⁾
2018-2019 Actuals, 2019-2020 Modified Budget and 2020-21 Adopted Budget
(in thousands)

	2018-2019 Actuals	% of Total	2019-2020 Modified Operating Budget⁽²⁾	% of Total	2020-2021 Adopted Operating Budget	% of Total
Property Tax	\$330,199	23.67%	\$364,000	30.28%	\$370,500	32.08%
Sales and Use Tax	263,530	18.89	249,300	20.74	242,500	21.00
Other Revenue	247,368	17.73	37,796	3.14	48,512	4.20
Utility Taxes	99,253	7.12	96,645	8.04	95,800	8.30
Real Property Transfer Taxes	--	--	--	--	30,000	2.60
Franchise Fees	48,397	3.47	48,641	4.05	45,921	3.98
Business Taxes	74,903	5.37	70,200	5.84	70,900	6.14
Licenses and Permits	65,295	4.68	62,009	5.16	20,023	1.73
Revenue from Local Agencies	16,685	1.20	17,365	1.44	18,195	1.58
Fees, Rates and Charges	55,703	3.99	50,236	4.18	25,576	2.21
Telephone Line Tax	21,593	1.55	20,000	1.66	20,000	1.73
Revenue from the Federal Government	3,106	0.22	6,540	0.54	3,715	0.32
Fines, Forfeitures and Penalties	17,402	1.25	15,213	1.27	15,730	1.36
Revenue from the State Government	15,102	1.08	23,073	1.92	14,320	1.24
Transient Occupancy Tax	20,536	1.47	13,500	1.12	9,000	0.78
Revenue from Use of Money and Property	10,072	0.72	13,144	1.09	11,755	1.02
Total General Revenues	\$1,289,145	92.42%	\$1,087,662	90.49%	\$1,042,446	90.27%
Overhead Reimbursements	53,237	3.82	56,273	4.68	69,198	5.99
Transfers to the General Fund	35,295	2.53	40,758	3.39	27,409	2.37
Reimbursements for Services	17,200	1.23	17,275	1.44	15,746	1.36
Total Interfund Transfers and Reimbursements	105,732	7.58	114,307	9.51	112,352	9.73
TOTAL GENERAL FUND REVENUES⁽³⁾	\$1,394,877	100.00%	\$1,201,968	100.00%	\$1,154,798	100.00%

⁽¹⁾ Totals may not add due to independent rounding.

⁽²⁾ As of June 30, 2020.

⁽³⁾ Does not include the Beginning Fund Balance and Reserve for Encumbrances.

Source: City of San José.

COVID-19 Pandemic

The outbreak of COVID-19 has caused tremendous economic volatility in the United States and globally, producing significant declines and the onset of a national and global recession. Since the outbreak of COVID-19, the City and the County have been subject to various mandatory orders for all people to shelter in place, except to meet essential needs or to work to provide essential services ("shelter-in-place directives or orders"). [The County is currently on the Watch List, restricting retail and other activity]. The County's current shelter-in-place directive became effective on July 13, 2020, restricting activities that were previously re-opened following an increase in cases of COVID-19 in the County. The order will remain in effect until the County's health officer amends or rescinds it. The categories of businesses and activities no longer permitted include, but are not limited to, indoor dining at restaurants and other facilities, entertainment centers, places of worship, fitness centers and cardrooms. [UPDATE BEFORE POSTING]

The COVID-19 pandemic is ongoing, and its dynamic nature leads to uncertainties, including spread and severity of the virus, the duration of the outbreak, actions that may be taken by governmental authorities to contain or mitigate the outbreak, the development of medical treatments or vaccinations, and the impact of the outbreak on the local or global economy. The ultimate impact of COVID-19 on the City's operations and finances is not fully known, and it may be some time before the full adverse impact of the COVID-19 outbreak is known. The City continues to monitor the spread of COVID-19 and is working with local, state, and national agencies to address the potential impact of the COVID-19 pandemic upon the City. Although the overall potential impact of COVID-19 on the City cannot be fully quantified at this time, the City has attempted to project its future revenues in its 2020-2021 Adopted Operating Budget. Actual revenues and expenses of the City are likely to be different than those currently projected by the City.

The City has received an initial tranche of funding to help respond to the crisis, providing critical resources that pay for City costs to help address the impacts of the COVID-19 pandemic. See "- Relief Funds" below. The County's shelter-in-place order will likely impact almost all sectors of sales tax revenue, including retail sales, construction, transportation, and business-to-business. Additionally, high unemployment rates and recessionary economic conditions are likely to continue after the shelter-in-place restrictions are lifted.

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 11 sets forth the City's net assessed valuation for 2019-2020 and the previous ten fiscal years.

Table 11 City of San José Net Assessed Property Value <i>(in thousands)</i>		
Fiscal Year	Total Net Assessed Valuation⁽¹⁾	Percentage Change
2009-2010.....	\$121,995,117	--
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
2019-2020.....	195,150,554	7.3

⁽¹⁾ Valuations are as of the end of the fiscal year, include local secured, utility and unsecured valuations, are net of exemptions and include properties in the Former Agency's project areas.

Source: California Municipal Statistics, Inc.

Under current County policy, the City's allocation of total ad valorem taxes (excluding supplemental 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 has 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.

In an attempt to mitigate the effects of the COVID-19 pandemic on State property taxpayers, on May 6, 2020, the Governor signed Executive Order N-61-20 ("**Order N-61-20**"). Under Order N-61-20, certain provisions of the State Revenue and Taxation Code are suspended until May 6, 2021 to the extent said provisions require a tax collector to impose penalties, costs or interest for the failure to pay secured or unsecured property taxes, or to pay a supplemental bill, before the date that such taxes become delinquent. Said penalties, costs and interest shall be cancelled under the conditions provided for in Order N-61-20, including if the property is residential real property occupied by the taxpayer or the real property qualifies as a small business under certain State laws, the taxes were not delinquent prior to March 4, 2020, the taxpayer files a claim for relief with the tax collector, and the taxpayer demonstrates economic hardship or other circumstances that have arisen due to the COVID-19 pandemic or due to a local, state, or federal governmental response to COVID-19.

See "BONDOWNERS' RISKS - COVID-19 Pandemic" in the Official Statement.

There can be no assurance that the County will always maintain the Teeter Plan or will have sufficient funds available to distribute the full amount of the City's share of property tax collections to the City. The ability of the County to maintain the Teeter Plan may depend on its

financial resources and may be affected by future property tax delinquencies. It may also be affected by State and County action. Property tax delinquencies may be impacted by economic and other factors beyond the City's or the County's control, including the ability or willingness of property owners to pay property taxes during an economic recession or depression. An economic recession or depression could be caused by many factors outside the control of the City, including high interest rates, reduced consumer confidence, reduced real wages or reduced economic activity as a result of the spread of COVID-19 or other pandemic or natural or manmade disaster.

Property Taxes. Property Tax receipts collected for the City by the County in the recent fiscal years and as budgeted for 2019-2020 and 2020-2021 are set forth in Table 12.

Table 12
City of San José
Property Tax Receipts
(in thousands)

Fiscal Year	Property Tax Receipts	Percentage of General Fund Revenues	Percentage Change (Y/Y)
2016-2017 Actual.....	276,388	24.9%	5.1%
2017-2018 Actual.....	306,222	23.6	10.8
2018-2019 Actual.....	330,199 ⁽¹⁾	23.7	7.8
2019-2020 Modified Operating Budget ⁽²⁾	364,000	30.3	10.2
2020-2021 Adopted Operating Budget	370,500	32.1	1.8

⁽¹⁾ Increase in Property Tax Receipts beginning in 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.

⁽²⁾ As of June 30, 2020.

Source: City of San José.

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 has issued its "2019-2020 Assessor's Annual Report" documenting taxable fiscal year 2019-2020 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 7.35% from 2018-2019. 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 2019-2020 Modified Budget for Property Tax receipts shown in Table 12 takes into account the County Assessor's projections regarding changes in assessed valuations of property located in the City. Property tax revenues in fiscal year 2020-2021 are not expected to be materially impacted by COVID-19 because they are primarily based on assessed values as of

January 1, 2020. However, as the real estate market is anticipated to decline in calendar year 2020, the general Secured Property Tax revenue will likely be significantly negatively impacted in future years.

The low growth rate in total Property Tax receipts is primarily driven by reduced excess ERAF revenue in anticipation of calculation methodology changes, from \$23.0 million estimated to be received in 2019-2020 to \$11.5 million for 2020-2021, as well as a reduction to Unsecured Property Taxes of \$2.3 million, from \$15.4 million to \$13.1 million. See "STATE BUDGET – ERAF Legislation" above.

Largest Secured Property Taxpayers. Table 13 presents a list of the ten largest property taxpayers for 2019-2020 based on secured assessed valuations within the City, which collectively account for approximately 4% of the total secured assessed property valuation for 2019-2020. Some of the properties owned by these property owners are located in redevelopment project areas established by the Former Agency.

Table 13
City of San José
Ten Largest Local Secured Property Taxpayers

Name	Assessed Property Valuation	Percentage of Total⁽¹⁾
Essex Portfolio LP	\$1,325,065,483	0.71%
Cisco Technology Inc.	1,135,173,871	0.61
FRIT San Jose Town & Country Village LLC	867,937,430	0.47
VF Mall LLC	813,124,080	0.44
Sobrato Interests	687,494,139	0.37
River View Apartments	666,235,561	0.36
San Jose Water Works	627,757,253	0.34
Adobe Systems Inc.	504,293,475	0.27
Apple Inc.	500,167,325	0.27
Hitachi Global Storage Techs Inc.	429,099,597	0.23
Total	\$7,556,348,214	4.07%

⁽¹⁾ 2019-2020 Local Secured Assessed Valuation: \$186,157,577,548.

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 14. The total Sales Tax rate applicable within the City is currently 9.250% and is allocated as follows:

Table 14 City of San José Sales Tax Rates	
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) ⁽¹⁾	0.5000
Sub-Total Statewide Sales and Use Tax.....	7.2500
Local – City of San José ⁽²⁾	0.2500
Santa Clara County Transit District ⁽³⁾	0.5000
Santa Clara County Valley Transportation Authority ⁽⁴⁾	0.5000
Santa Clara VTA BART Operating and Maintenance Transactions and Use Tax ⁽⁵⁾	0.1250
Santa Clara County Retail Transactions and Use Tax ⁽⁶⁾	0.1250
Silicon Valley Transportation Solutions Tax ⁽⁷⁾	0.5000
Total	9.2500%

⁽¹⁾ Approximately 0.18% of this tax is allocated to the City. In 2018-2019, the most recent data available, the Santa Clara County share of the statewide allocation is 6.37%; the City receives approximately 2.78% of the allocation to the County.

⁽²⁾ Approved by voters in June 2016, and effective October 1, 2016, (limited to 15 years) to fund essential City services.

⁽³⁾ Approved by voters in 1976; does not expire. Imposed by VTA.

⁽⁴⁾ Approved by voters in November 2000, and effective April 1, 2006 (limited to 30 years). Imposed by VTA.

⁽⁵⁾ Approved by voters in November 2008 to support BART was implemented on July 1, 2012 (limited to 30 years). Imposed by VTA.

⁽⁶⁾ Approved by voters in November 2012 and effective April 1, 2013 (limited to 10 years).

⁽⁷⁾ 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.

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, an analysis of current and historical performance, economic trends, as well as the Wayfair Decision and Assembly Bill 147 ("**AB 147**"), as discussed below. The City develops estimates for General Sales Tax category, which reflects the 1.0% allocation, the 0.25% 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 15 shows actual and budgeted Sales Tax receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2016-17.

Table 15 City of San José Sales Tax Receipts <i>(in thousands)</i>			
Fiscal Year	Sales Tax Receipts	Percentage of General Fund Revenues	Percentage Change (Y/Y)
2016-2017 Actual	\$207,695	18.7%	2.9%
2017-2018 Actual	226,337	17.4	9.0
2018-2019 Actual ⁽¹⁾	263,530	18.9	16.4
2019-2020 Modified Operating Budget ⁽²⁾	249,300	20.7	(5.4)
2020-2021 Adopted Operating Budget	242,500	21.0	(2.7)

⁽¹⁾ Due to a CDTFA processing issue, 2018-2019 collections included revenue that was attributed to 2017-2018 activity.

⁽²⁾ As of June 30, 2020.

Source: City of San José.

The County's shelter-in-place directive will likely impact almost all sectors of sales tax revenue, including retail sales, construction, transportation, and business-to-business. Additionally, high unemployment rates and recessionary economic conditions are likely to continue after the shelter-in-place restrictions are lifted. See "MAJOR GENERAL FUND REVENUES - COVID-19 Pandemic."

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 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.

In September 2019, the City and eBay entered into a Revenue Capture Agreement, effective October 1, 2019 through June 30, 2034 (the "**Revenue Capture Agreement**"), which allows the City to capture additional sales tax on the sale of goods where eBay acts as the marketplace facilitator as the sales are recognized to occur in the City. In exchange, eBay receives 30% of the new sales tax revenues to the City in excess of a minimum threshold of \$5 million. The minimum threshold is increased by 3% annually, commencing on July 1, 2020.

The 2020-2021 Adopted Operating Budget reflects a 1.7% decline in sales taxes from the 2019-2020 Modified Budget (which are projected to account for 21.0% of total General Fund revenues for fiscal year 2020-2021). The proceeds from the Revenue Capture Agreement (which are included in the 2020-2021 Adopted Operating Budget) are anticipated to yield ongoing sales tax revenues for the City, estimated in 2020-2021 at \$22 million. It is important to note that although this revenue is included in the current sales tax estimates, the Revenue Capture Agreement is under review by the California Department of Tax and Fee Administration.

Other Revenue

The Other Revenue category in 2018-2019 totaled approximately \$247.4 million, and included the issuance of \$150.0 million Tax and Revenue Anticipation Notes (the "**2018 TRAN**") to prefund employer retirement contributions for the City's pension plans. The City did not issue Tax and Revenue Anticipation Notes in 2019-2020. In July of 2020, the City issued \$130.0 million in Tax and Revenue Anticipation Notes (the "**2020 TRAN**") to prefund a portion of its employer retirement contributions for the City's pension plans. The 2020 TRAN is not included in the Other Revenue category of the 2020-2021 Adopted Operating Budget.

For a discussion of the 2020 TRAN, see "BONDED AND OTHER INDEBTEDNESS." 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 25th 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 16 shows Utility Tax receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2016-2017.

Table 16
City of San José
Utility Tax Receipts
(in thousands)

Fiscal Year	Utility Tax Receipts	Percentage of General Fund Revenues	Percentage Change (Y/Y)
2016-2017 Actual.....	\$100,786	9.1%	7.9%
2017-2018 Actual.....	99,753	7.7	(1.0)
2018-2019 Actual.....	99,253	7.1	(0.5)
2019-2020 Modified Operating Budget ⁽¹⁾	96,645	8.0	(2.6)
2020-2021 Adopted Operating Budget	95,800	8.3	(0.9)

⁽¹⁾ As of June 30, 2020.

Source: City of San José.

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 17 shows Franchise Fee receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2016-2017.

Table 17
City of San José
Franchise Fees
(in thousands)

Fiscal Year	Franchise Fee Receipts	Percentage of General Fund Revenues	Percentage Change (Y/Y)
2016-2017 Actual.....	\$49,641	4.5%	1.4%
2017-2018 Actual.....	51,180	3.9	3.1
2018-2019 Actual.....	48,397	3.5	(5.4)
2019-2020 Modified Operating Budget ⁽¹⁾	48,641	4.1	0.5
2020-2021 Adopted Operating Budget	45,921	4.0	(5.6)

⁽¹⁾ As of June 30, 2020.

Source: City of San José.

Business Taxes

This category comprises four major subcategories: general business taxes, cardroom business taxes, cannabis business taxes, and disposal facility taxes. Due to the impacts of COVID-19, the City is projecting a 1.8% decline in business taxes from the 2019-2020 Adopted Budget. See “MAJOR GENERAL FUND REVENUE SOURCES - COVID-19 Pandemic.”

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 José, 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.

In 2020-2021 business tax revenues are anticipated to decrease by approximately 8%, net of the increase of the Consumer Price Index adjustment that will be assessed in 2020-2021 offset by a 10% anticipated reduction to general business tax proceeds as a result of the COVID-19 pandemic's impact on local businesses.

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.

On December 3, 2019, the Bureau of Gambling Control released proposed regulations regarding player-dealer rotation that the cardroom industry projected may cause a 60-70% loss in revenue. In June of 2019 Senate Constitutional Amendment 6 (“**SCA 6**”) was introduced, which proposed amending the State Constitution in order to allow for current player-dealer rotation to continue, avoiding the projected revenue loss. The Bureau of Gambling Control has not initiated its formal rulemaking process for the proposed regulations, and SCA 6 is not expected appear on the State ballot before November 2022.

During the shelter-in-place mandate, cardrooms have not been operational. As a result, the revised budgeted estimate for Cardroom Tax revenues are estimated at \$14.5 million in 2019-2020, which represents an 11.5% drop from 2018-2019 actual collections. Due to uncertainty regarding when the cardrooms will be operational again and social distancing requirements that

will be in place when they do re-open, 2020-2021 revenue is estimated at \$17.1 million, which is approximately \$2 million below average yearly receipts.

The City has placed a ballot measure on the November 3, 2020 ballot, which would increase Cardroom Tax revenues, if approved. See “FISCAL OUTLOOK - 2020 Ballot Measures.”

Cannabis Business Tax. On November 2, 2010, San José voters approved Measure U, which allows the City to impose a tax on all cannabis 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 cannabis 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 cannabis 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 cannabis 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 Cannabis 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.

During the shelter-in-place mandate, cannabis dispensaries have had limited operations. As a result, Cannabis Business Tax revenues are estimated for 2019-2020 are expected to drop 2% from 2018-2019 actual collections. In 2020-2021, Cannabis Business Tax receipts are anticipated to return to a normalized level of \$17.0 million.

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. Table 18a shows actual and budgeted Business Tax receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2016-2017.

As a result of the shelter-in-place mandate, revenues are anticipated to fall in 2019-2020. and to drop again by approximately 10% in 2020-2021.

Table 18a
City of San José
Business Tax Receipts
(in thousands)

Fiscal Year	Business Tax Receipts	Percentage of General Fund Revenues	Percentage Change (Y/Y)
2016-2017 Actual.....	\$54,159	4.9%	6.5%
2017-2018 Actual.....	70,673	5.4	30.5
2018-2019 Actual ⁽¹⁾	74,903	5.4	6.0
2019-2020 Modified Operating Budget ⁽¹⁾	70,200	5.8	(6.3)
2020-2021 Adopted Operating Budget	70,900	6.1	1.0

⁽¹⁾ As of June 30, 2020.

Source: City of San José.

Table 18b shows actual and budgeted Business Tax receipts by major subcategory since 2016--2017.

Table 18b
City of San José
Business Tax Receipts By Major Subcategory
(in thousands)

Subcategory	2016-2017	2017-2018	2018-2019	2019-2020 Modified Operating Budget⁽¹⁾	2020-2021 Adopted Operating Budget
Cardroom Tax	\$18,484	\$18,891	\$18,871	\$16,700	\$17,100
Business Tax	13,047	26,486	28,048	28,000	25,700
Disposal Facility Tax	12,157	12,278	12,093	12,000	11,100
Cannabis Business Tax	10,471	13,018	15,890	13,500	17,000
Total	\$54,159	\$70,673	\$74,903	\$70,200	\$70,900

⁽¹⁾ As of June 30, 2020.

Source: City of San José.

Transfer Taxes

On March 3, 2020, voters approved a ballot measure to enact a real property transfer tax ordinance ("**Transfer Tax**"), effective on July 1, 2020 ("**Measure E**"). The Transfer Tax is a general tax imposed whenever a deed, instrument, or writing, whether recorded or not, transfers real property in the City for consideration. Consideration means the amount paid for, or the value of, the transferred property and includes the amount of any debt and special assessments secured by the transferred property. The Transfer Tax also applies to a transfer of ownership interests in a legal entity (e.g., a corporation, partnership, or limited liability company) that would be considered an ownership change of real property under State law. Payment of the tax is the responsibility of the parties to the transfer and may be paid by either party.

Real property transfers under \$2,000,000 are exempt from the Transfer Tax. Real property transfers of \$2,000,000 or more are taxed at one of the following rates applied to the full value of the consideration:

<u>Value of Consideration</u>	<u>Rate</u>
\$2,000,000 to \$5,000,000	0.75%
\$5,000,001 to \$10,000,000	1.0%
Over \$10,000,000	1.5%

Beginning July 1, 2025, the exemption threshold of under \$2,000,000 (i.e., \$1,999,999.99) will automatically be adjusted based on a consumer price index every five (5) years. The City Council may also increase the exemption threshold at any time, but in no event can the exemption threshold be less than \$1,999,999.99.

The Transfer Tax is in addition to the existing real property conveyance tax ("Conveyance Tax"), also imposed on a transfer of real property, where the value of consideration exceeds \$100, at the rate of \$1.65 for each \$500 of consideration or fractional part thereof, and is a special tax that is required to be used for certain specified purposes.

On June 16, 2020, the City Council adopted a resolution approving revisions to City Council Policy 1-18, entitled the "Operating Budget and Capital Improvement Program Policy," to set forth a spending plan related to the revenues from Measure E. Although Measure E is a general tax and the revenues derived from the tax can be used for any governmental purpose, the revised Policy 1-18 allocates Measure E revenues towards addressing homelessness including, but not limited to, homeless prevention and developing new affordable housing, and sets forth the procedural requirements for changing the allocation. The 2020-2021 Adopted Operating Budget includes a transfer tax revenue estimate for the General Fund of \$30.0 million

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 19 shows actual and budgeted Licenses and Permits receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2016-2017.

Table 19
City of San José
Licenses and Permits Receipts
(in thousands)

Fiscal Year	Licenses and Permits Receipts	Percentage of General Fund Revenues	Percentage Change (Y/Y)
2016-2017 Actual.....	\$58,075	5.2%	8.0%
2017-2018 Actual.....	60,505	4.7	4.2
2018-2019 Actual.....	65,295	4.7	7.9
2019-2020 Modified Operating Budget ⁽¹⁾	62,009	5.2	(5.0)
2020-2021 Adopted Operating Budget	20,023	1.7	(67.7)

⁽¹⁾ As of June 30, 2020.

Source: City of San José.

The 2020-2021 Adopted Operating Budget reflects a 67.7% decline in license and permit fees from the 2019-2020 Adopted Budget (which are projected to account for approximately 1.7% of the total General Fund revenues for fiscal year 2020-2021). Historically, a significant portion (approximately 70%) of the revenue captured in this category were associated with Building and Fire development-related fees (the "**Development Fee Program**"). However, beginning in 2020-2021, all revenue and expenditures related to the Development Fee Program will no longer be captured in the General Fund, but will be allocated to specific Development Fee Program funds. The 2020-2021 Adopted Operating Budget estimates revenue from Licenses and Permits at \$20.0 million, which reflects growth of 1.1% from the 2019-2020 Modified Budget estimate of \$19.8 million when excluding the development fee program.

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 20 shows actual and budgeted Revenue from Local Agencies, its respective percentage of General Fund revenues, and year-over-year changes since 2016-2017.

Table 20
City of San José
Revenue from Local Agencies
(in thousands)

Fiscal Year	Revenue from Local Agencies	Percentage of General Fund Revenues	Percentage Change (Y/Y)
2016-2017 Actual.....	\$27,717	2.5%	61.7%
2017-2018 Actual.....	38,623 ⁽¹⁾	3.0	39.3
2018-2019 Actual.....	16,685	1.2	(56.8)
2019-2020 Modified Operating Budget ⁽²⁾	17,365	1.4	4.1
2020-2021 Adopted Operating Budget	18,195	1.6	4.8

⁽¹⁾ The increase in Revenue from Local Agencies from 2016-2017 to 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 2017-2018, the City also received a reimbursement from the Successor Agency for enforceable obligations totaling approximately \$12.2 million.

⁽²⁾ As of June 30, 2020.

Source: City of San José.

Transient Occupancy Tax

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

Table 21 shows actual and budgeted TOT receipts, their respective percentage of General Fund revenues, and year-over-year changes since 2016-2017.

Table 21 City of San José Transient Occupancy Tax <i>(in thousands)</i>			
Fiscal Year	Transient Occupancy Tax	Percentage of General Fund Revenues	Percentage Change (Y/Y)
2016-2017 Actual	\$18,275	1.6%	10.3%
2017-2018 Actual	19,531	1.5	6.9
2018-2019 Actual	20,536	1.5	5.1
2019-2020 Modified Operating Budget ⁽¹⁾	13,500	1.1	(34.3)
2020-2021 Adopted Operating Budget	9,000	0.8	(33.3)

⁽¹⁾ As of June 30, 2020.
Source: City of San José.

The 2020-2021 Adopted Budget reflects a 33.3% decline in TOT from the 2019-2020 Modified Operating Budget. The City assesses a 10% TOT on the rental price for transient lodging. Of these receipts, 6% are placed in the Transient Occupancy Tax Fund and 4% are deposited in the General Fund. Hotel occupancy from mid-March through June 2020, is estimated at only 15% occupancy. As a result of COVID-19 and the resulting shelter-in-place directive in the County and declines in business-related travel, TOT receipts are anticipated to be heavily impacted for the remainder of 2019-2020 through 2020-2021. In 2020-2021, TOT revenues are anticipated to continue to be impacted as business-related travel and conventions will likely not resume for an extended period of time.

Relief Funds

The City has received federal and State funding to help respond to the crisis, providing critical resources to pay for City costs to help address the impacts of the COVID-19 pandemic. The following table summarizes such sources and the amount of funding received or estimated to be received from such sources.

SOURCES OF RELIEF FUNDS	MBA #20 COVID-19 Related Estimated Funding	Granted Following MBA #20	Total Estimated Sources	Received/ Obligated as of August 1, 2020
Coronavirus Relief Fund	\$178,295,248	-	\$178,295,248	\$178,295,248
Community Development Block Grant Supplemental Funding	5,263,414	-	5,263,414	5,263,414
Emergency Solutions Grant	2,683,479	\$32,836,839	35,520,318	35,520,318
Housing Opportunities for Person with AIDS Coronavirus Emergency Supplemental Funding Program	209,618 -	- 865,998	209,618 865,998	209,618 865,998
FEMA - Stafford Act Public Assistance Program	37,591,157	-	37,591,157	5,846,340
FEMA - Assistance to Firefighters Program	-	301,124	301,124	301,124
California Emergency Homeless Housing California Homeless Housing, Assistance & Prevention Grant	3,919,821 23,832,511	- -	3,919,821 23,832,511	3,919,821 23,832,511
Total	\$251,795,248	\$34,003,961	\$285,799,209	\$254,054,393

CARES Act. The federal Coronavirus Aid, Relief, and Economic Security Act ("CARES Act"), that became law on March 27, 2020, addresses the economic crisis created by the COVID-19 pandemic. The CARES Act provides funding to cover costs related to necessary expenses incurred due to the public health emergency created by COVID-19 that were not previously accounted for in the City's budget process and that were incurred between March 1, 2020 and December 30, 2020. The City received funding under several provisions of the CARES Act; the most significant allocation is approximately \$178 million from the Coronavirus Relief Fund.

U.S. Treasury – Coronavirus Relief Fund. On May 12, 2020, the City Council took various budgetary actions to establish a new special fund referred to as the Coronavirus Relief Fund to recognize the \$178 million of the Coronavirus Relief Fund moneys from the CARES Act to the City. As described in Manager's Budget Addendum #3, Coronavirus Relief Fund and General Fund Adjustments, and Manager's Budget Addendum #20, Coronavirus Relief Fund and Resident Assistance, the Coronavirus Relief Fund provides resources for the City to respond to the broad range of impacts and needs experienced by the San José community due to the COVID-19 pandemic. This includes an allocation of \$35 million for food and necessities distribution as a form of economic support to City's residents as well as residents outside the City in the County who have been impacted by the shelter-in-place order that was issued to mitigate the spread of COVID-19. The City must abide by specific restrictions on how its allocation of the Coronavirus Relief Fund is spent. Without further guidance from the U.S. Treasury that clearly states the City may expend Coronavirus Relief Fund moneys outside the boundaries of the City for economic support purposes such as food distribution and necessities, the City may be required to expend legally available moneys from its General Fund if the County or other cities within the County do not reimburse the City in the event the U.S. Treasury seeks to recover the Coronavirus Relief Fund moneys spent by the City to serve non-residents. It is not clear at this time whether

legislative, regulatory and other governmental actions, including the CARES Act, will have the intended mitigating effect.

U.S. Department of Housing and Urban Development. The City has received supplemental funding under the CARES Act through the following U.S. Department of Housing and Urban Development (“**HUD**”) Office of Community Planning and Development statutory formula programs: Community Development Block Grants (“**CDBG**”); Housing Opportunities for Persons with AIDS (“**HOPWA**”); and Emergency Solutions Grants (“**ESG**”).

Community Development Block Grant Supplemental Funding. The CDBG program is aimed to assist low to moderate-income communities in community development projects. Every year, each city with more than 50,000 people and each county with a population with more than 200,000 automatically receive this funding from the federal government. The City has received \$5,263,414 in supplemental CDBG funding under the CARES Act.

Housing Opportunities for Persons with AIDS. The HOPWA program was established to provide housing assistance and related supportive services for low-income persons living with HIV/AIDS and their families. The City has received \$209,618 in supplemental HOPWA funding under the CARES Act.

Emergency Solutions Grant. The ESG program provides funding to: (1) engage homeless individuals and families living on the street; (2) improve the number and quality of emergency shelters for homeless individuals and families; (3) help operate these shelters; (4) provide essential services to shelter residents, (5) rapidly rehouse homeless individuals and families, and (6) prevent families/individuals from becoming homeless. On April 2, the City was awarded \$2,683,479 in supplemental ESG funding under the CARES Act. An additional \$32,836,839 of supplemental ESG funding under the CARES Act was awarded on June 9, 2020.

U.S. Department of Justice. As an eligible recipient of Edward Byrne Memorial Justice Assistance Grant Program funds through the U.S. Department of Justice Bureau of Justice Assistance, the City was allocated and, on May 29, 2020, subsequently applied for \$865,998 in Coronavirus Emergency Supplemental Funding (CESF) Program funding for City Fire and Police Departments projects and programs to prevent, prepare for and respond to the coronavirus.

U.S. Department of Homeland Security – Federal Emergency Management Agency.

Stafford Act Public Assistance Program. On March 13, 2020, the President declared a nationwide emergency for the COVID-19 pandemic for all states, tribes, territories, and the District of Columbia under the Robert T. Stafford Disaster Relief and Emergency Assistance Act (“**Stafford Act**”). The Stafford Act Public Assistance program, which is managed by the U.S. Department of Homeland Security through its Federal Emergency Management Agency (“**FEMA**”), provides disaster assistance to state and local governments and certain private nonprofit organizations for emergency work and the repair or replacement of disaster-damaged facilities. The City is eligible for FEMA funding under the Public Assistance program on a reimbursement basis. The City has submitted \$15.6 million to FEMA under its expedited application program, with the intention to submit an additional \$22.0 million in expenditures to FEMA. While the FEMA Public Assistance program is a known, available funding source for which the City is eligible, the final determination regarding eligibility and subsequent reimbursement of City expenditures remains with FEMA. The City also must meet a local share requirement for FEMA funding,

ranging from 6.25% to 25% of total expenditures submitted, depending on the participation level of the State of California, through its California Office of Emergency Services.

Assistance to Firefighters Grant Program. The Assistance to Firefighters Grant Program – COVID-19 Supplemental (“**AFG-S**”) provides financial assistance directly to eligible fire departments, nonaffiliated emergency medical service organizations, and State Fire Training Academies for critical personal protective equipment and supplies needed to prevent, prepare for, and respond to the COVID-19 public health emergency. The City has been awarded \$301,124 in AFG-S funding

California Emergency Homeless Housing (SB 89). On March 17, 2020, the Governor of California signed State Bill (SB 89) which provides funding to protect the health and safety of the homeless population in response to the COVID-19 pandemic. The City was awarded and has received \$3,919,821 in SB 89 funds.

California Homeless Housing, Assistance & Prevention Grant (HHAP). The State of California Housing, Assistance and Prevention (“HHAP”) is a \$650 million one-time block grant through AB 101 (signed July 31, 2019 by the Governor of California) that provides local jurisdictions with funds to support regional coordination and expand or develop local capacity to address their immediate homelessness challenges. The City has been allocated and received \$23,832,511 in HHAP moneys to fund emergency and crisis intervention services for the homeless.

City Manager’s Budget Addenda #3 and #20. On May 27, 2020, the City Manager released the Manager’s Budget Addendum #3 (“**MBA #3**”), which proposes certain adjustments to the Proposed Operating Budget. With the subsequent Coronavirus Relief Fund guidance provided by the U.S. Treasury Department on May 4, 2020 (subsequently reiterated on May 28, 2020) and additional analysis performed by City staff, MBA #3 incorporates the City’s planned use of anticipated expenditures and known available funding sources, into the Proposed Budget to respond to the COVID-19 pandemic. MBA #3 identifies COVID-19 estimated costs and proposed funding in the amount of \$251,795,248 to address the estimated COVID-19 costs. On June 6, 2020, the City Manager released the Manager’s Budget Addendum #20 (“**MBA #20**”), which modifies the recommendations in MBA #3 by reallocating \$15 million from Food and Necessities to Local Assistance due to revised analysis and needs assessments for both programs

The funding sources are comprised of the Coronavirus Relief Funds in the amount of \$178,295,248 and a variety of other funding sources in the amount of \$107,503,961, which includes potential FEMA reimbursement which has not yet been awarded to the City. Of the *Sources of Relief Funds* shown above, the Coronavirus Relief Funds were received as an advance of other federal financial assistance, the U.S. Department of Housing and Urban Development and U.S. Department of Homeland Security moneys were allocated to the City through federal statutory formula and available through drawdown, while the California moneys also have been allocated and have been received. On May 12, 2020, the City Council approved the budgeting of \$8.9 million of potential FEMA reimbursable expenditures in the General Fund for 2019-2020. As of August 1, 2020, additional potential FEMA reimbursable expenditures have not been budgeted in the 2020-2021 Modified Budget.

MBA #3 further recommends that the City Council reimburse the General Fund for COVID-19 expenditures incurred in 2019-2020. Of the \$79.3 million estimated for allocation in 2019-2020, \$50,000,000 in COVID-19 Personal Services expenses is recommended to reimburse the General Fund with Coronavirus Relief Funds. As part of the Approval of Various Budget Actions for Fiscal Year 2019-2020, approved by the City Council at its meeting on June 23, 2020, the amount of funding to reimburse the General Fund increased to \$55 million, with an additional \$5 million necessary to reimburse various other City funds whose personnel were redeployed to respond to the COVID-19 pandemic. The reallocation of resources within the Coronavirus Relief Fund, to reflect the *Approval of Various Budget Actions for Fiscal Year 2019-2020* reassignment of Coronavirus Relief Funds to personal services, is anticipated to occur in September 2020.

<u>MBA #20 Publication</u>				
USES OF RELIEF FUNDS	Coronavirus Relief Fund	Other Sources	Granted After MBA #20	Total Estimated Uses
Communications and Translation Services	\$500,000	-	-	\$500,000
Consulting and Planning Support	2,000,000	-	-	2,000,000
COVID-19 Personal Services	50,000,000	-	\$865,998	50,865,998
Digital Inclusion	5,000,000	-	-	5,000,000
Facilities Improvements	5,000,000	-	-	5,000,000
FEMA Local Match	7,000,000	-	-	7,000,000
Food and Necessities	35,000,000	\$10,040,000	-	45,040,000
Homeless Sheltering and Support	45,000,000	35,910,000	32,836,839	113,746,839
Local Assistance	25,000,000	-	-	25,000,000
PPE & Janitorial Services	1,500,000	11,550,000	301,124	13,351,124
Remote Work Facilitation	1,000,000	-	-	1,000,000
Testing, Tracing and Isolation	-	16,000,000	-	16,000,000
COVID-19 Emergency Response Reserve	1,295,248	-	-	1,295,248
Total	\$178,295,248	\$73,500,000	\$34,003,961	\$285,799,209

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 22 and 23 on the following pages summarize financial information contained in the City's Basic Financial Statements as of June 30 for 2014-2015 through 2018-2019. The tables include information solely on the General Fund of the City.

Table 22
City of San José
General Fund
Balance Sheet
2014-2015 through 2018-2019
(in thousands)

	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
ASSETS					
Cash and Pooled Investments	\$308,829	\$281,607	\$299,728	\$296,597	\$435,353
Receivables:					
Taxes	39,953	72,606	55,039	54,281	62,075
Accrued Interest.....	510	629	1,440	1,986	2,536
Grants	1,207	1,352	822	3,081	1,106
Other	35,160	36,963	39,782	39,965	36,057
Less: allowance for uncollectibles	(21,715)	(28,759)	(27,904)	(26,398)	(23,618)
Due from Other Funds.....	1,942	1,450	1,823	1,797	1,653
Due from Outside Agencies	655	459	341	185	58
Loans Receivable (net of allowance for uncollectibles)	1,241	1,241	1,241	1,241	1,241
Advances and Deposits.....	203	186	170	153	137
Advances to Other Funds.....	3,297	3,297	3,297	3,297	3,297
Advances to Receivable from SARA.....	6,404	26,182	28,950	13,863	12,742
Restricted Assets:					
Cash and Pooled Investments.....	1,269	1,277	1,289	1,308	1,331
Cash and Investments held with fiscal agent.....	19,250	4,564	2,852	682	1
TOTAL ASSETS	\$398,205	\$403,054	\$408,870	\$392,038	\$533,969
LIABILITIES					
Accounts Payable.....	14,805	14,105	14,125	9,001	11,901
Accrued Salaries, Wages and Payroll Taxes	20,260	23,305	30,536	33,975	34,437
Due to Other Funds.....	--	--	--	--	--
Due to Successor Agency	--	--	--	--	--
Due to Outside Agency	373	373	373	372	373
Unearned Revenue	6,363	6,205	6,302	6,483	6,548
Advance, Deposits, and Reimbursement Credits	7	7	7	7	37
Advances from Other Funds	8,112	--	--	--	--
Other Liabilities.....	32,331	29,803	32,553	36,736	53,432
TOTAL LIABILITIES	\$82,251	\$73,798	\$83,896	\$86,574	106,728
DEFERRED INFLOW OF RESOURCES	--	10,217	12,142	12,442	12,742
FUND EQUITY					
Fund Balances:					
Nonspendable.....	203	186	170	153	153
Restricted.....	10,599	1,265	690	1,057	1,370
Committed.....	94,748	84,998	96,026	97,809	100,147
Assigned	143,398	167,239	136,093	111,509	168,961
Unassigned	67,006	65,351	79,853	82,494	143,868
TOTAL FUND EQUITY	315,954	319,039	312,832	293,022	414,499
TOTAL LIABILITIES AND FUND EQUITY	\$398,205	\$403,054	\$408,870	\$392,038	533,969

Source: City of San José Comprehensive Annual Financial Reports, 2014-2015 through 2018-2019.

Table 23
City of San José
General Fund
Statement of Revenues, Expenditures and Changes in Fund Balance
2014-2015 through 2018-2019
(in thousands)

	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
REVENUES					
Taxes:					
Property Taxes.....	\$247,258	\$263,300	\$276,388	\$306,222	\$344,458
Sales Taxes and Shared Revenue.....	180,407	201,797	207,695	226,337	263,530
Utility Taxes.....	112,645	113,474	121,045	120,234	120,846
State of California in-lieu Tax.....	419	410	467	551	505
Franchise Taxes.....	46,909	48,949	49,642	51,180	48,397
Business Taxes.....	47,431	50,864	54,159	70,673	77,011
Miscellaneous Taxes.....	14,734	16,565	18,275	19,531	20,535
Total Taxes.....	649,803	695,359	727,671	794,728	875,282
Licenses, Permits, and Fines.....	62,000	69,856	75,173	74,859	80,725
Intergovernmental.....	11,385	9,103	11,132	11,773	8,349
Charges for Current Services.....	42,731	48,110	46,049	52,303	55,646
Interest and Investment income.....	1,749	4,658	2,222	2,228	7,303
Other Revenues.....	40,998	44,582	38,821	42,905	40,888
TOTAL REVENUES	\$808,666	\$871,668	\$901,068	\$978,796	\$1,068,193
EXPENDITURES					
Current:					
General Government.....	71,792	92,093	95,861	100,732	137,732
Public Safety.....	485,327	513,921	536,068	593,162 ⁽¹⁾	622,250
Capital Maintenance.....	75,493	85,324	111,737	120,158	89,758
Community Services.....	122,614	132,115	133,409	139,593	115,441
Sanitation.....	1,291	1,690	2,444	4,148	4,844
Capital Outlay.....	21,766	26,832	14,535	14,264	12,464
Debt Service:					
Principal.....	13,623	1,463	1,526	39,119 ⁽²⁾	1,420
Interest.....	1,250	1,200	1,328	2,184	838
TOTAL EXPENDITURES	\$793,156	\$854,638	\$896,908	\$1,013,360	\$984,747
Excess (Deficiency) of Revenues over Expenditures	15,510	17,030	4,160	(34,564)	83,446
OTHER FINANCING SOURCES (USES)					
Transfers In.....	9,124	10,253	20,461	11,409	18,751
Proceeds from capital lease financing.....	--	--	--	--	--
Proceeds for sale of capital assets.....	37,482	3,848	157	38,187	132,703
Transfers Out.....	(50,226)	(28,046)	(30,985)	(34,842)	(46,423)
TOTAL OTHER FINANCING SOURCES (USES)	\$(3,620)	\$(13,945)	\$(10,367)	\$14,754	38,031
Excess (Deficiency) of Revenues and Other Sources over Expenditures and Other Uses	11,890	3,805	(6,207)	(19,810)	121,477
Fund Balance - July 1	304,064	315,954	319,039	312,832	293,022
Fund Balance - June 30	\$315,954	\$319,039	\$312,832	\$293,022	\$414,499

⁽¹⁾ 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."

⁽²⁾ 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, 2014-2015 through 2018-2019.

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 2014-2015, 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, 2019, total net OPEB liability was \$9.2 billion, which included \$840.5 million in governmental activities and \$82.8 million in business-type activities. The actuary for the OPEB plan stated that the total net OPEB liability decreased by \$148 million or 13.8 percent due to changes of benefits resulting from the implementation of the Voluntary Employee Beneficiary Association Plans, and changes to health assumptions in both plans.

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 2018-2019, 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 2018-19 Management Report noted two "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, and noted, in connection with one such instance, that "[l]imited resources within the Department and lack of accounting expertise contributed to this error."

The City's management, in its response to this finding, noted that new accountants have been hired in order to reallocate resources and ensure that sufficient training, monitoring and outreach efforts are undertaken. Five significant deficiencies were set forth in the Management Report for 2017-2018, five of which were corrected and one of which was partially corrected.

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 auto liability exposure at 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, that also provides coverage for business interruption losses. The City's property policy includes coverage for flood; however, 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, 2019 to October 1, 2020 is provided in Table 24.

Table 24
City of San José
Summary of Citywide Property Insurance Coverage
(For Policy period October 1, 2019 – October 1, 2020)

	Coverage Per Occurrence	Deductible Per Occurrence
Property, including Business Interruption ⁽¹⁾	\$1.0 billion	\$100,000
Flood Zone, High and Moderate Hazard ⁽²⁾⁽³⁾⁽⁴⁾	\$10 million (and annual aggregate)	\$500,000
Flood, Other Locations	\$100 million (and annual aggregate)	\$100,000

⁽¹⁾ Acts of terrorism as defined by the Terrorism Risk Insurance Act are covered.

⁽²⁾ High and Moderate Hazard Exposed Flood Locations as defined in the insurance policy.

⁽³⁾ Mineta San José International Airport and the McEnery Convention Center are subject to a \$10,000,000 deductible for flood.

⁽⁴⁾ The San José – Santa Clara Regional Wastewater Facility is subject to a \$5,000,000 deductible for flood.

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

To mitigate the impact of reduction to the base flood coverage from \$25,000,000 to \$10,000,000, the City has obtained an excess policy for locations in high and moderate hazard flood zones. The excess policy provides \$15,000,000 in limits excess of the primary property policy on a 50/50 quota share basis, where the City and excess insurer share the financing of losses on a 50/50 basis.

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 and advertising 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 \$5,000,000 in excess of the underlying limit of \$1,000,000, which is provided by a separate automobile liability 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 subject to a \$250,000 per accident retention. Physical damage coverage is available for the Airport Shuttle Bus Fleet and is subject to a \$10,000 comprehensive collision deductible. As part of general support services, the City charges the Airport for the cost of liability and property insurance coverage.

Aircraft (Hull & Liability) Policy. The City maintains an aircraft policy covering physical damage coverage for City aircraft used by the San Jose Police Department’s Air Support Unit as well as liability coverage for bodily injury and property damage arising from the use of covered aircraft. The aircraft policy provides up to \$50,000,000 in aggregate liability coverage for bodily injury, personal injury, or property damage caused by war and other perils and is subject to a deductible of \$0 per occurrence. To supplement the aircraft policy, the City extended the aircraft policy effective June 17, 2020, to include liability and physical damage coverage for the unmanned aerial systems (UAS) used in the San Jose Police Department’s UAS program (“Drone Coverage”). The Drone Coverage provides up to \$2,000,000 in aggregate liability coverage for bodily injury, personal injury, or property damage.

Law Enforcement Liability Policy. The City maintains a law enforcement liability policy that provides coverage that results in third party bodily injury, property damage, or personal injury arising from the law enforcement activities conducted on behalf of approved third party employers by City police officers who have been approved to participate in the Secondary Employment program. The law enforcement liability policy provides \$2,000,000 in aggregate limits and is subject to a \$100,000 per occurrence deductible.

Fiduciary Liability Coverage. The City also maintains fiduciary liability insurance policies covering the City’s defined contribution employee benefit plans: the Deferred Compensation Plans, the Voluntary Employees’ Beneficiary Association (“VEBA”) Plans; and the Defined Contribution 401(a) Plan. The policies protect the City and the members of the applicable Board from legal liability arising from fiduciary obligations to plan beneficiaries. The policy covering the Deferred Compensation Plans provides \$5,000,000 in aggregate limits subject to a \$25,000 per claim retention except a \$100,000 per claim retention for class action claims. The policy covering the VEBA Plans provides \$5,000,000 in aggregate limits subject to a \$25,000 per claim retention. The policy covering the Defined Contribution 401(a) Plan provides \$1,000,000 in aggregate limits subject to a \$25,000 per claim retention.

Crime Coverage. The City maintains government fidelity/crime coverage for City losses arising from employee dishonesty. 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. The policy also provides a \$1,000,000 per occurrence limit for computer fraud, funds transfer fraud, money orders and counterfeit currency.

All coverages are subject to a per occurrence deductible of \$100,000, with the exception of forgery and alteration coverage which is subject to a per occurrence deductible of \$50,000.

Workers' Compensation. The City is self-insured for workers' compensation, with all claims administered by third party administrator Intercare Holdings Services, Inc. ("**Intercare**"). Every year, the City reviews a five-year forecast for worker's compensation expenditures based on the prior year payout. Based on this review, the City's budget for 2019-2020 is \$21,000,500 and the budget for 2020-2021 is \$20,257,000.

The City entered a three-year agreement with Intercare beginning July 1, 2019, to provide comprehensive workers' compensation services including claims administration services, bill review, utilization review, medical case management, and other ancillary services at a total compensation not to exceed \$15,963,931 based on an estimated caseload of 2,330 to 2,850 claims. As of June 30, 2020, the open claims inventory handled by Intercare was 2,520.

Third Party Liability Claims. The City is also self-insured for third party liability claims, other than those involving the Airport. The Plant also maintains an automobile liability policy issued to provide coverage for the off-premise operations of scheduled Plant vehicles with a limit of \$1,000,000 per occurrence, combined single limit for bodily injury and property damage and subject to a \$250,000 per accident retention.

Generally, third party liability claims are handled by the City Attorney's Office. The City maintains a budgeted allocation for the potential payment of third-party liability claims – this amount is \$14,500,000 in the 2020-2021 Adopted Operating Budget. The City also maintains an emergency reserve to 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, 2019, the workers' compensation and general liability catastrophic reserve totaled \$15,000,000 of the unassigned fund balance and was re-budgeted in the same amount for 2020-2021.

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 2.0% for the amounts recorded.

With respect to the general liability accrual in the City's financial statements, the City has numerous unsettled lawsuits filed or claims asserted against it as of June 30, 2019. 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, 2019, the provision for losses in its claims liability for loss contingencies totaled approximately \$140.9 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, 2019 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 and lawsuits 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 is maintained, as recommended by an actuary. During 2019-2020, the claims reserve is an amount equal to three months of claims. Based upon a recommendation from the City’s benefit consultant actuary, beginning July 1, 2020, the City has reduced the claims reserve to 1.5 months of claims in alignment with industry trends.

Medical Insurance. On June 25, 2019, the City Council approved a fully insured medical plan to replace the self-insured medical plan effective January 1, 2020. The self-insured plan was closed as of December 31, 2019. The City’s actuary has estimated the cost of claims through the run-out period which ends on December 31, 2020. During this period, the City is responsible for all the claims that occurred prior to the end of the plan on December 31, 2019, but are received in 2020. Based on the actuary’s estimate of projected expenditures for the claims during the runout period, there is sufficient budget and further subsidy will not be required from the General Fund.

Since January 1, 2017 the City has maintained a stop loss insurance policy for the self-insured medical plan 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 each 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. Since January 2017, the attachment point has not been reached. Individual claims have exceeded \$300,000 on a few occasions resulting in payments from the insurance carrier of \$82,433 in 2017-2018, \$62,946 in 2018-2019, and \$1,140,240 in 2019-2020.

Airport Owner-Controlled Insurance Programs

Terminal Area Improvement Program. On March 15, 2007, the City obtained additional liability insurance through AIG 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 25 City of San José Summary of Airport Owner-Controlled Insurance Program – TAIP		
Coverages	Limit	Deductible Per Occurrence
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 AIG in the amount of \$8,900,000. The claims loss reserve fund is available to AIG 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 AIG in 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 AIG, a total amount of \$2,236,000 has been returned to the Airport as of March 31, 2020. The balance of the TAIP reserve fund as of March 31, 2020 was approximately \$1.39 million.

The TAIP Project has been completed and the policies expired on June 30, 2011. AIG 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, and contractor's pollution liability insurance to cover liabilities associated with the work.

The City was also required to establish and post a cash collateral fund of \$2,657,395, 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:

Table 26 City of San José Summary of San José-Santa Clara Regional Wastewater Facility Capital Improvement Program		
Coverages	Limit	Deductible Per Occurrence
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 & 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 11 recognized employee bargaining units. The table below shows the representation and agreement expiration dates for the 11 bargaining units. In addition to its represented employees, the City has 349 unrepresented employees budgeted for 2020-2021.

Table 27
City of San José
Summary of Labor Agreements

	Agreement Expiration Date	Full-Time Equivalent Employment ⁽¹⁾⁽²⁾
San José Police Officers' Association	6/30/21	1,157
Association of Maintenance Supervisory Personnel	6/30/21	116
Association of Engineers and Architects ⁽³⁾	6/30/21	334
Association of Legal Professionals	6/30/21	45
International Brotherhood of Electrical Workers	6/30/21	77
International Union of Operating Engineers, Local #3	6/30/21	740
City Association of Management Personnel	6/30/21	493
Municipal Employees Federation	6/30/21	2,476
Assoc. of Building, Mechanical and Electrical Inspectors	6/30/23	88
International Association of Firefighters, Local 230	6/30/23	701
Peace Officer Park Rangers Association	6/20/23	16
Total		6,243

⁽¹⁾ 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 2020-2021 Adopted Operating Budget, and have been rounded to the nearest FTE.

⁽²⁾ The total number of employees does not include 349 unrepresented positions budgeted in 2020-2021.

⁽³⁾ 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.

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.

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 City has previously reported that the agreement expired as of January 1, 2018. In fact, the agreement was extended annually from 2008 through December 31, 2017, at which time the agreement was modified to have the tolling period be subject to either revocation by either party upon 90 days' written notice or termination on the 60th day following the issuance by the California Public Utilities Commission of a final decision or resolution denying approval of the parties' settlement. The parties have not reached a settlement 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 described above, 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 the 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 is ongoing.

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 the Federated City Employees' Retirement System (the "**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 and the Board. 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. The City has accepted the tendered defense of the Board.

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. [A second amended complaint was filed following the demurrer, and a demurrer and motion to strike portions of that complaint have been filed and heard on July 10, 2020. The judge granted the motion with leave to file an amended complaint. On July 30, 2020, a Third Amended Complaint was filed. 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 300 non-duplicated claims, previously reported as 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. Eighteen lawsuits on behalf of approximately 200 plaintiffs were filed against the City, the County, Santa Clara Valley Water District, and state agencies. The court has since dismissed the complaints against the state agencies and the County leaving the City and the Santa Clara Valley Water District as defendants. One plaintiff that had alleged damages in the amount of approximately \$6 million dismissed its complaint against the defendants without prejudice.

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's ruling is not on the merits of the last three causes of action.

[The parties have selected a retired judge as a discovery master and settlement conference judge. Currently, the parties have engaged in both written and oral discovery. At this stage discovery is aimed at issues related to dangerous conditions of public property, inverse condemnation and the amount of economic damage incurred by the plaintiffs. The parties attended mediation during the first week of August, 2020. The parties anticipate returning to mediation in the second week of September.]

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 José Municipal Water" challenging the fees charged for water service from 1997 to 2016. The plaintiffs claimed 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. They also challenged the City's former rate structure that included tiered rates.

The plaintiffs filed a second lawsuit essentially identical to the original lawsuit, regarding alleged overcharges and improper transfers in 2015-2016, as well as the tiered rates. In both cases, the plaintiffs asked for the funds to be transferred back to the Water Utility Fund or 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 on the tiered rate issue. Briefing has commenced on plaintiffs' appeal and City's cross-appeal. Plaintiffs have filed their appellate brief challenging the denial of their attorneys' fees and the award of costs to City.

In addition to these two lawsuits, the plaintiffs filed a third lawsuit with similar allegations related to the water fees charged in 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. On November 25, 2019, the trial court denied the plaintiffs' motion for class certification, and the plaintiffs did not file an appeal of the judge's decision. No trial date has been set in this case, which is stayed pending the resolution of the appeal in the case that was tried.

On February 19, 2020, 82 cities and other water providers, including the City, were collectively sued in *Kessner et al. v. City of Santa Clara, et al.*, in Santa Clara County

Superior Court, which amounts to 81 class action challenges to the water rates of 82 public water suppliers in the State of California. Although not entirely clear, plaintiffs allege defendant water providers charged more than the cost of recovery for water service in violation of Proposition 218. On March 9, 2020, the court determined that this action constitutes a complex case under California Rules of Court, and a case management conference was scheduled for June 19, 2020 and then was subsequently vacated pending Plaintiffs' request to the state Judicial Council that the *Kessner* action be coordinated with two other Proposition 218 cases filed in other counties. The court ordered a stay on discovery and responsive pleadings, including answers to the complaint, motions to strike, demurrers, motions for change of venue and cross-complaints until a date is set at the case management conference for such filings and hearings. The Judicial Council has referred the motion to coordinate proceedings to the Santa Cruz Superior Court. No specific judge has been assigned. At this time, the City is unable to state the potential exposure for damages in this case.

SEE "CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS – Articles XIII C and XIII D 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 filed an appeal and on May 7, 2020, the California Court of Appeal, Sixth Appellate District issued its decision affirming the judgment in favor of the City. The former employee has filed a petition for review with the California Supreme Court.

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 2012-2013, 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 entered judgment in favor of the City on all claims. The plaintiff filed an appeal from the judgment and the matter is pending before the California Court of Appeal, Sixth Appellate District Court. Briefing in the case has not been completed.

The cardroom business and the City Administration have been in settlement negotiations. It is anticipated that a settlement agreement will be brought forward to the City Council for consideration in September 2020. Subject to City Council approval, the settlement agreement provides that pending the outcome of the vote on the Cardroom Measure on November 3, 2020, the litigation would be stayed. If the voters do not approve the Cardroom Measure, the cardroom business is required to dismiss the litigation with

prejudice within 10 days of the date the Santa Clara County Registrar of Voters has certified the results of the election.

If the voters approve the Cardroom Measure, the cardroom business is not required to dismiss the litigation until certain amendments to the City's gaming regulations under Title 16 of the Municipal Code have become effective and the cardroom receives final approval from the City for at least fifteen (15) additional tables. Within ten (10) days of the date when all of these conditions have occurred, the cardroom business is required to dismiss with prejudice.

In addition to these terms, the settlement agreement revises a prior settlement agreement (1) requiring the City to provide certain documentation to the cardroom business to support the calculation of the cardroom regulatory fee as part of an annual reconciliation of the City's costs and provides for an administrative process and mediation prior to the filing of a lawsuit by the cardroom challenging the amount of the regulatory fee; and (2) providing for the cardroom business's contributions to designated nonprofits that address gambling addiction.

See "CONSTITUTIONAL AND STATUTORY PROVISIONS AFFECTING CITY REVENUES AND APPROPRIATIONS — Articles XIIC 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 filed an appeal in the Ninth Circuit Court of Appeal. On January 15, 2020, the Ninth Circuit affirmed the district court's decision based on plaintiffs' failure to demonstrate that there was a genuine issue of material fact.

Subsequent to the decertification of the *Wallace* case, seven 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 were stayed pending the results of the appeal in the *Wallace* case. On February 20, 2020, a case management conference was held. Following the case management conference, the district court judge issued an order lifting the stay and directing the plaintiffs to file a consolidated complaint by March 12, 2020. On March 9, 2020, plaintiffs filed their complaint. [The City filed a motion to dismiss, which the district court judge denied after a hearing on July 16, 2020. The next status conference is set for September 17, 2020.]

Curb Ramp Claim. Plaintiffs have filed a class action lawsuit in the case of *Lashbrook v. City of San Jose*, pending in the United States District Court for the Northern District of California. This lawsuit alleges that the City violated federal and state disability access laws by failing to ensure that its pedestrian right of way contains curb ramps that are necessary to ensure that the pedestrian right of way is accessible to individuals with mobility disabilities. On April 14, 2020, the City Council approved a proposed settlement of this case in the form of a Consent Decree whereby Mr. Lashbrook will recover a total of \$55,000. The City will pay attorney's fees and costs in the amount of \$734,627.50. The

City will be required to expend \$13 million each year until 2030 to remediate curb ramps and after 2030 will expend 10% of its pavement maintenance budget to remediate curb ramps, which is accounted for within the City's pavement maintenance budget. The Court preliminarily approved the Consent Decree on May 27, 2020. It will conduct a Fairness Hearing on September 2, 2020, during which it will determine whether to grant final approval of the Consent Decree.

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 City has anticipated receiving claims from several people who have publicly claimed to have been injured as a result of police crowd clearance activities related to local protests similar to the national protests in late May and early June 2020 concerning the death of George Floyd and other police-related incidents resulting in deaths. In July 2020, the City, the police chief and a number of police officers were served with a complaint filed in federal district court by seven plaintiffs alleging various constitutional violations involving excessive use of force, failure to protect, failure to intervene, and violation of plaintiffs' First Amendment right to peacefully assemble and unlawful crowd control tactics including shooting projectiles at demonstrators. Additional lawsuits may be filed involving claims of police excessive force, wrongful arrest and/or other civil rights and state law violations.

In addition to these cases, a lawsuit has been filed against the City, Santa Clara County, and a number of individuals who were involved in the investigation and prosecution of a crime that resulted in a conviction and lengthy prison term for the accused individual. The suit alleges that the investigation by City police was based on a faulty identification, that they focused on the suspect to the exclusion of other suspects, and that the police failed to identify and report information that would have been exculpatory. The plaintiff in the lawsuit was recently released from prison after serving almost 20 years following a conviction integrity investigation by the District Attorney's Office; the City understands that the District Attorney decided not to re-prosecute the plaintiff. At this time, the City is not able to evaluate the potential liability exposure for the City, or potential damages, in this matter.

The pending cases are in various civil procedure stages 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 serious injury or wrongful death claims. The paraplegia 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. Currently, these cases are at various stages. The lawsuit involving the City's sign ordinance is in federal district court. The district court granted partial summary judgment in favor of the City, and the plaintiffs, with the remaining issues proceeding to trial. 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. Under the settlement frameworks, the City agreed to pay the litigants attorneys' fees: \$1,500,000 to the SJPOA and the International Association of Firefighters, Local 230 ("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 SJPOA and IAFF, Local 230, Operators and the International Union of Operating Engineers, Local No. 3 ("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 SJPOA has demanded binding arbitration pursuant to the terms of the settlement framework entered into with the SJPOA and IAFF, Local 230 and seeks additional attorneys' fees in the amount of \$1,050,000. That amount was later reduced to approximately \$500,000 and on February 4, 2020 the City and the SJPOA entered into a settlement agreement for payment in the amount of \$300,000. In addition, IAFF, Local 230, OE #3, and IFPTE, Local 21 have formally demanded binding arbitration as well. The fee demands from those parties in the aggregate total less than \$250,000. 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

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 2012-2013 and ending in 2018-2019. 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 2015-2016, 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 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. [On June 16, 2020, the Administrative Law Judge in the proceeding issued a draft Resolution denying the City's appeal in its entirety. The CPUC will consider the draft Resolution on August 27, 2020, which the City submitted comments to on July 14, 2020. The CPUC may adopt all or part of the draft Resolution, amend, or modify it, or set it aside and prepare its own order. If the draft Resolution is adopted by the CPUC without modification or amendment, then payment of the CPUC Penalty will be due within 30 days of the Resolution's effective date. This is true even if the City chooses to make an application for rehearing on the Resolution before the CPUC or later challenges the decision in court.]

On March 10, 2020, the City received a second notice of citation (the “**Second CPUC Citation**”) issued on the same day for allegedly failing to meet its 2020 Year Ahead System RA obligations. The scheduled penalty for SJCE is \$1,116,149.40. On April 9, 2020, the City filed a notice of appeal to challenge the Second CPUC Citation, again arguing that the penalty was excessive and unconstitutional because the City, among other things, undertook all reasonable steps to comply with the 2020 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 Second CPUC Citation.

Clean Water Compliance

The federal Clean Water Act (the “CWA”) establishes the structure for federal regulation of the discharge of pollutants into the waters of the United States. Under the CWA, it is unlawful to discharge any pollutant into these waters unless the discharger has a permit under the National Pollutant Discharge Elimination System (the “NPDES”) and the permittee abides by its terms.

The City is a permittee under an NPDES permit (the “**Stormwater Permit**”) issued by the Regional Water Quality Control Board – San Francisco Bay Region (the “**Regional Water Board**”). This Regional Stormwater Permit governs 76 entities, including the City, and will expire

in December 2020. On July 1, 2020, the Santa Clara Valley Urban Runoff Pollution Prevention Program (the “**SCVURPPP**”) applied to the Regional Water Board for a renewed permit on behalf of fifteen co-permittees, including the City.

The regional Stormwater Permit identifies pollutants which contribute to the impairment of water bodies and sets a total maximum daily load (“**TMDL**”) for some of these contaminants. For waters connected to the City (e.g. the San Francisco Bay), the Stormwater Permit identifies two pollutants of concern with TMDL limitations, mercury and polychlorinated biphenyls (“**PCBs**”). The City, through its work with SCVURPPP, meets the TMDL requirements for both mercury and PCBs. It is unknown if the Regional Water Board will add additional TMDLs requirements for other pollutants of concern in the next Stormwater Permit.

The Stormwater Permit also set a goal of 100% trash load reduction, or no adverse impact to receiving waters from trash by July 1, 2022, and established interim mandatory targets. The City exceeded the interim target of 80% by July 1, 2019 with a trash load reduction of 96.8% by implementing a combination of structural trash controls, source controls, trash assessments, and creek cleanups, and direct discharge programming. Fifteen percent of the City’s trash load reduction is from an offset allowed under the current Stormwater Permit for the City’s implementation of the Direct Discharge Trash Control Program, approved by the Regional Water Board in 2016.

The Regional Water Board could modify, reduce, phase out, or eliminate trash load reduction off-sets and credits in the next Stormwater Permit. If that occurs, the City will need to identify alternate measures to achieve compliance, including possibly implementing additional structural controls such as large trash capture devices. The City cannot estimate the cost of compliance without the offsets but, without them, meeting the trash load reduction by July 1, 2022 will be exceedingly difficult. The City also faces challenges with an increased population of those without permanent housing and the impacts upon the creeks. The Regional Water Board may include additional requirements to address this issue.

The City continues to cooperate with the Regional Water Board, on the terms and conditions of the next Stormwater Permit. The Regional Water Board anticipates issuing a draft permit by the end of 2020 or early 2021, and to hold public hearings prior to its approval in June 2021.

The Regional Water Board and private parties can enforce the CWA and the terms of the Stormwater Permit. Violations can result in significant civil penalties of up to \$55,800.00 per pollutant per day, plus criminal fines, and attorney’s fees.

Consent Decrees

Overview. San Francisco Baykeeper (“**Baykeeper**”) filed a lawsuit in federal district court against the City in February 2015. Baykeeper’s complaint alleged violations of the CWA and the Stormwater Permit. Specifically, the complaint alleged that the City was not in compliance with trash reduction requirements, and that there were violations resulting from the discharge of sewage from the City’s Sanitary Sewer System that infiltrated into the City’s municipal separate storm sewer systems (“**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; and
 - Identify and design an additional \$15,000,000 (\$50,000,000 aggregate) in total projects by the termination date of the consent decree.

If 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 its 10-year term and caps Baykeeper litigation fees for dispute resolution 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 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. In April 2019, the City and Baykeeper entered into the Second Amendment to the Consent Decree ("**Second Amendment**"), 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 mechanisms to fund its obligations under the Consent Decree. However, polling to date on parcel tax measures indicates that the measures would not attain the required two-thirds voter approval.

Status of Green Stormwater Infrastructure Projects. On September 10, 2019, City Council approved the 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 GIP 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.

Before City Council approval and 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 Decree to consider Baykeeper's comments in good faith. The City and Baykeeper continue to meet and confer about the adequacy of the GIP.

Baykeeper contends that the City should identify additional projects in the GIP. The City submitted the GIP to the Regional Water Board and is awaiting approval. The Board has not provided an estimate of when it may act on the City's GIP. The City staff is working on the River

Oaks Project identified in the GIP. However, it 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 (the “**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 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 José is seeking monetary tort damages from Monsanto. The cities of Oakland and Berkeley, California subsequently filed similar lawsuits which were joined with the San José 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. Monsanto and its related companies and the plaintiff public entities, including the City of San José, have filed a class action lawsuit in federal court in California as part of a negotiated proposed nationwide global settlement. The full amount of the settlement proceeds that San José will receive are subject to certain conditions in the proposed settlement for which court approval is being sought. 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.

Opioid litigation. On August 2, 2019, the City filed a lawsuit against a number of pharmaceutical manufacturers and companies who have produced and/or distributed opioid drugs. The lawsuit was filed in the Federal District Court for the Northern District of California and was subsequently consolidated with other similar cases brought by public entities pending in federal court in Ohio. At this time, the City is not able to evaluate the potential recovery that it may obtain through this litigation for costs and damages related to opioid use and addiction in the San José community.

Census litigation. On July 21, 2020, the President of the United States issued an Executive Order providing that undocumented persons residing in the United States should not be considered for purposes of congressional representation. The effect of this policy would be to lessen Congressional representation in areas with large immigrant populations, many of whom may be undocumented, such as in the City. The U.S. Constitution requires that all persons be counted in the decennial census and that the census be the basis to apportion representation across the nation. The City has joined a challenge to the Executive Order due to the concern that the order may be extended to include the allocation of certain federal funds nationally and

potentially decrease the City's share. The remedy sought in the litigation is injunctive to prevent the administration from moving forward with the direction in the Executive Order.

RETIREMENT PLANS

In June 2012, approximately 70% of San José voters passed an amendment to the City's Charter provisions related to the Retirement Plans ("**Measure B**"), 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.

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 10, 2020, 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 June 30, 2020, the book value of the City's pooled investment fund was \$2,392,587,218 while the market value was \$2,426,534,346. 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 below. The General Fund portion of the pool was approximately 26.27% as of June 30, 2020.

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 28
City of San José
Pooled Investment Fund – General Pool Investments ⁽¹⁾
As of June 30, 2020

	Book Value	Percent of Portfolio	Market Value	Weighted Average Days to Maturity	Weighted Average Yield
U.S. Treasury Bills and Notes	\$72,020,234	3.01%	\$73,268,060	359	1.92
Federal Agency Securities ⁽²⁾	742,265,430	31.02	751,256,241	1078	1.59
Supranational Securities ⁽³⁾	197,112,697	8.24	201,197,269	754	1.87
Negotiable Certificate of Deposit	46,000,000	1.92	46,251,570	128	1.73
Commercial Paper	109,587,950	4.58	109,977,050	24	1.22
Corporate Notes	597,369,918	24.97	607,775,595	411	2.27
Asset Backed Securities	21,497,392	0.9	21,978,085	1310	1.69
Municipal Bonds	265,067,916	11.08	269,854,474	612	2.16
Mortgage Backed Bonds	158,387,720	6.62	161,698,043	1178	1.8
Money Market Mutual Fund	33,277,958	1.39	33,277,958	1	0.11
State of California Local Agency Investment Fund ⁽⁴⁾	150,000,000	6.27	150,000,000	1	2.03
Total ⁽⁴⁾	\$2,392,587,214	100.00	\$2,426,534,346	672	1.86

(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 7, 2017. 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 \$195 billion, which results in a total debt limit of approximately \$29.3 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).

On November 6, 2018, the City received voter authorization to issue \$650,000,000 principal amount of general authorization bonds. On July 25, 2019, the City issued \$239,900,000 of such general obligation bonds, leaving \$410,100,000 in unused authorization remaining. The City has other series of general obligation and general obligation refunding bonds outstanding pursuant to prior voter authorizations.

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, 2020, the City had approximately \$484 million in non-voter approved bonded or certificated lease obligations outstanding. The City has never failed to pay principal of or interest on any debt or any lease obligation when due.

Table 29 summarizes City's outstanding general obligation bonds and the long-term obligations of the City payable from the General Fund as of June 30, 2020.

Table 29
City of San José
General Obligation Bonds and Bonded and Certificated General Fund Lease Obligations
As of June 30, 2020
(In thousands)

Issuer/Issue	Amount Issued	Issue Date	Purpose	Final Maturity	Amount Outstanding
<u>City of San José General Obligation Bonds</u>					
Series 2019A-1 (Disaster Preparedness, Public Safety, and Infrastructure)	\$140,360	07/25/2019	Community Facilities	09/01/2049	140,360
Series 2019B (Disaster Preparedness, Public Safety, and Infrastructure)	66,500	07/25/2019	Community Facilities	09/01/2027	66,500
Series 2019C (Refunding, Libraries, Parks, Public Safety)	158,185	07/25/2019	Community Facilities	09/01/2035	158,185
Series 2019D (Refunding, Libraries, Parks, Public Safety)	103,935	07/25/2019	Community Facilities	09/01/2024	103,935
	\$468,980				\$468,980
<u>City of San José General Fund Debt</u>					
Equipment Lease-Purchase Agreement (Taxable) ESCO	\$19,286	5/29/2014	Equipment Lease	06/01/2034	\$12,431 ^(1/2)
<u>City of San José Financing Authority-Lease Revenue Bonds:</u>					
Series 2003A (Central Service Yard)	\$22,625	09/18/2003	Refunding	10/15/2023	\$6,045
Series 2006A (Civic Center Project)	57,440	06/01/2006	Refunding	06/01/2039	51,670 ^(1/2)
Series 2007A (Recreational Facilities)	36,555	06/28/2007	Refunding	08/15/2030	9,195 ^(1/2)
Series 2008E-1 (Taxable) (Ice Centre)	13,015	07/03/2008	Refunding	06/01/2025	5,590 ^(1/2)
Series 2008E-2 (Taxable) (Ice Centre)	13,010	07/03/2008	Refunding	06/01/2025	5,585 ^(1/2)
Series 2011A (Convention Center)	30,985	04/12/2011	Convention Center	05/01/2042	28,040
Series 2013A (Civic Center Project)	305,535	05/28/2013	Refunding	06/01/2039	267,830 ^(1/2)
Series 2013B (Civic Center Garage Project)	30,445	06/19/2013	Refunding	06/01/2039	25,685
	\$509,610				\$ 399,640
<u>City of San José Financing Authority Short-Term Debt:</u>					
Lease Revenue Commercial Paper Notes ⁽¹⁾	\$125,000	Various	Various	Various	\$72,526
Grand Total	\$1,122,876				\$953,277

(1) Expected to be refunded, in full, with proceeds of the Bonds.

(2) Expected to be refunded, in full, with proceeds of the [2020A/2020B] Bonds.

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, 2019, Note III.F.2" for a description of such debt as of June 30, 2019.

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.

Tax and Revenue Anticipation Notes. The City began prefunding certain employer retirement contributions in 2008 for budgetary savings. Beginning in 2010-2011, and in each fiscal year thereafter through 2018-2019, the City entered into short-term borrowings to avoid a negative cash balance in the General Fund portion of the City Investment Pool as a result of prefunding its employer retirement contribution. The City did not issue Tax and Revenue Anticipation Notes in 2019-2020 as prefunding would not have resulted in sufficient budgetary savings. On July 1, 2020 the City issued the 2020 TRAN in the aggregate principal amount of \$130 million directly to two Banks in separate private placements to fund a portion of its retirement contribution. The interest expense for the 2020 TRAN is estimated to be \$1,486,875, and costs associated with the financing were \$73,000, resulting in a total projected cost of borrowing at approximately \$1,554,875 (the 2020-2021 Proposed Budget assumed that the total projected borrowing cost would be approximately \$1.4 million). For additional information about expected savings to the City for pre-funding retirement contributions for 2020-2021, see BUDGET – 2020-2021 PROPOSED OPERATING BUDGET above.

For additional information about the City's employer retirement contributions, see APPENDIX B – "THE CITY OF SAN JOSE: RETIREMENT PLANS - PENSION PLANS - Pension Plan Contributions."

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, 2020, is shown in Table 30 below. The City makes no representations as to the completeness or accuracy of such statement.

Table 30
City of San José
Statement of Direct and Overlapping Debt

2019-2020 Assessed Valuation: \$195,150,553,764

	% Applicable⁽¹⁾	Debt 6/30/2020
<u>Direct and Overlapping Tax and Assessment Debt:</u>		
Santa Clara County	37.856%	\$ 333,683,605
Foothill-DeAnza Community College District	3.955	24,044,841
Gavilan Joint Community College District	5.135	6,370,995
San Jose-Evergreen Community College District	85.246	730,759,349
West Valley Community College District	32.068	197,965,384
Morgan Hill Unified School District	11.878	14,097,404
San Jose Unified School District	98.448	518,839,690
Santa Clara Unified School District	22.237	231,970,825
Campbell Union High School District	59.601	220,318,077
East Side Union High School District	96.041	838,734,263
Fremont Union High School District	8.788	45,742,866
Los Gatos-Saratoga Joint Union High School District	0.881	783,473
Alum Rock Union School District	77.889	76,241,648
Berryessa Union School District	94.904	76,191,808
Cambrian School District	64.267	31,169,459
Campbell Union School District	47.580	104,133,699
Cupertino Union School District	15.795	44,512,411
Evergreen School District	99.405	143,137,844
Franklin-McKinley School District	99.500	137,464,203
Los Gatos Union School District	1.806	1,384,389
Luther Burbank School District	18.975	3,481,344
Moreland School District	74.212	73,441,866
Mount Pleasant School District	88.404	24,966,566
Oak Grove School District	99.919	228,363,970
Orchard School District	100.000	36,281,612
Union School District	72.617	81,410,342
City of San Jose	100.000	468,980,000
City of San Jose Community Facilities Districts	100.000	7,540,000
City of San Jose Special Assessment Bonds	100.000	7,505,000
Midpeninsula Regional Open Space District	0.011	9,769
Santa Clara Valley Water District Benefit Assessment District	37.856	24,793,787
Total Direct and Overlapping Tax and Assessment Debt		\$4,734,320,489

(continued)

Table 30 (continued from previous page)
City of San José
Statement of Direct and Overlapping Debt

	% Applicable⁽¹⁾	Debt 6/30/2020
<u>Direct and Overlapping General Fund Debt:</u>		
Santa Clara County General Fund Obligations.....	37.856%	\$ 365,963,454
Santa Clara County Pension Obligation Bonds	37.856	131,359,048
Santa Clara County Board of Education Certificates of Participation	37.856	1,317,389
Foothill-DeAnza Community College District General Fund Obligations	3.955	952,863
Gavilan Joint Community College District General Fund Obligations.....	5.135	669,091
San Jose-Evergreen Community College District Benefit Obligations.....	85.246	40,449,227
West Valley-Mission Community College District General Fund Obligations	32.068	16,284,130
Morgan Hill Unified School District Certificates of Participation	11.878	1,604,124
San Jose Unified School District Certificates of Participation	98.448	9,249,190
Santa Clara Unified School District Certificates of Participation	22.237	3,017,561
Campbell Union High School District General Fund Obligations	96.041	26,387,265
East Side Union High School District Post Employment Obligations.....	0.881	23,206
Los Gatos-Saratoga Joint Union High School District Certificates of Participation.....	59.601	11,920,200
Alum Rock Union School District Certificates of Participation	77.889	12,399,929
Berryessa Union School District Certificates of Participation.....	94.904	3,701,089
Campbell Union School District General Fund Obligations	47.580	1,160,952
Franklin-McKinley School District Certificates of Participation.....	99.500	2,994,950
City of San Jose General Fund Obligations	100.000	407,780,000
Midpeninsula Regional Open Space Park District General Fund Obligations	0.011	12,318
Santa Clara County Vector Control District Certificates of Participation.....	37.856	760,906
TOTAL GROSS DIRECT AND OVERLAPPING GENERAL FUND DEBT		\$1,038,006,892
Less: Santa Clara County supported obligations		27,769,660
Total Direct and Overlapping General Fund Debt		\$1,010,237,232
 OVERLAPPING TAX INCREMENT DEBT (Successor Agency)	 100.000%	 \$1,476,820,000
 Gross Combined Total Debt		 \$7,249,147,381
Net Combined Total Debt		\$7,221,377,721 ⁽²⁾
<u>Ratios to 2019-2020 Assessed Valuation:</u>		
Direct Debt (\$468,980,000)	0.24%	
Total Direct and Overlapping Tax and Assessment Debt	2.43%	
Combined Direct Debt (\$890,355,000)	0.45%	
Gross Combined Total Debt	3.71%	
Net Combined Total Debt	3.70%	
 <u>Ratios to Redevelopment Valuation (\$32,973,204,937):</u>		
Total Overlapping Tax Increment Debt	4.48%	

⁽¹⁾ Excludes Bonds to be sold.

⁽²⁾ 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

General

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 [Series 2020A/B] 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 following documents:

- the City’s Basic Financial Statements for the Fiscal Year Ended June 30, 2019 included in the City’s Comprehensive Annual Financial Report (“**City of San José Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2019**”),
- the City of San José Federated City Employees’ Retirement System Actuarial Valuation Report as of June 30, 2019 (the “**Federated 2019 Pension Plan Actuarial Report**”),
- the City of San José Police and Fire Department Retirement Plan Actuarial Valuation Report as of June 30, 2019 (the “**Police and Fire 2019 Pension Plan Actuarial Report**”),
- the City of San José Federated Postemployment Healthcare Plan Actuarial Valuation Funding Report as of June 30, 2019 (the “**Federated 2019 Healthcare Plan Actuarial Report**”),
- the City of San José Police and Fire Department Postemployment Healthcare Plan Actuarial Valuation Funding Report as of June 30, 2019 (the “**Police and Fire 2019 Healthcare Plan Actuarial Report**”),

- the Federated City Employees' Retirement System Comprehensive Annual Financial Report for the Fiscal Years ended June 30, 2019 and June 30, 2018 (the "**Federated 2019 CAFR**"), and
- the Police and Fire Department Retirement Plan Comprehensive Annual Financial Report for the Fiscal Years ended June 30, 2019 and June 30, 2018 (the "**Police and Fire 2019 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. In instances where information relating to the Retirement Plans in this Appendix B is available from a comprehensive annual financial report and an actuarial report, such information has been obtained from the comprehensive annual financial report. In some instances, there may be differences in financial figures between reports because the figures in the comprehensive annual financial reports are based on a valuation one year prior to the measurement date used in the actuarial reports rolled forward using roll-forward procedures. However, the City does not believe that such differences are material.

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.

The City maintains a number of websites, including a website for each of the 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.

COVID-19

The most recent actuarial valuations reports for the Retirement Plans that are available are for the valuations as of June 30, 2019. There has been substantial economic impacts and tremendous volatility in the markets in the United States and globally associated with the COVID-19 outbreak, resulting in significant declines and speculation of a national and global recession. Such impacts and volatility may impact the respective market values of the Retirement Plans' assets and the funded status of the Retirement Plans. As a result, such valuation reports and the information presented in this Appendix B do not reflect the impact of recent market volatility and its effect on the Retirement Plans. In particular, the projections contained herein on future City contributions do not reflect the impact of the COVID-19 pandemic on the Retirement Plans, including likely impacts on investment returns, health care costs, salaries, employment levels, or other factors that may affect the valuation and future City contributions. Consequently, such projections should be used with extreme caution as actual contribution requirements could differ substantially. The City expects its unfunded accrued liability and actuarially determined required contributions to the Retirement Plans to increase in the future as result. The City cannot at this time project the magnitude or timing of such increases. The City makes no prediction as to the degree of the impact of COVID-19 on the value of the assets of the Retirement Plans or any effect on the future City contributions to the Retirement Plans. See "BOND OWNERS' RISKS – COVID-19 Pandemic" in the forepart of this Official Statement for further discussion regarding the COVID-19 pandemic and associated risks.

RETIREMENT PLANS IN GENERAL

Overview

General. 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 postemployment healthcare plan. The single-employer tax-qualified defined benefit pension plans 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 plans offered under the Federated Plan and the Police and Fire 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.

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. See “PENSION PLANS.”

The Healthcare Plans pay all, or a portion of, health and dental insurance premiums for eligible retirees and their survivors and dependents. The Healthcare Plans consist of trusts (herein referred to as the Federated 115 Trust, the Police 115 Trust and the Fire 115 Trust and, collectively, the “**Section 115 Trusts**”) formed under Section 115 of the Internal Revenue Code (the “**Code**”) to supplement accounts previously established by the City under Section 401(h) of the Code (collectively, the “**401(h) accounts**” and each, a “**401(h) account**”). The 401(h) accounts were previously established within each Pension Plan, a single account for the Federated Healthcare Plan, and a single account for the Police and Fire Healthcare Plan. The 401(h) account for the Federated Healthcare Plan was depleted in fiscal year 2018-2019. As a result, all Federated Healthcare Plan benefits are now paid from the Federated 115 Trust. See “HEALTHCARE PLANS – Establishment of 115 Trusts for Healthcare Plans; Tax Limitations” for a discussion regarding the Section 115 Trusts.

Participation by covered employees in the Pension Plans is mandatory, except for employees excluded under the City Charter as described below in “RETIREMENT PLANS IN GENERAL – Retirement Plans’ Governance” and 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. For those employees who participate in the Pension Plans, participation in the Healthcare Plans is mandatory, except for (i) Federated members hired or rehired after the dates specified in Table B-1a or who elected to opt-in to the VEBA, and (ii) Police and Fire members hired or rehired after dates specified in Table B-1b or who elected to opt-in to the VEBA. See “CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS – Implementation of Measure F and Settlement Frameworks – VEBA Establishment” for a discussion of the establishment of the VEBAs.

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 covered employees make regular contributions to the Retirement Plans. Contributions to the Pension Plans by the City and covered employees are actuarially determined. The San José Municipal Code (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 by the City are actuarially determined while contributions by employees are determined based on rates established by the Municipal Code and the Settlement Frameworks (as hereinafter defined).

See “PENSION PLANS – Pension Plan Contributions” and “HEALTHCARE PLANS – Funding Policy and Healthcare Plan Contributions” for a discussion of historical and projected contributions to the Pension Plans and the Healthcare Plans, respectively.

Implementation of Certain Accounting Changes Relating to Retirement Plans. In June 2012, the Governmental Accounting Standards Board (“**GASB**”) issued Statement No. 67, Financial Reporting for Pension Plans – an Amendment of GASB Statement No. 25 (“**GASB Statement No. 67**”) and Statement No. 68, Accounting and Financial Reporting for Pensions - an amendment of GASB Statement No. 27 (“**GASB Statement No. 68**”), which address the accounting and financial reporting requirements for pensions. The provisions of GASB Statements No. 67 and 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. They also include 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. The City implemented GASB Statements No. 67 and 68 in fiscal years 2013-2014 and 2014-2015, respectively. When the City implemented GASB Statement No. 68, 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.

In June 2015, the GASB issued Statement No. 74, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans (“**GASB Statement No. 74**”). This statement replaces GASB Statement No. 43, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans, as amended (“**GASB Statement No. 43**”), and No. 57, OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans. It also includes requirements for defined contribution OPEB plans that replace the requirements for those OPEB plans in GASB Statement No. 25, Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans, as amended, GASB Statement No. 43, and GASB Statement No. 50, Pension Disclosures. The City implemented GASB Statement No. 74 in fiscal year 2016-2017.

In June 2015, the GASB issued Statement No. 75, Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions (“**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 (“**GASB Statement No. 45**”), and Statement No. 57, for OPEB. GASB Statement No. 75 addresses accounting and financial reporting for OPEB and establishes standards for recognizing and measuring liabilities, deferred outflows/inflows of resources, and expenses/expenditures. The City implemented GASB Statement No. 75 in fiscal year 2017-2018. Because GASB Statements No. 74 and 75

have been implemented, the annual required contribution formerly required under GASB Statements No. 43 and 45 is no longer applicable to OPEB plans such as the Healthcare Plans.

Plan Actuary. 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 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 Board shall be appointed and removed by the City Council in a manner prescribed by ordinance.

The Board of the Police and Fire Plan consists of nine-members (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 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.

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 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

The 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 (\$285,000 for 2020) 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 2020, the maximum annual payment is \$230,000; 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 conformed benefit payments to certain retirees within the Federated Plan to the applicable Code limits as of July 1, 2015 after becoming aware of pension overpayments to such retirees. 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 thereafter entered into a settlement under which the overpayment amount of \$866,000 as of June 2016 was included as an actuarial loss in the calculation of the Federated Plan's unfunded actuarial accrued liability, and as a result, 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 and the Federated Plan Board and have since filed a lawsuit against the City and the Board. 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 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. The City has accepted the tendered defense of the Board. See “SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND COURT DECREES – Other Significant Proceedings – *Retirement Benefits Litigation*” in Appendix A for a description regarding the status of such lawsuit.

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 had underperformed their respective investment benchmarks over the then previous five fiscal years while their staffing and administrative expenses had 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, as well as website upgrades to promote transparency and ease of navigation for stakeholders and the Plans’ members. 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.

2019 Grand Jury Report on Unfunded Pension Liabilities

General. On June 19, 2019, the 2018-2019 Santa Clara County Civil Grand Jury (the “**Grand Jury**”) released publicly its final report entitled, “SAN JOSE – UNFUNDED PENSION LIABILITIES – A Growing Concern” (the “**Grand Jury Report**”). In the Grand Jury Report, the Grand Jury made six findings with respect to the Pension Plans and provided seven recommendations with respect to such findings for consideration by the City and the Boards. Under the California Constitution and Penal Code, the Grand Jury, a body composed of volunteer citizens, may at its discretion investigate the operations of cities within the County,

including the City, and make such recommendations as it sees fit. However, the Grand Jury's recommendations are not binding on the City or the Boards.

In the Grand Jury Report, the Grand Jury requested responses from the City and each of the Boards to certain findings and recommendations in accordance with the Penal Code. The City and the Boards submitted their respective responses to the Grand Jury Report in September 2019.

Grand Jury Findings and Recommendations; Responses of Boards and City.
Below is a summary of the findings and recommendations of the Grand Jury and the responses of the City and the Boards thereto. The City and the Boards responded to such findings and recommendations only if requested in the Grand Jury Report.

- **Finding 1:** Moving the City's mature Pension Plans to a more risk-averse investment portfolio has contributed in part to poor investment returns.
 - **Board Response:** The Boards respectfully disagree with this finding. The Boards have considered the risk/return balance of their portfolios in the context of their benefit payment obligations and cash flow needs, the risk tolerances of the Boards and the City plan sponsor, and all other factors affecting the diversification of their respective portfolios.
- **Recommendation 1:** The Boards should conduct a comprehensive review of respective plan investment portfolios that should be made public by June 30, 2020 and consider investment strategies used by other state and government pension organizations with similar risk profiles that have higher returns.
 - **Board Response:** The Boards will implement this recommendation and make public a report in a timely manner, once the data has been obtained and analyzed.
- **Finding 2:** The Pension Plans are overburdened with a large number of investment managers and excessive investment management fees.
 - **Board Response:** The Boards respectfully disagree with this finding. The plans invest through multiple, diversified investment vehicles across global markets and incur fees commensurate with the Boards' judgment as to the prudent investment of the assets of the plans and expected returns from those investments. The fees paid to investment managers are in line with those paid by comparable plans with similar investment profiles.
- **Recommendation 2:** The Boards should study ways to reduce the number and cost of investment managers.
 - **Board Response:** This recommendation is being implemented. The Boards strive to reduce fees through negotiation and competitive pricing, when available. Each selected investment vehicle plays an intentional role in the plans' diversified portfolios. The Boards will continue to study ways to make the investment portfolio more cost efficient and will report publicly on their success in a timely manner.

- **Finding 3:** The City's mandatory required contributions to Pension Plans are putting an ever-increasing burden on the City's General Fund, which impedes the ability of the City to provide essential services to its residents.
 - **Board Response:** The Boards can neither agree nor disagree with this finding; only the City can address the impact of retirement contributions on its General Fund.
 - **City Response:** The City agrees with this finding. The City is committed to providing its residents and customers with essential services, and has taken several steps to address the high cost of retirement benefits for City employees. This includes the Settlement Frameworks, which contained several cost saving measures and protections against further benefit enhancements without a vote of the electorate.¹
- **Recommendation 3:** The City should work collaboratively with its bargaining units to find ways to reduce the burden on the City's General Fund no later than June 30, 2020.
 - **Board Response:** This recommendation is addressed only to the City and its recognized bargaining units. The design of the benefit program administered by the Boards is beyond the jurisdiction of the Boards. Once the City and its employees reach agreement on the benefit package, the Boards are obligated to collect the contributions necessary to pay the promised benefits.
 - **City Response:** The City agrees with this recommendation. The anticipated outcome of the Retirement Stakeholder Solutions Working Group is that a list of recommendations will be developed (see "– Retirement Stakeholder Solutions Working Group" below), which may not be available until after June 2020. With respect to the benefits agreed to in the Settlement Frameworks, legal impediments to changing such benefits exist.
- **Finding 4:** Maintaining two separate Boards has resulted in inefficiencies including duplication of various tasks and responsibilities.
 - **Board Response:** The Boards respectfully disagree with this finding. The two Boards maintain a single administrative staff (unlike the practice found in other large California charter cities, like Los Angeles), which is cost efficient and effective. The Boards also typically engage the same professionals to advise them on investments, actuarial and legal matters, thus avoiding considerable duplication of effort. The Boards often invest in investment vehicles together, assuring them of favorable fees and terms. Finally, the Boards often conduct joint committee meetings, to coordinate their activities and benefit from their respective views on common issues. The fact that each Board meets once a month to conduct business on behalf of its own unique membership does not itself result in "inefficiencies."

¹ In October 2019, the City formed the Retirement Stakeholder Solutions Working Group to identify potential solutions to the high cost of funding the Retirement Plans. See "– Retirement Stakeholder Solutions Working Group" below.

- **City Response:** The City agrees with this finding in general. While the two Boards maintain a shared administrative staff and typically engage the same professionals to advise them on investment, actuarial, and legal matters, it appears that there is some inherent duplication of effort and expenses that need to be explored further.
- **Recommendation 4a:** The City should consider opportunities for streamlining and identify areas for administrative cost reduction, including establishing one Board to administer both Pension Plans.
 - **City Response:** This recommendation requires further analysis. One of the goals of the Retirement Stakeholder Solutions Working Group is to examine the issues and challenges surrounding the retirement systems. Several issues will be reviewed and researched by the Retirement Stakeholder Solutions Working Group, and the Retirement Stakeholder Solutions Working Group could address the different opportunities to streamline the administration of the Boards.
- **Recommendation 4b:** The Boards should implement employee reviews based on measurable goals and performance metrics for the Chief Executive Office and the Chief Investment Officer of the Office of Retirement Services by December 31, 2019.
 - **Board Response:** This recommendation is being implemented. The Boards' Joint Personnel Committee is in the process of developing additional performance metrics for the CEO and CIO positions. These metrics are expected to enhance the current practice of evaluating the CEO and CIO's annual work plans and utilizing the City's standard executive management evaluation measures. As of June 2020, the Boards have adopted updated annual performance evaluation and performance metrics for the CEO and CIO positions. Annual performance evaluations are anticipated to commence in fiscal year 2021-22.
- **Finding 5:** The expertise of the public members of the Boards is heavily weighted toward investment professionals; while other more successful pension funds have boards that have a much wider range of expertise.
 - **City Response:** The City partially disagrees with this finding. The City agrees that the expertise of the current public Board members is heavily weighted toward investment professionals. The City made significant changes to the composition of the retirement boards in 2010, based on recommendations from a consultant's review of the retirement board structure and the qualifications of its members. The changes made to the required qualifications for the public Board members were meant to help select individuals who had relevant expertise to understand the complex issues that occur in the administration of defined benefit retirement plans. The City disagrees that broadening the qualifications for the public members of the Boards beyond the qualifications enumerated above would necessarily make the pension systems more successful without further analysis.

- **Recommendation 5:** The City should broaden the occupational expertise requirements for appointment of the public Board members.
 - **City Response:** The recommendation has not yet been implemented, but will be implemented as Board members' terms expire.
- **Finding 6:** The cost of living adjustments ("**COLA**") for Tier 1 retirees has a major impact on the unfunded liability, increasing the burden on the City's General Fund and further impeding the ability of the City to provide essential services to its residents.
 - **City Response:** The City agrees with this finding. The City recognizes that the 3% COLA has an impact on the cost of pension benefits for Tier 1 employees. To contain costs related to post-retirement benefits, the City and the bargaining units agreed to a lesser level of benefits for Tier 2 when compared to Tier 1 pension benefits in recognition of the unsustainable retirement costs. As stated in the Grand Jury's report, the Tier 2 COLA benefits are tied with the consumer price index and capped at a maximum of 2%.
- **Recommendation 6:** The City should examine ways in which the Tier 1 members' COLA liability can be reduced by considering options such as reducing COLAs in exchange for a lump sum buyout.
 - **City Response:** The City disagrees with this recommendation. There are legal issues relating to changes to the current Tier 1 COLA structure. The City's prior attempt to modify Tier 1 COLAs was found invalid by a County Superior Court in the Measure B litigation.

A copy of the Grand Jury Report can be accessed on the website of the Santa Clara County Superior Court at: http://www.sccscourt.org/documents/San%20Jos%C3%A9%20-%20Unfunded%20Pension%20Liabilities%20-%20Rev.%2006.19.19_Signed.pdf. A copy of the City's responses to the Grand Jury Report can be accessed on the website of the Santa Clara County Superior Court at: http://www.sccscourt.org/court_divisions/civil/cgj/2019/Responses/City%20of%20San%20Jose%2009.23.19.pdf. A copy of the joint responses by the Boards to the Grand Jury Report can be accessed on the website of the Santa Clara County Superior Court at: http://www.sccscourt.org/court_divisions/civil/cgj/2019/Responses/Federated%20City%20Retirement%20System.pdf. The foregoing websites are referenced for informational purposes only and none are incorporated into this Appendix B by reference. The City and the Underwriters make no representation whatsoever as to the accuracy or completeness of any of the information on such websites.

Retirement Stakeholder Solutions Working Group

In November 2019, the City formed the Retirement Stakeholder Solutions Working Group (the "**Working Group**") with the stated purpose of developing a shared understanding of the issues facing the City's retirement systems and to collaboratively develop a list of recommendations to be presented to City Council for review and consideration. The Working Group is comprised of representatives from a range of active and retired stakeholder groups and meets on a monthly basis. These groups represent active City bargaining groups,

Federated and Police and Fire retirees, community groups, City Council, two members of each Retirement Board and City staff. The Working Group's meetings were put on hold due to the City's response to COVID-19. As such, the Working Group has not presented any recommendations to the City Council for review and consideration.

APPENDIX B DEFINITIONS

The following terms are used in this Appendix B:

Actuarial Liability ("AL"): That portion of the present value of future benefits not provided for by future Normal Costs. The Actuarial Liability 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 Retirement Plans, there are two components to the contribution: (i) the Normal Cost (including administrative expenses), and (ii) an amortization payment on the Unfunded Actuarial Liability.

Amortization Payment: The portion of the pension plan or OPEB contribution that is designed to pay interest and principal on the UAL in a given number of years.

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 or healthcare plan trust.

Funded Ratio: Either the Market Value of Assets or Actuarial Value of Assets divided by the AL. 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 less the Fiduciary Net Position.

Net Pension Liability: The liability reported by the City for a Pension Plan on its statement of net position. It is calculated as the Total Pension Liability 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 AL 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 AL 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 AL over the Actuarial Value of Assets. The UAL typically results from gains and losses recognized as result of investment returns that differ from the discount rate 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 (i.e., the AL) 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 AL. 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,” respectively.

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 subject to IRS approval; (3) place limitations on disability retirements; (4) authorize the City Council to temporarily suspend the COLA 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. For additional information and discussion regarding claims made by various bargaining units seeking the City’s payment of additional attorneys’ fees related to the settlement of the Measure B litigation, please see “SIGNIFICANT LITIGATION, CLAIMS, PROCEEDINGS AND CONSENT DECREES – Potentially Significant Litigation – *Claims for Additional Attorneys’ Fees Related to Measure B*” in Appendix A.

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 related to Measure B (“**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 agreement 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: (i) revised Tier 2 pension benefits that increased pension benefits for Tier 2 employees while preserving the 50/50 cost sharing between the City and Tier 2 employees; (ii) closed the defined benefit retiree healthcare benefit under the Healthcare Plans to new employees, as well as agreement on a new lowest cost medical plan associated with retiree healthcare; (iii) allowed 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); (iv) allowed Tier 1 employees who terminated employment with the City and either subsequently returned, or that return in the future, to return as Tier 1 employees; and (v) continued the elimination of the Supplemental Retiree Benefit Reserve (“**SRBR**”). In the Settlement Frameworks, the City also agreed that a ballot measure regarding the Settlement Frameworks would be placed on the November 2016 election. The City submitted the approval of the Settlement Frameworks to voters in the City through Measure F on the November 2016 election, as described below.

The Settlement Frameworks also contemplated that the City and the respective bargaining units within each Retirement Plan would enter into memorandums of agreement (“**MOA**”) memorializing the terms of the Settlement Frameworks, with each such MOA having an expiration date of June 30, 2025. To date, the City has not entered into any MOAs, but has received requests from bargaining units representing members of the Police and Fire Retirement Plan to enter into an MOA. The City believes that the terms of the Settlement Frameworks are binding upon the City, the members of the Retirement Plans, and the Retirement Plans notwithstanding MOAs not having been entered into to date.

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 then 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 25% 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 of their Tier 2 service on a 1:1 basis with the City. The employees' portion of liability for reclassifications costs are paid over individually determined amortization periods and includes payment of interest set by the Boards at 6.75%. The side letter agreements with the bargaining units were agreed to in June 2018, and the Municipal Code amendments were approved by the City Council in December 2018.

In June 2020, the City and the bargaining units agreed that the City would pay future interest costs on Tier 1 Rehire employees' unpaid liability. The changes arose in response to contribution rates of some Tier 1 Rehire employees being insufficient to pay amortization payments of both a portion of the liability relating to the reclassification and interest accruing on the unpaid liability. On August 4, 2020, the City Council adopted an ordinance amending the Municipal Code in order to implement the City's agreement to pay the future interest costs, which is scheduled to become effective on September 4, 2020. As of June 2020, the interest cost to be paid by the City was estimated to total approximately \$307,000.

The terms of the Retirement Plans as of June 30, 2019 are described below and in APPENDIX C – "BASIC FINANCIAL STATEMENTS FOR THE FISCAL YEAR ENDED JUNE 30, 2019," 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 members of the Federated Plan (with the exception of Tier 1 Classic members hired after September 27, 2013), Tier 2A members of the Federated Plan, and Tier 1 members of the Police and Fire Plan to make 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. In addition, the City will not make contributions into the VEBAs. The VEBAs are not subject to the jurisdiction of the Boards and are instead 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 Section 115 Trust to their VEBA accounts (see "HEALTHCARE PLANS – Establishment of 115 Trusts for Healthcare Plans; Tax Limitations" for a discussion regarding such trusts). 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 such Healthcare Plan, without interest, was required to be contributed to the member's VEBA account from the applicable Section 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 applicable Healthcare Plan, 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 was to 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 accounts, the opt-in by employees who are members of the Healthcare Plans, and the transfer of Section 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 “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 the 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 of 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 if they were not employed during the initial opt-in period 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, 2017. 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 membership categories for the Retirements Plans effective June 18, 2017, are described below in Table B-1a and Table B-1b.

**Table B-1a
Federated Plan Membership Tiers**

Tier	Hire Date	Pension	Defined Benefit Retiree Healthcare (Medical/Dental)
Tier 1	<ul style="list-style-type: none"> On or before September 29, 2012 Former Tier 1 rehired on or after June 18, 2017 who did not take a return of contributions 	Tier 1	Medical/Dental ⁽²⁾⁽⁴⁾
Tier 1 Rehire	<ul style="list-style-type: none"> Former Tier 1 rehired on or after September 30, 2012 through June 17, 2017 	Tier 1 ⁽¹⁾	Medical/Dental ⁽²⁾⁽⁴⁾⁽⁵⁾
Tier 1 Classic	<ul style="list-style-type: none"> "Classic" membership with California Public Employees' Retirement System ("CalPERS")/reciprocal agency hired on or after September 30, 2012, but before September 27, 2013 "Classic" membership with CalPERS/reciprocal agency hired on or after September 27, 2013 	Tier 1 ⁽⁶⁾	Medical/Dental
Tier 2 (or Tier 2A)	<ul style="list-style-type: none"> Hired/rehired/reinstated on or after September 30, 2012, but before September 27, 2013 	Tier 2	Medical/Dental ⁽²⁾⁽⁴⁾
Tier 2B	<ul style="list-style-type: none"> Hired/rehired/reinstated after September 27, 2013 and have not met City's eligibility for retiree healthcare 	Tier 2	Not Eligible ⁽³⁾⁽⁴⁾

⁽¹⁾ 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.

⁽²⁾ 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.

⁽³⁾ Employees in these tiers were mandatorily placed into the Federated VEBA.

⁽⁴⁾ Unrepresented employees were eligible to opt into the Federated VEBA but are not eligible to make ongoing contributions to the Federated VEBA.

⁽⁵⁾ 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.

⁽⁶⁾ 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, 2019; Cheiron Inc.

Table B-1b
Police and Fire Plan Membership Tiers

Tier	Hire Date	Pension	Defined Benefit Retiree Healthcare (Medical/Dental)
Police Tier 1	<ul style="list-style-type: none"> • Before August 4, 2013 • Former Tier 1 rehired on or after June 18, 2017 who did not take a return of contributions 	Tier 1 ⁽¹⁾	Medical/Dental ⁽²⁾⁽⁴⁾
Police Tier 1 Rehire	<ul style="list-style-type: none"> • Tier 1 employee rehired between August 4, 2013 through June 17, 2017 	Tier 1 ⁽¹⁾	Medical/Dental ⁽²⁾⁽⁴⁾
Fire Tier 1	<ul style="list-style-type: none"> • Before January 2, 2015 • Former Tier 1 rehired on or after June 18, 2017 who did not take a return of contributions 	Tier 1	Medical/Dental ⁽²⁾⁽⁴⁾
Fire Tier 1 Rehire	<ul style="list-style-type: none"> • Tier 1 employee rehired between January 2, 2015 through June 17, 2017 	Tier 1 ⁽¹⁾	Medical/Dental ⁽²⁾⁽⁴⁾
Tier 1 Classic	<ul style="list-style-type: none"> • “Classic” membership with CalPERS/reciprocal agency hired on or after August 4, 2013 for Police and January 2, 2015 for Fire 	Tier 1 ⁽⁵⁾	Not Eligible
Police Tier 2	<ul style="list-style-type: none"> • On or after August 4, 2013 	Tier 2	Not Eligible ⁽³⁾⁽⁴⁾
Fire Tier 2	<ul style="list-style-type: none"> • On or after January 2, 2015 	Tier 2	Not Eligible ⁽³⁾⁽⁴⁾

⁽¹⁾ 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.

⁽²⁾ 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.

⁽³⁾ Employees in these tiers were mandatorily placed into the Police and Fire VEBA.

⁽⁴⁾ 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.

⁽⁵⁾ 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, 2019; Cheiron Inc.

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 298 members from 2018 to 2019. For the Police and Fire Plan, total membership increased by 139 members from June 30, 2018 to June 30, 2019. However, as of June 30, 2019, 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 1.63 to 1 in the Federated Plan and 1.56 to 1 in the Police and Fire Plan. The Plan Actuary has indicated that the Federated Plan ratio appears to have stabilized but there is no indication yet of a return to a lower ratio. According to the Plan Actuary, the growth in active members in the Police and Fire Plan in the previous two years has resulted in slight declines in this ratio. The Plan Actuary further notes that because there are more retired and vested terminated members to be supported by each active member, future contributions may 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 2019 CAFR and Police and Fire 2019 CAFR indicate that over 70% of the Retirement Plans' membership is in Tier 1. Because Tier 1 is closed, the ratio of Tier 1 membership to Tier 2 membership will continue to decrease. As of June 30, 2019, the division of membership between Tiers 1 and 2 within the Retirement Plans is as follows:

- 73.9% Tier 1 and 26.1% Tier 2 in the Federated Pension Plan;
- 46.1% Tier 1 active members and 53.9% Tier 2 active members in the Federated Pension Plan;
- 98.5% Tier 1 and 1.5% Tier 2 in the Federated Healthcare Plan;
- 87.0% Tier 1 and 13.0% Tier 2 in the Police and Fire Pension Plan;
- 71.4% Tier 1 active members and 28.6% Tier 2 active members 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, 2018</u>	<u>June 30, 2019</u>	<u>% Change</u>
Pension Plan Membership			
Federated Plan			
Retirees & beneficiaries receiving benefits ⁽¹⁾	4,225	4,359	3.2%
Terminated vested members not yet receiving benefits	1,434	1,535	7.0%
Active members	<u>3,554</u>	<u>3,617</u>	<u>1.8%</u>
Total	9,213	9,511	3.2%
Police and Fire Plan			
Retirees & beneficiaries receiving benefits ⁽¹⁾	2,250	2,318	3.0%
Terminated vested members not yet receiving benefits	323	333	3.1%
Active members	<u>1,639</u>	<u>1,700</u>	<u>3.7%</u>
Total	4,212	4,351	3.3%
Healthcare Plan Membership			
Federated Plan			
Retirees & beneficiaries receiving benefits	3,627	3,654	0.7%
Terminated vested members not yet receiving benefits	164	165	0.6%
Active members	<u>1,751</u>	<u>1,582</u>	<u>(9.7%)</u>
Total⁽²⁾	5,542	5,401	(2.5%)
Police and Fire Plan			
Retirees & beneficiaries receiving benefits	2,102	2,153	2.4%
Terminated vested members not yet receiving benefits	16	16	--
Active members	<u>1,218</u>	<u>1,142</u>	<u>(6.2%)</u>
Total⁽²⁾	3,336	3,311	(0.7%)

⁽¹⁾ The combined domestic relations orders are not included in the count above as their benefit is included in the member count.

⁽²⁾ Excludes members that are eligible for catastrophic disability benefits only from the Healthcare Plans.

Source: Federated 2019 CAFR; Police and Fire 2019 CAFR.

Summary of Retirement Plans Historical and Projected Contributions

Forward Looking Statements. 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 actual obligations to the Retirement Plans to be higher or lower than those projected by the Plan Actuary in any particular year.

Plan Risks. In the Federated 2019 Pension Plan Actuarial Report and the Police and Fire 2019 Pension Plan Actuarial Report, the Plan Actuary states that the assumptions about future economic and demographic experience therein represent a reasonable estimate of future experience, but that actual experience will undoubtedly be different and may be significantly different. The Plan Actuary further notes while there are a number of factors that could lead to contributions becoming unaffordable, the Plan Actuary believes the primary risks for the Pension Plans are investment risk, interest rate risk, and assumption change risk as described below. The following discussion is only a summary of the risks identified by the Plan Actuary in the Federated 2019 Pension Plan Actuarial Report and the Police and Fire 2019 Pension Plan Actuarial Report. For a further discussion of such risks see the Federated 2019 Pension Plan Actuarial Report and the Police and Fire 2019 Pension Plan Actuarial Report .

Investment Risk. Investment risk is the potential for investment returns to be different than expected. Lower investment returns than anticipated will increase the UAL thereby resulting in higher contributions in the future unless other gains offset such losses. The potential volatility of future investment returns is determined by the allocation of assets and the affordability of the investment risk is determined by the amount of assets invested relative to the size of the City. Losses recognized as a result of actual investment returns below the discount rate have been a significant contributor to the growth of UAL of the Pension Plans.

Interest Rate Risk. Interest rate risk is the potential for interest rates to be different than expected. For public plans like the Pension Plans, short-term fluctuations in interest rates have little or no effect as the plan's liability is usually measured based on the expected return on assets. Longer-term trends in interest rates, however, can have a powerful effect. As interest rates have declined, pension plans have faced the choice of maintaining the same level of risk and reduce the expected rate of return or maintain the same expected rate of return and take on additional investment risk or some combination of the two.

Assumption Change Risk. Assumption change risk is the potential for the environment to change such that future valuation assumptions are different than the current assumptions. Assumption rate risk is an extension of the other risks described above, but rather than capturing the risk as it is experienced, it captures the cost of the recognizing a change in the environment when the current assumption is no longer reasonable. Since 2010, there have been substantial changes in actuarial assumptions with respect to the Pension Plans that have caused the UAL of the Pension Plans to increase. Most of the changes are due to the reduction in the discount rate from 7.95% to 6.75% for the Federated Pension Plan and from 7.75% to 6.75% for the Police and Fire Pension Plan.

In addition, in the Federated 2019 Pension Plan Actuarial Report and the Police and Fire 2019 Pension Plan Actuarial Report, the Plan Actuary also noted that the future financial condition of a mature plan is more sensitive to each of the risks described above when compared to less mature plans. The Plan Actuary identified the support ratio and leverage ratios as two measures of the maturity of a plan, as follows:

Support Ratio. The support ratio is the ratio of number of inactive members (those receiving benefits or entitled to a deferred benefit) to the number of active employees. The Plan Actuary notes the support ratio of the Pension Plans has increased dramatically from approximately 0.50 in 2001 (in the 25th to 50th percentile of support

ratios for plans in the Public Plans Database) to approximately 1.60 in 2019 (in 75th to 95th percentile of support ratios for plans in the Public Plans Database).

Leverage Ratios. Leverage or volatility ratios measure the size of the plan compared to its revenue base more directly. Such ratios include the asset leverage ratio and actuarial liability ratio. The Plan Actuary notes that the leverage ratios for the Federated Pension Plan are higher than most plans and are significantly higher when combined with the Police and Fire Pension Plan, indicating that the Pension Plans are much more sensitive to risk than most plans.

Historical and Projected Contributions. 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 historical 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 losses recognized as a result of actual investment returns below the discount rate and assumption changes.

**Table B-3a
Federated and Police and Fire Retirement Plans
Pension and Healthcare Contributions**

Fiscal Year Ended June 30	Federated Plan	Police and Fire Plan	Total
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	121,042,000	245,402,000
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
2019	199,416,000	205,362,000	404,778,000

Source: City of San José Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2019; Office of Retirement Services.

In January 2020, 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, 2019 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 reality, actual experience will deviate from the assumptions. 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 the Retirement Plans for fiscal years 2020-2021 through 2024-2025 are shown in Table B-3b and Table B-3c. In such projections, with respect to the Police and Fire Healthcare Plan, the City contribution rate is not projected to exceed the City's optional contribution limit of 11.0%. 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. The information presented in this Appendix B does not take into account any impacts of COVID-19 on the Retirement Plans. In particular, the projections contained herein on future City contributions do not reflect the impact of the COVID-19 pandemic on the Retirement Plans, including likely impacts on investment returns, health care costs, salaries, employment levels, or other factors that may affect the valuation and future City contributions. The City expects its unfunded accrued liability and actuarially determined required contributions to the Retirement Plans to increase in the future as result. The City cannot at this time project the magnitude or timing of such increases. See "INTRODUCTION TO APPENDIX B – COVID-19."

Table B-3b
Federated Plan
Projected City Contributions – Pension and Healthcare
(in millions)

Fiscal Year Ended June 30	Federated Payroll	Pension Contribution	Pension Rate	Healthcare Contribution	Healthcare Rate	Total Contribution	Total Rate
2021	\$ 322.7	\$ 190.9	59.16%	\$ 21.0	6.49%	\$ 211.9	65.66%
2022	332.4	198.7	59.78	20.2	6.08	218.9	65.85
2023	342.4	204.1	59.63	19.4	5.66	223.5	65.29
2024	352.6	210.0	59.55	19.6	5.56	229.6	65.11
2025	363.2	215.7	59.38	19.8	5.46	235.5	64.83

Source: Cheiron 5-Year Budget Projections for Federated Plan, January 15, 2020.

Table B-3c
Police and Fire Plan
Projected City Contributions – Pension and Healthcare
(in millions)

Fiscal Year Ended June 30	Police and Fire Payroll	Pension Contribution	Pension Rate	Healthcare Contribution	Healthcare Rate	Total Contribution	Total Rate
2021	\$ 243.5	\$ 205.9	84.59%	\$ 25.4	10.42%	\$ 231.3	95.01%
2022	251.3	215.7	85.82	26.6	10.59	242.3	96.41
2023	259.6	206.9	79.72	27.5	10.58	234.4	90.30
2024	268.0	212.7	79.39	28.7	10.70	241.4	90.09
2025	276.7	213.8	77.28	29.8	10.77	243.6	88.05

Source: Cheiron 5-Year Budget Projections for Police and Fire Pension and Healthcare Plans, January 29, 2020.

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 the Pension Plans and the Healthcare Plans, please see "PENSION PLAN – Pension Plans' Actuarial Valuations" and "HEALTHCARE PLANS – Healthcare Plans' Actuarial Valuations and Funding Status," respectively. In addition, for the Healthcare Plans, the Plan Actuary's projections include changes to the healthcare plans offered to active employees as described in "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. 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, 2019," Notes to Basic Financial Statements, Section IV Other Information, and Title 3 of the Municipal Code.

As more fully described in "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, 2019, are described in Table B-4a and Table B-4b.

Table B-4a
Federated Plan Service Pension Formulas

	Normal Retirement Age	Minimum Vesting Service⁽¹⁾	Pension Allowance	Final Compensation
Tier 1	<ul style="list-style-type: none"> • 55 with 5 years service • 30 years service at any age 	5 years of service	<ul style="list-style-type: none"> • $2.5\% \times \text{years of service} \times \text{final compensation}$ (75% max) 	Average monthly base pay in highest one year compensation ⁽²⁾
Tier 2	<ul style="list-style-type: none"> • 62 with 5 years of Federated Plan covered service • 55 with 5 years of Federated Plan covered service with reduction by a factor of 5% per year prior to age 62 prorated to closest month 	5 years of Federated Plan covered City service	<ul style="list-style-type: none"> • $2.0\% \times \text{years of service} \times \text{final compensation}$ (70% max) 	Average monthly (or biweekly) base pay in highest consecutive three year compensation ⁽³⁾

⁽¹⁾ Terminated employees with less than minimum vesting service who are not employed by a reciprocal agency must withdraw all contributions from the plan.

⁽²⁾ For separations that take place prior to July 1, 2001, final compensation is the highest average monthly base pay in highest consecutive three year compensation.

⁽³⁾ Excludes premium pay or additional compensation.

Source: Federated 2019 CAFR.

Table B-4b
Police and Fire Plan Service Pension Formulas

	Normal Retirement Age	Minimum Vesting Service⁽¹⁾	Pension Allowance	Final Compensation
Police Tier 1	<ul style="list-style-type: none"> • 50 with 25 years service • 55 with 20 years service • 30 years service at any age (with reciprocity must be 50 years of age) • Mandatory retirement at 70 years of age 	10 years of service	<ul style="list-style-type: none"> • First 20 years of Service: 50% of final compensation (2.5% per year) • 21-30 years service: 4% per year of service x final compensation (90% max) 	Highest one year average compensation
Fire Tier 1	<ul style="list-style-type: none"> • 50 with 25 years service • 55 with 20 years service • 30 years service at any age (with reciprocity must be 50 years of age) • Mandatory retirement at 70 years of age 	10 years of service	<ul style="list-style-type: none"> • First 20 years of service: 50% of final compensation (2.5% per year) • Beginning 21st year of service: 3% x years of service x final compensation (90% max). • All years convert to 3% after 20 years 	Highest one year average compensation
Police and Fire Tier 2	<ul style="list-style-type: none"> • 57 with 5 years of Police and Fire Department Plan covered service • 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 prorated to closest month 	5 years of Police and Fire Department Plan covered service	<ul style="list-style-type: none"> • First 20 years of service: 2.4% per year of service x final compensation. • Beginning of 21st year: 3.0% per year of service x final compensation. • Beginning of 26th year: 3.4% per year of service x final compensation. • Maximum benefit is 80% of final compensation 	Average annual base pay plus any premium pays authorized by ordinance for the highest 3 consecutive years of service

⁽¹⁾ 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 2019 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 Assets of each Pension Plan and the applicable Actuarial Value of Assets for purposes of comparison. Table B-5a separately compares the Market Value of Assets and Actuarial Value of Assets 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 of the Pension Plans is less than their respective Actuarial Value, 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.

Table B-5a Pension Assets & Liabilities <i>(in millions)</i>			
	June 30, 2018	June 30, 2019	% Change
Federated Pension Plan			
Total Actuarial Liability	\$ 4,101	\$ 4,201	2.4%
Market Value Assets	2,069	2,132	3.0
Actuarial Value Assets	2,179	2,229	2.3
Unfunded Actuarial Liability ⁽¹⁾	2,031	2,069	1.8
Unfunded Actuarial Liability ⁽²⁾	1,921	1,972	2.6
Funded Ratio – Market Value	50.5%	50.8%	0.6
Funded Ratio – Actuarial Value	53.1%	53.1%	--
Police and Fire Pension Plan			
Total Actuarial Liability	\$ 4,696	\$ 4,988	6.2%
Market Value Assets	3,496	3,588	2.6
Actuarial Value Assets	3,597	3,706	3.1
Unfunded Actuarial Liability ⁽¹⁾	1,200	1,400	16.6
Unfunded Actuarial Liability ⁽²⁾	1,100	1,282	16.6
Funded Ratio – Market Value	74.4%	71.9%	(2.5)
Funded Ratio – Actuarial Value	76.6%	74.3%	(2.3)

⁽¹⁾ UAL amount based on Market Value of Assets.

⁽²⁾ UAL amount based on Actuarial Value of Assets.

Source: Federated 2019 Pension Plan Actuarial Report; Police and Fire 2019 Pension Plan Actuarial Report.

Table B-5b
Federated Pension Plan -
Market and Actuarial Value of Pension Assets
(in thousands)

	June 30, 2018	June 30, 2019
Market Value, Beginning of Year	\$ 1,972,792	\$ 2,069,333
Contributions		
Member	20,501	22,606
City	156,770	173,006
Total	\$ 177,271	195,612
Net Investment Earnings ⁽¹⁾	117,493	76,855
Benefit Payments	(193,400)	(205,066)
Administrative Expenses	(4,823)	(4,582)
Market Value, End of Year	\$ 2,069,333	\$ 2,132,152
Actuarial Value of Assets	\$ 2,179,488	\$ 2,228,802

⁽¹⁾ Gross investment earnings less investment expenses.

Source: Federated 2019 CAFR for Market Value of Assets; Federated 2019 Pension Plan Actuarial Report for Actuarial Value of Assets.

Table B-5c
Police and Fire Pension Plan -
Market and Actuarial Value of Pension Assets
(in thousands)

	June 30, 2018	June 30, 2019
Market Value, Beginning of Year	\$ 3,293,257	\$ 3,496,191
Contributions		
Member	23,841	24,811
City	157,712	176,618
Total	\$ 181,553	\$ 201,429
Net Investment Earnings ⁽¹⁾	233,474	114,179
Benefit Payments	(206,630)	(218,008)
Administrative Expenses	(5,464)	(5,369)
Market Value, End of Year	\$ 3,496,190	\$ 3,588,422
Actuarial Value of Assets	\$ 3,596,590	\$ 3,706,302

⁽¹⁾ Gross investment earnings less investment expenses.

Source: Police and Fire 2019 CAFR for Market Value of Assets; Police and Fire 2019 Pension Plan Actuarial Report for Actuarial Value of Assets.

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 are summarized in "HEALTHCARE PLANS." The schedules of the funding progress for both Pension Plans are set forth in the Federated 2019 Pension Plan Actuarial Report and the Police and Fire 2019 Pension Plan Actuarial Report, representing the current data available for the funding progress for both Pension Plans as shown in Tables B-6a and B-6b.

Table B-6a and Table B-6b 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 10 years, both Pension Plans have experienced significant increases in the UAL, primarily attributable to the recognition of prior unfavorable investment returns (resulting in an increase in the UAL for the Federated Pension Plan and the Police and Fire Pension Plan of approximately \$631 million and \$756 million, respectively) and actuarial assumption changes primarily relating to the reduction in the discount rate (resulting in an increase in the UAL for the Federated Pension Plan and the Police and Fire Pension Plan of approximately \$583 million and \$541 million, respectively). The Federated Pension Plan's actual investment returns on the Actuarial Value of Assets have only exceeded the expected investment return in one of the 10 most recent fiscal years. The Police and Fire Pension Plan's actual investment returns on the Actuarial Value of Assets have only exceeded the expected investment return in two of the 10 most recent fiscal years. During that period, the respective UAL of the Federated Pension Plan and the Police and Fire Pension Plan increased in each fiscal year for a total increase of approximately \$1.2 billion and \$0.63 billion, respectively. The Federated Pension Plan and the Police and Fire Pension Plan had a positive investment return on their respective Market Value of Assets in 5 of the last 10 years and 6 of the last 10 years, respectively.

In addition, according to the Plan Actuary, actual contributions to the Federated Pension Plan have been less than the Normal Cost plus interest on the UAL in 9 of the 10 most recent fiscal years resulting in an increase of approximately \$151 million in the UAL of the Federated Pension Plan. Such increases in the UALs of the Pension Plans were offset by gains on other assumptions (resulting in a reduction in the UAL for the Federated Pension Plan and the Police and Fire Pension Plan of approximately \$95 million and \$289 million, respectively) and, with respect to the Police and Fire Pension Plan, contributions above the Normal Cost plus interest in the UAL (resulting in a reduction in the UAL for the Police and Fire Pension Plan of approximately \$125 million).

See "PENSION PLANS – Pension Plans' Actuarial Valuations," the Federated 2019 Pension Plan Actuarial Report, and the Police and Fire 2019 Pension Plan Actuarial Report for a description of the impact of assumption, investment, and demographic changes on the Federated Pension Plan and Police and Fire Pension Plan valuations for the years covered in Tables B-6a and B-6b.

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 629% of total covered annual payroll as of the June 30, 2019 valuation date of the Federated 2019 Pension Plan Actuarial Report. This means it would require contributing more than six times the 2019-covered payroll to fund all of the Federated Pension Plan's Unfunded Actuarial Liability. In fiscal year 2018-2019, the Federated Pension Plan contribution exceeded the amount necessary to keep the UAL amount level. The Plan Actuary anticipates the

Federated Pension Plan contribution to be above such level, gradually paying down the UAL in the future if all assumptions are met.

Table B-6a
Federated Pension Plan - Schedule of Pension Funding Progress
(in thousands)

Valuation Date (June 30)	Actuarial Value of Assets	Actuarial Liability	UAL	Funded Ratio⁽¹⁾	Covered Payroll	UAL as % of Covered Payroll⁽¹⁾
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
2019	2,228,802	4,200,708	1,971,906	53	313,310	629

⁽¹⁾ Rounded to the nearest whole percent.

Source: Federated 2019 Pension Plan Actuarial Report.

As below, the UAL for the Police and Fire Pension Plan was 544% of total covered annual payroll in fiscal year 2018-2019. This means that it would require contributing almost five and one half times the 2019-covered payroll to fund all of the Police and Fire Pension Plan's Actuarial Liability.

Table B-6b
Police and Fire Pension Plan - Schedule of Pension Funding Progress
(in thousands)

Valuation Date (June 30)	Actuarial Value of Assets	Actuarial Liability	UAL	Funded Ratio⁽¹⁾	Covered Payroll	UAL as % of Covered Payroll⁽¹⁾
2010	\$ 2,576,705	\$ 3,230,456	\$ 653,751	80%	\$ 251,058	260%
2011	2,685,721	3,196,007	510,286	84	190,726	268
2012	2,703,539	3,397,792	694,253	80	187,959	369
2013	2,771,924	3,578,031	806,107	78	184,645	437
2014	3,025,101	3,813,825	788,724	79	188,189	419
2015	3,212,776	4,058,410	845,634	79	184,733	458
2016	3,303,550	4,355,990	1,052,440	76	194,072	542
2017	3,439,922	4,464,402	1,024,480	77	203,816	503
2018	3,596,590	4,696,428	1,099,838	77	218,429	504
2019	3,706,302	4,988,427	1,282,125	74	235,818	544

⁽¹⁾ Rounded to the nearest whole percent.

Source: Police and Fire 2019 Pension Plan Actuarial Report.

Funding Progress - Net Pension Liability

GASB Statement No. 68 requires the 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." For purposes of its financial statements, the City calculates the Net Pension Liability of the Pension Plans using a measurement date that is one fiscal year prior to the Net Pension Liability measurement date used for the Retirement 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, 2018 and the June 30, 2019 measurement dates. The Total Pension Liability for the Pension Plans as of June 30, 2018 and June 30, 2019 shown in Table B-7 is based on results of an actuarial valuation date of June 30, 2017 and June 30, 2018, respectively, and rolled-forward to June 30, 2018 and 2019 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.

Table B-7 Components of Net Pension Liability <i>(in thousands)</i>			
	June 30, 2018	June 30, 2019	% Change
Federated Pension Plan			
Total pension liability	\$ 4,057,348	\$ 4,229,613	4.3%
Plan fiduciary net position	2,069,333	2,132,152	3.0
Net pension liability	\$ 1,988,015	\$ 2,097,461	5.5
Plan fiduciary net position as a percentage of the total pension liability	51.0%	50.4%	(0.6)
Police and Fire Pension Plan			
Total pension liability	\$ 4,635,937	\$ 4,872,791	5.1
Plan fiduciary net position	3,496,191	3,588,422	2.6
Net pension liability	\$ 1,139,746	\$ 1,284,369	12.7
Plan fiduciary net position as a percentage of the total pension liability	75.4%	73.6%	(1.8)
<i>Source: Federated 2019 CAFR; Police and Fire 2019 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 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 2019, the Federated Board adopted certain economic and demographic changes based on an experience study covering a period from 2015 to 2019 performed by the Plan Actuary. The Plan Actuary determined that the assumption changes in 2019 decreased the UAL of the Federated Plan by \$2.9 million or 0.1% of the Actuarial Liability. The Police and Fire Board also adopted economic and demographic changes recommended by the Plan Actuary based on an experience study covering plan experience through June 30, 2019. Amortization changes to the Police and Fire Pension Plan were also made to smooth future City contributions to such plan. The Plan Actuary determined that the assumption changes in 2019 caused an increase in the UAL of the Police and Fire Pension Plan of \$80.9 million or 1.6% of Actuarial Liability.

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. Both the Federated Board and the Police and Fire Board continued to use a discount rate of 6.750% for the June 30, 2019 valuation. The Boards for the Pension Plans have incrementally reduced their respective assumed rates of return in the previous ten years from 7.95% and 7.75% beginning July 1, 2010 for the Federated Pension Plan and the Police and Fire Pension Plan, respectively. Table B-8 shows the historical discount rates for the Pension Plans from the June 30, 2010 valuation through the June 30, 2019 valuation.

Table B-8
Historical Discount Rates

Federated Pension Plan									
2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
7.95%	7.50%	7.50%	7.25%	7.00%	7.00%	6.875%	6.875%	6.750%	6.750%
Police and Fire Pension Plan									
2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
7.75%	7.50%	7.25%	7.125%	7.00%	7.00%	6.875%	6.875%	6.750%	6.750%

Source: Federated 2019 Pension Plan Actuarial Report; Police and Fire 2019 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. Tier 1 assumption changes are amortized over 25-year periods beginning with the valuation date in which they first arise. For members who were reclassified under Measure F from Tier 2 to Tier 1, a portion of the increase in liability for the reclassification is to be paid by members. Rehired members who were reclassified pay an additional contribution rate of 3.0 percent of payroll until the amount they owe has been paid off. All Classic members pay an additional contribution rate based on a 20-year amortization of the increase in liability for Classic members who were reclassified from Tier 2 to Tier 1 under Measure F.

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 for the Federated Pension Plan are scheduled to increase 2.75% each year while aggregate payroll is expected to grow 3.00% each year. As a result, contributions to the Federated Pension Plan are expected to become a slightly smaller percentage of combined Tier 1 and Tier 2 payroll each year.

With respect to the Police and Fire Pension Plan, actuarial gains and losses and plan changes are amortized 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 over a 20-year period (16 years for changes prior to June 30, 2011) beginning with the valuation date on which they are effective. Effective June 30, 2019, the remaining amortization periods for several components of the City's Tier 1 UAL amortization were adjusted to smooth the pattern of amortization payments. Effective June 30, 2019, all prior assumption amortization base periods were increased by four years so they have the same remaining period as if they had originally been amortized over 20 years. Amortization payments for the Police and Fire Pension Plan are now scheduled to increase 2.50% each year, a decrease from the prior rate of 3.25%, while aggregate payroll is expected to grow 3.25% each year. Tables B-9 and B-10 summarize actuarial assumptions including future rates of return used by both Pension Plans for the 2019 valuations.

Table B-9
Federated Pension Plan – Pension Actuarial Assumptions

Valuation Date	June 30, 2019
Actuarial funding method	Entry Age Normal
Amortization method	Level percent of pay, closed, layered
Amortization payment growth rate	2.75% compounded annually
Asset valuation method	5-year smoothing of return
Actuarial Assumptions:	
Discount Rate	6.75%
Wage inflation ⁽¹⁾	3.00% compounded annually
Cost-of-Living Adjustments ⁽²⁾	Tier 1-3.0% per year; Tier 2-1.25% - 2.0% per year depending on years of service

⁽¹⁾ Additional merit salary increases of 0.10% to 3.75% based on a participant's years of service are also assumed.

⁽²⁾ 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 2019 Pension Plan Actuarial Report.

Table B-10
Police and Fire Pension Plan – Pension Actuarial Assumptions

Valuation Date	June 30, 2019
Actuarial funding method	Entry Age Normal
Amortization method	Level percent of pay, closed, layered
Amortization payment growth rate	2.50% compounded annually
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 ⁽¹⁾	3.25% compounded annually
Cost-of-Living Adjustments ⁽²⁾	Tier 1-3.0% per year; Tier 2-2.0% per year

⁽¹⁾ Additional merit salary increases of 0.5% to 6.5% based on a participant's years of service are also assumed.

⁽²⁾ 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 2019 Pension Plan Actuarial Report.

Federated Pension Plan 2019 Valuation Summary. The most recent actuarial valuation of the Federated Pension Plan was performed by the Plan Actuary and summarized in the Federated 2019 Pension Plan Actuarial Report. 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 (6.750% for fiscal year 2018-2019, 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 2019 Pension Plan Actuarial Report, the Plan Actuary concluded that as of June 30, 2019:

- The Funded Ratio based on the Actuarial Value of Assets for the Federated Pension Plan was 53.1%, unchanged from 53.1% as of June 30, 2018.
- The Funded Ratio based on the Market Value of Assets for the Federated Pension Plan was 50.8% compared to 50.5% as of June 30, 2018.
- The UAL using the Actuarial Value of Assets for the Federated Pension Plan was approximately \$1.972 billion as compared to a UAL using the Actuarial Value of Assets of approximately \$1.921 billion as of June 30, 2018. The UAL using the Market Value of Assets for the Federated Pension Plan increased from \$2.031 billion as of June 30, 2018 to \$2.069 billion.
- The Actuarial Value of Assets for the Federated Pension Plan was approximately \$2.229 billion and the Actuarial Liability for the Federated Pension Plan was approximately \$4.201 billion. The Federated Pension Plan's Total Actuarial Liability increased by 2.4% and the Market Value of Assets increased by 3.0% when compared to the June 30, 2018 valuation.
- The UAL using the Actuarial Value of Assets for the Federated Pension Plan increased approximately \$51 million since the June 30, 2018 valuation. Such increase was due to losses recognized as a result of actual investment returns below the discount rate and plan liability experience, including member salary increases exceeding assumptions. These increases were only partially offset by decreases from assumption changes, contributions in excess of normal cost plus interest on the UAL, and aggregate plan liability experience, including data corrections reducing the number of beneficiaries. See "– Actuarial Funding Progress" above and Table B-5a.
- Actual investment returns on the Actuarial Value of Assets for the Federated Pension Plan have only exceeded the expected investment return in one of the 10 most recent fiscal years. During that period, the UAL for the Federated Pension Plan increased in each fiscal year for a total increase of approximately \$1.2 billion. However, the Federated Pension Plan had investment returns on the Market Value of Assets that exceeded the expected investment return in 5 of the last 10 years.

Police and Fire Pension Plan 2019 Valuation Summary. The most recent actuarial valuation of the Police and Fire Pension Plan, was performed by the Plan Actuary and is

summarized in the Police and Fire 2019 Pension Plan Actuarial Report. 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 (6.750% for fiscal year 2018-2019, 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 2019 Pension Plan Actuarial Report, the Plan Actuary concluded that as of June 30, 2019:

- The Funded Ratio based on the Actuarial Value of Assets for the Police and Fire Pension Plan was 74.3%, down from 76.6% as of June 30, 2018.
- The Funded Ratio based on the Market Value of Assets for the Police and Fire Pension Plan was 71.9%, down from 74.4% as of June 30, 2018.
- The UAL using the Actuarial Value of Assets for the Police and Fire Pension Plan was approximately \$1.282 billion as compared to the UAL using the Actuarial Value of Assets of approximately \$1.100 billion as of June 30, 2018.
- The Actuarial Value of Assets for the Police and Fire Pension Plan was approximately \$3.706 billion and the Actuarial Liabilities for the Police and Fire Pension Plan were approximately \$4.988 billion. For the Police and Fire Pension Plan, the Total Actuarial Liability increased by 6.2% and the actuarial value of assets increased by 3.1% compared to the prior valuation.
- The UAL using the Actuarial Value of Assets for the Police and Fire Pension Plan increased approximately \$182 million since the June 30, 2018 valuation. Such increase was due to losses recognized as a result of actual investment returns below the discount rate, assumption changes, and plan liability experience, including member salary increases exceeding assumptions. These increases were partially offset by decreases attributable to contributions in excess of aggregate Normal Cost and interest accruing on the prior UAL. See “– Actuarial Funding Progress” above and Table B-5a.
- Actual investment returns on the Actuarial Value of Assets for the Police and Fire Pension Plan have only exceeded the expected investment return in two of the 10 most recent fiscal years. During that period, the UAL increased a total of approximately \$0.63 billion. However, the Police and Fire Pension Plan had investment returns on the Market Value of Assets that exceeded the expected investment return in 6 of the last 10 years.

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, such rates and amounts become the legally required contribution rates and amounts of the City and employees 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 Pension Plans employ a “floor funding method” for setting the City’s funding policy contribution amount for Tier 1 for the Normal Cost portion (which includes administrative expenses). Under such method, beginning in fiscal year 2016-2017, the City’s Normal Cost 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 UAL portion of the City’s contribution is set at the dollar amount recommended by the Plan Actuary and adopted by the Board in the annual actuarial valuation.

The Pension Plans do not employ a “floor funding method” for determining the City’s contribution for Tier 2 members. 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. Similarly, 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.”

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. 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. The amount of the prefunded annual contribution is the actuarial equivalent of contributions made regularly over the course of a year as established by each Board. To the extent contributions are made after the beginning of the fiscal year, the amounts are adjusted for interest. To determine the City’s “prefunded” annual contribution amount, the Boards, based on the advice of the Plan Actuary and outside investment consultants, each set an interest discount rate to be applied by the Plan Actuary to the required contributions to account for the fact that contributions are made and invested at the beginning of the year instead of made throughout the year and invested thereafter by the Pension Plans. The Boards have each implemented an “incremental reduction approach” to set the interest discount rate in a given year. The approach applies the Pension Plan’s discount rate for the year of the contribution reduced incrementally based on certain broad economic and market benchmarks. The incremental reduction approach is intended to incentivize the City to prefund contributions to the Pension Plans when market valuations may be lower and an economic cycle may be in early stages of expansion and disincentivize for prefunding contributions when market valuations and/or economic expansions may exceed historic patterns.

The City prefunded its contributions for Tier 1 employees under the Pension Plans for fiscal year 2020-2021 with funds on hand and proceeds of tax and revenue anticipation notes in the aggregate principal amount of \$130,000,000 issued in July 2020. See “BONDED AND OTHER INDEBTEDNESS” in Appendix A for a description of such notes. The Boards used the

respective Pension Plan's interest discount rate, 6.75% for the Federated Plan and 6.75% for the Police and Fire Plan, without reduction to calculate the City's prefunding contribution for fiscal year 2020-2021. The projected contributions set forth in this Appendix B do not take into account the prefunding of the City's contributions for fiscal year 2020-2021 or any future fiscal years.

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 2013-2014 to fiscal year 2018-2019.

Table B-11
Schedule of City Pension Plan Contributions
(in thousands)

	2013- 2014⁽¹⁾	2014- 2015	2015- 2016⁽¹⁾	2016- 2017	2017- 2018	2018- 2019
Federated Pension Plan						
Actuarially Determined Contribution	\$102,811	\$ 114,751	\$ 129,456	\$ 138,483	\$ 156,770	\$ 173,006
Actual Contribution	<u>107,544</u>	<u>114,751</u>	<u>124,723</u>	<u>138,483</u>	<u>156,770</u>	<u>173,006</u>
Contribution Deficiency (excess)	(\$ 4,733)	\$ 0	\$ 4,733	\$ 0	\$ 0	\$ 0
 Police and Fire Pension Plan						
	\$					
Actuarially Determined Contribution	123,583	\$ 129,279	\$ 132,480	\$ 136,957	\$ 157,712	\$ 176,618
Actual Contribution	<u>123,583</u>	<u>129,279</u>	<u>132,480</u>	<u>136,957</u>	<u>157,712</u>	<u>176,618</u>
Contribution Deficiency (excess)	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0

⁽¹⁾ 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, 2019.

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.

The information presented in this Appendix B does not take into account any impacts of COVID-19 on the Retirement Plans. In particular, the projections contained herein on future City contributions do not reflect the impact of the COVID-19 pandemic on the Retirement Plans, including likely impacts on investment returns, health care costs, salaries, employment levels, or other factors that may affect the valuation and future City contributions. The City expects its unfunded accrued liability and actuarially determined required contributions to the Retirement Plans to increase in the future as result. The City cannot at this time project the magnitude or timing of such increases. See "INTRODUCTION TO APPENDIX B – COVID-19."

Table B-12
20-Year Projections of Pension Contributions
(in thousands)
(middle of the year)

Fiscal Year Ended June 30	Federated Pension Plan		Police and Fire Pension Plan	
	Projected City Contribution Amount	Projected Total Contribution Rate (% of Payroll)	Projected City Contribution Amount	Projected Total Contribution Rate (% of Payroll)
2021	\$ 190,926	59.16%	\$ 205,963	84.6%
2022	198,694	59.78	215,744	85.8
2023	204,148	59.63	206,923	79.7
2024	210,000	59.55	212,762	79.4
2025	215,663	59.38	213,835	77.3
2026	220,443	58.92	217,686	76.2
2027	225,427	58.50	221,585	75.1
2028	230,640	58.11	223,651	73.4
2029	235,429	57.59	225,050	71.6
2030	241,075	57.25	215,347	66.3
2031	246,932	56.94	193,121	57.6
2032	245,994	55.07	185,610	53.6
2033	252,460	54.87	168,878	47.3
2034	248,834	52.51	141,693	38.4
2035	245,343	50.26	134,761	35.4
2036	255,136	50.75	109,971	28.0
2037	262,628	50.71	90,560	22.3
2038	231,150	43.34	81,053	19.3
2039	228,358	41.57	96,063	22.2
2040	219,824	38.85	84,644	18.9

Source: Cheiron 5-Year Budget Projections for Federated Plan, January 15, 2020; Cheiron 5-Year Budget Projections for Police and Fire Pension Plan, January 29, 2020.

For the Federated Pension Plan, the 20-year projections show contribution rates increasing for the next few years due to recognition of recent losses recognized as result of investment returns below the discount rate. Thereafter, the City's contribution rate is projected to gradually decrease until 2036. The gradual decrease in the City contribution rate is driven by the gradual decrease in the Normal Cost rate as Tier 2 becomes a greater proportion of the active membership and the gradual decrease in the UAL rate as payroll is expected to grow slightly faster than amortization payments. The Plan Actuary indicated in the Federated 2019 Pension Plan Actuarial Report that, if all assumptions are met, the Federated Pension Plan will reach a funded status of 82% by 2034.

For the Police and Fire Pension Plan, the 20-year projections show contribution rates declining substantially from 85.8% of total projected payroll in 2022 to 18.9% of total projected payroll in 2040 as the UAL is paid off. Due to the volatility in projected contributions under amortization policy previously in place, the Police and Fire Board in 2019 adjusted some amortization periods and reduced the amortization payment increase rate from 3.25% to 2.50%. The Plan Actuary indicated in the Police and Fire 2019 Pension Plan Actuarial Report that, if all assumptions are met, the Police and Fire Pension Plan will reach a funded status of 99% by 2035. In the Federated 2019 Pension Plan Actuarial Report and the Police and Fire 2019 Pension Plan Actuarial Report, the Plan Actuary notes that there may be significant volatility in future City contribution rates to the Pension Plans due to investment return volatility, resulting

from the plan asset to payroll ratio and the standard deviation of the current investment portfolio. See “– Summary of Retirement Plans Historical and Projected Contributions – *Plan Risks*” above for a summary of the such risks.

It is certain that not all assumptions will be exactly met each and every year. The Plan Actuary indicated in the Federated 2019 Pension Plan Actuarial Report and the Police and Fire 2019 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. See “– Summary of Retirement Plans Historical and Projected Contributions – *Plan Risks*.”

The next two sections provide, for both Pension Plans, information on the contribution rates and dollar amounts for fiscal year 2019-2020 and the contribution rates and dollar amounts for fiscal year 2020-2021. As previously mentioned, the projected contributions set forth in this Appendix B do not take into account the prefunding of the City’s contributions for fiscal year 2020-2021 or any future fiscal years.

Federated Plan Pension Contribution. The member contribution rate for Tier 1 of the Federated Pension Plan 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 (i.e., 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. The Federated Board set a contribution rate of 3.0% of pay that applies to each such individual member until such member has paid off their individual UAL amount for reclassification. 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 member and City contribution rates each cannot be less than 50% of the Normal Cost rate. The Plan Actuary has stated that the most significant portion of the City’s contribution is the Tier 1 UAL payment which is substantially attributable to members who no longer work for the City.

Table B-13a below summarizes the pension contribution rates for employee members of the Federated Plan for fiscal year 2019-2020, as adopted by the Federated Board, and fiscal year 2020-2021 as determined by the Plan Actuary and set forth in the Federated 2019 Pension Plan Actuarial Report. 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). For fiscal year 2020-2021, the Plan Actuary projected payroll to total \$142.1 million for Tier 1 and \$180.6 million for Tier 2.

Table B-13a
Federated Pension Plan Member Contribution Rates

	2019-2020			2020-2021		
	<u>Basic</u>	<u>COLA</u>	<u>Total</u>	<u>Basic</u>	<u>COLA</u>	<u>Total</u>
<u>Tier 1</u>						
Total Member Normal Cost/Admin Rate ⁽¹⁾	5.08%	1.98%	7.06%	5.15%	2.07%	7.22%
<u>Tier 2</u>						
Member Normal Cost/Admin Rate	6.92%	1.14%	8.06%	6.60%	1.08%	7.68%
Member UAL Rate	0.18	0.09	0.27	0.15	0.09	0.24
Total Member Rate	7.10%	1.23%	8.33%	6.75%	1.17%	7.92%

⁽¹⁾ Excludes additional reclassified rate (UAL) for Classic and Reclassified Tier 1 Members

Source: 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; Resolution No. 9094 of the Federated Board, approved by the Federated Board on May 21, 2020; Resolution No. 9095 of the Federated Board, approved by the Federated Board on May 21, 2020.

According to the Plan Actuary, the increase in the Tier 1 member contribution rate for fiscal year 2020-2021 shown in Table B-13a is primarily due to assumption changes. Table B-13b illustrates the City's contribution dollar amounts for the Federated Pension Plan for fiscal year 2019-2020, as adopted by the Federated Board, and fiscal year 2020-2021 as determined by the Plan Actuary and set forth in the Federated 2019 Pension Plan Actuarial Report. Because Tier 1 is closed, the payroll for Tier 1 is anticipated to decrease over time as members leave the system and thereby cause the City's contribution rate for Tier 1 members as a percentage of Tier 1 payroll to increase over time. The amounts set forth in Table B-13b assume 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)

	2019-2020			2020-2021		
	<u>Basic</u>	<u>COLA</u>	<u>Total</u>	<u>Basic</u>	<u>COLA</u>	<u>Total</u>
<u>Tier 1</u>						
City Normal Cost/Admin ⁽¹⁾	\$ 20,747	\$ 8,120	\$ 28,867	\$ 20,062	\$ 8,099	\$ 28,161
City UAL Cost ^{(2) (3)}	70,032	67,377	137,409	77,179	71,281	148,460
Total City Contribution	\$ 90,779	\$ 75,497	\$ 166,276	\$ 97,241	\$ 79,380	\$ 176,621
<u>Tier 2</u>						
City Normal Cost/Admin	\$ 11,034	\$ 1,817	\$ 12,851	\$ 11,922	\$ 1,951	\$ 13,873
City UAL Cost	287	144	431	271	163	434
Total City Contribution	\$ 11,321	\$ 1,961	\$ 13,282	\$ 12,193	\$ 2,114	\$ 14,307

⁽¹⁾ Includes the reciprocity rate for the prefunding of the liability for reciprocal benefits with certain other California public pension plans.

⁽²⁾ Includes the deficiency rate for the amortization of the funding deficiency.

⁽³⁾ Includes the golden handshake rate for the cost for funding additional benefits granted in the past to certain retiring employees.

Source: 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; Resolution No. 9094 of the Federated Board, approved by the Federated Board on May 21, 2020; Resolution No. 9095 of the Federated Board, approved by the Federated Board on May 21, 2020.

According to the Plan Actuary, the decrease in the City's Normal Cost Tier 1 contribution for fiscal year 2020-2021 shown in Table B-13b is due to the decline in Tier 1 active members offset by increases due to assumption changes. The increase in the City's UAL contribution for such fiscal year is primarily due to scheduled increases in UAL amortization payments and the current year's recognized investment loss. The increase in the City's total Tier 2 contribution for fiscal year 2020-2021 shown in Table 13b is primarily due to the growth in the Tier 2 population.

Police and Fire Plan Pension Contribution. The member contribution rate for Tier 1 of the Police and Fire Pension Plan is a proportion (3/11ths) of the Normal Cost (excluding reciprocity), plus the employee member's historical 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 Pension Plan, members and the City share the total contribution rate equally, except that increases in members' UAL contribution are limited to one-third of one percent of compensation each year.

Table B-14a and Table B-14b summarize the pension contribution rates for the members of the Police and Fire Pension Plan for fiscal year 2019-2020, as adopted by the Police and Fire Board, and fiscal year 2020-2021 as determined by the Plan Actuary and set forth in the Police and Fire 2019 Pension Plan Actuarial Report.

Table B-14a Police and Fire Pension Plan Tier 1 Member Pension Contribution Rates (% of Payroll)						
	2019-2020			2020-2021		
	<u>Basic</u>	<u>COLA</u>	<u>Total</u>	<u>Basic</u>	<u>COLA</u>	<u>Total</u>
<u>Fire Tier 1</u>						
Member Normal Cost/Admin Rate	7.88%	3.58%	11.46%	8.01%	3.71%	11.72%
Member UAL Rate ⁽¹⁾	--	--	--	--	--	--
Total Member Rate	7.88%	3.58%	11.46%	8.01%	3.71%	11.72%
<u>Police Tier 1</u>						
Member Normal Cost/Admin Rate	7.32%	3.30%	10.62%	7.35%	3.33%	10.68%
Member UAL Rate ⁽¹⁾	0.05	0.03	0.08	0.03	0.01	0.04
Total Member Rate	7.37%	3.33%	10.70%	7.38%	3.34%	10.72%

⁽¹⁾ Excludes additional reclassified rate (UAL) for Classic and Reclassified Tier 1 Members
Source: 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; Resolution No. 4816 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020; Resolution No. 4817 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020; Resolution No. 4818 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020; Resolution No. 4819 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020.

Table B-14b
Police and Fire Plan Tier 2 Member Pension Contribution Rates
(% of Payroll)

	2019-2020			2020-2021		
	<u>Basic</u>	<u>COLA</u>	<u>Total</u>	<u>Basic</u>	<u>COLA</u>	<u>Total</u>
<u>Fire Tier 2</u>						
Member Normal Cost/Admin Rate	12.11%	3.23%	15.34%	12.22%	3.32%	15.54%
Member UAL Rate	(0.01)	0.06	0.05	(0.06)	0.05	(0.01)
Total Member Rate	12.10%	3.29%	15.39%	12.16%	3.37%	15.53%
<u>Police Tier 2</u>						
Member Normal Cost/Admin Rate	11.13%	2.89%	14.02%	11.21%	2.94%	14.15%
Member UAL Rate	(0.03)	0.07	0.04	(0.04)	0.07	0.03
Total Member Rate	11.10%	2.96%	14.06%	11.17%	3.01%	14.18%

Source: 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; Resolution No. 4816 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020; Resolution No. 4817 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020; Resolution No. 4818 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020; Resolution No. 4819 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020.

Table B-14c below shows the estimated City's contributions in dollars for the Police and Fire Pension Plan for 2019-2020, as adopted by the Police and Fire Board, and fiscal year 2020-2021, as determined by the Plan Actuary and set forth in the Police and Fire 2019 Pension Plan Actuarial Report. The amounts set forth in Table B-14c below assume 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)

	2019-2020			2020-2021		
Police	Basic	COLA	Total	Basic	COLA	Total
<u>Tier 1</u>						
City Normal Cost/Admin	\$ 20,140	\$ 8,910	\$ 29,050	\$ 20,526	\$ 9,122	\$ 29,649
City UAL Cost	30,376	39,648	70,024	35,445	44,539	79,984
Total City Contribution	\$ 50,516	\$ 48,558	\$ 99,074	\$ 55,971	\$ 53,661	\$ 109,633
<u>Tier 2</u>						
City Normal Cost/Admin	\$ 4,869	\$ 1,264	\$ 6,133	\$ 6,545	\$ 1,716	\$ 8,261
City UAL Cost	(13)	31	18	(23)	41	18
Total City Contribution	\$ 4,856	\$ 1,295	\$ 6,151	\$ 6,522	\$ 1,757	\$ 8,279
Fire						
<u>Tier 1</u>						
City Normal Cost/Admin	\$ 16,146	\$ 7,291	\$ 23,437	\$ 16,164	\$ 7,470	\$ 23,634
City UAL Cost	23,917	31,114	55,031	27,219	33,995	61,214
Total City Contribution	\$ 40,063	\$ 38,405	\$ 78,468	\$ 43,383	\$ 41,465	\$ 84,848
<u>Tier 2</u>						
City Normal Cost/Admin	\$ 2,020	\$ 539	\$ 2,559	\$ 2,521	685	3,206
City UAL Cost	(2)	10	8	(12)	10	(2)
Total City Contribution	\$ 2,018	\$ 549	\$ 2,567	\$ 2,509	\$ 695	\$ 3,204

Source: 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; Resolution No. 4816 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020; Resolution No. 4817 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020; Resolution No. 4818 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020; Resolution No. 4819 of the Police and Fire Board, approved by the Police and Fire Board on June 4, 2020.

Tier 1 rates are projected to increase from 2019-2020 to 2020-2021, due to assumption changes, losses recognized as result of investment returns below the discount rate and plan liability experience only partially offset by amortization changes. Tier 2 rates are projected to increase slightly primarily due to assumption changes.

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 Plans, and defraying reasonable expenses of administering the Pension Plans. The Boards for both Retirement Plans have retained investment consultants to advise them.

Table B-15 below illustrates the historical 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 March 31, 2020.

Table B-15 Historical Investment Performance For Pension Plans (As of March 31, 2020)		
Measurement Period	Federated Pension Plan⁽¹⁾	Police and Fire Pension Plan⁽²⁾
Since Inception	6.1%	8.1%
10 Years	4.0	4.9
5 Years	1.9	2.9
3 Years	1.7	2.5
1 Year	(4.4)	(3.4)

⁽¹⁾ The returns for certain investments (fixed income, private debt and real assets) are gross of fees through June 2015 and net of fees thereafter.
⁽²⁾ Net of fees.
⁽³⁾ Measurement Period Beginning January 1994.
⁽⁴⁾ Measurement Period Beginning March 1971.
Source: Meketa Investment Group Federated Pension Plan Quarterly Review March 31, 2020; Meketa Investment Group Police and Fire Pension Plan Quarterly Review March 31, 2020.

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.

On March 18, 2020, and March 27, 2020, the Police and Fire Board and the Federated Board, respectively, updated their respective investment asset allocations to increase the allocation of growth assets. Such increases were made in an attempt to balance potential increased return expectations going forward with the investment risk tolerance of the City after assessing the impact of COVID-19 on Pension Plans' assets at such time, potential effects on the City, and fiscal and monetary stimulus. Subsequently, the Federated Board and the Police and Fire Board adopted revised investment policies, which included further updated target asset allocation targets on April 16, 2020 and May 7, 2020, respectively. Table B-16 illustrates such 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. The Pension Plans are currently in the process of transitioning the asset allocations to new asset allocation targets in Table B-16. Changes to the weights of illiquid asset classes may take several quarters to implement.

Table B-16
Target Asset Allocations for Pension Plans

Asset Class	Federated Target %	Police and Fire Target %
Growth	75	70
Public Equity	49	46
Private Markets	21	19
Private Equity	8	6
Venture/Growth Capital	4	4
Private Debt	3	3
Growth Real Estate	3	3
Private Real Assets	3	3
Emerging Markets Bonds	3	3
High Yield Bonds	2	2
Low Beta	8	8
Market Neutral Strategies	3	3
Bonds (Immunized Cash Flows)	5	5
Other	17	22
Core Real Estate	5	5
Long-Term Government Bonds	2	3
Investment Grade Bonds	8	12
TIPS	2	2
<i>10-Year Expected Return ⁽¹⁾</i>	<i>6.9</i>	<i>6.6</i>
<i>20-Year Expected Return⁽¹⁾</i>	<i>7.8</i>	<i>7.5</i>
<i>Standard Deviation ⁽¹⁾</i>	<i>13.6</i>	<i>12.7</i>

⁽¹⁾ Neither the City nor the Underwriters can provide any assurance that actual returns will not be less than those expected by the respective Board.

Source: Federated City Employees' Retirement System Investment Policy Statement, Approved by the Federated Board on April 16, 2020, and the Police and Fire Department Plan Investment Policy Statement, Approved by the Police and Fire Board on May 7, 2020.

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 16, 2020, and the Police and Fire Department Plan Investment Policy Statement, Approved by the Police and Fire Board on May 7, 2020, which may be respectively found at http://www.sjretirement.com/Uploads/Fed/200518_May%202020%20IPS%20Fed.pdf, and http://www.sjretirement.com/Uploads/PF/200518_May%202020%20IPS%20PoliceFire.pdf. None of the foregoing websites or webpages are incorporated into this Appendix B. They are referenced for informational purposes only. The City and the Underwriters make no representation whatsoever as to the accuracy or completeness of any of the information on such websites or webpages. See also the Police and Fire 2019 CAFR and the Federated 2019 CAFR.

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 “CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS,” the Healthcare Plans are closed to new members. Generally, members of the Retirement Plans that were hired before July 2013 and 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 in Fiscal Years 2017-2018 and 2018-2019:

Table B-17a Healthcare Plans VEBA Transfers (as of June 30, 2019)		
	Members	Transferred Amounts (in thousands)
Federated Healthcare Plan	240	\$ 13,516
Police and Fire Healthcare Plan ⁽¹⁾	273	7,897
Total	513	\$ 21,413

⁽¹⁾ Includes members who elected or who were required to participate in the Police and Fire VEBA and all associated employee contributions.
Source: Federated 2019 CAFR; Police and Fire 2019 CAFR; 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. Eligible employees who are rehired by the City during calendar years 2018 through 2022 may opt into the applicable VEBA if they were not employed during the initial opt-in period and transfer the retiree healthcare contributions from the applicable Healthcare Plan to their individual VEBA accounts. 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. 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. 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. See “RETIREMENT PLANS IN GENERAL – Implementation of Certain Accounting Changes Relating to Retirement Plans.”

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 when: (1) a separate account (i.e., a 401(h) account) is 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 Section 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. The 401(h) account for the Federated Healthcare Plan was depleted in fiscal year 2018-2019, leaving only the Federated 115 Trust in the Healthcare Plan. As a result, all Federated Healthcare Plan benefits are now paid from the Federated 115 Trust. Assets in each of the Section 115 Trusts are not available to satisfy liabilities of other Section 115 Trusts. Certain information this Appendix B relating to the Police 115 Trust and Fire 115 Trust of the Police and Fire and Healthcare Plan have been presented in the aggregate. However, the assets of the Police 115 Trust are not available to satisfy the obligations of the Fire 115 Trust, including the UAL thereof, and vice versa. Nor are the obligations of the Police 115 Trust the obligations of the Fire 115 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 Section 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 annual required contribution for the retiree health and dental benefits provided by both Healthcare Plans as calculated pursuant to GASB Statements No. 43 and 45 as then in effect. However, the contribution rates for the City and members of the Healthcare Plans were capped before the full annual required contribution 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 Plan Actuary commenced calculating the Actuarially Determined Contribution for each Healthcare Plan in fiscal year 2018-2019. See "CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS" for a discussion of Measure F.

The Plan Actuary in the Federated 2019 Healthcare Plan Actuarial Report and the Police and Fire 2019 Healthcare Plan Actuarial Report indicates that because new entrants to the Healthcare Plans are only entitled to catastrophic disability benefits and do not contribute to the Healthcare Plans, 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 slightly as the member contributions decrease. In the Federated 2019 Healthcare Plan Actuarial Report and the Police and Fire 2019 Healthcare Plan Actuarial Report, the Plan Actuary noted that it expects that the Federated Healthcare Plan will have net positive cash flow for fiscal year 2020-2021 and negative cash flow thereafter. The Plan Actuary further noted that it expects that the Police and Fire Healthcare Plan will have positive cash flow through fiscal year 2025-2026.

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 Statements No. 74 and 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 Plans. The implicit subsidy is shown in such statements 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.

In January 2020, 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, 2019 actuarial valuations. The projections assume that all valuation assumptions were exactly met and are exactly met each and every year for the projection period. Table B-17b below summarizes the estimated OPEB payroll and Actuarially Determined Contribution amounts for the next five fiscal years based on such projections. 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.

Table B-17b
5-Year Projections of Healthcare Plans Contributions
(in thousands)
(Throughout the Year)

Federated Healthcare Plan				
Fiscal Year Ended June 30	Full Benefit Payroll	Total Payroll	Estimated City Contribution Cap	Actuarially Determined Contribution
2021	\$ 124.7	\$ 322.7	\$ 43.1	\$ 21.0
2022	114.9	332.4	44.4	20.2
2023	106.1	342.4	45.7	19.4
2024	98.0	352.6	47.1	19.6
2025	90.2	363.2	48.5	19.8

Police and Fire Healthcare Plan				
Fiscal Year Ended June 30	Full Benefit Payroll	Total Payroll	Estimated City Contribution Cap	Actuarially Determined Contribution
2021	\$ 148.3	\$ 243.4	\$ 26.8	\$ 25.4
2022	137.5	251.4	27.7	26.6
2023	124.9	259.6	28.6	27.5
2024	113.8	268.0	29.5	28.7
2025	103.9	276.7	30.4	29.8

Source: Cheiron 5-Year Budget Projections for Federated Plan, January 15, 2020; Cheiron 5-Year Budget Projections for Police and Fire Department Healthcare Plan, January 29, 2020.

The five-year projections as of January 2020 summarized in Table B-17b show that the City contributions to the Federated Healthcare Plan are projected to decrease gradually over the next five years and remain significantly below the City's contribution cap of 14% of the pay of the active members of the Federated Plan. In such five-year projections, the City's contributions to the Police and Fire Healthcare Plan are projected to increase over the next five years but not exceed the City's contribution cap of 11%. The City can elect to limit its contribution, if the Actuarially Determined Contribution exceeds the contribution cap in the future, to 11% of the pay of the active members of the Police and Fire Retirement Plan.

The information presented in this Appendix B does not take into account any impacts of COVID-19 on the Retirement Plans. In particular, the projections contained herein on future City contributions do not reflect the impact of the COVID-19 pandemic on the Retirement Plans, including likely impacts on investment returns, health care costs, salaries, employment levels, or other factors that may affect the valuation and future City contributions. The City expects its unfunded accrued liability and actuarially determined required contributions for the Retirement Plans to increase in the future as result. The City cannot at this time project the magnitude or timing of such increases. See "INTRODUCTION TO APPENDIX B – COVID-19."

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 to 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 shows the components of the Actuarially Determined Contribution for the Federated Healthcare Plan for fiscal years 2019-2020 and 2020-2021.

Table B-18 Federated Healthcare Plan Actuarially Determined Contribution Explicit Subsidy Only (in thousands)			
	2019-2020	2020-2021	% Change
Normal Cost	\$ 6,108	\$ 5,805	(5.0)%
UAL Payment	25,572	24,500	(4.2)
Total Contribution	\$ 31,680	\$30,305	(4.3)
Projected Member Contributions	9,890	9,356	(5.4)
City ADC Amount	\$ 21,790	\$ 20,949	(3.9)
Projected Total Payroll	\$ 308,702	\$ 307,972	(0.2)
City ADC Percentage	7.1%	6.8%	(4.2)
<i>Source: Federated 2019 Healthcare Plan 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. The City's contribution toward the explicit subsidy is actuarially determined separately for Police and Fire. The City pays 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 total payroll.

Table B-19 provides the components of the Actuarially Determined Contribution for the Police and Fire Healthcare Plan for fiscal years 2019-2020 and 2020-2021.

Table B-19 Police and Fire Healthcare Plan Actuarially Determined Contribution (Explicit Subsidy Only) (in thousands)			
	2019-2020	2020-2021	% Change
Police			
Normal Cost	\$ 5,728	\$ 5,716	(0.2)%
Administrative Expense	106	81	(24.0)
UAL Payment	15,632	16,189	3.6
Total Contribution	\$ 21,466	\$ 21,985	2.4
Projected Member Contributions	6,871	6,666	(3.0)
City ADC Amount	\$ 14,595	\$ 15,320	5.0
Projected Payroll	\$136,175	\$ 151,638	11.4
City ADC Percentage	10.7%	10.1%	(5.7)
Fire			
Normal Cost	\$ 4,989	\$ 4,966	(0.5)
Administrative Expense	73	55	(24.6)
UAL Payment	9,822	10,237	4.2
Total Contribution	\$ 14,885	\$ 15,258	2.5
Projected Member Contributions	5,477	5,196	(5.1)
City ADC Amount	\$ 9,408	\$ 10,062	7.0
Projected Payroll	\$89,354	\$ 91,844	2.8
City ADC Percentage	10.5%	11.0%	4.8
Total			
City ADC Amount	\$ 24,003	\$ 25,382	5.7
Projected Total Payroll	225,528	243,482	8.0
City ADC Percentage	10.6%	10.4%	(1.9)

Source: Police and Fire 2019 Healthcare Plan Actuarial Report.

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-employment 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.

Table B-20a Healthcare Plans' Assets and Liabilities <i>(in thousands)</i>			
	June 30, 2018	June 30, 2019	% Change
Federated Plan			
Total Actuarial Liability	\$ 650,114	\$ 631,752	(2.8)%
Market Value Assets	277,256	294,489	6.2
Explicit Subsidy Unfunded Actuarial Liability	286,450	246,326	(14.0)
Explicit Subsidy Funded Percentage	49.2%	54.5%	10.7%
Total Unfunded Actuarial Liability	\$ 372,858	\$ 337,263	(9.5)
Total Funded Percentage	42.6%	46.6%	9.3
Police and Fire Plan			
Total Actuarial Liability	\$ 747,274	\$ 693,329	(7.2)
Market Value Assets	162,519	185,957	14.4
Explicit Subsidy Unfunded Actuarial Liability	436,407	424,123	(2.8)
Explicit Subsidy Funded Percentage	27.1%	30.5%	12.5
Total Unfunded Actuarial Liability ⁽¹⁾	\$ 584,754	\$ 507,372	(13.2)
Total Funded Percentage ⁽¹⁾	21.7%	26.8%	23.5
⁽¹⁾ Includes explicit and implicit subsidies. Source: Federated 2019 Healthcare Plan Actuarial Report; Police and Fire 2019 Healthcare Plan Actuarial Report.			

See “– Federated 2019 Healthcare Plan Actuarial Valuation” and “– Police and Fire 2019 Healthcare Plan Actuarial Valuation” below for a discussion of the changes in valuation described in Table B-20a.

Table B-20b and Table B-20c provide a comparison of the changes in the Market Value Assets of the Healthcare Plans for the prior two fiscal years.

Table B-20b Federated Healthcare Plan - Market Value of Plan Assets <i>(in thousands)</i>		
	2017-2018	2018-2019
Market Value, Beginning of Year	\$ 260,370	\$ 277,257
Contributions		
Member	15,545	10,578
City	28,579	22,328
Implicit Subsidy	3,818	4,082
Total	\$ 47,942	\$ 36,988
Net Investment Earnings ⁽¹⁾	12,336	9,472
Benefit Payments ⁽²⁾	(29,724)	(28,826)
Admin Expense	(170)	(384)
VEBA Transfer	(13,497)	(19)
Market Value, End of Year	\$ 277,257	\$ 294,488

⁽¹⁾ Gross investment earnings less investment expenses.
⁽²⁾ 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: Federated 2019 CAFR.

Table B-20c Police and Fire Healthcare Plan - Market Value of Plan Assets <i>(in thousands)</i>		
	2017-2018	2018-2019
Market Value, Beginning of Year	\$ 149,682	\$ 162,520
Contributions		
Member	16,127	13,315
City	19,666	23,028
Implicit Subsidy	5,716	5,716
Total	\$ 41,509	\$ 42,059
Net Investment Earnings ⁽¹⁾	7,071	7,907
Benefit Payments ⁽²⁾	(27,686)	(26,403)
Administrative Expenses	(159)	(126)
VEBA Transfer	(7,897)	--
Market Value, End of Year	\$ 162,520	\$ 185,957

⁽¹⁾ Gross investment earnings less investment expenses.
⁽²⁾ 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 2019 CAFR.

Federated 2019 Healthcare Plan Actuarial Valuation. As with the Federated Pension Plan, the Plan Actuary performed an actuarial valuation of the Federated Healthcare Plan as of June 30, 2019, which valuation is set forth in the Federated 2019 Healthcare Plan Actuarial Report. According to the Federated 2019 Healthcare Plan Actuarial Report, as of June 30, 2019, the Actuarial Liability for the explicit and implicit subsidies of the Federated Healthcare Plan totaled approximately \$631.8 million, with Market Value of Assets of approximately \$294.5 million, resulting in a UAL for the explicit and implicit subsidies of the Federated Healthcare Plan of approximately \$337 million (a decrease of approximately \$35.6 million (or 9.5%) from the UAL as of June 30, 2018). According to the Plan Actuary, the aggregate decrease in the UAL of the Federated Healthcare Plan was due primarily to plan experience which was mainly driven by lower than expected increases in the Medicare eligible premium rates (resulting in an aggregate decrease in the UAL of the Federated Healthcare Plan of approximately \$25.6 million), assumption changes primarily due to health trend changes (resulting in an aggregate decrease in the UAL of the Federated Healthcare Plan of approximately \$14.8 million), and contributions in excess of the Normal Cost plus interest on the UAL (resulting in an aggregate decrease in the UAL of the Federated Healthcare Plan of approximately \$5.8 million). Such decreases were offset mainly by losses recognized as result of investment returns below the discount rate (resulting in an aggregate increase in the UAL of the Federated Healthcare Plan of approximately \$10.7 million) and additional transfers to the Federated VEBA. In the Federated 2019 Healthcare Plan Actuarial Report, the Plan Actuary further notes 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.

See Table B-20a for a summary of the changes in valuations for the prior two fiscal years with respect to the Federated Healthcare Plan as set forth in the Federated 2019 Healthcare Plan Actuarial Report.

The 401(h) account for the Federated Healthcare Plan was depleted in fiscal year 2018-2019 as a result of Federated Healthcare Plan contributions having been made solely to the Federated 115 Trust while at the same time benefits having been paid only from the Federated Healthcare Plan 401(h) account. All Federated Healthcare Plan benefits are now paid from the Federated 115 Trust. The expected investment returns for the Federated Healthcare Plan will be based solely on the investment policy of the Section 115 Trust.

Table B-21 shows the UAL, Funded Ratio and discount rates of the Federated Healthcare Plan from fiscal year 2010-2011 through fiscal year 2018-2019.

Table B-21 Federated Healthcare Plan Historical UAL, Funded Ratios and Discount Rates (UAL in millions) (Implicit and Explicit Subsidies)									
	2011	2012	2013	2014	2015	2016	2017	2018	2019
Funded Ratio	14.5%	18.6%	23.9%	30.0%	29.1%	30.7%	39.4%	42.6%	46.6%
UAL	\$ 800.5	\$ 604.7	\$ 501.3	\$ 465.2	\$ 511.9	\$ 510.9	\$ 381.9	\$ 372.9	\$ 337.3
Discount Rate	7.50%	7.50%	7.25%	7.00%	7.00%	6.875%	6.875%	6.75%	6.75%

Source: Federated 2019 Healthcare Plan Actuarial Valuation Report.

Police and Fire 2019 Healthcare Plan Actuarial Valuation. The Plan Actuary performed an actuarial valuation of the Police and Fire Healthcare Plan as of June 30, 2019, which valuation is set forth in the Police and Fire 2019 Healthcare Plan Actuarial Report. According to the Police and Fire 2019 Healthcare Plan Actuarial Report, as of June 30, 2019, the Actuarial Liability for the explicit and implicit subsidies of the Police and Fire Healthcare Plan totaled approximately \$693.3 million, with Market Value of Assets of approximately \$186.0 million, resulting in a UAL of approximately \$507.4 million (a decrease of approximately \$77.4 million (or 13.2%) from the UAL as of June 30, 2018). According to the Plan Actuary, the decrease in the UAL for the explicit subsidy of the Police and Fire Healthcare Plan was due primarily to plan experience which was mainly driven by lower than expected increases in the Medicare eligible premium rates and changes to the premium tier structure (resulting in a decrease in the UAL of the Police and Fire Healthcare Plan of approximately \$99.3 million). The Plan Actuary further reports that such decrease was offset by losses recognized as result of investment returns below the discount rate (resulting in an increase in the UAL of the Police and Fire Healthcare Plan of approximately \$4.0 million) and assumption changes (resulting in an increase in the UAL of the Police and Fire Healthcare Plan of approximately \$8.6 million). According to the Plan Actuary, the assumption changes were primarily due to health trend changes and demographic assumption updates. In addition, contributions to the Police and Fire Healthcare Plan were below the Normal Cost plus interest in the UAL of the Police and Fire Healthcare Plan (resulting in an increase in the UAL of the Police and Fire Healthcare Plan of approximately \$9.3 million). In the Police and Fire 2019 Healthcare Plan Actuarial Report, the Plan Actuary notes 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 2043.

See Table B-20a for a summary of the changes in valuations for the prior two fiscal years with respect to the Police and Fire Healthcare Plan as set forth in the Police and Fire 2019 Healthcare Plan Actuarial Report.

Table B-22 shows the UAL, Funded Ratio and discount rates of the Police and Fire Healthcare Plan from fiscal year 2010-2011 through fiscal year 2018-2019.

Table B-22
Police and Fire Healthcare Plan
Historical UAL, Funded Ratios and Discount Rates
(UAL in millions)
(Implicit and Explicit Subsidies)

	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>2019</u>
Funded Ratio	6.0%	6.7%	10.7%	13.2%	15.5%	17.4%	21.0%	21.7%	26.8%
UAL	\$ 943.1	\$ 930.9	\$ 625.5	\$ 613.1	\$ 625.2	\$ 643.7	\$ 537.7	\$ 584.8	\$ 507.4
Discount Rate	7.50%	7.25%	7.125%	7.00%	7.00%	6.875%	6.875%	6.50%	6.50%

Source: Police and Fire Healthcare Plan 2018 Actuarial Valuation Report; Cheiron Inc.

Funding Progress - Net OPEB Liability

The Healthcare Plans and the City implemented GASB Statement No. 74 in fiscal year 2016-2017. The City implemented GASB Statement No. 75 in fiscal year 2017-2018. GASB Statements No. 74 and 75 require the Healthcare 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 Retirement Plans' financial statements show Net OPEB Liability one year later in date.

Table B-23 sets forth the Total OPEB Liability as of June 30, 2019 and June 30, 2018 based on results of an actuarial valuation date of June 30, 2018 and June 30, 2017, respectively, rolled-forward to June 30, 2019 and June 30, 2018, respectively, using generally accepted actuarial procedures. As of the measurement date of June 30, 2019, the Net OPEB Liability totaled approximately \$377.7 million and \$598.1 million for the Federated Healthcare Plan and the Police and Fire Healthcare Plan, respectively. 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 <i>(in thousands)</i>			
	June 30, 2018	June 30, 2019	% Change
Federated Healthcare Plan			
Total OPEB Liability	\$ 651,222	\$ 672,193	3.2%
Plan fiduciary net position	(277,257)	(294,488)	6.2
Net OPEB Liability	\$ 373,965	\$ 377,705	1.0
Plan fiduciary net position as a percentage of the Total OPEB Liability	42.6%	43.8%	2.8%
Police and Fire Healthcare Plan			
Total OPEB Liability	\$ 711,832	\$ 784,082	10.1
Plan fiduciary net position	(162,520)	(185,957)	14.4
Net OPEB Liability	\$ 549,312	\$ 598,125	8.9
Plan fiduciary net position as a percentage of the Total OPEB Liability	22.8%	23.7%	3.9

Source: Federated 2019 CAFR; Police and Fire 2019 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 such funding has changed over the past several years. The Actuarial 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.

Funding Progress of Healthcare Plans. 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 <i>(in thousands)</i>					
Fiscal Year Ended June 30	Federated Healthcare Plan		Police and Fire Healthcare Plan		Total
	UAL	Funded Ratio	UAL	Funded Ratio	UAL
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
2019	337,263	47	507,373	26.8	844,636

Source: Federated 2019 Healthcare Plan Actuarial Report; Police and Fire 2019 Healthcare Plan Actuarial Report.

As shown in Table B-24a, the Funded Ratio for each of the Healthcare Plans has increased steadily since fiscal year 2009-2010, but they remain substantially underfunded.

Federated Funding Progress. Table B-24b shows an overall decrease in Actuarial Accrued Liability and UAL for the Federated Healthcare Plan from June 30, 2010 through June 30, 2019.

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
2019	294,489	631,752	337,263	47	299,002	113

Source: Federated 2019 Healthcare Plan Actuarial Report.

Police and Fire Healthcare Plan Funding Progress. Table B-24b shows an overall decrease in Actuarial Liability and UAL for the Police and Fire Healthcare Plan from June 30, 2010 through June 30, 2019. 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)

Valuation Date (June 30)	Market Value of Assets ⁽¹⁾	Actuarial Liability	UAL	Funded Ratio	Covered Payroll	UAL as % of Covered Payroll
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
2019	185,957	693,329	507,373	26.8	235,818	215

⁽¹⁾ Actuarial value of assets prior to fiscal year 2015-2016 and earlier.

Source: Police and Fire 2019 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 summarize the significant actuarial valuation methods and assumptions used for the June 30, 2019 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, 2019
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 ⁽¹⁾	Market Value
Actuarial Assumptions:	
Payroll Growth Rate	3.00%
Discount Rate	6.75%

⁽¹⁾ The market value of assets means the actual value of assets, and not the smoothed value, is used.
Source: Federated 2019 Healthcare Actuarial Report.

Table B-25b
Police and Fire Plan – Healthcare Actuarial Assumptions

Valuation Date	June 30, 2019
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 ⁽¹⁾	Market Value
Actuarial Assumptions:	
Payroll Growth Rate	3.25%
Discount Rate	6.50%

⁽¹⁾ The market value of assets means the actual value of assets, and not the smoothed value, is used.
Source: Police and Fire 2019 Healthcare Plan 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. As previously described, the 401(h) account for the Federated Healthcare Plan was depleted in fiscal year 2018-2019, leaving only the Federated 115 Trust in the Healthcare Plan. As a result, all Federated Healthcare Plan benefits are now paid from the Federated 115 Trust. In addition, the City has established Code the Section 115 Trusts to supplement the 401(h) accounts. The 401(h) accounts for the Police and Fire Healthcare Plan and the Section 115 Trusts are funded as described above in “Establishment of 115 Trusts For Healthcare Plans; Tax Limitations.”

Table B-26a below illustrates the historical annual returns net of fees for both Section 115 Trusts at the identified interval as reported by the Healthcare Plans' respective investment consultants in their respective quarterly reports for the period ending March 31, 2020.

Table B-26a		
Historical Investment Performance For Section 115 Trusts		
(As of March 31, 2020)		
Measurement Period	Federated 115 Trust	Police and Fire 115 Trust
Since Inception	2.9%	3.0%
10 Years	-	-
5 Years	0.9	1.1
3 Years	0.2	0.5
1 Year	(8.1)	(6.5)

⁽¹⁾ Measurement Period Beginning July 2011.
⁽²⁾ Measurement Period Beginning July 2012.
Source: Meketa Investment Group Federated Retiree Healthcare 115 Trust Quarterly Review March 31, 2020; Meketa Investment Group Police and Fire Retiree Healthcare 115 Trust Quarterly Review March 31, 2020.

Due to the smaller asset size of the Section 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 most recent target allocations for the Section 115 Trusts are shown in Table B-26b.

Table B-26b
Target Asset Allocations for Section 115 Trusts

Asset Class	Federated 115 Trust Target %	Police and Fire 115 Trust Target %
Growth	56	56
US Equity	28	28
Developed Market Equity (non-US)	13	13
Emerging Market Equity	15	15
Emerging Markets Bonds	0	0
Private Assets	0	0
Zero Beta	29	29
Hedge Funds	0	0
Short-Term Investment-Grade Bonds	29	29
Cash	0	0
Other	15	15
Core Real Estate	10	10
Commodities	5	5
Public Natural Resources	0	0
Investment Grade Bonds	0	0
TIPS	0	0
<i>20-Year Expected Return ⁽¹⁾</i>	<i>6.8</i>	<i>6.8</i>
<i>Standard Deviation ⁽¹⁾</i>	<i>11.8</i>	<i>11.8</i>

⁽¹⁾ Neither the City nor the Underwriter can provide any assurance that actual returns will not be less than those expected by the respective Board.

Source: Meketa Investment Group City of San Jose Police and Fire Department Retirement Plan Health Care Trust Asset Allocation Review and Risk Analysis, Asset Allocation Approved by the Police and Fire Board on September 6, 2018; Meketa Investment Group San Jose Federated City Employees' Health Care 115 Asset Allocation Review and Risk Analysis, Asset Allocation Approved by the Federated Board on September 20, 2018.

For a description of the types of investments in each asset class for the Healthcare Plans' target asset allocations identified in Table B-26b, 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 assets class descriptions are substantially the same. These may be found respectively 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-7926B4EAEC97&Options=info&Search=>. None of the foregoing websites or webpages are incorporated into this Appendix B. They are referenced for informational purposes only. The City and the Underwriters make no representation whatsoever as to the accuracy or completeness of any of the information on such websites or webpages.

APPENDIX C

BASIC FINANCIAL STATEMENTS OF THE CITY OF SAN JOSE FOR THE FISCAL YEAR ENDED JUNE 30, 2019

APPENDIX D
SUMMARY OF PRINCIPAL LEGAL DOCUMENTS

APPENDIX E
PROPOSED FORM OF OPINION OF BOND COUNSEL

APPENDIX F

FORM OF CONTINUING DISCLOSURE CERTIFICATE

\$ _____
City of San José Financing Authority
Taxable Lease Revenue Bonds, Series 2020B
(Ice Centre Project)

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 San José Financing Authority (the “Authority”) of the bonds captioned-above (the “Bonds”). The Bonds are being issued pursuant to a resolution adopted by the Authority on [August 25, 2020] and an Indenture of Trust (the “Indenture”), dated as of October 1, 2020, by and between the City and Wilmington Trust, National Association, as trustee (the “Trustee”).

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 Indenture, 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 30th).

“*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, 2021, the Current Fiscal Year means the 2020-21 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, 2021, the Preceding Fiscal Year means the 2019-20 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, 2021 with the report for the 2019-20 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) Summary information relating to the City's adopted operating budget for the then-current Fiscal Year, substantially in the form set forth in Table 9 of Appendix A to the Official Statement (provided that the categories set forth in said Table 9 may be revised to reflect the then current budgeting and budget reporting practices of the City)

(ii) Particular section or sections of the budget demonstrating that the City has budgeted for Base Rental Payments and Additional Rental payments for the current Fiscal Year.

(iii) General Fund summary of revenues and expenditures substantially in the form set forth on page 30 of the City's fiscal year 2018-19 comprehensive annual financial report.

(iv) General fund balance sheet substantially in the form set forth on page 26 of the City's fiscal year 2018-19 comprehensive annual financial report.

(v) General fund tax revenues by source substantially in the form set forth on page 190 of the City's fiscal year 2018-19 comprehensive annual financial report.

(vi) Assessed valuation of property in the City substantially in the form set forth on page 270 of the City's fiscal year 2018-19 comprehensive annual financial report, and the current property tax levy and collections substantially in the form set forth on page 273 of the City's fiscal year 2018-19 comprehensive annual financial report.

(vii) Balance in the Reserve Account and a statement of the Reserve Requirement.

(viii) A description of any event of default under the Indenture.

(ix) A description of any event resulting in the abatement of Lease Payments under the Lease.

(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 Indenture.

(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 Indenture for amendments to the Indenture 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 Indenture, 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 attorney 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:

City of San José - Finance
Debt Management
200 East Santa Clara Street, 13th 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: _____, 2020

CITY OF SAN JOSE

By: _____
Julia H. Cooper
Director of Finance

APPROVED AS TO FORM: Nora Frimman,
Acting 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 Financing Authority

Name of Bond Issue: City of San José Financing Authority Taxable Lease Revenue Bonds, Series 2020A (Ice Centre Project)

Date of Issuance: _____, 2020

NOTICE IS HEREBY GIVEN that the City of San José (the "City") has not provided an Annual Report with respect to the above-named Bonds as required by the Continuing Disclosure Certificate, dated _____, 2020. The City anticipates that the Annual Report will be filed by _____.

Dated: [DISSEMINATION AGENT]

By: _____
Name:
Title:

APPENDIX G

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 Authority (the “Issuer”) nor the Trustee (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”), New York, NY, 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 at www.dtcc.com and www.dtc.org. *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 shall 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. A Beneficial Owner shall give notice to elect to have its Securities purchased or tendered, through its Participant, to the Agent, and shall effect delivery of such Securities by causing the Direct Participant to transfer the Participant's interest in the Securities, on DTC's records, to the Agent. The requirement for physical delivery of Securities in connection with an optional tender or a mandatory purchase will be deemed satisfied when the ownership rights in the Securities are transferred by Direct Participants on DTC's records and followed by a book-entry credit of tendered Securities to the Agent's DTC account.

10. 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.

11. 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.

12. 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.