

TWO NEW ISSUES—BOOK-ENTRY ONLY

RATING:
S&P: “AA+”
See “RATING” herein.

In the opinion of Jones Hall, A Professional Law Corporation, San Francisco, California, Special Counsel, subject, however to certain qualifications described herein, under existing law, the portion of Lease Payments designated as and comprising interest and received by the owners of the 2019A Certificates is excluded from gross income for federal income tax purposes, and such interest is not an item of tax preference for purposes of the federal alternative minimum tax. The portion of Lease Payments designated as and comprising interest and received by the owners of the 2019B Certificates is not intended by the City to be excluded from gross income for federal income tax purposes. In the further opinion of Special Counsel, such interest on the Certificates is exempt from California personal income taxes. See “TAX MATTERS” herein.



\$26,785,000
CITY OF PALO ALTO
2019 Certificates of Participation, Series A
(California Avenue Parking Garage)
(Tax-Exempt)

\$10,585,000
CITY OF PALO ALTO
2019 Certificates of Participation, Series B
(California Avenue Parking Garage)
(Federally Taxable)

Dated: Date of Delivery

Due: November 1, as shown on the inside cover

The \$26,785,000 City of Palo Alto 2019 Certificates of Participation, Series A (California Avenue Parking Garage) (Tax-Exempt) (the “2019A Certificates”) and the \$10,585,000 City of Palo Alto 2019 Certificates of Participation, Series B (California Avenue Parking Garage) (Federally Taxable) (the “2019B Certificates” and, with the 2019A Certificates, the “Certificates”) are being sold to provide funds to (a) finance the costs of the construction of a 636 space parking garage (see “THE PROJECT” herein), and (b) pay delivery costs incurred in connection with the execution, delivery and sale of the Certificates.

The Certificates represent direct, undivided fractional interests of the owners thereof in Lease Payments (as defined herein) to be made by the City of Palo Alto (the “City”) to the Palo Alto Public Improvement Corporation (the “Corporation”) for the use and occupancy of the Leased Property (as defined herein) under and pursuant to a Lease Agreement, dated as of March 1, 2019, by and between the Corporation and the City (the “Lease Agreement”). The Corporation will assign its right to receive Lease Payments from the City under the Lease Agreement and its right to enforce payment of the Lease Payments when due or otherwise protect its interest in the event of a default by the City thereunder to U.S. Bank National Association, San Francisco, California, as trustee (the “Trustee”), for the benefit of the registered owners of the Certificates.

The Certificates will be executed and delivered pursuant to a Trust Agreement, dated as of March 1, 2019, by and among the City, the Corporation and the Trustee, in book-entry form only, and will be initially registered in the name of Cede & Co. as nominee of The Depository Trust Company (“DTC”). Purchasers of the Certificates (the “Beneficial Owners”) will not receive physical certificates representing their interest in the Certificates. Interest with respect to the Certificates accrues from their date of delivery and is payable semiannually by check mailed on each May 1 and November 1, commencing November 1, 2019. The Certificates will be executed and delivered in denominations of \$5,000 or any integral multiple thereof. Payments of principal and interest with respect to the Certificates will be paid by the Trustee to DTC for subsequent disbursement to DTC Participants who will remit such payments to the Beneficial Owners of the Certificates. See “THE CERTIFICATES—Book-Entry System” herein and APPENDIX F—DTC’S BOOK-ENTRY ONLY SYSTEM.

The Certificates are subject to optional and mandatory prepayment. See “THE CERTIFICATES—Prepayment” herein.

The City will covenant in the Lease Agreement to make all Lease Payments due under the Lease Agreement, subject to abatement during any period in which by reason of damage or destruction of the Leased Property, or by reason of eminent domain proceedings with respect to the Property, there is substantial interference with the use and occupancy by the City of the Leased Property or any portion thereof. The City will covenant in the Lease Agreement to take such action as may be necessary to include all Lease Payments in its annual budgets and to make the necessary annual appropriations for all such Lease Payments. **A reserve fund will not be funded for the Certificates.**

NEITHER THE CERTIFICATES NOR THE OBLIGATION OF THE CITY TO MAKE LEASE PAYMENTS UNDER THE LEASE AGREEMENT CONSTITUTES A DEBT OR INDEBTEDNESS OF THE CITY OR THE STATE OF CALIFORNIA OR ANY POLITICAL SUBDIVISION THEREOF WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATIONS OR RESTRICTION OR 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.

MATURITY SCHEDULE

SEE THE INSIDE COVER

The cover page contains certain information for general reference only. It is *not* a summary of all the provisions of the Certificates. Investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision. See “RISK FACTORS” herein for a discussion of special risk factors that should be considered, in addition to the other matters set forth herein, in evaluating the investment quality of the Certificates.

The Certificates will be offered when, as and if delivered and received by the Underwriter subject to approval by Jones Hall, A Professional Law Corporation, San Francisco, California, as Special Counsel. Certain matters will be passed upon for the City by the City Attorney and by Quint & Thimmig LLP, Larkspur, California, as Disclosure Counsel, and for the Underwriter by Stradling Yocca Carlson & Rauth, a Professional Corporation, Newport Beach, California. It is anticipated that the Certificates will be available for through the facilities of DTC on or about March 21, 2019.

STIFEL

\$26,785,000
CITY OF PALO ALTO
2019 Certificates of Participation, Series A
(California Avenue Parking Garage)
(Tax-Exempt)

\$18,075,000 Serial Certificates

CUSIP† Prefix: 697364

Maturity (November 1)	Principal Amount	Interest Rate	Yield	Price	CUSIP† Suffix
2022	\$ 310,000	5.000%	1.430%	112.519	EH6
2023	690,000	5.000	1.490	115.583	EJ2
2024	720,000	5.000	1.550	118.470	EK9
2025	760,000	5.000	1.660	120.829	EL7
2026	795,000	5.000	1.790	122.743	EM5
2027	835,000	5.000	1.880	124.695	EN3
2028	880,000	5.000	1.990	126.210	EP8
2029	920,000	5.000	2.120	124.921c	EQ6
2030	970,000	5.000	2.270	123.452c	ER4
2031	1,015,000	5.000	2.390	122.291c	ES2
2032	1,065,000	5.000	2.520	121.048c	ET0
2033	1,120,000	5.000	2.630	120.009c	EU7
2034	1,175,000	5.000	2.690	119.446c	EV5
2035	1,235,000	5.000	2.760	118.794c	EW3
2036	1,295,000	5.000	2.840	118.053c	EX1
2037	1,360,000	5.000	2.900	117.501c	EY9
2038	1,430,000	5.000	2.960	116.953c	EZ6
2039	1,500,000	5.000	3.020	116.407c	FA0

\$8,710,000 5.000% Term Certificates maturing November 1, 2044; Price: 115.145c, to yield 3.160%; CUSIP† 697364 FB8

\$10,585,000
CITY OF PALO ALTO
2019 Certificates of Participation, Series B
(California Avenue Parking Garage)
(Federally Taxable)

\$2,005,000 Serial Certificates

CUSIP† Prefix: 697364

Maturity (November 1)	Principal Amount	Interest Rate	Yield	Price	CUSIP† Suffix
2019	\$375,000	2.532%	2.532%	100.000	FC6
2020	630,000	2.632	2.632	100.000	FD4
2021	645,000	2.732	2.732	100.000	FE2
2022	355,000	2.798	2.798	100.000	FF9

\$8,580,000 4.351% Term Certificates maturing November 1, 2048; Price: 100.000, to yield 4.351%; CUSIP† 697364 FG7

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c Priced to the November 1, 2028, par call date

No dealer, broker, salesperson or other person has been authorized to give any information or to make any representation other than those contained herein and, if given or made, such other information or representation must not be relied upon as having been authorized. This Official Statement does not constitute an offer to sell or the solicitation of any offer to buy, nor shall there be any sale of the Certificates by a person in any jurisdiction in which it is unlawful for such person to make an offer, solicitation or sale.

This Official Statement is not to be construed as a contract with the purchasers of the Certificates. Statements contained in this Official Statement which involve estimates, forecasts or matters of opinion, whether or not expressly so described herein, are intended solely as such and are not to be construed as representations of facts.

The information set forth herein has been obtained from the City and from other sources and is believed to be reliable but is not guaranteed as to accuracy or completeness. The information and expressions of opinions herein are subject to change without notice and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the City since the date hereof. This Official Statement is submitted in connection with the sale of the Certificates referred to herein and may not be reproduced or used, in whole or in part, for any other purpose, unless authorized in writing by the City. All summaries of the Certificates, the Lease Agreement, the Trust Agreement, the Assignment Agreement, the Property Lease (each as defined herein), or other documents, are made subject to the provisions of such documents and do not purport to be complete statements of any or all of such provisions. Reference is hereby made to such documents on file with the Director of Finance for further information. See “INTRODUCTION—Other Information.”

The Underwriter has provided the following sentence for inclusion in this Official Statement: The Underwriter has reviewed the information in this Official Statement in accordance with, and as part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITER MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE CERTIFICATES AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME. THE UNDERWRITER MAY OFFER AND SELL THE CERTIFICATES TO CERTAIN DEALERS, INSTITUTIONAL INVESTORS AND OTHERS AT PRICES LOWER THAN THE PUBLIC OFFERING PRICES STATED ON THE INSIDE COVER PAGE HEREOF AND SUCH PUBLIC OFFERING PRICES MAY BE CHANGED FROM TIME TO TIME BY THE UNDERWRITER.

Certain statements included or incorporated by reference in this Official Statement constitute “forward-looking statements.” Such statements are generally identifiable by the terminology used such as “plan,” “expect,” “estimate,” “budget” or other similar words. The achievement of certain results or other expectations contained in such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements described to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. No assurance is given that actual results will meet the City’s forecasts in any way. Neither the City nor the Corporation is obligated to issue any updates or revisions to the forward-looking statements if or when its expectations, or events, conditions or circumstances on which such statements are based occur or do not occur.

The execution, sale and delivery of the Certificates has not been registered under the Securities Act of 1933 or the Securities Exchange Act of 1934, both as amended, in reliance upon exemptions provided thereunder by Sections 3(a)(2) and 3(a)(12), respectively, for the issuance and sale of municipal securities.

The City maintains a website. Unless specifically indicated otherwise, the information presented on such website is *not* incorporated by reference as part of this Official Statement and should not be relied upon in making investment decisions with respect to the Certificates.

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CITY OF PALO ALTO LOCATION MAP



CITY OF PALO ALTO
250 Hamilton Avenue
Palo Alto, California 94301
<http://www.cityofpaloalto.org>

CITY COUNCIL MEMBERS

Eric Filseth, *Mayor*
Adrian Fine, *Vice Mayor*
Alison Cormack, *Councilmember*
Tom DuBois, *Councilmember*
Liz Kniss, *Councilmember*
Lydia Kou, *Councilmember*
Greg Tanaka, *Councilmember*

CITY OFFICIALS

Edward K. Shikada, *City Manager*
Michelle Flaherty, *Deputy City Manager*
Kiely Nose, *Interim Chief Financial Officer/Administrative Services Director*
Christine Paras, *Assistant Director of Administrative Services*
Brad Eggleston, *Director of Public Works*
Matt Raschke, *Senior Engineer*
Tarun Narayan, *Manager of Treasury, Debt & Investments*
Harriet Richardson, *City Auditor*
Molly S. Stump, *City Attorney*
Beth Minor, *City Clerk*

SPECIAL SERVICES

Special Counsel

Jones Hall, A Professional Law Corporation
San Francisco, California

Disclosure Counsel

Quint & Thimmig LLP
Larkspur, California

Financial Advisor

PFM Financial Advisors LLC
San Francisco, California

Trustee

U.S. Bank National Association
San Francisco, California

\$26,785,000
CITY OF PALO ALTO
2019 Certificates of Participation, Series A
(California Avenue Parking Garage)
(Tax-Exempt)

\$10,585,000
CITY OF PALO ALTO
2019 Certificates of Participation, Series B
(California Avenue Parking Garage)
(Federally Taxable)

INTRODUCTION

This introduction does not purport to be complete and reference is made to the body of this Official Statement, appendices and the documents referred to herein for more complete information with respect to matters concerning the captioned Certificates. Potential investors are encouraged to read this entire Official Statement. Capitalized terms used and not defined in this Introduction shall have the meanings assigned to them elsewhere in this Official Statement and in APPENDIX E—SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS—DEFINITIONS.

General

This Official Statement, including the cover page, the inside cover page and appendices hereto, is provided to furnish information in connection with the execution, sale and delivery of \$26,785,000 City of Palo Alto 2019 Certificates of Participation, Series A (California Avenue Parking Garage) (Tax-Exempt) (the “2019A Certificates”) and the \$10,585,000 City of Palo Alto 2019 Certificates of Participation, Series B (California Avenue Parking Garage) (Federally Taxable) (the “2019B Certificates” and, with the 2019A Certificates, the “Certificates”). The Certificates are being executed and delivered pursuant to a Trust Agreement, dated as of March 1, 2019 (the “Trust Agreement”), by and among the City of Palo Alto (the “City”), the Palo Alto Public Improvement Corporation (the “Corporation”) and U.S. Bank National Association, as trustee (the “Trustee”).

The proceeds of the Certificates will provide funds to (a) finance the costs of a 636 space parking garage (the “Project”) and (b) pay delivery costs incurred in connection with the execution, delivery and sale of the Certificates. See “THE PROJECT.”

The City will lease certain existing property (the “Leased Property”) to the Corporation pursuant to a Property Lease, dated as of March 1, 2019 (the “Property Lease”). The Corporation will lease the Leased Property back to the City pursuant to a Lease Agreement, dated as of March 1, 2019 (the “Lease Agreement”). The 2019A Certificates are payable solely from and secured by a portion of the lease payments (the “Tax-Exempt Lease Payments”) to be made by the City to the Corporation pursuant to the Lease Agreement. The 2019B Certificates are payable solely from and secured by a portion of the lease payments (the “Taxable Lease Payments” and, with the Tax-Exempt Lease Payments, the “Lease Payments”) to be made by the City to the Corporation pursuant to the Lease Agreement. See “SOURCE OF PAYMENT FOR THE CERTIFICATES” and “THE LEASED PROPERTY.”

Interest with respect to the Certificates is payable on May 1 and November 1 of each year, commencing November 1, 2019. The Certificates will mature in the amounts and on the dates and be payable at the interest rates shown on the inside cover of this Official Statement. See “THE CERTIFICATES.”

The Certificates will be delivered in fully registered form only, in the name of Cede & Co., as nominee of the Depository Trust Company, New York, New York (“DTC”). DTC will act as the depository for the Certificates and all payments due with respect to the Certificates will be made to Cede & Co., DTC’s nominee. Ownership interests in the Certificates may be purchased only in book-entry form. See “THE CERTIFICATES—Book-Entry System” and APPENDIX F—DTC’S BOOK-ENTRY ONLY SYSTEM.

Source of Payment for the Certificates

The Certificates represent direct, undivided interests of the Owners thereof in the Lease Payments to be paid by the City to the Corporation pursuant to the Lease Agreement. The Lease Payments are payable by the City from its general fund for the right to use and possess the Leased Property. The Lease Payments are subject to abatement during any period in which by reason of damage or destruction there is substantial interference with the use and occupancy by the City of the Leased Property or any portion thereof. The City will covenant under the Lease Agreement to take such action as necessary to include the Lease Payments in its annual budget and to make all necessary appropriations therefor (subject to abatement under certain circumstances described in the Lease Agreement). Pursuant to an Assignment Agreement, dated as of March 1, 2019 (the “Assignment Agreement”), by and between the Corporation and the Trustee, the Corporation will assign to the Trustee, for the benefit of the Owners of the Certificates, certain of its rights under the Lease Agreement, including its right to receive Lease Payments from the City. See “SOURCE OF PAYMENT FOR THE CERTIFICATES” and “RISK FACTORS.”

A reserve fund will *not* be funded for the Certificates.

NEITHER THE CERTIFICATES NOR THE OBLIGATION OF THE CITY TO MAKE LEASE PAYMENTS UNDER THE LEASE AGREEMENT CONSTITUTES A DEBT OR INDEBTEDNESS OF THE CITY OR THE STATE OF CALIFORNIA (THE “STATE”) OR ANY POLITICAL SUBDIVISION THEREOF WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATIONS OR RESTRICTION OR 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

Redemption

The Certificates are subject to optional and mandatory prepayment. See “THE CERTIFICATES—Prepayment.”

The City

The City is located in northern Santa Clara County (the “County”), approximately 35 miles south of the City of San Francisco. It is part of the San Francisco Bay metropolitan area. The City was incorporated in 1894. Its first Charter was granted by the State in 1909, and the City continues to operate

as a charter city. The City shares its borders with East Palo Alto, Mountain View, Los Altos, Los Altos Hills, Stanford, Portola Valley, and Menlo Park. The City's current population is approximately 69,721. The City's adopted fiscal year 2018-19 general fund budget projects total revenue of \$194.725 million. See "THE CITY," "CITY FINANCIAL INFORMATION" and APPENDIX A—GENERAL, ECONOMIC AND DEMOGRAPHIC INFORMATION RELATING TO THE CITY AND THE COUNTY.

Continuing Disclosure

The City will covenant in two substantially identical Continuing Disclosure Certificates to prepare and deliver annual reports to the Municipal Securities Rulemaking Board (the "MSRB") through the MSRB's Electronic Municipal Market Access system. See "CONTINUING DISCLOSURE" and APPENDIX G—FORMS OF CONTINUING DISCLOSURE CERTIFICATES.

Summaries of Documents

This Official Statement contains descriptions of the Certificates, the Trust Agreement, the Property Lease, the Lease Agreement, the Assignment Agreement and various other agreements and documents. The descriptions and summaries of documents herein do not purport to be comprehensive or definitive and reference is made to each such document for the complete details of all terms and conditions. All statements herein are qualified in their entirety by reference to each such document and, with respect to certain rights and remedies, to laws and principles of equity relating to or affecting creditors' rights generally. Copies of the various documents described herein are available for inspection during business hours at the corporate trust office of the Trustee at One California Street, Suite 1000, San Francisco, CA 94111.

Other Information

This Official Statement speaks only as of its date as set forth on the cover hereof, 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 create any implication that there has been no change in the affairs of the City since the date hereof.

Unless otherwise expressly noted, all references to internet websites in this Official Statement, including without limitation, the City's website, are shown for reference and convenience only and none of their content is incorporated herein by reference. The information contained within such websites has not been reviewed by the City and the City makes no representation regarding the accuracy or completeness of the information therein.

ESTIMATED SOURCES AND USES OF FUNDS

The following table shows the estimated sources and uses of the proceeds from the sale of the Certificates and other moneys:

	2019A Certificates	2019B Certificates	Total
Sources			
Par Amount of the Certificates	\$26,785,000.00	\$10,585,000.00	\$37,370,000.00
Plus: Original Issue Premium	4,926,606.10	—	4,926,606.10
Total Sources	\$31,711,606.10	\$10,585,000.00	\$42,296,606.10
Uses			
Deposit to the Tax-Exempt Account of the Construction Fund ⁽¹⁾	\$31,496,250.00	—	\$31,496,250.00
Deposit to the Taxable Account of the Construction Fund ⁽¹⁾	—	\$10,498,750.00	10,498,750.00
Costs of Issuance ⁽²⁾	215,356.10	86,250.00	301,606.10
Total Uses	\$31,711,606.10	\$10,585,000.00	\$42,296,606.10

⁽¹⁾ Amounts deposited in the Tax-Exempt Account and the Taxable Account of the Parking Garage Construction Fund will be used to finance the Project. See “THE PROJECT.”

⁽²⁾ Costs of Issuance include the Underwriter’s discount, fees and expenses of the municipal advisor, special counsel, disclosure counsel and the Trustee, printing expenses, rating fees, title insurance and other costs.

THE PROJECT

Proceeds of the Certificates will be used to (a) finance the costs of the Project and (b) pay a portion of the delivery costs incurred in connection with the execution, delivery and sale of the Certificates.

The Project consists of construction of the California Avenue Parking Garage at 350 Sherman Avenue in the City. Construction of the garage is a key step in the delivery of a new Public Safety Building. The Public Safety Building will be built on the adjacent property at 250 Sherman Avenue that currently provides approximately 150 public parking stalls. The proposed parking garage will be located on the City’s existing surface Parking Lot C-7. The parking garage will include four levels above grade and two stories below grade, with 636 public parking spaces serving the needs of the California Avenue business district. Construction will involve a cut-off wall to limit groundwater impact, cast-in-place post-tensioned structural concrete, and provisions for an integrated solar canopy.

THE LEASED PROPERTY

Pursuant to the Property Lease, the City will lease the Leased Property to the Corporation. Pursuant to the Lease Agreement, the Corporation will, in turn, lease the Leased Property back to the City. See APPENDIX E—SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS—Property Lease and APPENDIX E—SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS—Lease Agreement.

The Leased Property consists, initially, of the City’s Rinconada Library. The Rinconada Library (formerly the Main Library), was designed by Edward Durell Stone, and opened in 1958 following a voter approved bond measure that also funded the construction of the Mitchell Park Library. The library is located on Newell Road across from the Palo Alto Art Center. The building is 28,716 square feet,

including a 5,000 square foot basement. This library has the largest collection in the system, including the principal reference collection and the archives of the Palo Alto Historical Association. It serves primarily adults and teens and has a very small children's collection.

While the building has received small remodels over the years, it needed a total renovation to bring it up to current codes and standards and to provide spaces to accommodate needs of its users. In 2014, an over \$21.7 million renovation occurred that was funded by voter approved \$76 million General Obligation bonds. The renovation brought the building to current codes and standards and included significant seismic improvements. A new wing was built off of the south entrance including a meeting room seating 100, additional restrooms, four small group study rooms, a dedicated room for teens, upgraded lighting and electrical systems to support use of technology, new mechanical systems, including radiant heating and cooling system in the floor, and new carpet and paint.

The value of the Leased Property, including the real property, is approximately \$62,000,000.

Upon the construction and the substantial readiness of the Project for use and occupancy by the City, as shall be evidenced by a certificate of completion delivered by the City, the Project will be the Leased Property subject to the Property Lease and the Lease Agreement, and the Rinconada Library initial Leased Property, will be released.

For a description of certain terms of the Lease Agreement see "SOURCE OF PAYMENT FOR THE CERTIFICATES" and APPENDIX E—SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS—LEASE AGREEMENT.

Pursuant to the Lease Agreement, the City may substitute the Leased Property, in whole or in part, by other properties, upon the satisfaction of certain conditions. For more information regarding the substitution of property see "SOURCE OF PAYMENT FOR THE CERTIFICATES—Substitution or Removal of Leased Property" and APPENDIX E—SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS—LEASE AGREEMENT.

The City has not granted any security interest in the Leased Property for the benefit of the Certificates and there is no remedy of foreclosure on the Leased Property upon the occurrence of an Event of Default under the Lease Agreement. For a discussion of remedies upon an Event of Default under the Lease Agreement, see "RISK FACTORS—Limitations on Remedies."

DEBT SERVICE SCHEDULE

The following table shows the scheduled annual debt service for the Certificates:

Principal Payment Date (November 1)	2019A Certificates			2019B Certificates			Total
	Principal (1)	Interest (2)	Total	Principal (1)	Interest (2)	Total	
2019	—	\$ 818,430.56	\$ 818,430.56	\$ 375,000	\$ 260,911.87	\$ 635,911.87	\$ 1,454,342.43
2020	—	1,339,250.00	1,339,250.00	630,000	417,451.70	1,047,451.70	2,386,701.70
2021	—	1,339,250.00	1,339,250.00	645,000	400,870.10	1,045,870.10	2,385,120.10
2022	\$ 310,000	1,339,250.00	1,649,250.00	355,000	383,248.70	738,248.70	2,387,498.70
2023	690,000	1,323,750.00	2,013,750.00	—	373,315.80	373,315.80	2,387,065.80
2024	720,000	1,289,250.00	2,009,250.00	—	373,315.80	373,315.80	2,382,565.80
2025	760,000	1,253,250.00	2,013,250.00	—	373,315.80	373,315.80	2,386,565.80
2026	795,000	1,215,250.00	2,010,250.00	—	373,315.80	373,315.80	2,383,565.80
2027	835,000	1,175,500.00	2,010,500.00	—	373,315.80	373,315.80	2,383,815.80
2028	880,000	1,133,750.00	2,013,750.00	—	373,315.80	373,315.80	2,387,065.80
2029	920,000	1,089,750.00	2,009,750.00	—	373,315.80	373,315.80	2,383,065.80
2030	970,000	1,043,750.00	2,013,750.00	—	373,315.80	373,315.80	2,387,065.80
2031	1,015,000	995,250.00	2,010,250.00	—	373,315.80	373,315.80	2,383,565.80
2032	1,065,000	944,500.00	2,009,500.00	—	373,315.80	373,315.80	2,382,815.80
2033	1,120,000	891,250.00	2,011,250.00	—	373,315.80	373,315.80	2,384,565.80
2034	1,175,000	835,250.00	2,010,250.00	—	373,315.80	373,315.80	2,383,565.80
2035	1,235,000	776,500.00	2,011,500.00	—	373,315.80	373,315.80	2,384,815.80
2036	1,295,000	714,750.00	2,009,750.00	—	373,315.80	373,315.80	2,383,065.80
2037	1,360,000	650,000.00	2,010,000.00	—	373,315.80	373,315.80	2,383,315.80
2038	1,430,000	582,000.00	2,012,000.00	—	373,315.80	373,315.80	2,385,315.80
2039	1,500,000	510,500.00	2,010,500.00	—	373,315.80	373,315.80	2,383,815.80
2040	1,575,000	435,500.00	2,010,500.00	—	373,315.80	373,315.80	2,383,815.80
2041	1,655,000	356,750.00	2,011,750.00	—	373,315.80	373,315.80	2,385,065.80
2042	1,740,000	274,000.00	2,014,000.00	—	373,315.80	373,315.80	2,387,315.80
2043	1,825,000	187,000.00	2,012,000.00	—	373,315.80	373,315.80	2,385,315.80
2044	1,915,000	95,750.00	2,010,750.00	—	373,315.80	373,315.80	2,384,065.80
2045	—	—	—	2,010,000	373,315.80	2,383,315.80	2,383,315.80
2046	—	—	—	2,095,000	285,860.70	2,380,860.70	2,380,860.70
2047	—	—	—	2,190,000	194,707.26	2,384,707.26	2,384,707.26
2048	—	—	—	2,285,000	99,420.36	2,384,420.36	2,384,420.36
Total	\$26,785,000	\$22,609,430.56	\$49,394,430.56	\$10,585,000	\$10,628,734.09	\$21,213,734.09	\$70,608,164.65

(1) Principal payments with respect to the Certificates on each November 1 are derived from Lease Payments made by the City on the preceding October 15. Includes sinking fund payments.

(2) Interest payments with respect to the Certificates on each May 1 and November 1 are derived from Lease Payments made by the City on the preceding April 15 and October 15, respectively.

THE CERTIFICATES

General

The Certificates will be executed and delivered in the aggregate principal amount and will mature on the dates and interest with respect thereto will be payable at the rates per annum as set forth on the inside cover page of this Official Statement. The Certificates will be delivered in the form of fully registered Certificates without coupons in the denomination of \$5,000 or any integral multiple thereof. Interest with respect to the Certificates will be calculated on the basis of a 360-day year of twelve 30-day months and will be payable on May 1 and November 1 of each year, commencing November 1, 2019 (each an “Interest Payment Date”), until maturity or earlier prepayment thereof. The Certificates will be initially executed, delivered and registered in the name of “Cede & Co.” as nominee of DTC and will be evidenced by one Certificate maturing on each of the maturity dates in a denomination corresponding to the total principal therein designated to mature on such date. See “THE CERTIFICATES—Book-Entry System” and APPENDIX F—DTC’S BOOK-ENTRY ONLY SYSTEM.

Interest with respect to the Certificates will be payable from the Interest Payment Date next preceding the date of execution thereof, unless: (i) it is executed as of an Interest Payment Date, in which event interest with respect thereto shall be payable from such Interest Payment Date; or (ii) it is executed after a Record Date (i.e., the close of business on the 15th day of the month preceding each Interest Payment Date, whether or not such 15th day is a Business Day) and before the following Interest Payment Date, in which event interest with respect thereto shall be payable from such Interest Payment Date; or (iii) it is executed on or before October 15, 2019, in which event interest with respect thereto will be payable from its dated date; *provided, however*, that if, as of the date of execution of any Certificate, interest is in default with respect to any Outstanding Certificates, interest represented by such Certificate shall be payable from the Interest Payment Date to which interest has previously been paid or made available for payment with respect to the Outstanding Certificates. Payment of defaulted interest shall be paid by check mailed to the Owners as of a special record date to be fixed by the Trustee in its sole discretion, notice of which shall be given to the Owners not less than ten (10) days prior to such special record date.

Payment of interest due with respect to any Certificate on any Interest Payment Date will be made to the person appearing on the Registration Books as the Owner thereof as of the Record Date immediately preceding such Interest Payment Date, such interest to be paid by check mailed on the Interest Payment Date by first class mail to such Owner at his or her address as it appears on the Registration Books as of such Record Date or, upon written request filed with the Trustee prior to the Record Date by an Owner of at least \$1,000,000 in aggregate principal amount of Certificates, by wire transfer in immediately available funds to an account in the United States designated by such Owner in such written request. Any such written request shall remain in effect until rescinded in writing by the Owner. The principal and prepayment price with respect to the Certificates at maturity or upon prior prepayment shall be payable by check denominated in lawful money of the United States of America upon surrender of the Certificates at the Principal Corporate Trust Office.

Prepayment

Optional Prepayment.

2019A Certificates. The 2019A Certificates maturing on or before November 1, 2028, are not subject to optional prepayment prior to maturity. The 2019A Certificates maturing on and after November 1, 2029, are subject to optional prepayment in whole or in part in such order of maturity as shall be designated by the City and by lot within a maturity, on any date on or after November 1, 2028, at a prepayment price equal to the principal amount of the 2019A Certificates to be redeemed, together with accrued interest, without premium, to the date fixed for prepayment, from the proceeds of the optional prepayment of Tax-Exempt Lease Payments made by the City pursuant to the Lease Agreement.

2019B Certificates. The 2019B Certificates maturing on or before November 1, 2022, are not subject to optional prepayment prior to maturity. The 2019B Certificates maturing on November 1, 2048, are subject to optional prepayment in whole or in part by lot, on any date on or after November 1, 2028, at a prepayment price equal to the principal amount of the 2019B Certificates to be redeemed, together with accrued interest, without premium, to the date fixed for prepayment, from the proceeds of the optional prepayment of Taxable Lease Payments made by the City pursuant to the Lease Agreement.

Mandatory Sinking Fund Prepayment.

2019A Certificates. The 2019A Certificates maturing on November 1, 2044, are subject to mandatory prepayment in part on November 1, 2040, and on each November 1 thereafter, to and including November 1, 2044, from the principal components of scheduled Tax-Exempt Lease Payments required to be paid by the City pursuant to the Lease Agreement with respect to each such prepayment date (subject to abatement, as set forth in the Lease Agreement), at a prepayment price equal to the principal amount thereof to be redeemed, together with accrued interest to the date fixed for prepayment, without premium, as follows:

Year (November 1)	Principal Amount of 2019A Certificates to be Redeemed
2040	\$1,575,000
2041	1,655,000
2042	1,740,000
2043	1,825,000
2044†	1,915,000

†Maturity.

2019B Certificates. The 2019B Certificates maturing on November 1, 2048, are subject to mandatory prepayment in part on November 1, 2045, and on each November 1 thereafter, to and including November 1, 2048, from the principal components of scheduled Taxable Lease Payments required to be paid by the City pursuant to the Lease Agreement with respect to each such prepayment date (subject to abatement, as set forth in the Lease Agreement), at a prepayment price equal to the principal amount thereof to be redeemed, together with accrued interest to the date fixed for prepayment, without premium, as follows:

Year (November 1)	Principal Amount of 2019B Certificates to be Redeemed
2045	\$2,010,000
2046	2,095,000
2047	2,190,000
2048†	2,285,000

†Maturity.

Prepayment from Net Proceeds of Insurance and Condemnation. The Certificates are also subject to prepayment on any date, in whole or in part, from the net proceeds of insurance or condemnation with respect to the Leased Property, which Net Proceeds are deposited in the accounts within the Lease Payment Fund, on a *pro rata* basis, and credited towards the prepayment of the Lease Payments made by the City pursuant to the Lease Agreement, at a prepayment price equal to the principal amount of the Certificates to be prepaid, together with accrued interest to the date fixed for prepayment, without premium.

Selection of Certificates for Prepayment. Whenever provision is made for the prepayment of Certificates and less than all Outstanding Certificates are called for prepayment, the Trustee shall select Certificates for prepayment from the Outstanding Certificates not previously called for prepayment, among maturities in integral multiples of \$5,000 and by lot within a maturity in any manner deemed appropriate by the Trustee. For the purposes of such selection, Certificates shall be deemed to be composed of \$5,000 portions, and any such portion may be separately prepaid. The Trustee shall promptly notify the City and the Corporation in writing of the Certificates so selected for prepayment.

Notice of Prepayment. When prepayment is authorized or required pursuant to the Trust Agreement, the Trustee shall give notice of the prepayment of the Certificates. Such notice shall specify: (a) that the Certificates or a designated portion thereof are to be prepaid, (b) the date of prepayment, (c) the place or places where the prepayment will be made, and (d) that the City has the right to rescind the notice as provided below. Such notice shall further state that on the specified date there shall become due and payable upon each Certificate, the principal together with interest accrued to said date, and that from and after such date interest represented thereby shall cease to accrue and be payable.

Notice of such prepayment shall be mailed by first class mail to the respective Owners of Certificates designated for prepayment at their addresses appearing on the Registration Books, at least thirty (30) days but not more than forty-five (45) days prior to the prepayment date, which notice shall, in addition to setting forth the above information, set forth, in the case of each Certificate called only in part, the portion of the principal thereof which is to be prepaid; provided that neither failure to receive such notice so mailed nor any defect in any notice so mailed shall affect the sufficiency of the proceedings for the prepayment of such Certificates.

The City has the right to rescind any notice of the optional prepayment of Certificates by written notice to the Trustee on or prior to the date fixed for prepayment. Any notice of optional prepayment shall be cancelled and annulled if for any reason funds will not be or are not available on the date fixed for prepayment for the payment in full of the Certificates then called for prepayment, and such cancellation shall not constitute an Event of Default. The City and the Trustee have no liability to the Owners or any other party related to or arising from such rescission of prepayment. The Trustee shall mail notice of such rescission of prepayment to the respective Owners of the Certificates designated for prepayment at their

respective addresses appearing on the Registration Books, and to DTC and the Municipal Securities Rulemaking Board.

Partial Prepayment of Certificate. Upon surrender of any Certificate prepaid in part only, the Trustee shall execute and deliver to the Owner thereof, at the expense of the City, a new Certificate or Certificates of authorized denominations equal in aggregate principal amount to the unprepaid portion of the Certificate surrendered and of the same interest rate and the same maturity.

Effect of Notice of Prepayment. Notice having been given in compliance with the Trust Agreement, and moneys for the prepayment (including the interest to the applicable date of prepayment and including any applicable premium), having been set aside in the Lease Payment Fund, the Certificates shall become due and payable on said date of prepayment, and, upon presentation and surrender thereof at the Corporate Trust Office of the Trustee, said Certificates shall be paid at the unpaid principal amount (or applicable portion thereof) with respect thereto, plus interest accrued and unpaid to said date of prepayment.

If, on said date of prepayment, moneys for the prepayment of all the Certificates to be prepaid, together with interest to said date of prepayment, shall be held by the Trustee so as to be available therefor on such date of prepayment, and, if notice of prepayment thereof shall have been given as aforesaid, then, from and after said date of prepayment, interest represented by said Certificates shall cease to accrue and become payable. All moneys held by or on behalf of the Trustee for the prepayment of Certificates shall be held in trust for the account of the Owners of the Certificates so to be prepaid.

Transfer and Exchange of Certificates

The registration of any Certificate 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 his duly authorized attorney, upon surrender of such Certificate for cancellation at the Corporate Trust Office of the Trustee, accompanied by delivery of a written instrument of transfer in a form acceptable to the Trustee, duly executed. Whenever any Certificate or Certificates shall be surrendered for registration of transfer, the Trustee shall execute and deliver a new Certificate or Certificates of the same maturity and aggregate principal amount of the same series, in any authorized denominations.

Certificates may be exchanged at the Corporate Trust Office of the Trustee, for a like aggregate principal amount of Certificates of other authorized denominations of the same maturity and the same series. The City shall pay any costs of the Trustee incurred in connection with such exchange, except that the Trustee may require the payment by the Certificate Owner requesting such exchange of any tax or other governmental charge required to be paid with respect to such exchange.

Book-Entry System

The Certificates will be initially executed, delivered and registered as one fully registered certificate for each maturity, without coupons, in the name of Cede & Co., as nominee of DTC. DTC will act as securities depository of the Certificates. Individual purchases may be made in book-entry form only, in the principal amount of \$5,000 and integral multiples thereof. Purchasers will not receive physical certificates representing their interest in the Certificates purchased. Principal and interest will be paid to DTC which will in turn remit such principal and interest to its participants for subsequent disbursement to the beneficial owners of the Certificates as described herein. So long as DTC's book-entry system is in

effect with respect to the Certificates, notices to Owners of the Certificates by the City or the Trustee will be sent to DTC. Notices and communication by DTC to its participants, and then to the beneficial owners of the Certificates, will be governed by arrangements among them, subject to then effective statutory or regulatory requirements. See APPENDIX F—DTC’S BOOK-ENTRY ONLY SYSTEM.

In the event that such book-entry system is discontinued with respect to the Certificates, the City will cause the Trustee to execute and deliver replacements in the form of registered certificates and, thereafter, the Certificates will be transferable and exchangeable on the terms and conditions provided in the Trust Agreement.

SOURCE OF PAYMENT FOR THE CERTIFICATES

General

Each 2019A Certificate represents a direct, undivided fractional interest in the Tax-Exempt Lease Payments. Each 2019B Certificate represents a direct, undivided fractional interest in the Taxable Lease Payments. Pursuant to the Lease Agreement, the City will lease the Leased Property from the Corporation and agree to make Lease Payments. See “THE LEASED PROPERTY.” Upon satisfaction of certain conditions set forth in the Lease Agreement, the City may substitute the Leased Property with other properties. See “Substitution or Removal of Leased Property” and “Abatement” below.

As security for the Certificates, the Corporation will assign to the Trustee for the payment of principal and interest with respect to the Certificates, the Corporation’s rights, title and interest in the Lease Agreement (with certain exceptions), including the right to receive Lease Payments to be made by the City under the Lease Agreement. The Lease Payments are designed to be sufficient, in both time and amount, to pay when due, the principal and interest with respect to the Certificates. The Lease Payments are payable by the City from any source of legally available funds.

THE OBLIGATION OF THE CITY TO MAKE LEASE PAYMENTS UNDER THE LEASE AGREEMENT DOES NOT CONSTITUTE AN OBLIGATION OF THE CITY 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. NEITHER THE CERTIFICATES NOR THE OBLIGATION OF THE CITY TO MAKE LEASE PAYMENTS UNDER THE LEASE AGREEMENT CONSTITUTES AN INDEBTEDNESS OF THE CITY OR THE STATE OR ANY OF ITS POLITICAL SUBDIVISIONS WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATIONS.

Lease Payments; Covenant to Appropriate

Pursuant to the Lease Agreement, the City has agreed to make Lease Payments for the lease of the Leased Property. Lease Payments will be made by the City to the Trustee on April 15 and October 15 in each year, in advance of the corresponding May 1 and November 1 Interest Payment Dates. The City will also pay as additional payments (“Additional Payments”), amounts required for the payment of all costs and expenses incurred by the Corporation to comply with the provisions of the Trust Agreement or in connection with the execution and delivery of the Certificates. The City has covenanted under the Lease Agreement to take such action as may be necessary to include all Lease Payments in its annual budget and to make the necessary annual appropriations for all such payments. Under certain circumstances

described under the Lease Agreement, however, Lease Payments are subject to abatement during periods of substantial interference with the City's use and occupancy of the Leased Property or any portion thereof. See "SOURCE OF PAYMENT FOR THE CERTIFICATES—Abatement."

Insurance

The City is required to keep or cause to be kept casualty insurance against loss or damage by fire and lightning, with extended coverage and vandalism and malicious mischief insurance, in an amount at least equal to the lesser of (i) 100% of the replacement cost (without deducting for depreciation) of the Leased Property and (ii) the aggregate principal amount of Certificates at the time outstanding. Such insurance shall, 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.

To insure against loss of rental income caused by perils mentioned above, the City is required to maintain, or cause to be maintained throughout the term of the Lease Agreement, rental interruption or use and occupancy insurance to cover loss, total or partial, of the use of any part of the Leased Property as a result of any of the hazards described above in an amount at least equal to the maximum Lease Payments coming due and payable during any two consecutive fiscal years during the remaining term of the Lease Agreement.

Public liability and property damage insurance coverage is required in the minimum liability limits of \$1,000,000 for personal injury or death of each person and \$3,000,000 for personal injury or deaths of two or more persons in each accident or event, and in a minimum amount of \$150,000 (subject to a deductible clause of not to exceed \$250,000, or such higher amount as the City shall determine, provided that such higher deductible shall be considered a self-insured retention) for damage to property resulting from each accident or event. Such public liability and property damage insurance may, however, be in the form of a single limit policy in the amount of \$3,000,000 covering all such risks. Such liability insurance may be maintained as part of or in conjunction with any other liability insurance coverage carried by the City and may be maintained in the form of insurance maintained through a joint exercise of powers authority created for such purpose or in the form of self-insurance by the City. The net proceeds of such liability insurance shall be applied toward extinguishment or satisfaction of the liability with respect to which the insurance proceeds shall have been paid.

The City shall provide, from moneys in the Costs of Issuance Fund or at its own expense, on the Closing Date, a CLTA title insurance policy in the amount of not less than the principal amount of the Certificates, insuring the City's leasehold estate in the Leased Property, subject only to Permitted Encumbrances.

See APPENDIX E—SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS—LEASE AGREEMENT—Insurance.

Abatement

Pursuant to the Lease Agreement, the amount of Lease Payments will be abated, during any period in which by reason of damage or destruction (other than by eminent domain which is otherwise provided for) there is substantial interference with the use and occupancy by the City of the Leased Property or any portion thereof. The amount of such abatement shall be agreed upon by the City and the Corporation such that the resulting Lease Payments represent fair consideration for the use and

occupancy of the portions of the Leased Property not damaged or destroyed. Such abatement shall 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, the Lease Agreement shall continue in full force and effect and the City waives any right to terminate the Lease Agreement by virtue of any such damage and destruction. However, notwithstanding any other provisions of the Lease Agreement, there shall be no abatement of Lease Payments to the extent that the proceeds of an eminent domain or insurance award are available to pay Lease Payments, or to the extent that moneys are available in the Lease Payment Fund, it being declared that such proceeds and amounts constitute special funds for the payment of the Lease Payments. See “SOURCE OF PAYMENT FOR THE CERTIFICATES—Insurance,” APPENDIX E—SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS—Lease Agreement—Insurance and APPENDIX E—SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS—Lease Agreement—Abatement of Rental Payments in the Event of Damage or Destruction.

Eminent Domain

Pursuant to the Lease Agreement, 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 Agreement shall cease as of the day possession shall be so taken. If less than all of the Leased Property is taken permanently, or if the Leased Property or any part thereof shall be taken temporarily, under the power of eminent domain, (1) the Lease Agreement shall continue in full force and effect and shall not be terminated by virtue of such taking and the parties waive the benefit of any law to the contrary, and (2) there shall be a partial abatement of Lease Payments as a result of the application of the Net Proceeds of any eminent domain award to the prepayment of the Lease Payments, in an amount to be agreed upon by the City and the Corporation such that the resulting Lease Payments represent fair consideration for the use and occupancy of the remaining usable portion of the Leased Property. The City covenants to contest any eminent domain award which is insufficient to either: (i) prepay the Certificates in whole, if all of the Leased Property is condemned; or (ii) prepay a pro rata share of Certificates, in the event that less than all of the Leased Property is condemned.

No Reserve Fund

A reserve fund will *not* be funded for the Certificates.

Optional Prepayment

Pursuant to the Lease Agreement, the City has an option to prepay the principal components of the Lease Payments in full, by paying the aggregate unpaid principal components of the Lease Payments, in whole or in part, in a prepayment amount equal to the principal amount of Lease Payments to be prepaid, together with accrued interest to the date fixed for prepayment, without premium. See “THE CERTIFICATES—Prepayment—Optional Prepayment.”

Said option may be exercised on any date on or after October 15, 2028. In the event of prepayment in part, the partial prepayment will be applied against Lease Payments in such order of payment date as will be selected by the City. Lease Payments due after any such partial prepayment will be in the amounts set forth in a revised Lease Payment schedule which will be provided by, or caused to be provided by, the City to the Trustee and which will represent an adjustment to the schedule set forth in the Lease Agreement taking into account said partial prepayment.

Prepayment from Net Proceeds of Insurance and Condemnation

The City shall be obligated to prepay the Lease Payments for the Leased Property, in whole or in part on any date, from and to the extent of any Net Proceeds of insurance award or condemnation award with respect to the Leased Property that have been deposited with the Trustee in the Lease Payment Fund for such purpose. Such proceeds shall be applied to the prepayment of the principal component of the Lease Payments and the prepayment of the Certificates. See “THE CERTIFICATES—Prepayment—Prepayment from Net Proceeds of Insurance and Condemnation.”

Substitution or Removal of Leased Property

Substitution of Leased Property. The City has the option at any time and from time to time during the term of the Lease Agreement, to substitute other land, facilities, improvements or other property (a "Substitute Property") for the Leased Property or any portion thereof (a "Former Property"), provided that the City shall satisfy all of the following requirements which are hereby declared to be conditions precedent to such substitution:

(a) The City shall notify S&P in writing of such substitution, which notice shall contain the certification that all conditions for such substitution, as set forth in the Lease Agreement, are met with respect to such substitution;

(b) The City shall take all actions and shall execute all documents required to subject such Substitute Property to the terms and provisions of the Lease Agreement, including the filing with the Corporation and the Trustee of an amendment to the Lease Agreement which adds thereto a description of such Substitute Property and deletes therefrom the description of such Former Property, and including the recordation of the Lease Agreement or a memorandum hereof with respect to such Substitute Property in the office of the County Recorder;

(c) The City shall certify in writing that the estimated fair market value of such Substitute Property is at least equal to the aggregate principal components of the unpaid Lease Payments;

(d) The City shall certify in writing to the Corporation and the Trustee that such Substitute Property serves the public purposes of the City and constitutes property which the City is permitted to lease under the laws of the State;

(e) The City shall certify in writing to the Corporation and the Trustee that the estimated useful life of such Substitute Property at least extends to the date on which the final Lease Payment becomes due and payable hereunder;

(f) The City shall obtain a CLTA policy of title insurance meeting the requirements of the Lease Agreement with respect to such Substitute Property; and

(g) The Substitute Property shall not cause the City to violate any of its covenants, representations and warranties made in the Lease Agreement or in the Trust Agreement.

From and after the date on which all of the foregoing conditions precedent to such substitution are satisfied, the term of the Lease Agreement shall cease with respect to the Former Property and shall be

continued with respect to the Substitute Property, and all references herein to the Former Property shall apply with full force and effect to the Substitute Property. The City shall not be entitled to any reduction, diminution, extension or other modification of the Lease Payments whatsoever as a result of such substitution.

Notwithstanding any provision of the Lease Agreement the Trust Agreement, upon final completion of the Project, the City shall have the absolute right to make the Project and its related site the Leased Property, and to release the Rinconada Library initial Leased Property without meeting the conditions set forth in paragraphs (a) through (g) above. The City shall effectuate such release by (1) certifying, in a certificate of completion provided to the Trustee, that the final completion of the Project has occurred, (2) certifying that the fair rental value of the Project is at least equal to base lease payments, and (3) causing a Notice of Substitution and Release of Leased Property to be recorded in the real property records of Santa Clara County. Subsequent to the execution and recordation of such Notice of Substitution and Release of Leased Property, subject to any future authorized substitution or release of the Leased Property pursuant to the Lease Agreement, references to the Leased Property shall be deemed to refer to the Project and the related site and shall not be deemed to refer to the initial Leased Property so released.

Removal of Property from Leased Property. The City has the option at any time and from time to time during the term of the Lease Agreement, to remove any property from the description of the Leased Property, provided that the City shall satisfy all of the following requirements which are hereby declared to be conditions precedent to such removal:

(a) The City shall notify S&P in writing of such removal, which notice shall contain the certification that all conditions for such removal, as set forth in the Lease Agreement, are met with respect to such removal;

(b) The City shall file with the Corporation and the Trustee an amendment to the Lease Agreement which deletes therefrom the description of the property to be removed;

(c) The City shall certify in writing that the estimated fair market value of the Leased Property that will remain following such removal is at least equal to the aggregate principal components of the unpaid Lease Payments, and that the useful life of the Leased Property is not less than the final payment date of the unpaid Lease Payments; and

(d) The City shall obtain and cause to be filed with the Trustee and the Corporation an opinion of Bond Counsel stating that such removal is permitted under the Lease Agreement.

From and after the date on which all of the foregoing conditions precedent to such removal are satisfied, the term of the Lease shall cease with respect to the property which is so removed. The City shall not be entitled to any reduction, diminution, extension or other modification of the Lease Payments whatsoever as a result of such removal.

Events of Default and Remedies

The following shall be "events of default" under the Lease Agreement:

(a) Failure by the City to pay any Lease Payment when due and payable, or failure to pay any other payment when due and payable.

(b) Failure by the City to observe and perform any covenant, condition or agreement on its part to be observed or performed, other than as referred to in paragraph (a) above, for a period of thirty (30) days after written notice specifying such failure and requesting that it be remedied has been given to the City by the Corporation, the Trustee or the Owners of not less than twenty percent (20%) in aggregate principal amount of Certificates then outstanding; *provided, however*, if the failure stated in the notice can be corrected, but not within the applicable period, the Corporation, the Trustee and such Owners shall not unreasonably withhold their consent to an extension of such time if corrective action is instituted by the City within the applicable period and diligently pursued until the default is corrected.

(c) The filing by the City of a voluntary petition in bankruptcy under Title 11 of the United States Code or any substitute or successor statute.

Whenever any event of default shall have happened and be continuing, it shall be lawful for the Corporation to exercise any and all remedies available pursuant to law or granted pursuant to this Lease Agreement; *provided, however*, that notwithstanding anything in the Lease Agreement or in the Trust Agreement to the contrary, there shall be no right under any circumstances to accelerate the Lease Payments or otherwise declare any Lease Payments not then in default to be immediately due and payable. Each and every covenant to be kept and performed by the City under the Lease Agreement is expressly made a condition and upon the breach thereof the Corporation may exercise any and all rights of entry and re-entry upon the Leased Property, and also, at its option, with or without such entry, may terminate the Lease Agreement. In the event of such default and notwithstanding any re-entry by the Corporation, the City shall, as expressly provided in the Lease Agreement, continue to remain liable for the payment of the Lease Payments and/or damages for breach of the Lease Agreement and the performance of all conditions contained in the Lease Agreement and, in any event, such rent and/or damages shall be payable to the Corporation at the time and in the manner as provided in the Lease Agreement.

Amendment of Lease Agreement

Except as provided below, without the prior written consent of the Trustee, the City will not alter, modify or cancel, or agree or consent to alter, modify or cancel the Lease Agreement, excepting only such alteration or modification as may be permitted by the Trust Agreement.

In addition, the Lease Agreement may be amended to obligate the City to pay additional amounts of rental thereunder for the use and occupancy of the Leased Property or any portion thereof, but only if (a) such additional amounts of rental do not cause the total rental payments made by the City under the Lease Agreement to exceed the fair rental value of the Leased Property, (b) the City shall have obtained and filed with the Trustee and the Corporation a written certificate to the effect that the estimated fair market value thereof is not less than the aggregate unpaid principal components of such additional amount of rental plus the existing aggregate unpaid principal components of the Lease Payments, (c) such additional amounts of rental shall be pledged or assigned for the payment of any bonds, notes, leases or other obligations the proceeds of which shall be applied to finance the completion of public facilities and

(d) the City shall send notification of the additional financing to the rating agency then rating the Certificates.

THE CITY

The City is located in the northern portion of the County, approximately 35 miles south of the City of San Francisco. It is part of the San Francisco Bay metropolitan area. The City is considered the birthplace of the high technology industry and a center of the Silicon Valley. Stanford University covers a 700-acre area in the City, and the City is home to high-tech leaders such as Hewlett-Packard, SAP America, Varian Medical Systems, VMware, Tibco Software, the Electric Power Research Institute, Communications and Power Industries and Skype. The City is also a major employment center, including U.S. Department of Veterans Affairs, Palo Alto Health Care System, Stanford Hospitals and Clinics, Lockheed Martin Missiles and Space, Palo Alto Medical Foundation, Stanford Shopping Center, the law offices of Wilson Sonsini Goodrich and Rosati, and the Xerox Palo Alto Research Center.

The City was incorporated in 1894. Its first Charter was granted by the State in 1909, and the City continues to operate as a charter city. Municipal operations are conducted under the Council-Manager form of government. The seven City Council Members are elected at large for four-year, staggered terms. The Mayor and Vice Mayor are elected annually at the first City Council meeting in January. The Mayor presides over all City Council meetings. The City Manager is responsible for the operation of all municipal functions, except the offices of the City Attorney, City Clerk, and City Auditor. These officials are appointed by, and report directly to, the City Council.

See APPENDIX A—GENERAL, ECONOMIC AND DEMOGRAPHIC INFORMATION RELATING TO THE CITY AND THE COUNTY for a general description of the City as well as certain demographic and statistical information.

CITY FINANCIAL INFORMATION

Financial Statements and Budgetary Process

The City's accounting policies conform to generally accepted accounting principles. The audited financial statements also conform to the principles and standards for public financial reporting established by the Governmental Accounting Standards Board.

Basis of Accounting and Financial Statement Presentation. The government-wide financial statements are reported using the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures are recorded only when payment is due.

Audited Financial Statements. The City retained the firm of Macias Gini & O’Connell LLP (MGO), Walnut Creek, California (the “City’s Auditor”), to examine the general purpose financial statements of the City as of and for the year ended June 30, 2018. The audited financial statements for fiscal year ended June 30, 2018, are included in APPENDIX B—COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY FOR THE YEAR ENDED JUNE 30, 2018. The City has not requested, and the City’s Auditor has not provided, any review or update of such financial statements in connection with their inclusion in this Official Statement.

Budget Process. The City Council adopts an annual budget with appropriations for all City funds prior to the beginning of the fiscal year, which begins on July 1 of each year. The City Council has the legal authority to amend the budget at any time during the fiscal year. The City maintains budgetary controls to ensure compliance with legal provisions embodied in the appropriated budget approved by the City Council. The level of budgetary control (that is, the level at which expenditures cannot legally exceed the appropriated amount) for the City’s operating budget is at the fund level. For the operating budget, the City Manager has the authority to move appropriations between accounts (without dollar limitation) within a budget program and within the same fund. All other appropriation changes require the approval of the City Council.

All appropriations lapse at the end of the fiscal year unless specific carryovers are approved by the City Council.

The following table shows the City's audited general fund balance sheet for fiscal years 2013-14 through 2017-18.

Table 1
General Fund Balance Sheet
Fiscal Years 2013-14 through 2017-18
(Dollars in Thousands)

	FY2013-14 Audited	FY2014-15 Audited	FY2015-16 Audited	FY2016-17 Audited	FY2017-18 Audited
ASSETS					
Cash and Investments	\$ 42,013	\$ 54,730	\$ 53,113	\$ 47,779	\$ 49,250
Accounts and Intergovernmental Receivables	8,761	10,197	15,676	17,418	18,881
Interest Receivable	642	525	640	738	950
Notes and Loans Receivable	900	868	513	496	479
Prepaid Items	352	66	-	-	-
Deposits	-	-	-	-	15
Advance to Other Funds	935	1,695	2,211	2,915	3,128
Inventory of Materials and Supplies	4,001	3,667	4,364	4,298	4,427
Total Assets	57,604	71,748	76,517	73,644	77,130
LIABILITIES					
Accounts Payable and Accruals	4,094	3,647	3,832	4,984	4,293
Accrued Salaries and Benefits	2,852	3,114	3,859	1,466	1,525
Unearned Revenue	2,348	2,517	1,895	4,087	2,966
Total Liabilities	9,294	9,278	9,586	10,537	8,784
FUND BALANCES					
Nonspendable:					
Notes and Loans Receivable	900	868	513	496	479
Prepaid Items	352	66	-	-	-
Deposits	-	-	-	-	15
Inventories	4,001	3,667	4,364	4,298	4,427
Advances to Other Funds	935	1,695	2,211	2,915	3,128
Committed for:					
Development Services	-	-	-	-	373
Assigned for:					
Unrealized Gain on Investments	672	671	2,066	-	-
Other General Governmental Purposes	4,760	5,605	6,195	6,150	5,325
Reappropriations	1,607	1,700	-	1,130	1,773
Unassigned for:					
Budget Stabilization	35,083	48,198	51,582	48,118	52,826
Total Fund Balances	48,310	62,470	66,931	63,107	68,346
Total Liabilities and Fund Balances	57,604	71,748	76,517	73,644	77,130

Sources: City of Palo Alto 2013-14 through 2017-18 CAFRs and City of Palo Alto.

The following table shows the City's audited general fund revenues, expenditures and changes in fund balances for fiscal years 2014-15 through 2017-18 and the City's adopted budget for fiscal year 2018-19.

Table 2
General Fund Statement of Revenue, Expenditures and Changes in Fund Balances
Fiscal Years 2014-15 through 2017-18 and Adopted Budget for Fiscal Year 2018-19
(Dollars in Thousands)

	FY2014-15 Audited	FY2015-16 Audited	FY2016-17 Audited	FY2017-18 Audited	FY2018-19 Budget
REVENUES					
Property Tax	\$ 34,117	\$ 36,607	\$ 39,381	\$ 42,839	\$ 45,332
Sales Tax	29,675	30,018	29,923	31,091	31,246
Utility Users Tax	10,861	12,469	14,240	15,414	16,092
Transient Occupancy Tax	16,699	22,366	23,477	24,937	25,049
Documentary Transfer Tax	10,384	6,266	7,491	9,229	7,434
Other Taxes and Fines	1,900	2,238	2,167	2,141	2,032
Charges for Services	25,973	23,910	22,267	26,824	28,015
From Other Agencies	3,712	3,190	2,758	3,205	1,150
Permits and Licenses	7,056	7,912	7,437	8,560	8,949
Investment Earnings	1,177	2,494	(1,193)	(828)	1,166
Rental Income	14,911	15,769	15,692	15,896	15,806
Other Revenue	1,018	2,591	760	776	12,454
Total Revenues	157,483	165,830	164,400	180,084	194,725
EXPENDITURES					
City Council	270	330	316	337	488
City Manager	2,112	2,567	1,896	2,509	4,386
City Attorney	1,830	2,212	2,049	2,244	3,263
City Clerk	679	488	724	819	1,282
City Auditor	409	313	822	870	1,258
Administrative Services	3,746	3,545	4,975	5,347	7,963
Human Relations	1,570	1,843	2,194	2,369	3,634
Public Works	11,440	12,315	13,578	14,569	18,492
Planning and Community Environment	7,369	9,059	9,054	8,312	8,791
Development Services	11,152	10,643	10,908	11,749	12,561
Police ⁽¹⁾	61,226	35,247	39,597	40,326	41,951
Fire ⁽¹⁾	-(1)	28,312	31,419	33,522	33,335
Community Services	23,045	24,280	25,192	27,122	28,915
Library	7,980	7,960	8,953	9,120	9,664
Non-Departmental	5,578	5,680	5,906	5,973	3,961
Capital Outlay	-	-	-	-	-
Debt Service - Principal	383	395	406	416	461
Debt Service - Interest	46	36	26	16	325
Total Expenditures	138,835	145,225	158,015	165,620	180,730
EXCESS OF REVENUES OVER EXPENDITURES	18,648	20,605	6,385	14,464	13,995
OTHER FINANCING SOURCES					
Transfers In	17,796	18,317	19,222	20,310	19,772
Transfers Out	(22,284)	(34,461)	(29,431)	(29,535)	(30,898)
Total Other Financing Sources	(4,488)	(16,144)	(10,209)	(9,225)	(11,126)
Change in Fund Balances	14,160	4,461	(3,824)	5,239	2,869
FUND BALANCES, BEGINNING OF YEAR	48,310	62,470	66,931	63,107	68,346
FUND BALANCES, END OF YEAR	\$62,470	\$66,931	\$63,107	\$68,346	72,215

Sources: City of Palo Alto 2014-15 through 2017-18 CAFRs and City of Palo Alto 2018-19 Budget, adopted June 18, 2018.

(1) In fiscal year 2014-15 the Police and Fire totals were reported under a combined heading, Public Safety.

City Financial Management Policies

The City Council has adopted a comprehensive set of financial management policies to provide for: (i) establishing targeted general fund reserves; (ii) the prudent investment of City funds, and (iii) management of debt. The City’s practice is to incur debt only after deliberation over the effect of such debt on the City’s General Fund and other resources of the City, and in those circumstances where the use of debt would be appropriate to the scale and economic life of the asset being financed and the accumulation or availability of reserves to fund the capital requirement.

General Fund Budget Stabilization Reserve Policy. The following table shows the City’s general fund Budget Stabilization Reserve Policy guidance, actual reserves for fiscal year 2017-18 and budgeted reserve for fiscal year 2018-19.

Table 3
General Fund Budget Stabilization Reserve Policy

	Policy Guidance	Actual FY 2017-18	Budgeted FY 2018-19
% of Expenses	15% to 20%; target goal of 18.5%	20.1%	21.4%

Source: City of Palo Alto Finance Department.

Investment Policy. The investment of funds of the City (except pension and retirement funds) is made in accordance with the City’s Investment Policy, most recently approved in June 2017 (the “Investment Policy”), and section 53601 *et seq.* of the California Government Code. The Investment Policy is subject to revision at any time and is reviewed at least annually to ensure compliance with the stated objectives of safety, liquidity, yield, and current laws and financial trends. All amounts held under the Trust Agreement are invested at the direction of the City in Investment Securities, as defined in the Trust Agreement, and are subject to certain limitations contained therein. See APPENDIX C—INVESTMENT POLICY OF THE CITY and APPENDIX E—SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS—TRUST AGREEMENT—Investments.

Debt Management Policy. In accordance with section 8855(i) of the California Government Code the City adopted a debt management policy on April 11, 2017, to establish conditions for the use of debt; to ensure that debt capacity and affordability are adequately considered; to minimize the City’s interest and issuance costs; to maintain the highest possible credit rating; to provide complete financial disclosure and reporting; and to maintain financial flexibility for the City.

Capital Improvement Project Practices. While the City does not have an adopted capital improvement project policy, it does have certain criteria that must be adhered to before commencing a capital improvement project including (a) that the project must have a minimum cost of \$50,000 for each stand-alone unit or combined project, (b) that the project must have a useful life of at least five to seven years, and (c) that the project must extend the life of an existing asset or provide a new functional use for an existing asset for at least five years.

Current Investments

The City’s investment portfolio (par value), as of December 14, 2018, included cash and investments equal to \$521 million.

Principal Sources of General Fund Revenues

Property taxes were the single largest revenue source to the General Fund in fiscal year 2017-18, representing approximately 34% of revenues. Sales and use taxes represented approximately 24% of General Fund revenues. The City imposes a transient occupancy tax of 15.5% on short term (30 days or less) room rental. Transient occupancy tax represented approximately 19% of General Fund revenues in fiscal year 2017-18. For a discussion of potential State Budget impacts on general fund revenues, see “STATE BUDGET INFORMATION.” For a discussion of sales tax revenues and property taxes, see “—Sales and Use Taxes” and “—Property Taxes.”

In addition, the City receives the following local taxes:

Utility Users Tax. The Utility Users Tax is levied on electric, gas, and water consumption, as well as on telephone usage. Utility Users Tax represented approximately 12% of revenues in fiscal year 2017-18.

Documentary Transfer Tax. The Documentary Transfer Tax is based on the number and value of property sales.

The following table shows the City’s audited general fund tax revenues by source for the most recent four fiscal years and budgeted tax revenues for fiscal year 2018-19:

Table 4
Tax Revenues by Source
(Dollars in Thousands)

Source	FY2014-15 Audited	FY2015-16 Audited	FY2016-17 Audited	FY2017-18 Audited	FY2018-19 Budget
Property Tax	\$ 34,117	\$ 36,607	\$ 39,381	\$ 42,839	\$ 45,332
Sales Tax	29,675	30,018	29,923	31,091	31,246
Transient Occupancy Tax	16,699	22,366	23,477	24,937	25,049
Utility User Tax	10,861	12,469	14,240	15,414	16,092
Documentary Transfer Tax	10,384	6,266	7,491	9,229	7,434
Other Taxes and Fines	1,900	2,238	2,167	2,141	2,032
Total Revenues	\$103,636	\$109,964	\$116,679	\$125,651	\$127,185

Sources: City of Palo Alto fiscal years 2014-15 through 2017-18 CAFRs and City of Palo Alto fiscal year 2018-19 Budget, adopted June 18, 2018.

Property Taxes

Under Proposition 13, an amendment to the California Constitution adopted in 1978, the county assessor’s valuation of real property is established as shown on the fiscal year 1975-76 tax bill, or, thereafter, as the appraised value of real property when purchased, newly constructed, or a change in ownership has occurred. Assessed value of property may be increased annually to reflect inflation at a rate

not to exceed 2% per year or reduced to reflect a reduction in the consumer price index or comparable data for the area under taxing jurisdiction or in the event of declining property value caused by substantial damage, destruction, market forces or other factors. As a result of these rules, real property that has been owned by the same taxpayer for many years can have an assessed value that is much lower than that of similar properties more recently sold and may be lower than its own market value. Likewise, changes in ownership of property and reassessment of such property to market value commonly will lead to increases in aggregate assessed value even when the rate of inflation or consumer price index would not permit the full 2% increase on any property that has not changed ownership.

Taxes are levied by the County for each fiscal year on taxable real and personal property which is situated in the County as of the preceding January 1. Real property which changes ownership or is newly constructed is revalued at the time the change in ownership occurs or the new construction is completed. The current year property tax rate will be applied to the reassessment, and the taxes will then be adjusted by a proration factor to reflect the portion of the remaining tax year for which taxes are due.

Local agencies and schools will share the growth of “base” sources from the tax rate area. Each year’s growth allocation becomes part of each local agency’s allocation in the following year. The availability of revenue from growth in the tax bases in such tax rate areas may be affected by the existence of redevelopment agencies (including their successor agencies) which, under certain circumstances, may be entitled to sources resulting from the increase in certain property values. State law exempts \$7,000 of the assessed valuation of an owner-occupied principal residence. This exemption does not result in any loss of revenue to local agencies since an amount equivalent to the taxes that would have been payable on such exempt values is supplemented by the State.

For assessment and tax collection purposes, property is classified either as “secured” or “unsecured,” and is listed accordingly on separate parts of the assessment roll. The “secured roll” is that part of the assessment roll containing State-assessed property and property (real or personal) for which there is a lien on real property sufficient, in the opinion of the county assessor, to secure payment of the taxes. All other property is “unsecured,” and is assessed on the “unsecured roll.” Secured property assessed by the State Board of Equalization is commonly identified for taxation purposes as “utility” property.

Property taxes on the secured roll are due in two installments, on November 1 and February 1 of each fiscal year, and if unpaid become delinquent on December 10 and April 10, respectively. A penalty of 10% attaches immediately to any delinquent payment. Property on the secured roll, with respect to which taxes are delinquent, becomes tax defaulted on or about June 30 of the fiscal year. Such property may thereafter be redeemed by payment of delinquent taxes and the delinquency penalty, plus costs and prepayment penalty of one and one-half percent per month to the time of prepayment. If taxes are unpaid for a period of five years or more, the property is subject to sale by the county treasurer.

Property taxes on the unsecured roll are due as of the January 1 lien date and become delinquent, if unpaid, on August 31. A 10% penalty attaches to delinquent unsecured taxes. If unsecured taxes are unpaid at 5 p.m. on October 31, an additional penalty of one and one-half percent per month attaches to such taxes on the first day of each month until paid. A county has four ways of collecting delinquent unsecured personal property taxes: (1) bringing a civil action against the taxpayer; (2) filing a certificate in the office of the county clerk specifying certain facts in order to obtain a lien on certain property of the taxpayer; (3) filing a certificate of delinquency for record in the county clerk and county recorder’s office

in order to obtain a lien on certain property of the taxpayer; and (4) seizing and selling personal property, improvements, or possessory interests belonging or assessed to the delinquent taxpayer.

Alternative Method of Tax Apportionment. The Board of Supervisors of the County has approved the implementation of the Alternative Method of Distribution of Tax Levies and Collections and of Tax Sale Proceeds (the “Teeter Plan”), as provided for in section 4701 *et seq.* of the California Revenue and Taxation Code. The Teeter Plan guarantees distribution of 100% of the general taxes levied to the taxing entities within the County, with the County retaining all penalties and interest penalties affixed upon delinquent properties and redemptions of subsequent collections. Under the Teeter Plan, the County apportions secured property taxes on a cash basis to local political subdivisions, including the City, for which the County acts as the tax-levying or tax-collecting agency. At the conclusion of each fiscal year, the County distributes 100% of any taxes delinquent as of June 30th to the respective taxing entities.

The Teeter Plan is applicable to secured property tax levies. As adopted by the County, the Teeter Plan excludes Mello-Roos Community Facilities Districts, special assessment districts, and benefit assessment districts.

The Teeter Plan is to remain in effect unless the Board of Supervisors of the County 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 also, after holding a public hearing on the matter, discontinue the Teeter Plan with respect to any tax levying agency or assessment levying agency in the County if the rate of secured tax delinquency in that agency in any year exceeds 3% of the total of all taxes and assessments levied on the secured roll in that agency. If the Teeter Plan is discontinued subsequent to its implementation, only those secured property taxes actually collected would be allocated to political subdivisions (including the City) for which the County acts as the tax-levying or tax-collecting agency, but penalties and interest would be credited to the political subdivisions.

The City is not aware of any petitions for the discontinuance of the Teeter Plan in the County.

Assessed Valuation

The City uses the facilities of the County for property tax assessment and collection. City property taxes are assessed and collected at the same times and on the same tax rolls as County, school and special district taxes.

Under California law, two additional types of exemptions were authorized beginning in the tax year 1969-70. The first of these exempts 50% of the assessed valuation of business inventories from taxation. The second provides an exemption of \$7,000 of the assessed valuation of an owner-occupied dwelling from which application has been made to the County Assessor. Under a constitutional amendment that is effective in Fiscal Year 2018-19, the California Legislature can raise this exemption. Revenue estimated to be lost to local taxing agencies due to such exemption is reimbursed from State sources if funds are appropriated. The reimbursement is based upon total taxes due upon these exempt values and therefore is not reduced by any amounts for estimated delinquencies.

Summarized below is the assessed valuation record of the City for the five most recent fiscal years.

Table 5
Assessed Valuations
(Dollars in thousands)

Fiscal Year	Local Secured	Utility	Unsecured	Total ⁽¹⁾
2014-15	\$25,572,918	\$2,572	\$1,622,636	\$27,198,127
2015-16	27,618,260	2,572	1,794,921	29,415,754
2016-17	30,148,340	2,572	1,803,468	31,954,381
2017-18	32,509,995	2,572	1,922,170	34,434,739
2018-19	34,891,627	7,004	1,902,781	36,801,413

Source: California Municipal Statistics, Inc.

(1) Totals may not add due to rounding.

Principal Taxpayers. The following table sets forth the principal secured property taxpayers in the City as of the most recent fiscal year.

Table 6
Largest Local Secured Property Tax Payers
Fiscal Year 2018-19

	Property Owner	Primary Land Use	2018-19 Assessed Valuation	% of Total ⁽¹⁾
1.	Board of Trustees Leland Stanford Jr. University	Various Land Uses	\$5,446,309,461 ⁽²⁾	15.61%
2.	Space Systems Loral Land LLC	Industrial	248,246,753	0.71
3.	Google Inc.	Industrial/Office	213,981,535	0.61
4.	395 Page Mill LLC	Office Building	118,303,278	0.34
5.	ARE-San Francisco 69 LLC	Office Building	114,574,845	0.33
6.	SVF Sherman Palo Alto Corporation	Office Building	97,856,041	0.28
7.	Hohbach Realty Co. LP	Apartments	94,642,043	0.27
8.	SI 45 LLC	Office Building	81,145,206	0.23
9.	Gwin Property Inc.	Office Building	78,540,000	0.23
10.	BVK Hamilton Ave. LLC	Office Building	73,189,015	0.21
11.	530 Lytton Owner LLC	Office Building	71,138,440	0.20
12.	PA Hotel Holdings LLC	Hotel	70,028,201	0.20
13.	Ronald & Ann Williams Charitable Foundation	Shopping Center	66,211,990	0.19
14.	Donald Ferrando Trustee	Office Building	64,575,725	0.19
15.	Palo Alto Property Owner LLC	Office Building	63,543,895	0.18
16.	PPC Forest Towers LLC	Apartments	59,789,088	0.17
17.	130 Lytton Owner LLC	Office Building	57,100,623	0.16
18.	Pacific Land Development	Hotel	48,665,210	0.14
19.	Palmetto Hospitality of Palo Alto LLC	Hotel	48,249,572	0.14
20.	529 Bryant St. Parts LLC	Office Building	48,006,786	0.14
	Total Top 20		<u>\$7,164,097,707</u>	<u>20.53%</u>

Source: California Municipal Statistics, Inc.

(1) 2018-19 Local Secured Assessed Valuation: \$34,891,627,511.

(2) Net taxable value.

Sales and Use Taxes

A sales tax is imposed on the privilege of consuming personal property in California. California does not tax services. The tax rate is established by the State Legislature, and is presently 7.25%, statewide. In addition, many of California's cities, counties, towns and communities have special taxing jurisdiction to impose a transaction (sales) or use tax. These so-called district taxes increase the tax rate in a particular area by adding the local option tax to the statewide tax. These district taxes can vary up to 1%, and more than one district tax may be in effect for a particular location. The State collects and administers the tax, and makes distributions on taxes collected within the City as follows:

**Table 7
Current Sales Tax Rates**

State General Fund	5.75%
State Local Public Safety Fund	0.50
City General Fund	1.00
County Transportation	1.75
Total	9.00%

The State's actual administrative costs with respect to the portion of sales taxes allocable to the City are deducted before distribution and are determined on a quarterly basis.

Motor Vehicle In-Lieu Tax

Vehicle license fees are assessed in the amount of 2% of a vehicle's depreciation market value for the privilege of operating a vehicle on California's public highways. A program to offset (or reduce) a portion of the vehicle license fees ("VLF") paid by vehicle owners was established by Chapter 322, Statutes of 1998. Beginning January 1, 1999, a permanent offset of 25% of the VLF paid by vehicle owners became operative. Various pieces of legislation increased the amount of the offset in subsequent years to the existing statutory level of 67.5% of 2% (resulting in the current effective rate of 0.65%).

The following table sets forth the Motor Vehicle License Fees and Property Tax In-Lieu of VLF received by the City for the last four fiscal years.

**Table 8
Property Tax In-Lieu of VLF**

	FY2014-15	FY2015-16	FY2016-17	FY2017-18
Motor Vehicle License Fees	\$ 27,400	\$ 27,006	\$ 30,555	\$ 36,157
Property Tax In-Lieu of VLF	6,270,782	6,780,725	7,362,856	7,938,286
TOTAL	\$6,298,182	\$6,807,731	\$7,393,411	\$7,974,443

Source: City of Palo Alto Finance Department.

Other Revenue Sources

In addition to the tax revenues described above, the City receives the following general fund revenues:

Charges for Services. This category is comprised of external reimbursements and fee-based payments for services provided by General Fund departments.

Rental Income. These revenues include income from the City's Enterprise Funds and the Cubberley Community Center.

From Other Agencies. These revenues consist primarily of amounts received from a variety of other local government agencies, the State, and the federal government usually due to grants or contracts for services.

Permits and Licenses. These revenues consist primarily of building construction permit fees.

Investment Earnings. These revenues consist of returns on the City's portfolio.

The following table shows the City's audited other general fund revenue sources by source for the most recent four fiscal years and budgeted other revenues for fiscal year 2018-19:

**Table 9
Other Revenue Sources**

Source	FY2014-15 Audited	FY2015-16 Audited	FY2016-17 Audited	FY2017-18 Audited	FY2018-19 Budget
Charges for Services	\$25,973	\$23,910	\$22,267	\$26,824	\$28,015
Rental Income	14,911	15,769	15,692	15,896	15,806
From Other Agencies	3,712	3,190	2,758	3,205	1,150
Permits and Licenses	7,056	7,912	7,437	8,560	8,949
Investment Earnings (1)	1,177	2,494	(1,193)	(828)	1,166
Other Income	1,018	2,591	760	776	12,454
Total Revenues	\$53,847	\$55,866	\$47,721	\$54,433	\$67,540

Sources: City of Palo Alto 2014-15 through 2017-18 CAFRs and City of Palo Alto 2018-19 Budget, adopted June 18, 2018.

(1) Net of actual interest earnings and unrealized (paper) gain and loss.

OTHER FINANCIAL INFORMATION

Labor Relations

Most full-time City employees are represented by two labor union associations, the principal one being the SEIU, which represents approximately 42% of all City employees. Approximately 71% of all permanent City employees are covered by negotiated agreements with management, confidential, and city attorney employees being unrepresented. The City has never had an employee work stoppage. Negotiated agreements have the following expiration dates:

Table 10
Negotiated Employee Agreements

Employee Group	Contract Expiration Date	Number of Employees
International Association of Firefighters (IAFF)	June 30, 2018 (1)	83
Fire Chiefs' Association (FCA)	June 30, 2018 (1)	4
Palo Alto Peace Officers Association (PAPOA)	June 30, 2018 (1)	72
Palo Alto Police Managers Association (PAPMA)	June 30, 2018 (2)	6
Service Employees International Union (SEIU)	December 31, 2018	542
Service Employees International Union Hourly Unit (SEIU-H)	June 30, 2021	163
Utilities Management Professional Association of Palo Alto (UMPAPA)	No Existing Contract	46
Management and Professional Personnel and Council Appointees Compensation Plan	June 30, 2019	204
Limited Hourly Employees Compensation Plan	June 30, 2017 (1)	156
Total		<u>1,276</u>

Source: City of Palo Alto Finance Department.

(1) Contract negotiations are currently in progress. The existing contracts remain in effect during this process.

(2) PAPMA and City have mutually agreed to start negotiations after PAPOA negotiations are completed.

Risk Management

Coverage. The City provides dental coverage to employees through a City plan, which is administered by a third-party service agent. The City is self-insured for dental claims.

The City has a workers' compensation insurance policy with coverage up to the statutory limit set by the State. The City retains the risk for the first \$750,000 in losses for each accident and employee under this policy.

The City also has public employee dishonesty insurance with a \$5,000 deductible and coverage up to \$1.0 million per loss. The Director of Administrative Services and City Manager each have coverage up to \$4.0 million per loss.

The City's property, boiler, and machinery insurance policy has various deductibles and coverage based on the type of property.

The City is a member of the Authority for California Cities Excess Liability (ACCEL), which provides excess general liability insurance coverage, including auto liability, up to \$100 million per occurrence. The City retains the risk for the first \$1.0 million in losses for each occurrence under this policy.

ACCEL was established for the purpose of creating a risk management pool for central California municipalities. ACCEL is governed by a Board of Directors consisting of representatives of its member cities. The board controls the operations of ACCEL, including selection of claims management, general administration and approval of the annual budget.

The City's deposits with ACCEL equal the ratio of the City's payroll to the total payroll of all entities. Actual surpluses or losses are shared according to a formula developed from overall loss costs and spread to member entities on a percentage basis after a retrospective rating.

During the year ended June 30, 2018, the City paid \$0.9 million to ACCEL for current year coverage.

Claims Liability. The City provides for the uninsured portion of claims and judgments in the General Liabilities insurance program funds. Claims and judgments, including a provision for claims incurred but not reported, and claim adjustment expenses are recorded when a loss is deemed probable of assertion and the amount of the loss is reasonably determinable. As discussed above, the City has coverage for such claims, but it has retained the risk for the deductible or uninsured portion of these claims.

The City's liability for uninsured claims is limited to dental, general liability, and workers' compensation claims, as discussed above. Dental liability is based on a percentage of current year actual expense.

The City has not incurred a claim that has exceeded its insurance coverage limits in any of the last three years, nor have there been any significant reductions in insurance coverage.

See APPENDIX B—COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY FOR THE YEAR ENDED JUNE 30, 2018—Notes to Basic Financial Statements—NOTE 14.

Employee Retirement Plans

Plan Description. Substantially all permanent City employees are eligible to participate in the City's separate Safety (police and fire) and Miscellaneous (all other) Plans, agent multiple-employer defined benefit pension plans administered by California Public Employees' Retirement System (CalPERS), which acts as a common investment and administrative agent for its participating member employers. Benefits provisions under the Plans are established by State statute and City resolution. CalPERS issues publicly available reports that include a full description of the pension plans including benefits provisions, assumptions and membership information.

Benefits Provided. CalPERS provides retirement and disability benefits, annual cost of living adjustments and death benefits to Plan members, who must be public employees and beneficiaries. Benefits are based on years of credited service (equal to one year of full-time employment), age at retirement and final compensation. The death benefit is one of the following: the 1959 Survivor Benefit, or the pre-retirement option 2W Death Benefit for local fire members only.

Employees Covered. At June 30, 2017 (the last actuarial valuation date), the following employees were covered by the benefit terms for each Plan.

**Table 11
Covered Employees**

	Miscellaneous Plan	Safety Plan
Inactive employee or beneficiaries currently receiving benefits	1,098	427
Inactive employees entitled to but not yet receiving benefits	774	103
Active employees	818	172
Total	2,690	702

Source: City of Palo Alto 2017-18 CAFR.

Contributions. Section 20814(c) of the California Public Employees’ Retirement Law requires that the employer contribution rates for all public employers be determined on an annual basis by the actuary and shall be effective on the July 1 following notice of a change in the rate. Funding contributions for the Plans are determined annually on an actuarial basis as of June 30 by CalPERS. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The City is required to contribute the difference between the actuarially determined rate and the contribution rate of employees.

In April 2017, the City established a Section 115 irrevocable trust with the Public Agency Retirement Services (PARS) for pension expenses. The Council approved an initial deposit of \$2.1 million in General Fund proceeds into the General Fund subaccount of the City’s PARS Trust Account. The Trust Account allows more control and flexibility in investment allocations compared to City’s portfolio which is restricted by State regulations to fixed income instruments. As of June 30, 2018, the City reported the account balance of \$5.5 million as restricted cash in the General Benefits, an Internal Service Fund.

Net Pension Liability. The City’s net pension liability for both Plans is measured as the total pension liability, less the plan’s fiduciary net position. Net pension liability is measured as of June 30, 2017 (the last actuarial measurement date), using the Actuarial Valuation Report as of June 30, 2016 rolled forward to June 30, 2017 using standard update procedures. At June 30, 2018, the City reported a net pension liability of \$415.1 million for both plans.

The following table is based on the GASB 68 Accounting Valuation Report and shows the changes in the net pension liability for the Miscellaneous and Safety Plans (dollars in thousands):

Table 12
Changes in the Net Pension Liability
(Dollars in thousands)

	Miscellaneous Plan			Safety Plan		
	Total Pension Liability	Plan Net Position	Net Pension Liability	Total Pension Liability	Plan Net Position	Net Pension Liability
	\$	\$	\$	\$	\$	\$
Balances at July 1, 2017	714,019	469,782	244,237	383,556	250,474	133,082
Service Cost	14,423	-	14,423	6,584	-	6,584
Interest on total pension liability	52,831	-	52,831	28,272	-	28,272
Differences between actual and expected experience	(6,378)	-	(6,378)	(2,790)	-	(2,790)
Employer contribution	-	20,638	(20,638)	-	10,220	(10,220)
Employee Contribution	-	6,314	(6,314)	-	2,475	(2,475)
Net investment income	-	53,259	(53,259)	-	28,112	(28,112)
Benefit payments	(36,405)	(36,405)	-	(22,413)	(22,413)	-
Administrative expense	-	(694)	694	-	(370)	370
Net Changes	66,710	43,142	23,568	32,219	17,994	14,225
Balances at June 30, 2018	<u>780,729</u>	<u>512,924</u>	<u>267,805</u>	<u>415,775</u>	<u>268,468</u>	<u>147,307</u>

Source: City of Palo Alto 2017-18 CAFR.

For more information, including actuarial assumptions, a discussion of the discount rate used, and schedules of funding progress for the City’s various pension plans, see APPENDIX B—COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY FOR THE YEAR ENDED JUNE 30, 2018—Notes to Basic Financial Statements—NOTE 11.

Recent Actions Taken by CalPERS. At its April 17, 2013, meeting, CalPERS’ Board of Administration (the “Board of Administration”) approved a recommendation to change the CalPERS amortization and smoothing policies. Prior to this change, CalPERS employed an amortization and smoothing policy that spread investment returns over a 15-year period with experience gains and losses paid for over a rolling 30-year period. As a result, CalPERS now employs an amortization and smoothing policy that will pay for all gains and losses over a 20-year period with a five-year ramp-up, and five-year ramp-down, period. The new amortization and smoothing policy was used for the first time in the June 30, 2013 actuarial valuations in setting employer contribution rates for fiscal year 2015-16.

On February 18, 2014, the Board of Administration approved new demographic actuarial assumptions based on a 2013 study of recent experience. The largest impact, applying to all benefit groups, is a new 20-year mortality projection reflecting longer life expectancies and that longevity will continue to increase. Because retirement benefits will be paid out for more years, the cost of those benefits will increase as a result. The Board of Administration also assumed earlier retirements for Police 3%@50, Fire 3%@55, and Miscellaneous 2.7%@55 and 3%@60, which will increase costs for those groups. As a result of these changes, rates increased beginning in fiscal year 2016-17 (based on the June 30, 2014 valuation) with full impact in fiscal year 2020-21.

On November 18, 2015, the Board of Administration adopted a funding risk mitigation policy intended to incrementally lower its discount rate – its assumed rate of investment return – in years of good

investment returns, help pay down the pension fund's unfunded liability, and provide greater predictability and less volatility in contribution rates for employers. The policy establishes a mechanism to reduce the discount rate by a minimum of 0.05 percentage points to a maximum of 0.25 percentage points in years when investment returns outperform the existing discount rate, currently 7.25%, by at least four percentage points. CalPERS staff modeling anticipates the policy will result in a lowering of the discount rate to 6.5% in about 21 years, improve funding levels gradually over time and cut risk in the pension system by lowering the volatility of investment returns. More information about the funding risk mitigation policy can be accessed through CalPERS' web site at the following website address: <https://www.calpers.ca.gov/page/newsroom/calpers-news/2015/adopts-funding-risk-mitigation-policy>. *The reference to this Internet website is provided for reference and convenience only. The information contained within the website may not be current, has not been reviewed by the City and is not incorporated in this Official Statement by reference.*

On December 21, 2016, the Board of Administration voted to lower its discount rate from the current 7.5% to 7.0% over the next three years according to the following schedule.

<u>Fiscal Year</u>	<u>Discount Rate</u>
2017-18	7.375%
2018-19	7.250
2019-20	7.000

For public agencies like the City, the new discount rate took effect on July 1, 2018. Lowering the discount rate means employers that contract with CalPERS to administer their pension plans will see increases in their normal costs and unfunded actuarial liabilities. Active members hired after January 1, 2013, under the Public Employees' Pension Reform Act will also see their contribution rates rise. The three-year reduction of the discount rate will result in average employer rate increases of about 1 percent to 3 percent of normal cost as a percent of payroll for most miscellaneous retirement plans, and a 2 percent to 5 percent increase for most safety plans. Additionally, many CalPERS employers will see a 30 to 40 percent increase in their current unfunded accrued liability payments. These payments are made to amortize unfunded liabilities over 20 years to bring the pension fund to a fully funded status over the long-term.

PERS Amortization Period Reform. On February 13, 2018 the CalPERS Board voted to shorten the period over which actuarial gains and losses are amortized from 30 years to 20 years for new pension liabilities. The new 20-year amortization period begins with new gains or losses accrued starting with the June 30, 2019 actuarial valuations. The first payments on the new 20-year amortization schedule will take place in 2021.

A shorter amortization period will increase annual Unfunded Accrued Liability ("UAL") contributions for cities that participate in CalPERS so long as CalPERS remains underfunded. The shortened amortization period will also lead to reductions of periods of negative amortization of the UAL, interest cost savings, and faster recoveries of funded status after market downturns.

Cities that participate in CalPERS will also see additional volatility in their future UAL contributions due to market performance as gains or losses will be amortized faster under the new amortization period.

The City cannot currently estimate the impact the shorter amortization period will have on its required contributions for its Miscellaneous and Safety Plans but increased contributions are not expected to affect the City's ability to pay the Lease Payments.

Other Post-Employment Benefits

Plan Description. In addition to providing pension benefits, the City participates in the California Public Employees' Medical and Health Care Act program to provide certain health care benefits for retired employees. Employees who retire directly from the City are eligible for retiree health benefits if they retire on or after age 50 with 5 years of service and are receiving a monthly pension from CalPERS. Details of benefits provided to retirees are noted in the tables contained in APPENDIX B—COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY FOR THE YEAR ENDED JUNE 30, 2018—Notes to Basic Financial Statements—NOTE 12.

In fiscal year 2007-08, the City elected to participate in the California Employers' Retirees Benefit Trust (CERBT) (the "Trust") to provide a funding mechanism for retiree health benefits. The Trust is administrated by CalPERS and managed by a separately appointed board, which is not under control of the City Council.

Funding Policy and Actuarial Assumptions. The City's policy is to prefund these benefits by accumulating assets in the Trust discussed above pursuant to City Council Resolution. The annual required contribution (ARC) was determined as part of a June 30, 2017 actuarial valuation using the entry age normal actuarial cost method. This is a projected benefit cost method, which takes into account those benefits that are expected to be earned in the future as well as those already accrued. The actuarial assumptions are described in detail in in APPENDIX B—COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY FOR THE YEAR ENDED JUNE 30, 2018—Notes to Basic Financial Statements—NOTE 12.

The following table shows the changes in the net OPEB liability for the fiscal year ended June 30, 2018.

Table 13
Net OPEB Liability
(Dollars in thousands)

	Total OPEB Liability	Plan Fiduciary Net Position	Net OPEB Liability
Balance at June 30, 2016	\$ 234,580	\$ 79,843	\$ 154,737
Service cost	6,242	-	6,242
Interest on the total OPEB liability	15,853	-	15,853
Contributions – employer	-	14,739	(14,739)
Investment income	-	8,628	(8,628)
Administrative expenses	-	(44)	44
Benefit payments	(11,916)	(11,916)	-
Net Changes	10,179	11,407	(1,228)
Balance at June 30, 2017	244,759	91,250	153,509

Source: City of Palo Alto fiscal year 2017-18 CAFR.

For more information see APPENDIX B—COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY FOR THE YEAR ENDED JUNE 30, 2018—Notes to Basic Financial Statements—NOTE 12.

Short-Term General Fund-Secured Obligations

The City has no outstanding short-term obligations secured by its general fund.

Long-Term General Fund-Secured Obligations

On June 5, 2018, the City caused the execution and delivery of its \$8,970,000 City of Palo Alto 2018 Certificates of Participation (Capital Improvement Project; 2002B Refinancing) (Federally Taxable) (Green Bonds) (the “2018 Certificates”) to (a) finance the costs of the renovation of the Palo Alto Municipal Golf Course, and (b) prepay, on a current basis, the outstanding City of Palo Alto Certificates of Participation (Civic Center Refinancing and Downtown Parking Improvements Project), Series 2002B (Taxable). Principal payments are due annually on November 1 and interest payments are due semi-annually on May 1 and November 1 at an average rate of 4.10 percent. The City’s average annual payments with respect to the certificates is \$530,000 and the certificates mature on November 1, 2047.

The following tables shows the City's total general fund-secured debt service obligations, including the 2018 Certificates, the 2019A Certificates and the 2019B Certificates.

Table 14
Debt Service Requirements on General Fund-Secured Obligations

Year Ending November 1	2018 Certificates	2019A Certificates	2019B Certificates	Total
2019	\$ 532,589.50	\$ 818,430.56	\$ 635,911.87	\$ 1,986,931.93
2020	532,819.50	1,339,250.00	1,047,451.70	2,919,521.20
2021	532,510.00	1,339,250.00	1,045,870.10	2,917,630.10
2022	531,791.00	1,649,250.00	738,248.70	2,919,289.70
2023	530,707.00	2,013,750.00	373,315.80	2,917,772.80
2024	529,267.00	2,009,250.00	373,315.80	2,911,832.80
2025	532,317.50	2,013,250.00	373,315.80	2,918,883.30
2026	529,814.00	2,010,250.00	373,315.80	2,913,379.80
2027	531,916.00	2,010,500.00	373,315.80	2,915,731.80
2028	533,429.00	2,013,750.00	373,315.80	2,920,494.80
2029	529,453.00	2,009,750.00	373,315.80	2,912,518.80
2030	529,653.00	2,013,750.00	373,315.80	2,916,718.80
2031	529,453.00	2,010,250.00	373,315.80	2,913,018.80
2032	533,853.00	2,009,500.00	373,315.80	2,916,668.80
2033	532,653.00	2,011,250.00	373,315.80	2,917,218.80
2034	531,053.00	2,010,250.00	373,315.80	2,914,618.80
2035	529,053.00	2,011,500.00	373,315.80	2,913,868.80
2036	531,281.00	2,009,750.00	373,315.80	2,914,346.80
2037	532,891.00	2,010,000.00	373,315.80	2,916,206.80
2038	533,883.00	2,012,000.00	373,315.80	2,919,198.80
2039	529,257.00	2,010,500.00	373,315.80	2,913,072.80
2040	529,219.00	2,010,500.00	373,315.80	2,913,034.80
2041	533,563.00	2,011,750.00	373,315.80	2,918,628.80
2042	531,683.00	2,014,000.00	373,315.80	2,918,998.80
2043	529,170.00	2,012,000.00	373,315.80	2,914,485.80
2044	531,024.00	2,010,750.00	373,315.80	2,915,089.80
2045	532,034.00	—	2,383,315.80	2,915,349.80
2046	532,200.00	—	2,380,860.70	2,913,060.70
2047	531,522.00	—	2,384,707.26	2,916,229.26
2048	—	—	2,384,420.36	2,384,420.36
Total	<u>\$15,410,058.50</u>	<u>\$49,394,430.56</u>	<u>\$21,213,734.09</u>	<u>\$86,018,223.15</u>

In the next two to three years, the City plans a General Fund-secured financing to fund the construction of a new police building. The project costs are estimated in the range of \$80 to \$90 million.

Other Obligations

The City has certain other outstanding obligations including utility revenue bonds and general obligation bonds which are not secured by the City's general fund.

See APPENDIX B—COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY FOR THE YEAR ENDED JUNE 20, 2018—Notes to Basic Financial Statements—NOTE 7.

Overlapping Debt

Set forth below is a direct and overlapping debt report (the “Debt Report”) prepared by California Municipal Statistics, Inc. and effective September 1, 2018. The Debt Report is included for general information purposes only. The City has not reviewed the Debt Report for completeness or accuracy and makes no representation in connection therewith.

The Debt Report generally includes long-term obligations sold in the public credit markets by public agencies whose boundaries overlap the boundaries of the City in whole or in part. Such long-term obligations generally are not payable from revenues of the City (except as indicated) nor are they necessarily obligations secured by land within the City. In many cases, long-term obligations issued by a public agency are payable only from the general fund or other revenues of such public agency.

The contents of the Debt Report are as follows: (1) the first column indicates the public agencies which have outstanding debt as of the date of the Debt Report and whose territory overlaps the City; (2) the second column shows the respective percentage of the assessed valuation of the overlapping public agencies identified in column 1 which is represented by property located in the City; and (3) the third column is an apportionment of the dollar amount of each public agency’s outstanding debt (which amount is not shown in the table) to property in the City, as determined by multiplying the total outstanding debt of each agency by the percentage of the City’s assessed valuation represented in column 2.

Table 15
Direct and Overlapping Bonded Debt as of September 1, 2018

CITY OF PALO ALTO

2018-19 Assessed Valuation: \$36,801,413,139

<u>DIRECT AND OVERLAPPING TAX AND ASSESSMENT DEBT:</u>	<u>% Applicable⁽¹⁾</u>	<u>Debt 9/1/18</u>	
Santa Clara County	7.656%	\$ 72,519,163	
Foothill-De Anza Community College District	22.105	137,082,806	
Palo Alto Unified School District	90.084	242,483,017	
Fremont Union High School District	0.010	41,221	
Los Gatos-Saratoga Joint Union High School District	0.012	12,384	
Mountain View-Los Altos Union High School District	0.961	473,608	
Cupertino Union School District	0.017	44,006	
Los Altos School District	1.211	583,278	
Mountain View-Whisman School District	0.745	1,344,502	
Saratoga Union School District	0.026	6,131	
Whisman School District	1.959	256,727	
City of Palo Alto	100.000	60,500,000	
El Camino Hospital District	0.080	99,592	
Midpeninsula Regional Open Space District	12.970	11,992,062	
City of Palo Alto Special Assessment Bonds	100.000	22,370,000	
Santa Clara Valley Water District Benefit Assessment District	7.656	6,299,740	
TOTAL DIRECT AND OVERLAPPING TAX AND ASSESSMENT DEBT		556,108,237	
DIRECT AND OVERLAPPING GENERAL FUND DEBT:			
Santa Clara County General Fund Obligations	7.656%	\$ 43,835,421	
Santa Clara County Pension Obligation Bonds	7.656	26,978,127	
Santa Clara County Board of Education Certificates of Participation	7.656	381,652	
Foothill-DeAnza Community College District Certificates of Participation	22.105	6,244,850	
Los Gatos-Saratoga Joint Union High School District Certificates of Participation	0.012	531	
Mountain View-Los Altos Union High School District Certificates of Participation	0.961	16,769	
Los Altos School District Certificates of Participation	1.211	31,009	
Mountain View-Whisman School District Certificates of Participation	0.745	244,733	
Saratoga Union School District Certificates of Participation	0.026	919	
City of Palo Alto General Fund Obligations	100.000	8,970,000	(2)
Santa Clara County Vector Control District Certificates of Participation	7.656	189,103	
Midpeninsula Regional Open Space Park District General Fund Obligations	12.970	15,233,343	
TOTAL GROSS DIRECT AND OVERLAPPING GENERAL FUND DEBT		102,126,457	
Less: Santa Clara County supported obligations		25,824,425	
TOTAL NET DIRECT AND OVERLAPPING GENERAL FUND DEBT		76,302,032	
GROSS COMBINED TOTAL DEBT		658,234,694	(3)
NET COMBINED TOTAL DEBT		632,410,269	

Ratios to 2018-19 Assessed Valuation:

Direct Debt (\$60,500,000)	0.16%
Direct and Overlapping Tax and Assessment Debt	1.51%
Total Direct Debt (\$69,470,000)	0.19%
Gross Combined Total Debt	1.79%
Net Combined Total Debt	1.72%

Source: California Municipal Statistics, Inc.

(1) Based on 2017-18 ratios.

(2) Excludes Certificates to be sold.

(3) Excludes tax and revenue anticipation notes, enterprise revenue, mortgage revenue and non-bonded capital lease obligations.

THE CORPORATION

The Corporation is a nonprofit, 501(c)(4) corporation formed by the City in 1983 for the purpose, *inter alia*, of rendering financial assistance to the City by financing, acquiring, constructing, improving, leasing and selling buildings, improvements, equipment and other real and personal property for the benefit of residents of the City and surrounding areas. The City Council of the City sits as the Board of Directors of the Corporation.

RISK FACTORS

This section provides a general overview of certain risk factors which should be considered, in addition to the other matters set forth in this Official Statement, in evaluating an investment in the Certificates. This section is not meant to be a comprehensive or definitive discussion of the risks associated with an investment in the Certificates, and the order in which this information is presented does not necessarily reflect the relative importance of various risks. Potential investors in the Certificates are advised to consider the following factors, among others, and to review this entire Official Statement to obtain information essential to the making of an informed investment decision. Any one or more of the risk factors discussed below, among others, could lead to a decrease in the market value and/or in the marketability of the Certificates. There can be no assurance that other risk factors not discussed herein will not become material in the future.

Lease Payments Are Not Debt

The obligation of the City to make the Lease Payments under the Lease Agreement does not constitute an obligation of the City 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. The obligation of the City to make Lease Payments does not constitute a debt of the City, the State or any political subdivision thereof within the meaning of any constitutional or statutory debt limitation or restriction.

Although the Lease Agreement does not create a pledge, lien or encumbrance upon the funds of the City, the City is obligated under the Lease Agreement to pay the Lease Payments from any source of legally available funds and the City has covenanted in the Lease Agreement that, for so long as the Leased Property is available for its use, it will make the necessary annual appropriations within its budget for the Lease Payments. The City is currently liable and may become liable on other obligations payable from general revenues, some of which may have a priority over the Lease Payments, or which the City, in its discretion, may determine to pay prior to the Lease Payments.

The City has the capacity to enter into other obligations payable from the City's general fund, without the consent of or prior notice to the Owners of the Certificates. To the extent that additional obligations are incurred by the City, the funds available to make Lease Payments may be decreased. In the event the City's revenue sources are less than its total obligations, the City could choose to fund other municipal services before making Lease Payments. 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. The City's appropriations, however, have never exceeded the limitations on appropriations under Article XIII B of the California Constitution. For information on the City's current limitations on appropriations, see "CONSTITUTIONAL AND STATUTORY LIMITATIONS ON TAXES AND APPROPRIATIONS—Article XIII B of the California Constitution."

Valid and Binding Covenant to Budget and Appropriate

Pursuant to the Lease Agreement, the City covenants to take such action as may be necessary to include Lease Payments due in its annual budgets and to make necessary appropriations for all such payments. Such covenants are deemed to be duties imposed by law, and it is the duty of the public officials of the City to take such action and do such things as are required by law in the performance of the official duty of such officials to enable the City to carry out and perform such covenants. A court, however, in its discretion may decline to enforce such covenants. Upon delivery of the Certificates, Special Counsel will render its opinion (substantially in the form of APPENDIX D–FORM OF SPECIAL COUNSEL OPINION) to the effect that, subject to the limitations and qualifications described therein, the Lease Agreement constitutes a valid and binding obligation of the City.

Additional Obligations of the City

The Lease Agreement does not prohibit the City from incurring additional lease and other obligations payable from the City’s General Fund. In that regard, the City may, from time to time, incur general fund obligations to finance public improvements (see “OTHER CITY FINANCIAL INFORMATION—Long-Term General Fund-Secured Obligations”), which may also include lease obligations payable from its general fund.

Abatement

In the event of loss or substantial interference in the use and possession by the City of all or any portion of the Leased Property caused by material damage, title defect, destruction to or condemnation of the Leased Property, Lease Payments will be subject to abatement. In the event that such component of the Leased Property, if damaged or destroyed by an insured casualty, could not be replaced during the period of time that proceeds of the City’s rental interruption insurance will be available in lieu of Lease Payments, or in the event that casualty insurance proceeds or condemnation proceeds are insufficient to provide for complete repair or replacement of such component of the Leased Property or prepayment of the Certificates, there could be insufficient funds to make payments to Owners in full. Reduction in Lease Payments due to abatement as provided in the Lease Agreement does not constitute a default thereunder.

It is not possible to predict the circumstances under which such an abatement of rental may occur. In addition, there is no statute, case or other law specifying how such an abatement of rental should be measured. For example, it is not clear whether fair rental value is established as of commencement of the lease or at the time of the abatement. If the latter, it may be that the value of the Leased Property is substantially higher or lower than its value at the time of the execution and delivery of the Certificates. Abatement, therefore, could have an uncertain and material adverse effect on the security for and payment of the Certificates.

No Acceleration Upon Default

In the event of a default, there is no remedy of acceleration of the total Lease Payments due over the term of the Lease Agreement and the Trustee is not empowered to sell a fee simple interest in the Leased Property and use the proceeds of such sale to prepay the Certificates or pay debt service thereon. Any suit for money damages would be subject to limitations on legal remedies against public agencies in

the State, including a limitation on enforcement of judgments against funds needed to serve the public welfare and interest as described below. See “—Limitations on Remedies.”

Risk of Uninsured Loss

The City covenants under the Lease Agreement to maintain certain insurance policies on the Leased Property. See “SOURCE OF PAYMENT FOR THE CERTIFICATES—Insurance.” These insurance policies do not cover all types of risk, and the City need not obtain insurance except as available on the open market from reputable insurers. The City does not insure its facilities against the risk of earthquake. Additionally, the Leased Property could be the subject of an eminent domain proceeding. Under these circumstances an abatement of Lease Payments could occur and could continue indefinitely. There can be no assurance that the providers of the City’s liability and rental interruption insurance will in all events be able or willing to make payments under the respective policies for such loss should a claim be made under such policies. Further, there can be no assurances that amounts received as proceeds from insurance or from condemnation of the Leased Property will be sufficient to prepay the Certificates.

Under the Lease Agreement the City may obtain casualty insurance which provides for a deductible up to \$250,000. Should the City be required to meet such deductible expenses, the availability of general fund revenues to make Lease Payments may be correspondingly affected.

Eminent Domain

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 Agreement will cease as of the day possession is taken. If less than all of the Leased Property is taken permanently, or if the Leased Property or any part thereof is taken temporarily, under the power of eminent domain, (a) the Lease Agreement will continue in full force and effect and will not be terminated by virtue of such taking, and (b) there will be a partial abatement of Lease Payments as a result of the application of net proceeds of any eminent domain award to the prepayment of the Lease Payments, in an amount to be agreed upon by the City and the Corporation such that the resulting Lease Payments represent fair consideration for the use and occupancy of the remaining usable portion of the Leased Property. The City covenants in the Lease Agreement to contest any eminent domain award which is insufficient to either: (i) prepay the Lease Payments in whole, if all the Leased Property is condemned; or (ii) prepay a pro rata share of Lease Payments, in the event that less than all of the Leased Property is condemned.

Hazardous Substances

The existence or discovery of hazardous materials may limit the beneficial use of the Leased Property. In general, the owners and lessees of the Leased Property may be required by law to remedy conditions of such parcel relating to release 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 are also similarly stringent. Under many of these laws, the owner or lessee is obligated to remedy a hazardous substance condition of the property whether or not the owner or lessee had anything to do with creating or handling the hazardous substance.

Further it is possible that the beneficial use of the Leased Property may be limited in the future resulting from the current existence on the Leased Property of a substance currently classified as

hazardous, but which has not been released or the release of which is not presently threatened or may arise in the future resulting from the current existence on the Leased Property of a substance not presently classified as hazardous, but which may in the future be so classified. Further, such liabilities may arise not simply from the existence of a hazardous substance but from the method in which it is handled. All of these possibilities could significantly limit the beneficial use of the Leased Property.

The City is unaware of the existence of hazardous substances on the Leased Property site which would materially interfere with the beneficial use thereof.

Natural Calamities

General. From time to time, the City has been and could be subject to natural calamities, including, but not limited to, earthquake, flood or wildfire, that may adversely affect economic activity in the City, and which could have a negative impact on City finances. There can be no assurance that the occurrence of any natural calamity would not cause substantial interference to the Leased Property, or that the City would have insurance or other resources available to make repairs to the Leased Property in order to make the Lease Payments under the Lease. See “—Abatement” above.

Seismic. Like most regions in California, the City is in an area of significant seismic activity. There are numerous earthquake faults near the City, including particularly the San Andreas and Hayward faults. The San Andreas fault runs along the Marin and Sonoma Coast through the Santa Cruz Mountains. The Hayward fault covers the hills on the east side of the San Francisco Bay and into San Pablo Bay, directly north and east of the City. Both can cause damaging earthquakes. Numerous other faults are capable of producing damaging earthquakes similar in magnitude to the 1989 Loma Prieta earthquake. Soils in lowland areas away from major faults may also be unable to support buildings during major earthquakes. Landslides are likely on hillsides during major earthquakes. Coastal areas are also at risk of tsunamis, generated from earthquakes on local faults or across the Pacific.

If there were to be an occurrence of severe seismic activity in the City, there could be substantial damage to and interference with the City’s right to use and occupy all or a portion of the Leased Property, which could result in Lease Payments being subject to abatement. See “—Abatement” above. Damage resulting from such an event could have a material adverse effect on the City’s financial condition as well, through unexpected recovery costs and reduced tax and other revenues.

See “SOURCE OF PAYMENT FOR THE CERTIFICATES—Insurance” above. Also see “THE LEASED PROPERTY” for information about the Leased Property.

Flood. Like most of California, the City is subject to unpredictable seasonal rainfall, with periods of intense and sustained precipitation occurring every few years. The Leased Property is not located in the 100-year floodplain.

Climate Change/Sea Level Rise. Although very little of the property in the City directly abuts the San Francisco Bay, certain parcels may still be vulnerable to property damage or reductions in assessed value as a result of future sea level rise in the San Francisco Bay or other negative impacts resulting from climate change.

The predictions for sea level rise in the San Francisco Bay vary. A report released by the San Francisco Bay Conservation Development Commission (“BCDC”) predicts sea levels in the Bay to rise

16 inches by 2050 and 55 inches by 2100. The State's Fourth Climate Change Assessment, released in 2017, estimates sea level rise for the year 2100 in the range of 14 inches to 94 inches (36 cm to 239 cm) with an additional very low probability, worst case estimate that exceeds 108 inches (274 cm). A draft paper from the California Climate Change Center posits that increases in sea level will be a significant consequence of climate change over the next century.

Local impacts of climate change are not definitive, but parcels in the City could experience changes to local and regional weather patterns, rising bay water levels, increased risk of flooding, changes in salinity and tidal patterns of San Francisco Bay, coastal erosion, water restrictions and vegetation changes.

Bankruptcy

The City is a unit of State government and therefore is not subject to the involuntary procedures of the United States Bankruptcy Code (the "Bankruptcy Code"). However, pursuant to Chapter 9 of the Bankruptcy Code, the City may seek voluntary protection from its creditors for purposes of adjusting its debts. A City bankruptcy petition could have a material adverse effect on the payment of the Certificates. The following paragraphs present a discussion of certain potential consequences surrounding a potential City bankruptcy. It is not intended to be an exhaustive discussion of all potential adverse consequences or potential outcomes.

In the event the City were to become a debtor under the Bankruptcy Code, the City would be entitled to all of the protective provisions of the Bankruptcy Code as applicable in a Chapter 9 proceeding. Among the adverse effects of such a bankruptcy might be: (i) the application of the automatic stay provisions of the Bankruptcy Code, which, until relief is granted, would prevent collection of payments from the City or the commencement of any judicial or other action for the purpose of recovering or collecting a claim against the City; (ii) the avoidance of preferential transfers occurring during the relevant period prior to the filing of a bankruptcy petition; (iii) the existence of unsecured or court-approved secured debt which may have a priority of payment superior to that of Owners of Certificates; and (iv) the possibility of the adoption of a plan for the adjustment of the City's debt (a "Plan") without the consent of the Trustee or all of the Owners of Certificates, which Plan may restructure, delay, compromise or reduce the amount of any claim of the Owners if the Bankruptcy Court finds that the Plan is fair and equitable.

In addition, the City could either reject the Lease or assume the Lease despite any provision of the Lease which makes the bankruptcy or insolvency of the City an event of default thereunder. In the event the City rejects the Lease, the Trustee, on behalf of the Owners of the Certificates, would have a pre-petition claim that may be limited under the Bankruptcy Code and treated in a manner under a Plan over the objections of the Trustee or Owners of the Certificates. Moreover, such rejection would terminate the Lease and the City's obligations to make payments thereunder.

Pension Benefit Liability

Many factors influence the amount of the City's pension benefit liabilities, including, without limitation, inflationary factors, changes in statutory provisions of PERS retirement system laws, changes in the level of benefits provided or in the contribution rates of the City, increases or decreases in the number of covered employees, changes in actuarial assumptions or methods (including but not limited to the assumed rate of return), and differences between actual and anticipated investment experience of

PERS. Any of these factors could give rise to additional liability of the City to its pension plans as a result of which the City would be obligated to make additional payments to its pension plans in order to fully fund the City's obligations to its pension plans.

Early Prepayment Risk

Early prepayment of the Certificates may occur in whole or in part without premium, on any date if the Leased Property or a portion thereof is lost, destroyed or damaged beyond repair or taken by eminent domain and from the proceeds of title insurance, or on any Interest Payment Date, without a premium (see "THE CERTIFICATES—Prepayment"), if the City exercises its right to prepay Lease Payments in whole or in part pursuant to the provisions of the Lease Agreement and the Trust Agreement. If Certificates are purchased at a premium, the Owners may receive less than their purchase price in the event of a prepayment.

Limitations on Remedies

The enforcement of any remedies provided in the Lease Agreement and the Trust Agreement could prove both expensive and time consuming. Although the Lease Agreement provides that if the City defaults the Trustee may enter the Leased Property and re-let the Leased Property, portions of the Leased Property may not be easily recoverable, and even if recovered, could be of little value to others because of the Leased Property's specialized nature. Additionally, the Trustee may have limited ability to re-let the Leased Property to provide a source of rental payments sufficient to pay the principal of and interest with respect to the Certificates so as to preserve the tax-exempt nature of interest with respect to the Certificates. Furthermore, due to the governmental nature of the Leased Property, it is not certain whether a court would permit the exercise of the remedy of re-letting with respect thereto.

Alternatively, the Trustee may terminate the Lease Agreement and proceed against the City to recover damages pursuant to the Lease Agreement. Any suit for money damages would be subject to limitations on legal remedies against public agencies in the State, including a limitation on enforcement of judgments against funds needed to serve the public welfare and interest.

The rights of the Owners of the Certificates are subject to certain limitations on legal remedies against cities, redevelopment agencies and other governmental entities in the State, including but not limited to a limitation on enforcement against funds that are otherwise needed to serve the public welfare and interest. Additionally, the rights of the Owners of the Certificates may be subject to (i) bankruptcy, insolvency, reorganization, moratorium, or similar laws limiting or otherwise affecting the enforcement of creditors' rights generally (as such laws are now or hereafter may be in effect), (ii) equity principles (including but not limited to concepts of materiality, reasonableness, good faith and fair dealing) and the possible unavailability of specific performance or injunctive relief, regardless of whether considered in a proceeding in equity or law, (iii) the exercise by the United States of America of the powers delegated to it by the Constitution, and (iv) the reasonable and necessary exercise, in certain exceptional situations, of the police powers inherent in the sovereignty of the State and its governmental bodies in the interest of serving a significant and legitimate public purpose. Under Chapter 9 of the Bankruptcy Code (Title 11, United States Code), which governs bankruptcy proceedings for public agencies, there are no involuntary petitions in bankruptcy. If the City were to file a petition under Chapter 9 of the Bankruptcy Code, the Owners, the Trustee and the Corporation could be prohibited or severely restricted from taking any steps to enforce their rights under the Lease Agreement and from taking any steps to collect amounts due from the City under the Lease Agreement.

Special Counsel has limited its opinion as to the enforceability of the Lease Agreement to the extent that enforceability may be limited by bankruptcy, insolvency, reorganization, fraudulent conveyance or transfer, moratorium, or other similar laws affecting generally the enforcement of creditor's rights, by equitable principles and by the exercise of judicial discretion. Additionally, the Certificates are not subject to acceleration in the event of the breach of any covenant or duty under the Lease Agreement. The lack of availability of certain remedies or the limitation of remedies may entail risks of delay, limitation or modification of the rights of the Owners.

Dependence on State for Certain Revenues

A number of the City's revenues are collected and dispersed by the State (such as sales tax and motor-vehicle license fees) or allocated in accordance with State law (most importantly, property taxes). Therefore, State budget decisions can have an impact on City finances. In the event of a material economic downturn in the State, there can be no assurance that any resulting revenue shortfalls to the State will not reduce revenues to local governments (including the City) or shift financial responsibility for programs to local governments as part of the State's efforts to address any such related State financial difficulties. See "STATE BUDGET INFORMATION."

No Reserve Fund

No debt service reserve fund has been established with respect to the Certificates.

Secondary Market Risk

There can be no assurance that there will be a secondary market for purchase or sale of the Certificates, and from time to time there may be no market for them, depending upon prevailing market conditions, the financial condition or market position of firms who may make the secondary market and the financial condition of the City.

Changes in Law

There can be no assurance that the electorate of the State will not at some future time adopt additional initiatives or that the Legislature will not enact legislation that will amend the laws or the Constitution of the State resulting in a reduction of the general fund revenues of the City and consequently, having an adverse effect on the security for the Certificates.

STATE BUDGET INFORMATION

The following information concerning the State's budgets has been obtained from publicly available information which the City believes to be reliable; however, the City does not guarantee the accuracy or completeness of this information and has not independently verified such information. Furthermore, it should not be inferred from the inclusion of this information in this Official Statement that the principal or interest with respect to the Certificates is payable by or the responsibility of the State.

State Budget. Information about the State budget is regularly available at various State-maintained websites. Text of proposed and adopted budgets may be found at the website of the Department of Finance, www.dof.ca.gov, under the heading "California Budget." An impartial analysis of the budget is posted by the Office of the Legislative Analyst at www.lao.ca.gov. In addition, various State official statements, many of which contain a summary of the current and past State budgets and the impact of those budgets on cities in the State, may be found at the website of the State Treasurer, www.treasurer.ca.gov. The information referred to is prepared by the respective State agency maintaining each website and not by the City, and the City can take no responsibility for the continued accuracy of these internet addresses or for the accuracy, completeness or timeliness of information posted there, and such information is not incorporated herein by these references.

According to the State Constitution, the Governor of the State (the "Governor") is required to propose a budget to the State Legislature (the "Legislature") by no later than January 10 of each year, and a final budget must be adopted by the vote of each house of the Legislature no later than June 15, although this deadline has been routinely breached in the past. The State budget becomes law upon the signature of the Governor, who may veto specific items of expenditure.

Prior to Fiscal Year 2010-11, the State budget had to be adopted by a two-thirds vote of each house of the Legislature. However, in November 2010, the voters of the State passed Proposition 25, which reduced the vote required to adopt a budget to a majority vote of each house and which provided that there would be no appropriation from the current budget or future budget to pay any salary or reimbursement for travel or living expenses for members of the Legislature for the period during which the budget was presented late to the Governor.

Potential Impact of State Financial Condition on the City. During the most recent recession, the State faced a structural deficit that resulted in substantial annual deficits and reductions in expenditures. Although the State has had a budget surplus in the more recent fiscal years, according to the State there remain a number of major risks and pressures that threaten the State's financial condition, including the threat of recession, potential changes to federal fiscal policies and unfunded long-term liabilities of more than \$200 billion related to pensions and other post-retirement benefits. These risks and financial pressures could result in future reductions or deferrals in amounts payable to the City. The State's financial condition and budget policies affect local public agencies throughout California. To the extent that the State budget process results in reduced revenues to the City, the City will be required to make adjustments to its budget. State budget policies can also impact conditions in the local economy and could have an adverse effect on the local economy and the City's major revenue sources.

No prediction can be made by the City as to whether the State will encounter budgetary problems in future fiscal years, and if it were to do so, it is not clear what measures would be taken by the State to balance its budget, as required by law. In addition, the City cannot predict the final outcome of future

State budget negotiations, the impact that such budgets will have on City finances and operations or what actions will be taken in the future by the Legislature and the Governor to deal with changing State revenues and expenditures. There can be no assurance that actions taken by the State to address its financial condition will not materially adversely affect the financial condition of the City. Current and future State budgets will be affected by national and State economic conditions and other factors over which the City has no control.

State Legislative Shifts of Property Tax Allocation. From time to time, the State has realigned certain property tax revenue to deal with its budget problems. Since 1992-93, the State has required that local agencies including cities remit a portion of property taxes received to augment school funding. These funds are deposited in each county's Education Revenue Augmentation Fund ("ERAF"). These property taxes (approximately 17.5%) are permanently excluded from the City's property tax revenues.

On July 24, 2009, the Legislature approved amendments to the 2009-10 Budget to close its anticipated \$26.3 billion budget shortfall. The approved amendments included borrowing from local governments by withholding of the equivalent of 8% of Fiscal Year 2008-09 property related tax revenues from cities' and counties' property tax collections under provisions of Proposition 1A (approved by the voters in 2004), which the State was required to repay with interest within three years. The first (and to date, only) shift occurred in Fiscal Year 2009-10. The City's share of the withholding was \$355,977. Fiscal Year 2012-13 was the first year that another shift was allowable, but the State has not implemented another borrowing yet.

On March 2, 2004, voters approved a bond initiative formally known as the "California Economic Recovery Act." This act authorized the issuance of \$15 billion in bonds to finance the Fiscal Year 2002-03 and Fiscal Year 2003-04 State budget deficits, which would be payable from a fund to be established by the redirection of tax revenues through the "Triple Flip." Under the "Triple Flip," one-quarter of local governments' 1% share of the sales tax imposed on taxable transactions within their jurisdiction were redirected to the State. In an effort to eliminate the adverse impact of the sales tax revenue redirection on local government, the legislation provided for property taxes in the ERAF to be redirected to local government. Because the ERAF moneys were previously earmarked for schools, the legislation provided for schools to receive other state general fund revenues. The swap of sales taxes for property taxes terminated once the deficit financing bonds were repaid in September 2015. The City treated the Triple Flip property tax revenue as sales tax in its financial statements.

The City also received a portion of Department of Motor Vehicles license fees ("VLF") collected statewide. Several years ago, the State-wide VLF was reduced by approximately two-thirds. However, the State continued to remit to cities and counties the same amount that those local agencies would have received if the VLF had not been reduced, known as the "VLF backfill." The State VLF backfill was phased out and as of 2011-12 all of the VLF is now received through an in lieu payment from State property tax revenues.

2018-19 State Budget and Proposed 2019-20 State Budget

On June 27, 2018, Governor Jerry Brown signed into law the State budget for fiscal year 2018-19 (the "2018-19 Budget"). The following information is drawn from the Legislative Analyst's Office ("LAO") review of the 2018-19 Budget.

To protect against potential future economic recessions, the 2018-19 Budget fully funds the Budget Stabilization Account, the State's basic reserve account (the "BSA") with a total deposit of over \$4.4 billion, including a \$2.6 billion optional deposit in addition to the Constitutionally-required deposit, and adds two additional reserves to State law: the Safety Net Reserve Fund, intended to save money specifically for future expenditures of the CalWORKs and Medi-Cal programs; and the Budget Deficit Savings Account ("BDSA"), which for fiscal year 2018-19 will temporarily hold the \$2.6 billion optional BSA deposit until May 2019. In May 2019, the optional BSA deposit amount will be adjusted as necessary to reflect updated estimates of revenues, at which point it will be transferred to the BSA. The projected ending balance in the BSA at the end of fiscal year 2018-19 is expected to equal the BSA's current constitutional maximum of 10% of the estimated general fund revenues for fiscal year 2018-19.

For fiscal year 2017-18, the 2018-19 Budget projects total general fund revenues and transfers of \$129.8 billion and total expenditures of \$127.0 billion. The State is projected to end fiscal year 2017-18 with total available general fund reserves of \$16.7 billion, including \$7.3 billion in the traditional general fund reserve and \$9.4 billion in the BSA. For fiscal year 2018-19, the 2018-19 Budget projects total general fund revenues of \$133.3 billion and authorizes expenditures of \$138.7 billion. The State is projected to end fiscal year 2018-19 with total available general fund reserves of \$15.9 billion, including \$2.0 billion in the traditional general fund reserve, \$13.8 billion in the BSA and \$200 million in the Safety Net Reserve Fund.

On January 10, 2019, the Governor Gavin Newsom released his proposed State budget for fiscal year 2019-20 (the "Proposed 2019-20 Budget"). The following information is drawn from the State Department of Finance's summary of the Proposed 2019-20 Budget.

For fiscal year 2018-19, the Proposed 2019-20 Budget projects total general fund revenues and transfers of \$136.9 billion and total expenditures of \$144.1 billion. The State is projected to end fiscal year 2018-19 with total available general fund reserves of \$18.3 billion, including \$3.9 billion in the traditional general fund reserve, \$13.5 billion in the BSA and \$900 million in the Safety Net Reserve Fund. For fiscal year 2019-20, the Proposed 2019-20 Budget projects total general fund revenues of \$142.6 billion and authorizes expenditures of \$144.2 billion. The State is projected to end fiscal year 2019-20 with total available general fund reserves of \$18.5 billion, including \$2.3 billion in the traditional general fund reserve, \$15.3 billion in the BSA and \$900 million in the Safety Net Reserve Fund. The Governor notes that additional deposits to the BSA are premised on a recent opinion by the California Office of Legislative Counsel which concluded that supplemental payments made in prior fiscal years do not count towards calculating the BSA's constitutional maximum of 10%.

Future State Budgets

The City receives a portion of its funding from the State. Changes in the revenues received by the State can affect the amount of funding, if any, to be received from the State by the City and other cities in the State.

The City cannot predict the extent of the budgetary problems the State will encounter in this fiscal year or in any future fiscal years, and, it is not clear what measures would be taken by the State to balance its budget, as required by law. In addition, the City cannot predict the final outcome of current and future State budget negotiations, the impact that such budgets will have on its finances and operations or what actions will be taken in the future by the State Legislature and Governor to deal with changing State revenues and expenditures. Current and future State budgets will be affected by national and State

economic conditions and other factors, including the current economic downturn, over which the City has no control. See also “RISK FACTORS—Dependence on State for Certain Revenues.”

CONSTITUTIONAL AND STATUTORY LIMITATIONS ON TAXES 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.

Article XIII A of the California Constitution

Basic Property Tax Levy. On June 6, 1978, California voters approved Proposition 13 ("Proposition 13"), which added Article XIII A to the State Constitution ("Article XIII A"). Article XIII A limits the amount of any *ad valorem* tax on real property to 1% of the full cash value thereof, except that additional *ad valorem* taxes may be levied to pay debt service on (i) indebtedness approved by the voters prior to July 1, 1978, (ii) (as a result of an amendment to Article XIII A approved by State voters on June 3, 1986) on bonded indebtedness for the acquisition or improvement of real property which has been approved on or after July 1, 1978 by two-thirds of the voters on such indebtedness, and (iii) (as a result of an amendment to Article XIII A approved by State voters on November 7, 2000) bonded indebtedness incurred by a school district or community college district for the construction, reconstruction, rehabilitation or replacement of school facilities or the acquisition or lease of real property for school facilities, approved by 55% of the voters of the district, but only if certain accountability measures are included in the proposition. Article XIII A defines full cash value to mean "the county assessor's valuation of real property as shown on the 1975-76 tax bill under full cash value, or thereafter, the appraised value of real property when purchased, newly constructed, or a change in ownership have occurred after the 1975 assessment". This full cash value may be increased at a rate not to exceed 2% per year to account for inflation.

Article XIII A has subsequently been amended to permit reduction of the "full cash value" base in the event of declining property values caused by damage, destruction or other factors, to provide that there would be no increase in the "full cash value" base in the event of reconstruction of property damaged or destroyed in a disaster and in other minor or technical ways.

Legislation Implementing Article XIII A. Legislation has been enacted and amended a number of times since 1978 to implement Article XIII A. Under current law, local agencies are no longer permitted to levy directly any property tax (except to pay voter-approved indebtedness). The 1% property tax is automatically levied by the county and distributed according to a formula among taxing agencies. The formula apportions the tax roughly in proportion to the relative shares of taxes levied prior to 1979.

Increases of assessed valuation resulting from reappraisals of property due to new construction, change in ownership or from the annual adjustment not to exceed 2% are allocated among the various jurisdictions in the "taxing area" based upon their respective "situs." Any such allocation made to a local agency continues as part of its allocation in future years.

Inflationary Adjustment of Assessed Valuation. As described above, the assessed value of a property may be increased at a rate not to exceed 2% per year to account for inflation. On December 27, 2001, the Fresno County Superior Court, in *County of Fresno v. Fresno County Assessment Appeals Board No. 3*, held that where a home's taxable value did not increase for two years, due to a flat real estate market, the

Fresno County assessor violated the 2% inflation adjustment provision of Article XIII A, when the assessor tried to "recapture" the tax value of the property by increasing its assessed value by 4% in a single year. The assessors in most California counties, including the County, use a similar methodology in raising the taxable values of property beyond 2% in a single year. The State Board of Equalization has approved this methodology for increasing assessed values. On appeal, the Appellate Court held that the trial court erred in ruling that assessments are always limited to no more than 2% of the previous year's assessment. On May 10, 2004 a petition for review was filed with the California Supreme Court which petition was denied by the California Supreme Court. As a result of this litigation, the "recapture" provision described above may continue to be employed in determining the full cash value of property for property tax purposes.

Article XIII B of the California Constitution

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 California 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 adds 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.

Taxes. Article XIII C requires that all new local taxes be submitted to the electorate before they become effective. Taxes for general governmental purposes of the City (“general taxes”) require a majority vote; taxes for specific purposes (“special taxes”), even if deposited in the City’s General Fund, require a two-thirds vote.

Property-Related Fees and Charges. Article XIII D also adds several provisions making it generally more difficult for local agencies to levy and maintain property-related fees, charges, and assessments for municipal services and programs.

Reduction or Repeal of Taxes, Assessments, Fees and Charges. Article XIII C also removes limitations on the initiative power in matters of reducing or repealing local taxes, assessments, fees or charges. No assurance can be given that the voters of the City will not, in the future, approve an initiative or initiatives which reduce or repeal local taxes, assessments, fees or charges currently comprising a substantial part of the City’s General Fund. If such repeal or reduction occurs, the City’s ability to pay debt service on the Certificates could be adversely affected.

Burden of Proof. Article XIII C provides that local government “bears the burden of proving by a preponderance of the evidence that a levy, charge, or other exaction is not a tax, that the amount is no more than necessary to cover the reasonable costs of the governmental activity, and that the manner in which those costs are allocated to a payor bear a fair or reasonable relationship to the payor’s burdens on, or benefits received from, the governmental activity.” Similarly, Article XIII D provides that in “any legal action contesting the validity of a fee or charge, the burden shall be on the agency to demonstrate compliance” with Article XIII D.

Judicial Interpretation of Proposition 218. The interpretation and application of Articles XIII C and XIII D will ultimately be determined by the courts, and it is not possible at this time to predict with certainty the outcome of such determination.

Impact on City’s General Fund. The City does not believe that any material source of General Fund revenue is subject to challenge under Proposition 218 or Proposition 26.

The approval requirements of Articles XIII C and XIII D 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 the taxes, fees, charges or taxes in the future that it may need to meet increased expenditure needs.

Proposition 1A; Proposition 22

Proposition 1A. Proposition 1A, proposed by the Legislature in connection with the State’s Fiscal Year 2004-05 Budget, approved by the voters in November 2004 and generally effective in Fiscal Year 2006-07, provided 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 prohibited 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 had to be approved by two-thirds of both houses of the Legislature.

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 eliminates or reduces 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.

Proposition 26

Proposition 26 (“Proposition 26”), which was approved by California voters on November 2, 2010, revises the California Constitution to expand the definition of “taxes.” Proposition 26 re-categorizes many State and local fees as taxes and specifies a requirement of two-thirds voter approval for taxes levied by local governments.

Proposition 26 requires the State obtain the approval of two-thirds of both houses of the State Legislature for any proposed change in State statutes, which would result in any taxpayer paying a higher tax. Proposition 26 eliminates the previous practice whereby a tax increase coupled with a tax reduction that resulted in an overall neutral fiscal effect was subject only to a majority vote in the State Legislature. Furthermore, pursuant to Proposition 26, any increase in a fee above the amount needed to provide the specific service or benefit is deemed to be a tax and the approval thereof will require such two-thirds vote of approval to be effective. In addition, for State imposed fees and charges, any fee or charge adopted after January 1, 2010 with a majority vote of approval of the State Legislature which would have required a two-thirds vote of approval of the State Legislature if Proposition 26 were effective at the time of such adoption is repealed as of November 2011 absent the re-adoption by the requisite two-thirds vote.

Proposition 26 amends Article XIII C of the State Constitution to state that a “tax” means a levy, charge or exaction of any kind imposed by a local government, except (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; (3) a charge imposed for the reasonable regulatory costs to a local government for issuing licenses and permits, performing investigations, inspections and audits, enforcing agricultural marketing orders, and the administrative enforcement and adjudication thereof; (4) a charge imposed for entrance to or use of local government property or the purchase rental or lease of local government property; (5) a fine, penalty, or other monetary charge imposed by the judicial branch of government or a local government as a result of a violation of law; (6) a charge imposed as a condition of property development; or (7) assessments and property related fees imposed in accordance with the provisions of Proposition 218.

Proposition 26 applies to any levy, charge or exaction imposed, increased, or extended by local government on or after November 3, 2010, unless exempted, as stated above. Accordingly, fees adopted prior to that date are not subject to the measure until they are increased or extended or if it is determined

that an exemption applies. As of the date hereof, none of the City's fees or charges has been challenged in a court of law in connection with the requirements of Proposition 26.

If the local government specifies how the funds from a proposed local tax are to be used, the approval will be subject to a two-thirds voter requirement. If the local government does not specify how the funds from a proposed local tax are to be used, the approval will be subject to a fifty percent voter requirement. Proposed local government fees that are not subject to Proposition 26 generally are subject to the approval of a majority of the governing body. In general, proposed property charges will be subject to a majority vote of approval by the governing body although certain proposed property charges will also require approval by a majority of the affected property owners.

Possible Future Initiatives

Articles XIII A, XIII B, XIII C and XIII D and Propositions 62, 1A, 22 and 26 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. The nature and impact of these measures cannot be anticipated by the City.

ABSENCE OF LITIGATION

At the time of delivery of and payment for the Certificates, the City and the Corporation will certify that there is no action, suit, proceeding, inquiry, or investigation, at law or in equity, before or by any court or regulatory agency, public board, or body pending or threatened against the City or the Corporation affecting their existence or the titles of their respective officers or seeking to restrain or to enjoin the issuance, sale, or delivery of the Certificates, or the application of the proceeds thereof in accordance with the Trust Agreement, or in any way contesting or affecting the validity or enforceability of the Certificates, any agreement entered into between the City and any purchaser of the Certificates, the Lease Agreement, the Trust Agreement, the Assignment Agreement, the Property Lease or any other applicable agreements or any action of the City or the Corporation contemplated by any of said documents, or in any way contesting the completeness or accuracy of this Official Statement or any amendment or supplement thereto, or contesting the powers of the City or the Corporation or their authority with respect to the Certificates or any action of the City or the Corporation contemplated by any of said documents, nor, to the knowledge of the City or the Corporation, is there any basis therefor.

CONTINUING DISCLOSURE

Pursuant to Rule 15c2-12 of the Securities and Exchange Commission (the "Rule"), the City has agreed, for the benefit of holders of the Certificates, to provide certain financial information and operating data relating to the City and the balances of funds relating to the Certificates, by not later than March 31 of each year commencing with the report for the 2017-18 fiscal year (the "Annual Information"), and to provide notices of the occurrence of certain enumerated events. The Annual Information and notices of enumerated events will be filed by the City with the Municipal Securities Rulemaking Board (the "MSRB"), via its Electronic Municipal Market Access ("EMMA") system. The nature of the information to be provided in the Annual Information and the notices of material events is set forth in APPENDIX G—FORMS OF CONTINUING DISCLOSURE CERTIFICATES.

The City's annual filings for fiscal years 2012-13, 2013-14, 2014-15 and 2015-16 in connection with its outstanding 2011 utility revenue bonds omitted certain information relating to the top ten customers of its gas system. For fiscal years 2013 and 2015, certain information required in connection with an issue of assessment district bonds was not filed until approximately 124 days and 229 days, respectively, after the date required for such filings. For fiscal years 2014 through 2018, the City's annual report was not properly associated on EMMA with all appropriate CUSIPs. The omissions have been corrected and correcting EMMA filings have been made. The City has established internal policies to insure that all future required filings are made as required.

Substantially all of the City's required financial information and operating data is included in its comprehensive annual financial report (the "CAFR") which is historically filed in advance of the required March 31 deadline. The City's CAFR provides the debt service coverage of the City's 1999 Utility Bonds (the "1999 Bonds") but it is not substantially in the form of the table shown in the official statement for the 1999 Bonds.

Any financial information and operating data not included in the comprehensive annual financial report is compiled by the City's Treasury staff and its Assistant Administrative Services Director. The City has established a ticker system to provide staff with advance notice so that the reports are prepared in time to allow review and timely filing.

MUNICIPAL ADVISOR

PFM Financial Advisors LLC, San Francisco, California ("PFM"), is an independent financial advisory firm registered as a "Municipal Advisor" with the Securities Exchange Commission and Municipal Securities Rulemaking Board. PFM does not underwrite, trade or distribute municipal or other public securities. PFM has assisted the City in connection with the planning, structuring, sale and issuance of the Certificates. PFM is not obligated to undertake, and has not undertaken to make, an independent verification of or to assume responsibilities for the accuracy, completeness or fairness of the information contained in this Official Statement not provided by PFM. The fees of PFM in respect to the Certificates are contingent upon their sale and delivery.

LEGAL MATTERS

All legal matters in connection with the execution and delivery of the Certificates are subject to the approval of Jones Hall, A Professional Law Corporation, San Francisco, California, Special Counsel. Special Counsel's opinion with respect to the Certificates will be substantially in the form set forth in APPENDIX D—FORM OF SPECIAL COUNSEL OPINION. Certain legal matters will also be passed on for the City by Quint & Thimmig LLP, Larkspur, California, as Disclosure Counsel, and by the City Attorney. Certain matters will be passed on for the Underwriter by Stradling Yocca Carlson & Rauth, a Professional Corporation, Newport Beach, California. The fees and expenses of Special Counsel and Disclosure Counsel are contingent upon the execution and delivery of the Certificates.

TAX MATTERS

2019A Certificates

Federal Tax Status. In the opinion of Jones Hall, A Professional Law Corporation, San Francisco, California, Special Counsel, subject, however to the qualifications set forth below, under existing law, the portion of Lease Payments designated as and comprising interest and received by the owners of the 2019A Certificates is excluded from gross income for federal income tax purposes and such interest is not an item of tax preference for purposes of the federal alternative minimum tax.

The opinions set forth in the preceding paragraph are subject to the condition that the City comply with all requirements of the Internal Revenue Code of 1986, as amended (the "**Tax Code**") relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the 2019A Certificates. The City has made certain representations and covenants in order to comply with each such requirement. Inaccuracy of those representations, or failure to comply with certain of those covenants, may cause the inclusion of such interest in gross income for federal income tax purposes, which may be retroactive to the date of execution and delivery of the 2019A Certificates.

Tax Treatment of Original Issue Discount and Premium. If the initial offering price to the public at which a 2019A Certificate is sold is less than the amount payable at maturity thereof, then such difference constitutes "original issue discount" for purposes of federal income taxes and State of California personal income taxes. If the initial offering price to the public at which a 2019A Certificate is sold is greater than the amount payable at maturity thereof, then such difference constitutes "original issue premium" for purposes of federal income taxes and State of California personal income taxes. *De minimis* original issue discount and original issue premium is disregarded.

Under the Tax Code, original issue discount is treated as interest excluded from federal gross income and exempt from State of California personal income taxes to the extent properly allocable to each owner thereof subject to the limitations described in the first paragraph of this section. The original issue discount accrues over the term to maturity of the 2019A Certificate on the basis of a constant interest rate compounded on each interest or principal payment date (with straight-line interpolations between compounding dates). The amount of original issue discount accruing during each period is added to the adjusted basis of such 2019A Certificates to determine taxable gain upon disposition (including sale, redemption, or payment on maturity) of such 2019A Certificate. The Tax Code contains certain provisions relating to the accrual of original issue discount in the case of purchasers of the 2019A Certificates who purchase the 2019A Certificates after the initial offering of a substantial amount of such maturity. Owners of such 2019A Certificates should consult their own tax advisors with respect to the tax consequences of ownership of 2019A Certificates with original issue discount, including the treatment of purchasers who do not purchase in the original offering, the allowance of a deduction for any loss on a sale or other disposition, and the treatment of accrued original issue discount on such 2019A Certificates under federal individual minimum taxes.

Under the Tax Code, original issue premium is amortized on an annual basis over the term of the 2019A Certificate (said term being the shorter of the 2019A Certificate's maturity date or its call date). The amount of original issue premium amortized each year reduces the adjusted basis of the owner of the 2019A Certificate for purposes of determining taxable gain or loss upon disposition. The amount of original issue premium on a 2019A Certificate is amortized each year over the term to maturity of the 2019A Certificate on the basis of a constant interest rate compounded on each interest or principal

payment date (with straight-line interpolations between compounding dates). Amortized 2019A Certificate premium is not deductible for federal income tax purposes. Owners of premium 2019A Certificates, including purchasers who do not purchase in the original offering, should consult their own tax advisors with respect to State of California personal income tax and federal income tax consequences of owning such 2019A Certificates.

California Tax Status. In the further opinion of Special Counsel, the portion of Lease Payments designated as and comprising interest and received by the owners of the 2019A Certificates is exempt from California personal income taxes.

The complete text of the final opinion that Special Counsel expects to deliver upon the delivery of the 2019A Certificates is set forth in APPENDIX D—FORM OF OPINION OF SPECIAL COUNSEL.

2019B Certificates

Federal Tax Status. The portion of Lease Payments designated as and comprising interest and received by the owners of the 2019B Certificates is not intended by the City to be excluded from gross income for federal income tax purposes.

California Tax Status. In the further opinion of Special Counsel, the portion of Lease Payments designated as and comprising interest and received by the owners of the 2019B Certificates is exempt from California personal income taxes.

The complete text of the final opinion that Special Counsel expects to deliver upon the delivery of the 2019B Certificates is set forth in APPENDIX D—FORM OF OPINION OF SPECIAL COUNSEL.

Other Tax Considerations

Current and future legislative proposals, if enacted into law, clarification of the Tax Code or court decisions may cause interest with respect to the 2019A Certificates to be subject, directly or indirectly, to federal income taxation or may cause interest with respect to the Certificates to be subject to or exempted from state income taxation, or otherwise prevent beneficial owners from realizing the full current benefit of the tax status of such interest. The introduction or enactment of any such legislative proposals, clarification of the Tax Code or court decisions may also affect the market price for, or marketability of, the Certificates. It cannot be predicted whether or in what form any such proposal might be enacted or whether, if enacted, such legislation would apply to Certificates issued prior to enactment.

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

Owners of the Certificates should also be aware that the ownership or disposition of, or the accrual or receipt of interest with respect to, the Certificates may have federal or state tax consequences

other than as described above. Other than as expressly described above, Special Counsel expresses no opinion regarding any federal or state tax consequences arising with

UNDERWRITING

The 2019A Certificates are being purchased by Stifel, Nicolaus & Company, Incorporated (the “Underwriter”). The Underwriter will agree to purchase the 2019A Certificates at a price of \$31,656,950.22 (representing an aggregate principal amount of the 2019A Certificates of \$26,785,000.00, plus an original issue premium of \$4,926,606.10, less an Underwriter’s discount of \$54,655.88). The purchase agreement relating to the 2019A Certificates provides that the Underwriter will purchase all of the 2019A Certificates if any are purchased, the obligation to make such purchase being subject to certain terms and conditions set forth in said purchase agreement, approval of certain legal matters by counsel and certain other conditions. After a bona fide initial public offering at the prices stated on the inside cover page hereof, the Underwriter may offer and sell the 2019A Certificates to certain dealers and others at prices lower than the initial public offering prices. The offering prices may be changed from time to time by the Underwriter.

The 2019B Certificates are also being purchased by the Underwriter. The Underwriter will agree to purchase the 2019B Certificates at a price of \$10,563,400.88 (representing an aggregate principal amount of the 2019B Certificates of \$10,585,000.00, less an Underwriter’s discount of \$21,599.12). The purchase agreement relating to the 2019B Certificates provides that the Underwriter will purchase all of the 2019B Certificates if any are purchased, the obligation to make such purchase being subject to certain terms and conditions set forth in said purchase agreement, approval of certain legal matters by counsel and certain other conditions. After a bona fide initial public offering at the prices stated on the inside cover page hereof, the Underwriter may offer and sell the 2019B Certificates to certain dealers and others at prices lower than the initial public offering prices. The offering prices may be changed from time to time by the Underwriter.

RATING

S&P Global Ratings, a Standard & Poor’s Financial Services LLC business (“S&P”) has assigned the rating of “AA+” to the Certificates. Such rating reflects only the view of S&P and any desired explanation of the significance of such rating should be obtained from S&P at the following address: 55 Water Street, New York, NY 10041, (212) 208-8000. Generally, a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance such rating will continue for any given period of time or that such rating will not be revised downward or withdrawn entirely by S&P if, in the judgment of S&P, circumstances so warrant. Any such downward revision or withdrawal of such rating may have an adverse effect on the market price for the Certificates.

FINANCIAL STATEMENTS

The City’s Audited Financial Statements for fiscal year ended June 30, 2018, and the City’s Auditor’s Report regarding such financial statements, are set forth in APPENDIX B—COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY FOR THE YEAR ENDED

JUNE 30, 2018. The City's Auditor was not requested to consent to the inclusion of its report in Appendix B and it has not undertaken to update financial statements included in Appendix B. No opinion is expressed by the City's Auditor with respect to any event subsequent to its report. This and prior year's annual financial reports can also be obtained at: <https://www.cityofpaloalto.org/gov/depts/asd/reporting.asp>.

ADDITIONAL INFORMATION

To assist investors with complying with applicable Federal Home Loan Bank collateral regulations, the City presently contemplates that approximately 100% of the proceeds of the Certificates will be used to finance the acquisition, development, and/or improvement of real estate.

All of the preceding summaries of the Certificates, the Trust Agreement, the Lease Agreement, the Assignment Agreement, the Property Lease, and other documents are made subject to the provisions of such documents respectively and do not purport to be complete statements of any or all of such provisions. Reference is hereby made to such documents on file with the City for further information in connection therewith.

This Official Statement does not constitute a contract with the purchasers of the Certificates.

Any statements made in this Official Statement involving matters of opinion or estimates, whether or not so expressly stated, are set forth as such and not as representations of fact, and no representation is made that any of the estimates will be realized.

References are made herein to certain documents and reports which are brief summaries thereof which do not purport to be complete or definitive and reference is made to such documents and reports for full and complete statements of the contents thereof.

The City will furnish a certificate dated the date of delivery of the Certificates, from an appropriate officer of the City, to the effect that to the best of such officer's knowledge and belief, and after reasonable investigation, (i) neither the Official Statement or any amendment or supplement thereto contains any untrue statement of a material fact or omits to state any material fact necessary to make the statements therein, in light of the circumstances in which they were made, not misleading; (ii) since the date of the Official Statement, no event has occurred which should have been set forth in an amendment or supplement to the Official Statement which has not been set forth in such an amendment or supplement, and the Certificates, the Trust Agreement, the Lease Agreement, the Assignment Agreement, the Property Lease, and other applicable agreements conform as to form and tenor to the descriptions thereof contained in the Official Statement; and (iii) the City has complied with all the agreements and has satisfied all the conditions on its part to be performed or satisfied under the Trust Agreement at and prior to the date of the issuance of the Certificates.

The execution and delivery of the Official Statement by the City have been duly authorized by the City Council on behalf of the City.

CITY OF PALO ALTO

By _____ /s/ Edward K. Shikada _____
City Manager

APPENDIX A

GENERAL, ECONOMIC AND DEMOGRAPHIC INFORMATION RELATING TO THE CITY AND THE COUNTY

The City

Palo Alto (the “City”) is located in northern Santa Clara County (the “County”), approximately 35 miles south of the City of San Francisco. It is part of the San Francisco Bay metropolitan area. The City is considered the birthplace of the high technology industry and a center of the Silicon Valley. Stanford University covers a 700-acre area in the City, and the City is home to high-tech leaders such as Hewlett-Packard, SAP America, Varian Medical Systems, VMware, Tibco Software, the Electric Power Research Institute, Communications and Power Industries and Skype. The City is also a major employment center, including U.S. Department of Veterans Affairs, Palo Alto Health Care System, Stanford Hospitals and Clinics, Lockheed Martin Missiles and Space, Palo Alto Medical Foundation, Stanford Shopping Center, the law offices of Wilson Sonsini Goodrich and Rosati, and the Xerox Palo Alto Research Center.

The County

Located at the southern end of the San Francisco Bay, the County is the most populous county in the San Francisco Bay Area region, and one of the most affluent counties in the United States. The County was one of the original counties of California, formed in 1850 at the time of statehood. The County seat is San Jose, the tenth-most populous city in the United States. According to the U.S. Census Bureau, the county has a total area of 1,304 square miles (3,380 km²), of which 1,290 square miles (3,300 km²) is land and 14 square miles (36 km²) (1.1%) is water.

The highly urbanized Santa Clara Valley within the County is also known as Silicon Valley. The County is the headquarters for approximately 6500 high technology companies, including many of the largest tech companies in the world, among them hardware manufacturers AMD, Cisco Systems and Intel, computer and consumer electronics companies Apple Inc. and Hewlett-Packard, and internet companies eBay, Facebook, Google and Yahoo!

Population

The following table contains the population of the City, the County and the State of California (the “State”) for the last five years.

CITY OF PALO ALTO, SANTA CLARA COUNTY AND STATE OF CALIFORNIA

Population (as of January 1)

Year	City of Palo Alto	Santa Clara County	State of California
2014	67,633	1,880,197	38,568,628
2015	68,312	1,905,156	38,912,464
2016	69,184	1,924,582	39,179,627
2017	69,446	1,937,473	39,500,973
2018	69,721	1,956,598	39,809,693

Source: California Department of Finance, E-4 Population Estimate for Cities, Counties, and the State, 2010-2017, with 2010 Census Benchmark.

Employment

The following table summarizes the historical numbers of workers by industry in the County for the last five years:

SANTA CLARA COUNTY Labor Force and Industry Employment Annual Averages by Industry

	2013	2014	2015	2016	2017 ⁽¹⁾
Total, All Industries	950,700	991,000	1,028,900	1,060,600	1,086,900
Total Farm	3,300	3,500	3,700	3,900	3,500
Mining and Logging	300	300	200	300	200
Construction	36,700	38,800	42,900	47,600	48,300
Manufacturing	153,600	156,700	160,200	161,300	163,400
Wholesale Trade	36,000	36,900	36,800	37,400	35,200
Retail Trade	82,500	83,900	85,100	85,000	85,000
Transportation, Warehousing & Utilities	13,400	13,900	14,100	14,800	14,900
Information	58,600	65,600	70,400	74,500	85,000
Financial Activities	33,300	33,800	34,200	35,200	35,800
Professional & Business Services	190,100	201,800	215,200	224,100	226,400
Educational & Health Services	142,600	148,700	154,900	160,600	167,400
Leisure & Hospitality	86,300	90,700	94,500	97,600	100,800
Other Services	25,000	26,000	26,500	27,000	28,200
Government	89,000	90,600	90,100	91,200	92,800

Source: California Employment Development Department, based on March 2018 benchmark.

Note: Does not include proprietors, self-employed, unpaid volunteers or family workers, domestic workers in households, and persons involved in labor/management trade disputes. Employment reported by place of work. Items may not add to totals due to independent rounding.

(1) Last available full year data.

The following tables summarize historical employment and unemployment for the County, the State and the United States:

SANTA CLARA COUNTY, CALIFORNIA, and UNITED STATES
Civilian Labor Force, Employment, and Unemployment
(Annual Averages)

Year	Area	Labor Force	Employment	Unemployment	Unemployment Rate ⁽¹⁾
2013	Santa Clara County	923,200	860,100	63,200	6.8%
	California	18,811,400	17,397,100	1,414,300	7.5
	United States	155,389	143,929,000	11,460,000	7.4
2014	Santa Clara County	995,600	943,800	51,800	5.2
	California	18,981,800	17,798,600	1,183,200	6.2
	United States	155,922,000	146,305,000	9,617,000	6.2
2015	Santa Clara County	1,018,400	976,100	42,300	4.2
	California	19,102,700	18,065,000	1,037,700	5.4
	United States	157,130,000	148,834,000	8,296,000	5.3
2016	Santa Clara County	1,026,500	987,900	38,600	3.8
	California	19,102,700	18,065,000	1,037,700	5.4
	United States	159,187,000	151,436,000	7,751,000	4.9
2017 ⁽²⁾	Santa Clara County	1,042,000	1,008,600	33,400	3.2
	California	19,312,000	18,393,100	918,900	4.8
	United States	160,320,000	153,337,000	6,982,000	4.4

Source: California Employment Development Department, Monthly Labor Force Data for Counties, Annual Average 2010-2017, and US Department of Labor.

- (1) The unemployment rate is computed from unrounded data; therefore, it may differ from rates computed from rounded figures available in this table.
- (2) Latest available full-year data.

Major Employers

The following table lists the top 10 employers within the County as of June 30, 2018.

SANTA CLARA COUNTY Top 10 Employers as of June 30, 2018

Employer	Employees	% of Total County Employment
Apple Computer, Inc.	25,000	2.44%
Google Inc.	20,000	1.95
County of Santa Clara	18,806	1.84
Stanford University	16,919	1.65
Cisco Systems Inc.	14,120	1.38
Kaiser Permanente	12,500	1.22
Stanford Healthcare	10,034	0.98
Tesla Motors Inc.	10,000	0.98
Intel Corp	8,450	0.83
City of San Jose	6,159	0.60
Total Top 10	141,988	13.87

Source: Santa Clara County fiscal year 2017-18 CAFR.

Construction Activity

The following table reflects the five-year history of building permit valuation for the City and the County:

CITY OF PALO ALTO Building Permits and Valuation (Dollars in Thousands)

	2013	2014	2015	2016	2017 ⁽¹⁾
Permit Valuation:					
New Single-family	\$ 44,914	\$ 53,439	\$ 73,403	\$ 58,795	\$ 76,244
New Multi-family	17,243	1,611	68,911	5,764	9,262
Res. Alterations/Additions	31,663	47,974	41,848	36,423	70,538
Total Residential	93,821	103,025	184,163	100,983	156,046
Total Nonresidential	358,254	258,899	277,837	298,797	357,789
Total All Building	\$452,076	\$361,925	\$462,000	\$399,780	513,835
New Dwelling Units:					
Single Family	81	93	119	96	119
Multiple Family	100	6	210	30	28
Total	181	99	329	126	147

Source: Construction Industry Research Board: "Building Permit Summary."

(1) Latest available full year data.

Note: Totals may not add due to independent rounding.

SANTA CLARA COUNTY
Building Permits and Valuation
(Dollars in Thousands)

	2013	2014	2015	2016	2017 ⁽¹⁾
<u>Permit Valuation:</u>					
New Single-family	\$ 694,884	\$ 594,472	\$ 653,970	\$ 660,301	\$ 732,652
New Multi-family	941,420	1,196,127	706,781	564,761	1,027,651
Res. Alterations/Additions	423,739	439,747	505,844	484,820	547,991
Total Residential	<u>2,060,044</u>	<u>2,230,347</u>	<u>1,866,595</u>	<u>1,709,882</u>	<u>2,308,295</u>
Total Nonresidential	6,264,620	2,655,412	3,589,800	4,698,158	3,359,316
Total All Building	<u>\$8,324,665</u>	<u>\$4,885,760</u>	<u>\$5,456,396</u>	<u>\$6,408,041</u>	<u>5,667,612</u>
<u>New Dwelling Units:</u>					
Single Family	1,859	1,602	1,710	1,608	2,022
Multiple Family	<u>6,009</u>	<u>8,310</u>	<u>3,906</u>	<u>3,297</u>	<u>6,629</u>
Total	<u>7,868</u>	<u>9,912</u>	<u>5,616</u>	<u>4,905</u>	<u>8,631</u>

Source: Construction Industry Research Board: "Building Permit Summary."

(1) Latest available full year data.

Note: Totals may not add due to independent rounding.

Median Household Income

The following table summarizes the total effective buying income and the median household effective buying income for the City, the County, the State and the nation for the past five years.

CITY OF PALO ALTO, SANTA CLARA COUNTY STATE OF CALIFORNIA AND UNITED STATES Median Household Effective Buying Income

Year	Area	Total Effective Buying Income (000's Omitted)	Median Household Effective Buying Income
2014	City of Palo Alto	\$ 4,119,935	\$ 94,580
	Santa Clara County	66,130,110	75,008
	California	901,189,699	50,072
	United States	7,357,153,421	45,448
2015	City of Palo Alto	4,607,638	103,965
	Santa Clara County	73,637,380	79,345
	California	981,231,666	53,589
	United States	7,757,960,399	46,738
2016	City of Palo Alto	4,797,181	105,019
	Santa Clara County	77,917,425	81,466
	California	1,036,142,723	55,681
	United States	8,132,748,136	48,043
2017	City of Palo Alto	5,275,790	121,376
	Santa Clara County	85,859,495	88,243
	California	1,113,648,181	59,646
	United States	8,640,770,229	50,735
2018	City of Palo Alto	5,462,441	123,583
	Santa Clara County	91,332,099	92,773
	California	1,183,264,399	62,637
	United States	9,017,967,563	52,841

Source: Nielsen, Inc.

APPENDIX B

COMPREHENSIVE ANNUAL FINANCIAL REPORT OF THE CITY FOR THE YEAR ENDED JUNE 30, 2018

The Auditor was not requested to consent to the inclusion of its report in this Appendix B and it has not undertaken to update financial statements included in this Appendix B. No opinion is expressed by the Auditor with respect to any event subsequent to its report.

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2017 - 2018

Comprehensive Annual Financial Report



City of Palo Alto, California

Fiscal Year Ended: June 30, 2018





CITY OF
**PALO
ALTO**

Fiscal Year 2018 Comprehensive Annual Financial Report

City of Palo Alto, CA
Fiscal Year Ended June 30, 2018

City Council

Liz Kniss, Mayor

Eric Filseth, Vice Mayor

Tom DuBois

Adrian Fine

Karen Holman

Lydia Kou

Gregory Scharff

Greg Tanaka

Cory Wolbach

James Keene, City Manager

Edward K. Shikada, Assistant City Manager/Utilities General Manager

Kiely Nose, Interim Director of Administrative Services/Chief Financial Officer

Rima Lobo, Finance Manager

Prepared by: Administrative Services Department

CITY OF PALO ALTO
For the Year Ended June 30, 2018

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City of Palo Alto

Office of the City Manager

Transmittal Letter.....

November 19, 2018

THE HONORABLE CITY COUNCIL

Palo Alto, California

Attention: Finance Committee

COMPREHENSIVE ANNUAL FINANCIAL REPORT

YEAR ENDED JUNE 30, 2018

Members of the Council and Citizens of Palo Alto:

I am pleased to present the Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2018 in accordance with Article III, Section 16 and Article IV, Section 13 of the City of Palo Alto Charter. The format and content of this CAFR complies with the principles and standards of accounting and financial reporting adopted by the Governmental Accounting Standards Board (GASB), and contains all information needed for readers to gain a reasonable understanding of City of Palo Alto financial affairs. Management takes sole responsibility for the completeness and reliability of the information contained in this report, based upon a comprehensive framework of internal control that it has established for this purpose. The objective of internal controls is to provide reasonable, rather than absolute, assurance that the financial statements are free of any material misstatements.

The City of Palo Alto's financial statements have been audited by Macias Gini & O'Connell LLP, Certified Public Accountants. The goal of the audit is to obtain reasonable assurance that the financial statements are free of material misstatements and are fairly presented in conformity with generally accepted accounting principles (GAAP). Macias Gini & O'Connell issued an unqualified opinion for the fiscal year ended June 30, 2018. Their report is presented as the first component of the financial section of this report.

In addition, Macias Gini & O'Connell conducted the federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. The standards governing the Single Audit require the independent auditor to report on the fair presentation of the financial statements, government's internal controls and compliance with legal requirements. These reports are included in the Single Audit section of the CAFR.

An overview of the City's financial activities for the fiscal year is discussed in detail in the Management's Discussion and Analysis (MD&A) section of the CAFR. MD&A complements this transmittal letter and should be read in conjunction with it.

CITY OF PALO ALTO PROFILE

Palo Alto was incorporated in 1894 and named after a majestic coastal redwood tree which lives along the San Francisquito Creek where early Spanish explorers settled. Located between the cities of San Francisco and San Jose, Palo Alto is a largely built-out community of approximately 67,000 residents. Palo Alto delivers a full range of municipal services and public utilities under the Council-Manager form of government, and offers an outstanding quality of life for its residents. It covers an area of twenty-six square miles, and has dedicated almost one-half of the area to open spaces of parks and wildlife preserves. Public facilities include five libraries, four community centers, a cultural arts center, an adult and children’s theater, a junior museum and zoo, and a golf course. The City provides a diverse array of services for seniors and youth, an extensive continuing education program, concerts, exhibits, team sports and special events. The independent Palo Alto Unified School District (PAUSD) has achieved state and national recognition for the excellence of its programs.

City Council: Council consists of nine members elected at-large for four year staggered terms. At the first meeting of each calendar year, Council elects a Mayor and Vice-Mayor from its membership, with the Mayor having the duty of presiding over Council meetings. Council is the appointing authority for the positions of City Manager and three other officials, the City Attorney, City Clerk, and City Auditor, all of whom report to Council. Effective January 1, 2019, Council will be reduced from nine to seven members.

Finance Committee and Policy and Services Committee: While retaining the authority to approve all actions, Council has established two subcommittees to consider and make recommendations on matters relating to finance, budget, audits, capital planning and debt. Each of the subcommittee is comprised of four Council members. Staff provides the subcommittees and Council with reports such as the CAFR, quarterly budget-versus-actual results, and investment and performance measure reports, all of which are utilized in their review of the City’s financial position.

FISCAL/ECONOMIC CONDITIONS AND OUTLOOK

Employment Trends: The City of Palo Alto is located in the heart of Silicon Valley and is adjacent to Stanford University, one of the premier institutions of higher education in the nation which has produced much of the talent that founded many successful high-tech companies in Palo Alto and Silicon Valley. With varied and relatively stable employers such as Stanford University, Stanford Medical Center, Palo Alto Medical Foundation, Palo Alto Unified School District, Stanford Shopping Center and businesses such as Hewlett-Packard, VMware, Tesla, Palantir and Space Systems Loral, Palo Alto has enjoyed diverse employment and revenue bases. The City’s unemployment rate ended the year at 2.2 percent. This compares to Santa Clara County’s unemployment rate of 2.7 percent. The state’s unemployment rate was 4.5 percent.

Real Estate Market: In its most recent annual report, the Santa Clara County Assessor’s Office noted that Santa Clara County’s 2017/2018 assessment roll increased 7.4 percent, from \$419 billion to \$450 billion. The assessment roll growth was balanced throughout the County, with Santa Clara and Mountain View once again led the highest growth. Palo Alto’s assessment roll growth rate was 7.8 percent, compared to 8.6 percent in the prior report. Reassessment of changes in ownership, significant new construction and the increase in the value of new business property were the primary factors contributing to the robust growth. With its highly regarded school district, well-educated and high-income population, cultural amenities, and the presence of Stanford University, the City’s real estate activity continues to experience a pattern of high demand and short supply. The result of this continued pattern is reflected in the increase in FY 2018 property tax revenue.



Local Trends: National, state, regional and local economic indicators point toward continuously improving economic growth. Economically sensitive revenue sources such as transient occupancy tax and documentary transfer tax remain strong, while sales tax revenue has levelled off. The robust local economy and job growth are also driving increases in other revenues, such as permit and license fees.

Looking forward, funding sources are sufficient to cover projected FY 2019 and FY 2020 expenses, as written in the City’s Adopted Budget. The Council adopted a General Fund budget with expenses of \$210.7 million for FY 2019 an increase of 0.1 percent from the prior year Adopted Budget. This modest increase is due primarily to a downward adjustment in expenses of \$4.0 million as directed by the City Council. Through strategic actions taken over the past few years, the City was able to deal with increasing salary and benefit costs, increase its investments in infrastructure, and proactively contribute to the City’s irrevocable Section 115 Pension Trust Fund, while balancing the General Fund in FY 2019. Through the Budget Adoption process, the City Council directed staff to identify an additional \$4.0 million in savings, which is recognized as a contribution to the Budget Stabilization Reserve in the FY 2019 Adopted Operating Budget. Staff anticipates returning to the City Council to identify the \$4.0 million in savings during FY 2019 and incorporating the policy direction from City Council into the FY 2019 Operating Budget and into the development of the FY 2020 Operating Budget.

Pension and healthcare costs continue to dominate the conversation about long-term future costs. The most recent actuarial valuations show unfunded liabilities for pension and healthcare totaling \$558 million. The City has proactively taken steps over the past several years to mitigate increased costs by increasing employee contributions to the CalPERS retirement plan and capping the City’s share of healthcare premiums. Implementation of a second tier retirement plan in 2011 and adoption of the state-mandated third tier pension benefit plan in 2013 also helps mitigate future pension cost increases. The most recent labor agreements with the Safety units increase the employee pick-up of the employer share over the term of the agreement. The current labor agreements with the miscellaneous groups also include this cost-sharing mechanism. Further pension cost sharing with employees could be necessary to fund future cost increases. The City has established an irrevocable Section 115 Pension Trust Fund that is separate from CalPERS and could act as a mitigation reserve if the City were unable to meet its annual required contribution due to budget constraints in a given year. As of the end of Fiscal Year 2018, the City has contributed \$5.5 million to this trust, of which \$3.4 million is from the General Fund. Additional contributions are included in the FY 2019 Adopted Operating Budget to bring the total to \$7.6 million across all funds, of which \$4.6 million would be from the General Fund.

As economic growth continues to flourish in this area of Silicon Valley, it also underscores the challenges of increased traffic and congestion, affordable housing and demand for services. These issues were reflected in the setting of Council priorities for 2018:

- Transportation
- Housing
- Budget and Finance (focus on funding our infrastructure and pensions)
- Grade Separation (choose preferred alternative by end of year)



In keeping with these priorities, the City has begun to implement various strategies to address traffic congestion in the City, including: parking management (Residential Preferential Parking program, parking technology enhancements, garage wayfinding signage), CalTrain Grade Separation, transportation demand management (Transportation Management Association, enhanced shuttle

services, CalTrain GoPass program for employees) and short and long-term parking supply strategies (valet parking, construction of new garages). Recent budgets reflect longer-term goals of the City Council and position the City to be able to address increases in pension costs and new labor agreement negotiations, while highlighting the need to address the future year costs to complete the Infrastructure Plan.

In FY 2014, the City Council approved a \$125.8 million Infrastructure Plan (IP), which includes projects such as a new Public Safety Building, replacement of two Fire Stations, a Bike and Pedestrian plan and two parking garages. Through the development of the 2019-2023 CIP, the IP was updated for scope increases and cost escalations, resulting in a revised Infrastructure Plan of \$249.9 million. These projects will be funded partially by debt to be repaid with an increase in the transient occupancy tax (TOT) rate which went into effect in January 2015, TOT from newly opened hotels, and from other sources such as impact fees and Stanford University Medical Center development agreement monies totaling \$186.7 million. Staff was tasked with closing this funding gap in the FY 2019 budget process, and this was done through project prioritization within the 2019-2023 CIP and additional revenue assumptions. The 2019-2023 CIP assumes the opening of new Marriott hotels in FY 2020. Based on this, an additional \$3.6 million of annual TOT funding as well as one time COP issuance of \$35.2 million is estimated to cover the cost of the IP projects.

Rate increases will take effect in FY 2019 for electric, fiber optics, gas, storm drain, wastewater, and water services. In general, the size and timing of rate adjustments take into account current and future revenue requirements and reserve levels for needs such as increasing costs of commodity purchases, capital construction costs, and contractually obligated increases to compensate for inflation, usually based on the annual change to the Bay Area consumer price index (CPI).

Long Range Financial Forecast: The City produces a 10 year General Fund Long Range Financial Forecast (LRFF) annually. This comprehensive report analyzes local, state, and federal economic conditions, short and long-term revenue and expense trends, and addresses challenges such as funding long-term pension and healthcare liabilities and infrastructure needs. The forecast is designed to highlight finance issues which the City can address proactively. Moreover, it is a tool that allows policymakers an opportunity to prioritize funding needs over time. It sets the tone for the annual budget process and is one of the many tools and reports that Council uses for financial planning.

The FY 2019 – FY 2028 LRFF was presented to the Finance Committee in December 2017 and to the City Council in January 2018. The FY 2019 forecast anticipated a near-term gap in the General Fund. Staff identified and recommended a course of action that would structurally balance the General Fund in FY 2019 and largely balance the General Fund on an ongoing basis. As discussed above, during the adoption of the FY 2019 Operating Budget, the City Council directed that an additional \$4.0 million be reduced in the General Fund, which has been recognized in the Budget Stabilization Reserve (BSR) in the FY 2019 Budget. By policy, the City maintains a General Fund BSR level of 15 to 20 percent of the General Fund Operating Budget, with a target of 18.5 percent. As of June 30, 2018 the BSR balance is \$52.8 million. Staff will bring forward recommendations regarding the potential uses of the BSR as part of the FY 2018 year-end close process.

Both Moody’s and Standard and Poor’s (S&P) awarded their highest credit rating of Triple A to the City’s general obligation debt. This rating has been awarded to only a few cities in California.

SIGNIFICANT EVENTS AND ACCOMPLISHMENTS



The City of Palo Alto is a community dedicated to meeting the social, cultural, recreational, educational, commercial and retail needs of its citizens and businesses. As such, open space, the environment, education, recreational facilities, cultural events and safe streets and neighborhoods are important aspects of the community. The City has been recognized for its accomplishments with a wide variety of awards and recognitions over the past year. Following is a sampling:

- Recipient of the Acterra Business Environmental Award and the Acterra Award for Sustainability in recognition of the City’s overall approach, commitment and leadership in sustainability.
- Awarded Voice of the People Award for Excellence in the Natural Environment by the National Research Center for being a top performing jurisdiction in the National Citizen Survey.
- Santa Clara County presented Palo Alto with the Top Public Health Award for reducing second hand smoke, the Safe Routes to School program and offering healthier choices in public facilities like water bottle filling stations and healthy snacks.
- The World Health Organization recognized Palo Alto as an Age-Friendly City for involving older adults in decision-making, encouraging older adults to remain in the community and promoting their autonomy.
- Recipient of the Platinum Level Beacon Award – the highest level possible – for its effort and leadership in addressing climate change.
- Awarded gold level status as a Bicycle Friendly Community by the League of American Bicyclists based on a strong commitment to bicycling evidenced by major streets with bike lanes, high ratio of bike network mileage to road network mileage, and Bike to Work events;
- Awarded Tree Line USA award by the National Arbor Day Foundation in recognition of the Utilities exceeding the standard criteria for quality tree care, annual worker training, tree planting and public education, a tree-based energy conservation program, and an Arbor Day celebration.

Awards: During the past year, the City received an award for the prior fiscal year CAFR from the Government Finance Officers Association (GFOA) for “excellence in financial reporting.” The 2018 CAFR will be submitted to the GFOA award program to be considered for this distinguished financial reporting award.

Acknowledgments: This CAFR reflects the hard work, talent and commitment of the staff members of the Administrative Services Department. This document could not have been accomplished without their efforts and each contributor deserves sincere appreciation. Management wishes to acknowledge the support of the entire accounting staff for their high level of professionalism and dedication. Management would also like to express its appreciation to Macias Gini & O’Connell, the City’s independent external auditors, who assisted and contributed to the preparation of this Comprehensive Annual Financial Report.



Special acknowledgment must be given to City Council and the Finance and Policy and Services Committees for their dedication to directing the financial affairs of the City in a responsible, professional and progressive manner.

Respectfully submitted,

KIELY NOSE,
Interim Chief Financial Officer

JAMES KEENE,
City Manager



City of Palo Alto City Officials

City Council

Liz Kniss, **Mayor**
Eric Filseth, **Vice-Mayor**
Tom DuBois
Adrian Fine
Karen Holman
Lydia Kou
Gregory Scharff
Greg Tanaka
Cory Wolbach

Finance Committee

Gregory Scharff, **Chair**
Eric Filseth
Lydia Kou
Greg Tanaka

Policy and Services Committee

Adrian Fine, **Chair**
Tom DuBois
Karen Holman
Cory Wolbach

Council-Appointed Officers

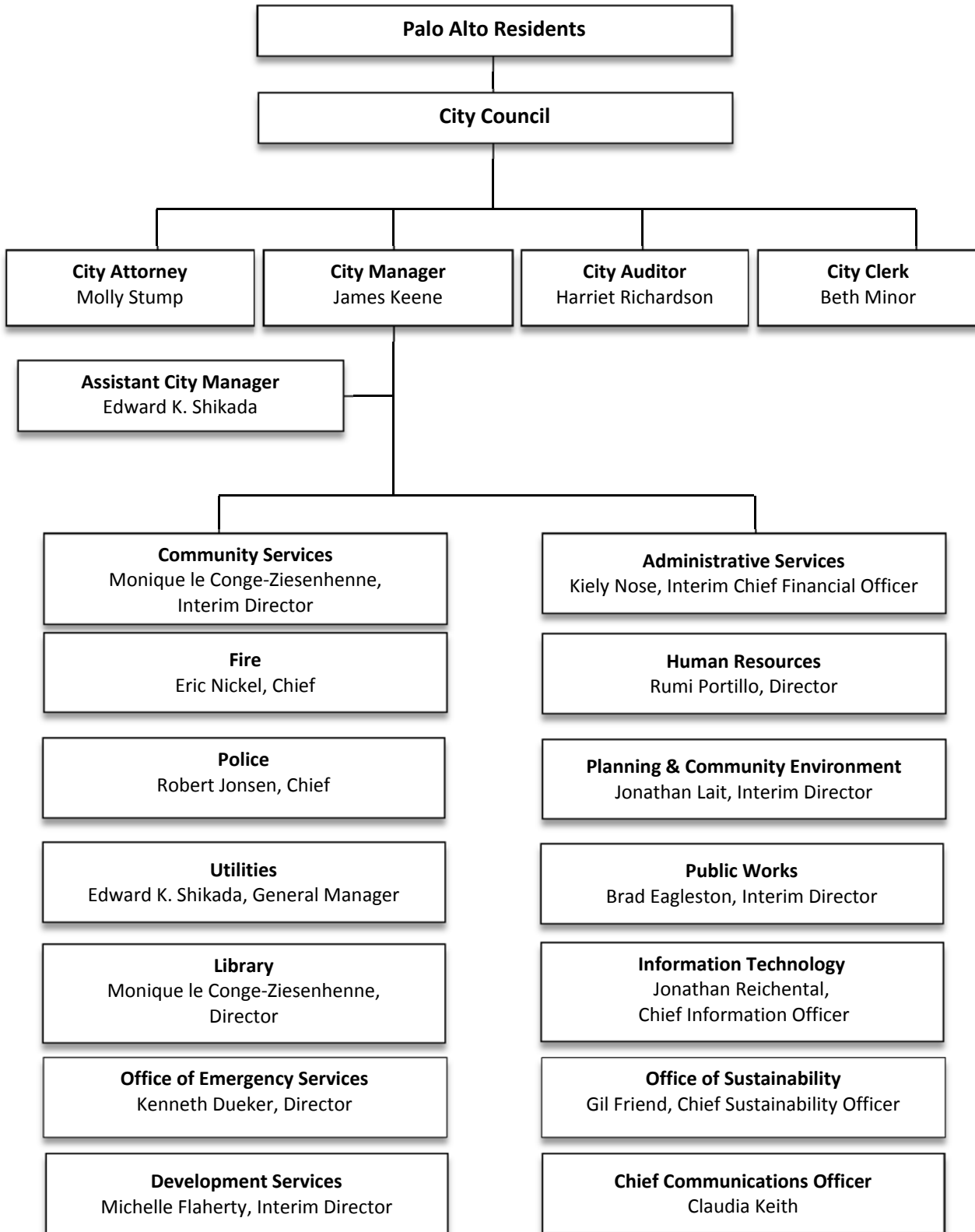
City Manager
James Keene

City Attorney
Molly Stump

City Clerk
Beth Minor

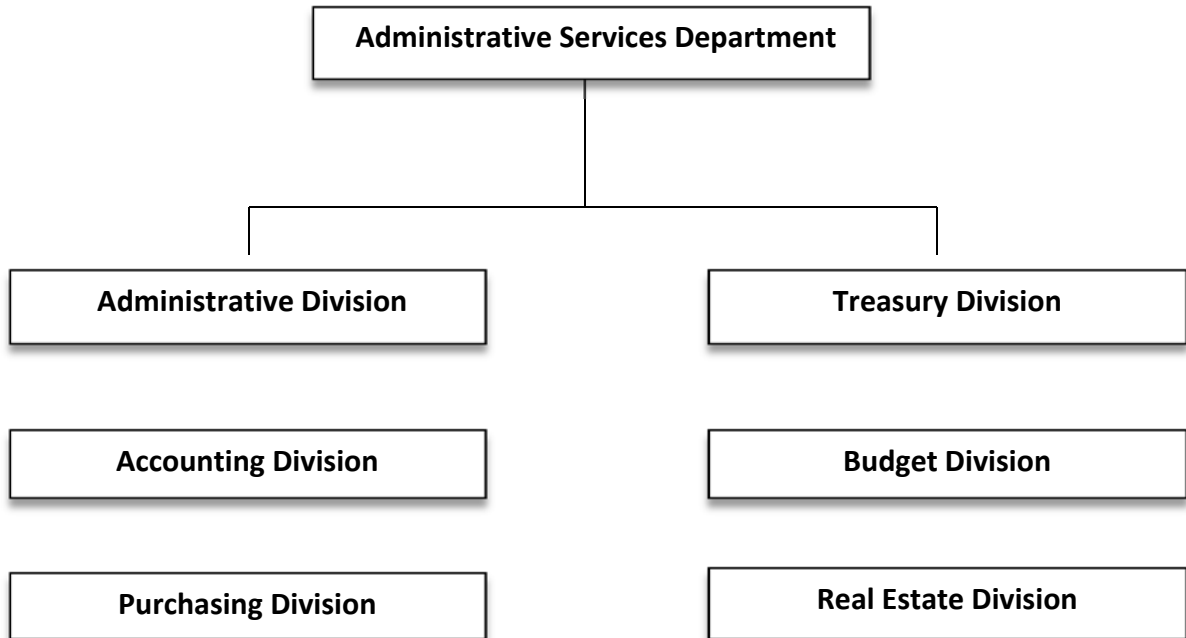
City Auditor
Harriet Richardson

City of Palo Alto Organization





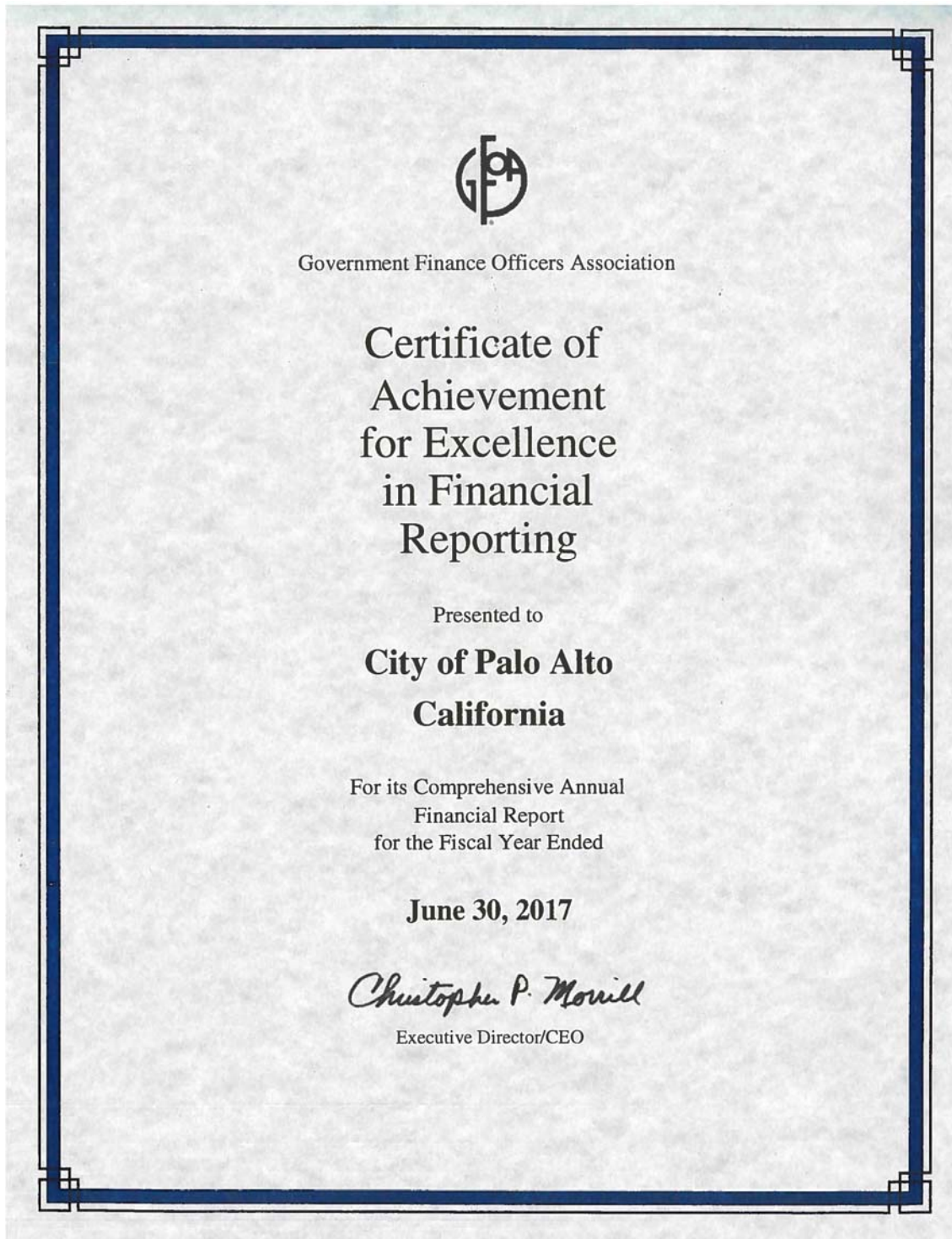
Administrative Services Organization



Mission Statement

To provide proactive administrative and technical support to City departments and decision makers, and to safeguard and facilitate the optimal use of City resources.

Government Finance Officers Association of the United States and Canada – Award





Independent Auditor's Report

Honorable Mayor and the Members
of the City Council of
City of Palo Alto, California

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Palo Alto, California (City), as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the City's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City as of June 30, 2018, and the respective changes in financial position, and, where applicable, cash flows thereof and the respective budgetary comparison for the General Fund for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1(n) to the financial statements, effective as of July 1, 2017, the City adopted the provisions of Governmental Accounting Standards Board Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the schedules of changes in net pension liability and related ratios and the schedules of contributions, the schedule of changes in net OPEB liability and related ratios, the schedule of employer OPEB contributions, as listed in the table of contents, be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City's basic financial statements. The introductory section, combining and individual nonmajor fund financial statements and schedules, statistical section and the schedule of expenditures of federal awards, as required by Title 2 U.S. Code of Federal Regulations Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards*, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The combining and individual nonmajor fund financial statements and schedules and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the combining and individual nonmajor fund financial statements and schedules and the schedule of expenditures of federal awards are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

The introductory and statistical sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated November 19, 2018 on our consideration of the City's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the City's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "Macias Gini & O'Connell LLP". The signature is written in a cursive, slightly slanted style.

Walnut Creek, California
November 19, 2018

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Management's Discussion and Analysis

Management's Discussion and Analysis (MD&A) provides an overview of the City of Palo Alto's financial performance for the fiscal year ended June 30, 2018. To obtain a complete understanding of the City's financial condition, this document should be read in conjunction with the accompanying Transmittal Letter and Basic Financial Statements.

Financial Highlights

- The assets and deferred outflows of resources of the City of Palo Alto (City) exceeded its liabilities and deferred inflows of resources at the close of Fiscal Year (FY) 2018 by \$1.1 billion. Of this amount, \$23.4 million represents unrestricted net position, which may be used to meet the government's ongoing obligations to citizens and creditors.
- At the close of FY 2018, the City's governmental funds reported combined fund balances of \$251.2 million, an increase of \$16.5 million from prior year. Approximately 21.1 percent of this amount, or \$52.8 million, is unassigned fund balance and available for spending at the government's discretion.
- At the end of the current fiscal year, unrestricted fund balance (the total of the committed, assigned and unassigned components of fund balance) for the General Fund was \$60.3 million, or 0.31 percent of total general fund expenditures, including transfers.
- The City's total outstanding long-term debt increased \$5.0 million during the current fiscal year. On June 1, 2018 the city issued \$9.0 million of Certificates of Participation (COPs) refinancing the 2002B Downtown parking Improvement projects COPs and providing new funding to finance the costs of the renovation of the Palo Alto Municipal Golf Course. The City received a loan of \$7.5 million from the State Water Resources Control Board (SWRCB) and was forgiven \$4.0 million of a prior loan under the terms of the contract with the SWRCB.
- The City implemented GASB Statement No.75, *Accounting and Reporting for Postemployment Benefits Other than Pensions*, effective July 1, 2017 and the balances were restated to reflect the impact. The City's net Other Postemployment Benefits (OPEB) liabilities of \$153.5 million was allocated to Governmental Activities (\$109.4 million or 71.3 percent) and Business-Type Activities (\$44.1 million or 28.7 percent) which reduced their unrestricted net positions by a like amount.

OVERVIEW OF THE COMPREHENSIVE ANNUAL FINANCIAL REPORT (CAFR)

The CAFR is presented in six sections:

- An introductory section that includes the Transmittal Letter and general information
- Management's Discussion and Analysis
- The Basic Financial Statements that include the Government-wide and Fund Financial Statements, along with the Notes to these statements
- Required and Other Supplemental Information
- Statistical Information
- Single Audit



Basic Financial Statements

The Basic Financial Statements contain the Government-wide Financial Statements, the Fund Financial Statements and the Notes to these financial statements. This report also includes supplementary information intended to furnish additional detail to support the Basic Financial Statements.

For certain entities and funds, the City acts solely as a depository agent. For example, the City has several Assessment Districts for which it produces fiduciary statements detailing the cash balances and activities of these districts. These entities are independent, and their balances are excluded from the City's government-wide financial statements.

Government-wide Financial Statements

The Government-wide Financial Statements provide a longer-term view of the City's activities as a whole. They include the Statement of Net Position and the Statement of Activities.

The Statement of Net Position includes the City's capital assets and long-term liabilities on a full accrual basis of accounting similar to that used by private sector companies. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the City is improving or deteriorating.

The Statement of Activities provides information about the City's revenues and expenses on a full accrual basis, with an emphasis on measuring net revenues or expenses for each of the City's programs. The Statement of Activities explains in detail the change in net position for the year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows.

The amounts in the Statement of Net Position and the Statement of Activities are separated into Governmental and Business-type Activities in order to provide a summary of each type of activity.

Governmental Activities - All of the City's basic services are considered to be governmental activities. Included in basic services are the City Council, City Manager, City Attorney, City Clerk, City Auditor, Administrative Services, Human Resources, Public Works, Planning and Community Environment, Development Services, Public Safety, Community Services, and Library. These services are supported by general City revenues such as taxes, and by specific program revenues such as fees and grants.

The City's governmental activities also include the activities of the Palo Alto Public Improvement Corporation, which is a separate legal entity financially accountable to the City.

Business-type Activities - All of the City's enterprise activities are reported as business-type activities, including Water, Electric, Fiber Optics, Gas, Wastewater Collection, Wastewater Treatment, Refuse, Storm Drainage and Airport. Unlike governmental services, these services are intended to recover all or a significant portion of their costs through user fees and charges, except for the Airport which is currently supported by a long-term advance from the General Fund, as discussed in Note 4.

The Government-wide Financial Statements can be found on pages 29-31 of this report.



Fund Financial Statements

The Fund Financial Statements provide detailed information about each of the City's most significant funds, called major funds. The concept of major funds, and the determination of which are major funds, was established by Governmental Accounting Standards Board (GASB) Statement No. 34 and replaced the concept of combining like funds and presenting them in total. Therefore, each major fund is presented individually, with all non-major funds combined in a single column on each fund statement. Subordinate schedules display these non-major funds in more detail. Major funds present the major activities of the City for the year. The General Fund is always considered a major fund, but other funds may change from year to year as a result of changes in the pattern of City activities.

The Fund Financial Statements display the City's operations in more detail than the Government-wide Financial Statements. Their focus is primarily on the short-term activities of the City's General Fund and other major funds.

Budget and actual financial comparison information is presented only for the General Fund. Fund Financial Statements include Governmental, Proprietary, and Fiduciary Funds.

Governmental Funds

Governmental Fund Financial Statements are prepared on the modified accrual basis of accounting, which means they measure only current financial resources and uses. Capital assets and other long-lived assets, along with long-term liabilities, are presented only in the Government-wide Financial Statements. In FY 2018, the City had two major governmental funds, the General Fund and the Capital Projects Fund. Data from the other governmental funds are combined into a single aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the Supplemental section of this report.

Because the focus of governmental funds is narrower than that of the Government-wide Financial Statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the Government-wide Financial Statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the Governmental Fund Balance Sheet and the Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The Governmental Fund Financial Statements can be found on pages 33-37 of this report.

Proprietary Funds

Enterprise and Internal Service Fund Financial Statements are prepared on the full accrual basis of accounting, similar to that used by private sector companies. These statements include all of their assets, deferred outflows and inflows of resources and liabilities, both current and long-term.

Since the City's Internal Service Funds provide goods and services exclusively to the City's governmental and business-type activities, their activities are only reported in total at the fund level. Internal Service Funds, such as Technology and General Benefits, cannot be considered major funds because their revenues are derived from other City funds. Revenues between funds are eliminated in the Government-wide Financial Statements, and any related profits or losses in Internal Service Funds are returned to the activities in which they were created, along with any residual net assets of the Internal Service Funds.

The Proprietary Fund Financial Statements can be found on pages 38-43 of this report.



Fiduciary Funds

The City is the fiduciary agent for certain assessment districts such as the University Avenue Area Off-Street Parking Assessment District. In this role, the City holds money collected from property owners and awaiting transfer to the districts' bond trustees. The City's fiduciary activities are reported in the separate Statement of Fiduciary Net Position and the supplemental Agency Funds Statement of Changes in Assets and Liabilities. These activities are excluded from the City's governmental-wide financial statements because the City cannot utilize these assets to finance its own operations.

The Fiduciary Fund Financial Statement can be found on page 44 of this report.

Notes to the Financial Statements

The Notes provide additional information that is necessary to acquire a full understanding of the data provided in the Government-wide and Fund Financial Statements. The Notes to the financial statements can be found on pages 47-106 of this report.

Other Information

The Required Supplementary Information related to the City's pension and OPEB plans is included after the Notes to the Financial Statements on pages 107-112. The combining statements referred to earlier in connection with non-major Governmental Funds and Internal Service Funds, are presented immediately following the Required Supplementary Information. Combining statements and individual fund statements and schedules can be found on pages 113-138 of this report.

Financial Analysis of Government-wide Financial Statements

This section focuses on the City's net position and changes in net position of its governmental and business-type activities for the fiscal year ending June 30, 2018. As noted earlier, the City's total assets and deferred outflows of resources exceeded total liabilities and deferred inflows of resources by \$1.1 billion at the end of the fiscal year, a change in net position of \$111.1 million.

STATEMENT OF NET POSITION
As of June 30, 2018
 (in millions)

	Governmental Activities		Business-type Activities		Government-wide Totals	
	2018	2017	2018	2017	2018	2017
Cash and investments	\$ 286.9	\$ 288.8	\$ 241.8	\$ 243.3	\$ 528.7	\$ 532.1
Other assets	62.5	63.7	42.1	44.7	104.6	108.4
Capital assets	547.7	522.5	636.7	595.2	1,184.4	1,117.7
Total Assets	897.1	875.0	920.6	883.2	1,817.7	1,758.2
Unamortized loss from refunding	-	-	0.2	0.3	0.2	0.3
Pension and OPEB related	78.8	52.8	28.9	19.2	107.7	72.0
Total Deferred Outflows of Resources	78.8	52.8	29.1	19.5	107.9	72.3
Net pension and OPEB liabilities	411.4	273.5	157.1	103.8	568.5	377.3
Long-term debt	75.1	69.3	66.1	67.0	141.2	136.3
Other liabilities	54.5	51.8	36.0	30.9	90.5	82.7
Total Liabilities	541.0	394.6	259.2	201.7	800.2	596.3
Pension and OPEB related	7.4	5.8	2.4	1.7	9.8	7.5
Total Deferred Inflows of Resources	7.4	5.8	2.4	1.7	9.8	7.5
Net Position						
Net investment in capital assets	473.2	453.9	573.7	532.0	1,046.9	985.9
Restricted	41.2	36.1	4.0	4.1	45.2	40.2
Unrestricted	(87.0)	37.3	110.4	163.2	23.4	200.5
Total Net Position	\$ 427.4	\$ 527.3	\$ 688.1	\$ 699.3	\$ 1,115.5	\$ 1,226.6

The largest portion of the City's net position (93.9 percent) is its net investment in capital assets such as land, buildings, infrastructure and vehicles, less any related outstanding debt that was used to acquire those assets. The City uses these capital assets to provide a variety of services to its citizens. Accordingly, these assets are not available for future spending. Although the City's investment in capital assets is reported net of related debt, it should be noted that the resources used to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.



The restricted portion of the City's net position (4.0 percent) represents resources that are subject to external restrictions on how they may be used. The remaining balance of \$23.4 million, representing 2.1 percent of the City's net position, is unrestricted and may be used to meet the government's ongoing obligations to its citizens and creditors.

The City implemented GASB 75 effective July 1, 2017. The beginning balance of FY 2017 net position was restated to reflect the impact of the implementation. The City's net OPEB asset that was reported in previous years, has been eliminated in accordance with the new OPEB standards. Compliance with GASB 75 resulted in reporting net OPEB liabilities on the Statement of Net Position for government-wide and proprietary fund financial statements, which reduces the unrestricted net position and, in some cases, creates a negative unrestricted net position.

Deferred OPEB contributions are the total amount of FY2018 contributions. The contributions are deferred to FY2019 because the measurement of the net OPEB liability balance is one year in arrears.

At June 30, 2018, the net OPEB liability represents the actuarially valued liability for OPEB benefits, less the amount of resources accumulated in the OPEB trust, as of June 30, 2017. The difference between expected and actual earnings on investments is the portion of investment gains that is deferred. The new accounting standards require the differences between the projected and actual investment returns be amortized on a straight-line basis over five years.

At the end of the current fiscal year, the City is able to report positive unrestricted net positions for the government as a whole. The unrestricted net position for governmental activities is negative due to the implementation of GASB Statement No 75. The business-type activities are positive except for two funds, Wastewater treatment fund and Airport fund are negative mainly due to the pension and OPEB related expenses.

Components of the \$111.1 million decrease in total net position are discussed in the following sections for governmental activities and business-type activities.

Governmental Activities – Net Position

The following analysis focuses on the net position and changes in net position of the City's Governmental Activities, presented in the Government-wide Statement of Net Position and Statement of Activities.

GOVERNMENTAL ACTIVITIES			
<i>Net Position at June 30</i>			
(in millions)			
	<u>2018</u>	<u>2017</u>	<u>Increase/ (Decrease)</u>
Cash and investments	\$ 286.9	\$ 288.8	\$ (1.9)
Other assets	62.5	63.7	(1.2)
Capital assets	547.7	522.5	25.2
Total Assets	<u>897.1</u>	<u>875.0</u>	<u>22.1</u>
Pension and OPEB related	78.8	52.8	26.0
Total Deferred Outflows of Resources	<u>78.8</u>	<u>52.8</u>	<u>26.0</u>
Net pension and OPEB liabilities	411.4	273.5	137.9
Long-term debt	75.1	69.3	5.8
Other liabilities	54.5	51.8	2.7
Total Liabilities	<u>541.0</u>	<u>394.6</u>	<u>146.4</u>
Pension and OPEB related	7.4	5.8	1.6
Total Deferred Inflows of Resources	<u>7.4</u>	<u>5.8</u>	<u>1.6</u>
Net investment in capital assets	473.2	453.9	19.3
Restricted	41.2	36.1	5.1
Unrestricted	(87.0)	37.3	(124.3)
Total Net Position	<u>\$ 427.4</u>	<u>\$ 527.3</u>	<u>\$ (99.9)</u>

The City's Governmental Activities total net position decreased \$99.9 million to \$427.4 million as of June 30, 2018. This decrease was a result of the following:

- Capital assets net of depreciation increased \$25.2 million due to major capital projects such as street and sidewalk improvements throughout the City, Bicycle Boulevard project, Fire station #3 project, Golf course reconfiguration, Baylands Athletic center project and Rinconada Park Improvements.
- Pension and OPEB related deferred outflows increased \$26 million due to the City implementing GASB 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pension* and for the changes in assumptions for pension.
- Net pension and OPEB liabilities increased \$137.9 million as the City implemented GASB 75, *Accounting and Financial Reporting for Postemployment Benefits Other than Pension* and for the changes in assumptions for pension.
- Long-term debt increased \$5.8 million due to the issuance of \$9.0 million in Certificates of Participation (COPs) to finance the renovation of the Palo Alto Municipal Golf Course and to refinance the 2002B Downtown Parking Improvement Project COPS.

- Net investment in capital assets increased \$19.3 million to \$473.2 million due to the current year capital additions noted above. Restricted net position increased \$5.1 million to \$41.2 million due primarily to the increased fund balance in the public benefit fund. Unrestricted net position decreased \$124.3 million from prior year. The unrestricted net position for governmental activities is negative primarily due to the implementation of GASB Statement No 75.

Governmental Activities – Revenues

The table below shows that Governmental Activities revenues totaled \$211.3 million in FY 2018, an increase of \$30.1 million from prior year revenues of \$181.2 million.

**GOVERNMENTAL ACTIVITIES
Revenues for the Year Ended June 30
(in millions)**

<u>Revenues by Source</u>	<u>2018</u>	<u>2017</u>	<u>Increase/ (Decrease)</u>
Program Revenues:			
Charges for services	\$ 63.4	\$ 57.3	\$ 6.1
Operating grants and contributions	14.1	2.0	12.1
Capital grants and contributions	1.5	1.9	(0.4)
Total Program Revenues	<u>79.0</u>	<u>61.2</u>	<u>17.8</u>
General Revenues:			
Property tax	47.2	44.0	3.2
Sales tax	31.1	29.9	1.2
Utility user tax	15.4	14.2	1.2
Transient occupancy tax	24.9	23.4	1.5
Documentary transfer tax	9.2	7.5	1.7
Other tax	2.1	1.5	0.6
Investment earnings	0.4	(0.7)	1.1
Rents and miscellaneous	2.0	0.2	1.8
Total General Revenues	<u>132.3</u>	<u>120.0</u>	<u>12.3</u>
Total Revenues	<u>\$ 211.3</u>	<u>\$ 181.2</u>	<u>\$ 30.1</u>

Program Revenues such as charges for services, operating grants and contributions, and capital grants and contributions are generated from or restricted to each activity. Total Program Revenues increased \$17.8 million from the prior year due to the following major factors:

- \$2.7 million increase in plan checking fee due to a decrease in deferred revenue.
- \$0.7 million increase in Golf Course related fees due to opening in May 2018.

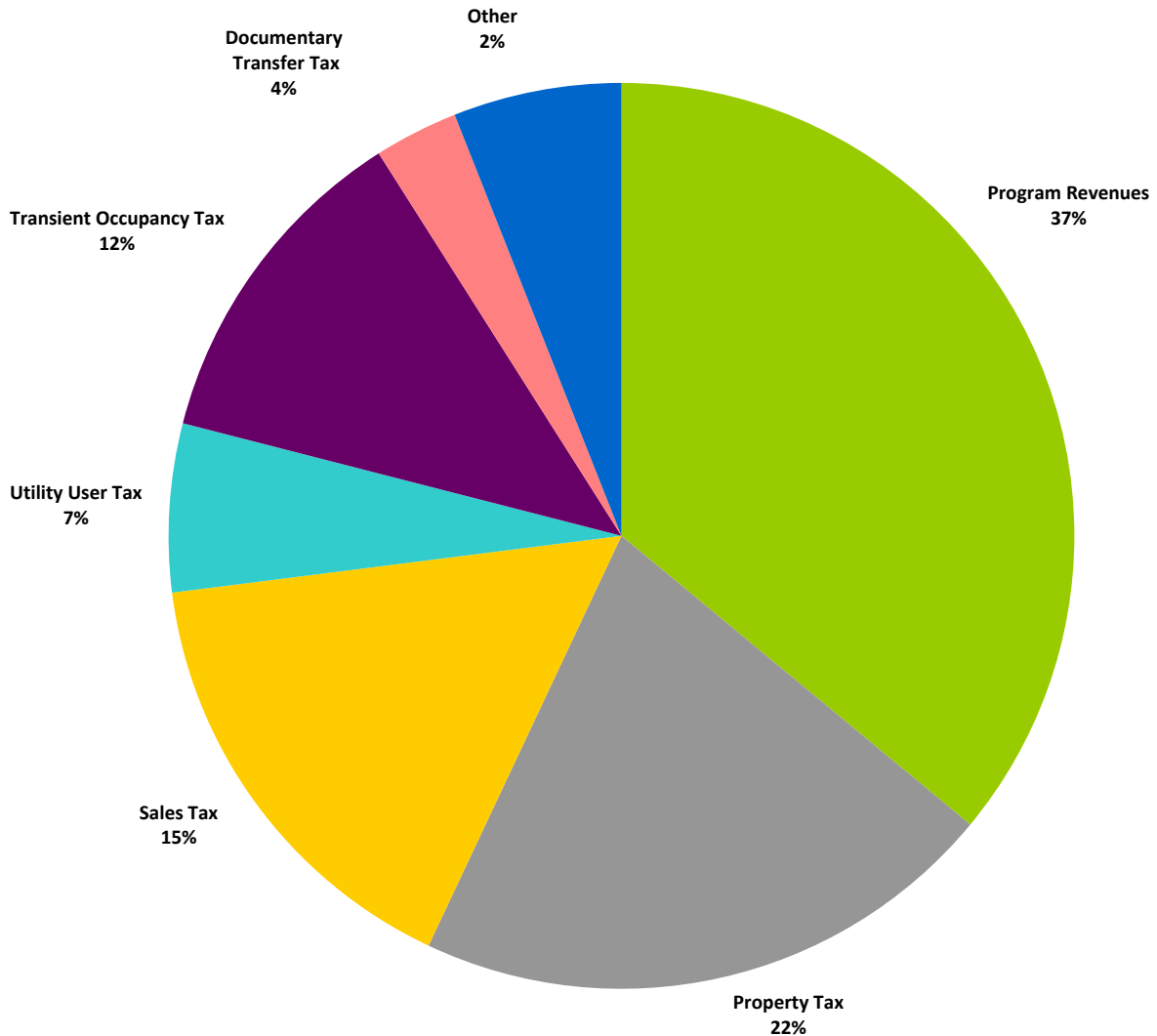


- \$1.1 million increase in permits and licenses.
- \$11.7 million increase in receipts from Stanford Hospital and Clinics, Lucile Salter Packard Children's hospital at Stanford and the Board of Trustees of the Leland Stanford Junior University (SUMC Parties) Development Agreement.

General Revenues increased \$12.3 million, or 10.3 percent, from the prior year primarily due to increased General Fund Tax revenues. Further analysis of general revenues can be found in the Financial Analysis of Governmental Funds section of MD&A.

Governmental Activities – Revenues by Source

The chart below presents revenues by source for Governmental Activities. General Revenues are composed of taxes and other revenues not specifically generated by, or restricted to, individual activities. All tax revenues and investment earnings are included in General Revenues.



Governmental Activities – Expenses

The table below presents a comparison of FY 2018 and FY 2017 expenses by function, along with interest and other expenses. Total Governmental Activities functional expense was \$211.1 million in FY 2018, an increase of \$27.9 million.

GOVERNMENTAL ACTIVITIES
Expenses and Change in Net Position for the Year Ended June 30
(in millions)

Activities	2018	2017	Increase/ (Decrease)
City Council	\$ 0.3	\$ 0.3	\$ -
City Manager	2.8	2.0	0.8
City Attorney	2.5	2.1	0.4
City Clerk	0.9	0.8	0.1
City Auditor	1.0	0.8	0.2
Administrative Services	13.9	11.9	2.0
Human Resources	2.7	2.3	0.4
Public Safety	83.9	73.3	10.6
Planning and Community Environment	11.4	10.9	0.5
Development Services	12.7	11.1	1.6
Public Works	30.3	25.5	4.8
Community Services	33.7	27.9	5.8
Library	12.2	11.4	0.8
Interest and Other Expense	2.8	2.9	(0.1)
Total Functional Expense	211.1	183.2	27.9
Increase (Decrease) in Net Position before Transfers	0.2	(2.0)	2.2
Transfers in	19.1	18.3	0.8
Change in Net Position	19.3	16.3	3.0
Net Position, Beginning	527.3	511.0	16.3
Restatement for implementation of GASB 75	(119.2)	-	(119.2)
Net Position, Ending	\$ 427.4	\$ 527.3	\$ (99.9)

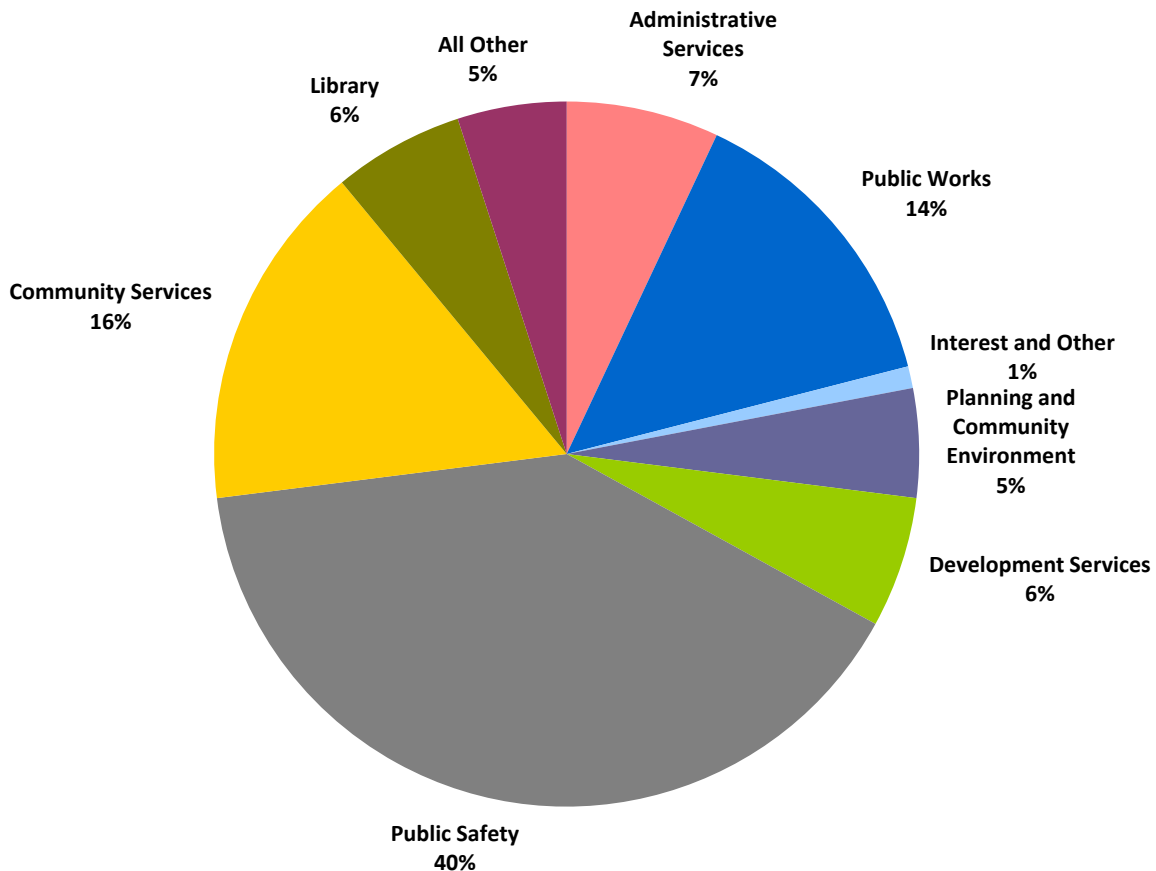


In addition to the variances at the fund level which are explained in the Financial Analysis of Governmental Funds section of the MD&A, year over year variances in Functional expenses at the government-wide level are due to the following:

- Change in pension related adjustments for GASB 68 of \$16.6 million;
- Change in OPEB related adjustments for GASB 75 of (\$3.6 million); and
- Capital asset activities such as depreciation and asset retirements of (\$22.1 million).

Governmental Activities – Functional Expenses

The functional expenses chart below includes only current year expenses. It does not include capital outlays, as those are added to the City's capital assets. Functions which comprise 1 percent or less of total expenses are combined into the All Other category in the chart below. All Other includes City Council, City Manager, City Attorney, City Clerk, City Auditor and Human Resources.



Business-type Activities – Net Position

The following analysis focuses on the net position and changes in net position of the City's Business-type Activities presented in the Government-wide Statement of Net Position and Statement of Activities.

BUSINESS-TYPE ACTIVITIES
Net Position at June 30
(in millions)

	<u>2018</u>	<u>2017</u>	<u>Increase/ (Decrease)</u>
Cash and investments	\$ 241.8	\$ 243.3	\$ (1.5)
Other assets	42.1	44.7	(2.6)
Capital assets	<u>636.7</u>	<u>595.2</u>	<u>41.5</u>
Total Assets	<u>920.6</u>	<u>883.2</u>	<u>37.4</u>
Unamortized loss from refunding	0.2	0.3	(0.1)
Deferred pension contribution	<u>28.9</u>	<u>19.2</u>	<u>9.7</u>
Total Deferred Outflows of Resources	<u>29.1</u>	<u>19.5</u>	<u>9.6</u>
Net pension and OPEB liabilities	157.1	103.8	53.3
Long-term debt	66.1	67.0	(0.9)
Other liabilities	<u>36.0</u>	<u>30.9</u>	<u>5.1</u>
Total Liabilities	<u>259.2</u>	<u>201.7</u>	<u>57.5</u>
Difference between expected and actual earnings on investments	<u>2.4</u>	<u>1.7</u>	<u>0.7</u>
Total Deferred Outflows of Resources	<u>2.4</u>	<u>1.7</u>	<u>0.7</u>
Net Position			
Net investment in capital assets	573.7	532.0	41.7
Restricted	4.0	4.1	(0.1)
Unrestricted	<u>110.4</u>	<u>163.2</u>	<u>(52.8)</u>
Total Net Position	<u>\$ 688.1</u>	<u>\$ 699.3</u>	<u>\$ (11.2)</u>

The City's Business-type Activities total net position decreased \$11.2 million to \$688.1 million as of June 30, 2018.

Capital assets increased \$41.5 million to \$636.7 million in FY 2018 primarily due to capital improvements in the Wastewater Treatment, Electric, Water and Airport Funds. These capital improvements contributed to the \$41.7 million increase in net investment in capital assets to \$573.7 million.

Unrestricted net position of \$110.4 million, a decrease of \$52.8 million from the prior year, represents assets available to finance day-to-day operations and other expenditures approved by Council. This amount includes

rate stabilization reserves (RSR) of \$48.1 million and operations reserves of \$56.9 million, along with the Electric special projects (Calaveras) reserve of \$41.7 million, and the hydro stabilization reserve of \$11.4 million. The positive balances in these reserves are offset by the GASB 68 adjustment pension reserve of \$91.9 million and GASB 75 OPEB reserve of \$38.7 million. Additional detail is included in Note 10.

Business-type Activities – Revenues

The table below presents the revenues for each of the City’s Business-type Activities or Enterprise Funds. The City operates the Water, Electric, Fiber Optics, Gas, Wastewater Collection, Wastewater Treatment, Refuse, Storm Drainage and Airport Funds.

BUSINESS-TYPE ACTIVITIES			
<i>Revenues for the Year Ended June 30</i>			
(in millions)			
Revenues by Source	2018	2017	Increase/ (Decrease)
Program Revenues:			
Charges for services	\$ 330.2	\$ 304.5	\$ 25.7
Operating grants and contributions	0.5	0.5	-
Capital grants and contributions	14.2	4.3	9.9
Total Program Revenues	344.9	309.3	35.6
General Revenues:			
Investment earnings	0.6	(0.5)	1.1
Total General Revenues	0.6	(0.5)	1.1
Total Revenues	\$ 345.5	\$ 308.8	\$ 36.7

Business-type Activities revenues totaled \$345.5 million, an increase of \$36.7 million from the prior year. Program revenues increased \$35.6 million year over year. Charges for services increased \$25.7 million from the prior year due to the rate increase in the Electric Fund and the increased billing for capital and operating costs in the Wastewater Treatment Fund.

Capital grants and contributions increased by \$9.9 million from the prior year due to an increase in grant revenues for the Airport Fund and \$4.0 million in capital contributions for the Wastewater treatment fund related to the forgiveness of a portion of the 2017 State Water Resources Loan.

Business-type Activities – Expenses

The table below presents a comparison of the FY 2018 and FY 2017 expenses for the City's Business-type Activities. Encumbrances and reappropriations are not included.

BUSINESS-TYPE ACTIVITIES
Expenses and Change in Net Position for the Year Ended June 30
(in millions)

<u>Business-type Activities</u>	<u>2018</u>	<u>2017</u>	<u>Increase/ (Decrease)</u>
Water	\$ 40.8	\$ 37.5	\$ 3.3
Electric	146.0	128.6	17.4
Fiber Optics	2.7	2.1	0.6
Gas	27.9	26.8	1.1
Wastewater Collection	16.8	16.4	0.4
Wastewater Treatment	27.5	23.5	4.0
Refuse	28.8	30.7	(1.9)
Storm Drainage	5.1	4.1	1.0
Airport	1.7	1.3	0.4
Total Functional Expense	<u>297.3</u>	<u>271.0</u>	<u>26.3</u>
Increase in Net Position before Transfers	48.2	37.8	10.4
Transfers out	<u>(19.1)</u>	<u>(18.3)</u>	<u>(0.8)</u>
Change in Net Position	29.1	19.5	9.6
Net Position, Beginning	<u>699.3</u>	<u>679.8</u>	<u>19.50</u>
Reinstatement for implementation for GASB 75	<u>(40.3)</u>	<u>-</u>	<u>(40.3)</u>
Net Position, Ending	<u>\$ 688.1</u>	<u>\$ 699.3</u>	<u>\$ (11.2)</u>

Business-type Activities expenses increased \$26.3 million for a total of \$297.3 million. Year over year expenses were significantly affected by the following events:

- Water Fund expenses increased \$3.3 million due to increased wholesale water rates to cover the cost of upgrades and improvements to the water supply distribution system and an increase in salaries and benefits.
- Electric Fund expenses increased \$17.4 million due to higher energy purchase costs offset by lower surplus energy costs.
- Wastewater Treatment Fund expenses increased \$4.0 million due to higher sewage treatment costs, higher operating costs and capital improvement costs for upgrades to the facilities plant.



FUND FINANCIAL STATEMENTS

Financial Analysis of Governmental Funds

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Governmental Funds

The focus of the City's Governmental Funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the City's financing requirements. In particular, the unassigned fund balance may serve as a useful measure of a government's net resources available for discretionary use as it represents the portion of fund balance not yet limited to use for a particular purpose by either an external party, the City itself, or an entity that has been delegated authority by the City Council to assign resources for use.

As of June 30, 2018, the City's Governmental Funds reported combined fund balances of \$251.2 million, an increase of \$16.5 million from the prior year. Approximately 21.0 percent, or \$52.8 million, constitutes unassigned fund balance, which is available for spending at the government's discretion and other purposes. The remainder of the fund balance is either non-spendable, restricted, committed, or assigned to indicate that it is: 1) not in spendable form (\$9.5 million); 2) restricted for particular purposes (\$40.3 million); 3) committed for particular purposes (\$73.2 million); or 4) assigned for particular purposes (\$75.4 million).

Governmental Fund revenues increased \$29.9 million, or 16.5 percent, from the prior year to \$211.3 million. Revenues in the General Fund increased \$15.7 million and Capital Projects Fund revenue decreased \$0.2 million. Other Governmental Funds revenue increased \$14.4 million due to increased plan checking fees, Golf course related fees, permits and licenses and \$11.7 million from Stanford University Medical Center (SUMC) parties of the Development agreement.

Governmental Fund expenditures were \$219.6 million, an increase of \$3.6 million from the prior year. General Fund expenditures increased \$7.6 million, Capital Projects Fund expenditures increased by \$1.3 million, and Non-major Fund expenditures increased by \$4.7 million. Details of significant changes are discussed in the following sections.

**General Fund
Balance Sheet**

The General Fund is the primary operating fund of the City. At the end of the current fiscal year, fund balance of the General Fund was \$68.3 million, compared to \$63.1 million in the prior year. The fund balance has been classified as \$8.0 million non-spendable, \$0.4 million committed, \$7.1 million assigned and \$52.8 million unassigned. The unassigned amount is designated by the Council for Budget Stabilization Reserve (BSR) and other purposes.

Statement of Revenues, Expenditures and Changes in Fund Balance
Revenues

The City's General Fund revenues totaled \$180 million in FY 2018. This represents an increase of \$15.6 million, or 9.5 percent, compared to the prior year. The year over year change in significant revenue sources is noted in the following table.

GENERAL FUND
Revenues for the Year Ended June 30
 (in millions)

<u>Revenues by Source</u>	<u>2018</u>	<u>2017</u>	<u>Increase/ (Decrease)</u>
Property tax	\$ 42.8	\$ 39.4	\$ 3.4
Sales tax	31.1	29.9	1.2
Utility user tax	15.4	14.2	1.2
Transient occupancy tax	24.9	23.5	1.4
Documentary transfer tax	9.2	7.5	1.7
Charges for services	26.8	22.3	4.5
Permits and licence	8.6	7.4	1.2
Rental income	15.9	15.7	0.2
All other	5.3	4.5	0.8
Total Revenues	\$ 180.0	\$ 164.4	\$ 15.6

Property tax revenue increased by \$3.4 million or 8.6 percent, due to increased property assessed value growth. Sales tax receipts were \$1.2 million higher compared to the prior fiscal year, and is driven by growth of auto leasing and sales, drug stores, recreation products, furniture/appliance, office equipment, and health services.

Utility user tax revenues were \$1.2 million or 8.5 percent, higher compared to the prior year due to increased utility rate. Transient occupancy tax (TOT) ended the year \$1.4 million, or 6.0 percent, higher than prior year due to higher room rates, newly opened hotels that performed better than expected, and revenue from short-term rentals.

Documentary transfer tax increased \$1.7 million to \$9.2 million or 22.7 percent, as real property turnover continued to trend as in prior years.

All other revenue increased from prior year by \$6.7 million primarily due to \$2.7 million increase in plan check fees, \$0.7 million increase in golf course related fees and \$1.1 million increase in permits and licenses.

Expenditures

General Fund expenditures totaled \$165.6 million for FY 2018 compared to \$158.0 in the prior year. This amount excludes encumbrances and reappropriations. The majority of increases were related to higher salary and benefit costs with the implementation of new bargaining agreements. In addition, the benefit costs, especially CalPERS retirement and retiree health costs, were substantially higher compared to the prior year. The year over year change for major functions is noted in the following table.

GENERAL FUND			
Expenditures for the Year Ended June 30			
(in millions)			
<u>Expenditures by Function</u>	<u>2018</u>	<u>2017</u>	<u>Increase/ (Decrease)</u>
Administrative Services	\$ 5.3	\$ 5.0	\$ 0.3
Public Works	14.6	13.6	1.0
Planning and Community Environment	8.3	9.1	(0.8)
Development Services	11.7	10.9	0.8
Police	40.3	39.6	0.7
Fire	33.5	31.4	2.1
Community Services	27.1	25.2	1.9
Library	9.1	9.0	0.1
Non-Departmental	6.0	5.9	0.1
All other	9.6	8.3	1.3
Total Expenditures	<u>\$ 165.5</u>	<u>\$ 158.0</u>	<u>\$ 7.5</u>

Public Works expenditures variance of \$1.0 million was mainly due to increased janitorial services and salary and benefit costs.

Fire department expenditures increased \$2.1 million due to \$1.5 million salary and overtime and \$0.6 million in other categories.

Community Services expenditures increased \$1.9 million mainly due to golf course maintenance and salary and benefit costs.

Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual

Original budget compared to final budget

Revenues were originally budgeted at \$175.1 million and were revised downward by \$0.2 million. Revenue categories that were adjusted are shown in the table below.

GENERAL FUND
Budgeted Revenues for the Year Ended June 30
(in millions)

<u>Budgeted Revenues</u>	<u>Adopted Budget</u>	<u>Final Budget</u>	<u>Increase/ (Decrease)</u>
Property tax	\$ 41.9	\$ 42.3	\$ 0.4
Sales tax	31.5	30.2	(1.3)
Utility user tax	13.9	15.4	1.5
Transient occupancy tax	25.1	24.4	(0.7)
Documentary transfer tax	6.9	6.9	-
All other	55.8	56.1	0.3
	<u>175.1</u>	<u>175.3</u>	<u>0.2</u>
Charges to other funds	11.1	11.1	-
Prior year encumbrances and appropriations	<u>-</u>	<u>8.1</u>	<u>8.1</u>
Total Budgeted Revenues	<u>\$ 186.2</u>	<u>\$ 194.5</u>	<u>\$ 8.3</u>

In FY 2018, there were no major changes to the Adopted Budget general fund revenues. These were minor changes in the taxes.

Actual revenues of \$182.5 million were \$7.2 million higher than final budgeted revenues of \$175.3 million due to the following:

- \$1.4 million higher than anticipated sales and property tax proceeds;
- \$2.3 million higher than expected documentary transfer tax;
- \$1.7 million higher than expected charges for services; and
- All other revenue categories also reported favorable variances.

Expenditures were originally budgeted at \$180.5 million and were revised upward by \$10.1 million, including prior year encumbrances and reappropriations of \$8.1 million, for a final budgeted amount of \$190.6 million.

GENERAL FUND
Budgeted Expenditures for the Year Ended June 30
(in millions)

<u>Budgeted Expenditures</u>	<u>Adopted Budget</u>	<u>Final Budget</u>	<u>Increase/ (Decrease)</u>	<u>Actuals, plus Encumbrances</u>
Community Services	\$ 27.6	\$ 28.8	\$ 1.2	\$ 28.4
Fire	31.8	34.1	2.3	34.1
Police	43.4	43.4	0.0	41.9
Library	9.4	9.8	0.4	9.4
Planning and Community Environment	8.5	10.7	2.2	10.4
Public Works	17.0	19.1	2.1	18.9
Development Services	12.5	13.2	0.7	12.6
Non-departmental	8.4	8.1	(0.3)	7.2
All other	21.9	23.5	1.6	22.1
Total Budgeted Expenditures	<u>\$ 180.5</u>	<u>\$ 190.7</u>	<u>\$ 10.2</u>	185.0
Less: Charges to Other Funds				(11.5)
Less: Encumbrances/reappropriations				(7.8)
Net General Fund Expenditures				<u>\$ 165.7</u>

The final budgeted expenditure amount of \$190.6 million compares to the actual expenditures plus encumbrances/reappropriations of \$184.9 million, a difference of \$5.7 million, of which \$7.8 million is encumbrances and reappropriations carried forward to FY 2019. The lower than budgeted expenditures were primarily due to vacancy and benefits savings higher than expected.

Transfers out were originally budgeted at \$29.8 million, with the final budget number at \$29.7 million, a decrease of \$0.1 million.

Capital Projects Fund

Capital Projects Fund expenditures and other uses were \$41.0 million in FY 2018 an increase of \$1.3 million from the prior year.

Non-major Funds

These funds are not presented separately in the Basic Financial Statements, but are individually presented as Supplemental Information.

Financial Analysis of Enterprise Funds

At June 30, 2018, the City's Enterprise Funds reported total net position of \$688.1 million, a decrease of \$11.2 million or 1.6 percent from the prior year, which includes the impact of the restatement from implementation of GASB 75 of \$40.3 million. The decrease was primarily from the Electric, Gas, Wastewater Collection and the Wastewater Treatment Funds. Further analysis is noted in the following section. Unrestricted net position for the Enterprise Funds totaled \$109.4 million, a 31.7 percent decrease from FY 2017. Of the \$50.9 million decrease, \$40.3 million is a result of the adjustment for the GASB 75 OPEB liability.

Following is a table which compares the year over year change in net position for each of the Enterprise Funds.

ENTERPRISE FUNDS			
Change in Net Position for the Year Ended June 30			
(in millions)			
Fund Name	2018	2017	Increase/ (Decrease)
Water	\$ 5.1	\$ 6.5	\$ (1.4)
Electric	(1.2)	(1.2)	-
Fiber Optics	1.7	2.2	(0.5)
Gas	1.5	2.4	(0.9)
Wastewater Collection	1.0	1.5	(0.5)
Wastewater Treatment	4.8	(0.1)	4.9
Refuse	6.1	3.3	2.8
Storm Drainage	1.8	2.5	(0.7)
Airport	10.1	2.4	7.7
Total Change in Net Position	\$ 30.9	\$ 19.5	\$ 11.4

The most significant factors in the year over year change in net position for Enterprise Funds are as follows:

- Wastewater Treatment increased its net position \$4.9 million as a result of increased billing to partners and \$4.0 million in federal grant revenues that represents forgiveness of a portion of the State Water Resources Control Board loan amount. The principal was forgiven for \$4.0 million for the sewage "bio-solids" incinerators project (2017 State Water Resources Loan).
- Net position for Refuse increased \$2.8 million. Revenues were higher due to a 5 percent rate increase in the current year and decrease in operating expenses due to rent and green waste costs.
- The net position for Airport increased \$7.7 million. Revenues were higher resulting from a federal grant reimbursement for \$9.3 million for capital improvement projects.

CAPITAL ASSETS

GASB 34 requires that the City record all its capital assets, including infrastructure and intangible assets. Infrastructure includes roads, bridges, signals and similar assets used by the entire population. The table below shows capital assets and the amount of accumulated depreciation for these assets for Governmental and Business-type Activities. Further detail can be found in Note 6 to the financial statements.

CAPITAL ASSETS AT JUNE 30			
(in millions)			
	<u>2018</u>	<u>2017</u>	<u>Increase/ (Decrease)</u>
Governmental activities			
Capital Assets			
Land and improvements	\$ 78.5	\$ 78.5	-
Street trees	14.8	14.9	(0.1)
Construction in progress	69.3	62.7	6.6
Building and improvements	246.5	225.4	21.1
Intangible assets	3.8	3.8	-
Equipment	12.6	11.9	0.7
Roadway network	334.3	324.8	9.5
Recreation and open space network	35.2	35.2	-
Less accumulated depreciation	(269.0)	(253.3)	(15.7)
Internal Service funds			
Construction in progress	1.9	3.2	(1.3)
Equipment	61.6	56.9	4.7
Less accumulated depreciation	(41.7)	(41.5)	(0.2)
Total Governmental Activities	<u>547.8</u>	<u>522.5</u>	<u>25.3</u>
Business-Type Activities			
Land	5.0	5.0	-
Construction in progress	153.4	110.3	43.1
Buildings and improvements	59.9	56.9	3.0
Capital Leases	0.5	-	0.5
Infrastructure	0.6	0.6	-
Transmission, distribution and treatment systems	779.3	765.8	13.5
Less accumulated depreciation	(362.0)	(343.4)	(18.6)
Total Business-type Activities	<u>\$ 636.7</u>	<u>\$ 595.2</u>	<u>\$ 41.5</u>

Governmental Activities' capital assets net of depreciation increased by \$25.2 million from the prior year. The increase was primarily due to Golf Course improvements, city facilities improvements and street and sidewalk improvements throughout the City.



Council approved a \$125.8 million Infrastructure Plan (IP) in June 2014, which includes projects such as a new Public Safety Building, replacement of two Fire Stations, a Bike and Pedestrian plan, and two parking garages. Through the developments of the 2019-2023 Capital Improvement Projects, the IP was updated for scope increases and cost escalations, resulting in a revised IP of \$249.9 million. Funding for these projects will come from a variety of sources, including TOT revenues, Stanford University Medical Center development agreement, grant revenue, developer impact fees and the one time issuance of COPs.

Major Governmental Activities' capital projects that are currently in progress, including the remaining capital commitment of each, are as follows:

- Fire Station 3 replacement - \$5.6 million
- Charleston Arastradero Corridor - \$10.2 million
- Bicycle Boulevards Implementation Project - \$9.3 million

Business-type Activities' capital assets net of depreciation increased by \$41.5 million over FY 2017. The increase is due primarily to Water, Electric, Wastewater Treatment, Storm Drainage and Airport infrastructure improvements.

Major Business-type Activities' capital projects that are currently in progress, including the remaining capital commitment of each, are as follows:

- Water Main Replacement for Water fund - \$4.7 million
- Dewatering & Loadout Facility Project for Wastewater Treatment Fund - \$12.3 million
- Gas Main Replacement for Gas Fund - \$6.8 million

The City depreciates its capital assets over their estimated useful lives, as required by GASB 34. The purpose of depreciation is to spread the cost of a capital asset over the years of its useful life so that an allocable portion of the cost of the asset is borne by all users. Additional information on capital assets and depreciable lives are in Note 6.

DEBT ADMINISTRATION

Each of the City's debt issues is discussed in detail in Note 7 to the financial statements. The City's debt as of June 30, 2018 is shown in the following table.

LONG-TERM DEBT AT JUNE 30			
(in millions)			
	<u>2018</u>	<u>2017</u>	<u>Increase/ (Decrease)</u>
Governmental Activities			
General Long-Term Obligations			
Certificates of Participation			
2002B Downtown Parking Improvements	\$ -	\$ 1.0	\$ (1.0)
General Obligation Bonds			
2010	45.8	47.0	(1.2)
2013A	16.3	16.7	(0.4)
2011 Lease Purchase Agreement	0.4	0.8	(0.4)
Add: unamortized premium	3.6	3.8	(0.2)
2018 Capital Improvement, COP	9.0	-	9.0
Total Governmental Activities	<u>\$ 75.1</u>	<u>\$ 69.3</u>	<u>\$ 5.8</u>
Business-type Activities			
Enterprise Long-Term Obligations			
Utility Revenue Bonds			
1995 Series A	\$ 1.3	\$ 1.8	\$ (0.5)
1999 Refunding	8.2	9.0	(0.8)
2009 Series A	27.7	28.7	(1.0)
2011 Refunding	10.2	11.3	(1.1)
Add: unamortized premium	0.6	0.7	(0.1)
Energy Tax Credit Bonds			
2007 Series A	0.4	0.5	(0.1)
Less: unamortized discount	(0.1)	(0.1)	-
State Water Resources Loan			
2007	5.0	5.4	(0.4)
2009	6.1	6.5	(0.4)
2017	6.7	3.2	3.5
Total Business-type Activities	<u>\$ 66.1</u>	<u>\$ 67.0</u>	<u>\$ (0.9)</u>

City-wide long-term debt increased a total of \$4.8 million due to an issuance of COPs that refinanced existing COPs and financed the Golf Course renovation and an addition to the 2017 State Water Resources Loan. As noted in the Statistical Section of the CAFR, the combined direct debt ratio to assessed valuation for the General Fund is 0.21 percent compared to the allowable legal debt margin of 15 percent.



SPECIAL ASSESSMENT DISTRICT DEBT

Special assessment districts throughout different parts of the City have also issued debt to finance infrastructure and facilities construction exclusively in their districts. As of June 30, 2018, the City had no special assessment district debt with City commitment outstanding.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

The CAFR is intended to provide citizens, taxpayers, investors, and creditors with a general overview of the City's finances. Questions about this report should be directed to the Administrative Services Department, at 250 Hamilton Avenue, 4th Floor, Palo Alto, California. The Department can also be contacted by email at: adminsvcs@cityofpaloalto.org. This report and other financial reports can be viewed on the City of Palo Alto website at: www.cityofpaloalto.org. On the home page, select Departments, select Administrative Services, and select Financial Reporting. Within Financial Reporting, there are links to reports by title and reporting date.

CITY OF PALO ALTO
Statement of Net Position
June 30, 2018
(Amounts in thousands)

	Governmental Activities	Business-Type Activities	Total
ASSETS:			
Cash and investments available for operations (Note 3)	\$ 280,681	\$ 237,800	\$ 518,481
Receivables, net:			
Accounts and intergovernmental	19,575	39,237	58,812
Interest receivable	1,872	1,373	3,245
Notes and loans receivable (Note 5)	34,295	-	34,295
Internal balances (Note 4)	2,122	(2,122)	-
Deposits	15	-	15
Due from other government agencies	-	3,300	3,300
Inventory of materials and supplies, prepaids and deposits	4,641	310	4,951
Restricted cash and investments with fiscal agents and trustees (Note 3)	6,185	4,014	10,199
Capital assets (Note 6):			
Nondepreciable	168,026	158,377	326,403
Depreciable, net of accumulated depreciation	379,715	478,337	858,052
Total assets	<u>897,127</u>	<u>920,626</u>	<u>1,817,753</u>
DEFERRED OUTFLOWS OF RESOURCES:			
Unamortized loss from refunding	-	239	239
Pension related (Note 11):	63,621	22,698	86,319
OPEB related (Note 12):	15,210	6,139	21,349
Total deferred outflows of resources	<u>78,831</u>	<u>29,076</u>	<u>107,907</u>
LIABILITIES:			
Accounts payable and accruals	14,012	28,426	42,438
Accrued salaries and benefits	1,714	720	2,434
Unearned revenue	2,966	-	2,966
Accrued compensated absences (Note 1):			
Due in one year	5,996	-	5,996
Due in more than one year	6,062	-	6,062
Claims payable (Note 14):			
Due in one year	5,835	-	5,835
Due in more than one year	17,913	-	17,913
Landfill post-closure liability (Note 9):			
Due in more than one year	-	6,825	6,825
Net pension liabilities (Note 11)	302,131	112,981	415,112
Net OPEB liabilities (Note 12)	109,377	44,132	153,509
Long-term debt (Note 7):			
Due in one year	2,259	4,533	6,792
Due in more than one year	72,887	61,586	134,473
Total liabilities	<u>541,152</u>	<u>259,203</u>	<u>800,355</u>
DEFERRED INFLOWS OF RESOURCES:			
Pension related (Note 11):	5,644	1,644	7,288
OPEB related (Note 12):	1,792	724	2,516
Total deferred inflows of resources	<u>7,436</u>	<u>2,368</u>	<u>9,804</u>
NET POSITION (Note 10):			
Net Investment in capital assets	473,233	573,688	1,046,921
Restricted for:			
Transportation, infrastructure and other	36,108	-	36,108
Debt service	3,571	4,014	7,585
Nonexpendable - Eyerly Family	1,498	-	1,498
Total restricted net position	<u>41,177</u>	<u>4,014</u>	<u>45,191</u>
Unrestricted	<u>(87,040)</u>	<u>110,429</u>	<u>23,389</u>
Total net position	<u>\$ 427,370</u>	<u>\$ 688,131</u>	<u>\$ 1,115,501</u>

See accompanying notes to the basic financial statements.

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CITY OF PALO ALTO
Statement of Activities
For the Year Ended June 30, 2018
(Amounts in thousands)

Functions/Programs	Expenses	Program Revenues			Net (Expense) Revenue and Changes in Net Position		Total
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-Type Activities	
Governmental Activities:							
City Council	\$ 345	\$ -	\$ -	\$ -	\$ (345)	\$ -	\$ (345)
City Manager	2,757	-	59	-	(2,698)	-	(2,698)
City Attorney	2,511	-	-	-	(2,511)	-	(2,511)
City Clerk	931	-	-	-	(931)	-	(931)
City Auditor	994	-	-	-	(994)	-	(994)
Administrative Services	13,949	6,536	-	-	(7,413)	-	(7,413)
Human Resources	2,674	-	-	-	(2,674)	-	(2,674)
Public Works	30,349	781	-	1,523	(28,045)	-	(28,045)
Planning and Community Environment	11,357	5,119	594	-	(5,644)	-	(5,644)
Development Services	12,664	16,000	-	-	3,336	-	3,336
Public Safety	83,923	13,507	1,656	-	(68,760)	-	(68,760)
Community Services	33,709	21,285	11,741	11	(672)	-	(672)
Library	12,208	145	4	-	(12,059)	-	(12,059)
Interest on long-term debt	2,761	-	-	-	(2,761)	-	(2,761)
Total Governmental Activities	211,132	63,373	14,054	1,534	(132,171)	-	(132,171)
Business-Type Activities:							
Water	40,836	45,087	501	531	-	5,283	5,283
Electric	146,033	154,142	-	-	-	8,109	8,109
Fiber Optics	2,653	4,529	-	-	-	1,876	1,876
Gas	27,930	37,044	-	-	-	9,114	9,114
Wastewater Collection	16,801	17,990	-	329	-	1,518	1,518
Wastewater Treatment	27,518	27,382	-	4,000	-	3,864	3,864
Refuse	28,808	34,647	-	-	-	5,839	5,839
Storm Drainage	5,059	6,964	-	-	-	1,905	1,905
Airport	1,656	2,382	-	9,334	-	10,060	10,060
Total Business-Type Activities	297,294	330,167	501	14,194	-	47,568	47,568
Total	\$ 508,426	\$ 393,540	\$ 14,555	\$ 15,728	(132,171)	47,568	(84,603)
General Revenues:							
Taxes:							
Property tax					47,170	-	47,170
Sales tax					31,091	-	31,091
Utility user tax					15,414	-	15,414
Transient occupancy tax					24,937	-	24,937
Documentary transfer tax					9,229	-	9,229
Other taxes					2,108	-	2,108
Investment earnings					420	596	1,016
Miscellaneous					1,973	-	1,973
Transfers (Note 4)					19,077	(19,077)	-
Total general revenues and transfers					151,419	(18,481)	132,938
Change in net position					19,248	29,087	48,335
Net Position, beginning of year, as previously stated					527,289	699,294	1,226,583
Restatement for implementation of GASB Statement No. 75					(119,167)	(40,250)	(159,417)
Net position, beginning of year, as restated					408,122	659,044	1,067,166
Net position, end of year					\$ 427,370	\$ 688,131	\$ 1,115,501

See accompanying notes to the basic financial statements.

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CITY OF PALO ALTO
Governmental Funds
Balance Sheet
June 30, 2018
(Amounts in thousands)

	General Fund	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
ASSETS:				
Cash and investments available for operations (Note 3)	\$ 49,250	\$ 82,525	\$ 70,655	\$ 202,430
Receivables, net:				
Accounts and intergovernmental	18,881	242	399	19,522
Interest receivable	950	27	432	1,409
Notes and loans receivable (Note 5)	479	-	33,816	34,295
Deposits	15	-	-	15
Advance to other fund (Note 4)	3,128	-	-	3,128
Inventory of materials and supplies	4,427	-	-	4,427
Restricted cash and investments with fiscal agents (Note 3)	-	638	-	638
Total assets	\$ 77,130	\$ 83,432	\$ 105,302	\$ 265,864
LIABILITIES AND FUND BALANCES:				
Liabilities:				
Accounts payable and accruals	\$ 4,293	\$ 5,452	\$ 358	\$ 10,103
Accrued salaries and benefits	1,525	70	16	1,611
Unearned revenue	2,966	-	-	2,966
Interfund payables and advances	-	-	13	13
Total liabilities	8,784	5,522	387	14,693
Fund balances (Note 10):				
Nonspendable:				
Notes and loans receivable	479	-	-	479
Deposits	15	-	-	15
Inventories	4,427	-	-	4,427
Advance to other fund	3,128	-	-	3,128
Eyerly family	-	-	1,498	1,498
Restricted for:				
Transportation mitigation	-	-	10,511	10,511
Federal revenue	-	-	5,080	5,080
Street improvement	-	-	562	562
Local law enforcement	-	-	322	322
Library bond project	-	638	-	638
Public benefit	-	-	19,633	19,633
Debt service	-	-	3,571	3,571
Committed for:				
Development Services	373	-	-	373
Roth Building Rehabilitation	-	4,020	-	4,020
Cubberley Improvements	-	4,991	-	4,991
Developer impact fees	-	-	13,764	13,764
Housing in-lieu	-	-	44,863	44,863
Special districts	-	-	5,143	5,143
Assigned for:				
Capital projects	-	68,261	-	68,261
Other general government purposes	5,325	-	-	5,325
Reappropriations	1,773	-	-	1,773
Unassigned for:				
Budget Stabilization	52,826	-	-	52,826
Downtown business	-	-	(32)	(32)
Total fund balances	68,346	77,910	104,915	251,171
Total liabilities and fund balances	\$ 77,130	\$ 83,432	\$ 105,302	\$ 265,864

See accompanying notes to the basic financial statements.

CITY OF PALO ALTO
Reconciliation of the Balance Sheet of Governmental Funds to
the Statement of Net Position - Governmental Activities
June 30, 2018
(Amounts in thousands)

Total fund balances reported on the governmental funds balance sheet	\$ 251,171
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Amounts reported for governmental activities in the statement of net position are different from those reported in the governmental funds balance sheet because of the following:

Deferred outflows and inflows of resources in governmental activities are not financial resources and, therefore, are not reported in the governmental funds.

Deferred outflows of resources	78,831
Deferred inflows of resources	(7,436)

Capital assets used in governmental activities are not current assets or financial resources and therefore are not reported in the governmental funds (Note 6)	547,741
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Internal service funds are used by management to charge the costs of activities such as insurance, equipment acquisition and maintenance, and certain employee benefits to individual funds. The assets and liabilities of the internal service funds are therefore included in governmental activities in the statement of net position (excludes capital assets, deferred outflows of resources, deferred inflows of resources, net pension liabilities and net OPEB liabilities reported herein)	44,922
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Some liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the governmental funds:

Interest payable	(1,205)
Net pension liabilities (Note 11)	(302,131)
Net OPEB liabilities (Note 12)	(109,377)
Long-term debt (Note 7)	<u>(75,146)</u>

Net position of governmental activities	<u><u>\$ 427,370</u></u>
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CITY OF PALO ALTO
Governmental Funds
Statement of Revenues, Expenditures and Changes in Fund Balances
For the Year Ended June 30, 2018
(Amounts in thousands)

	General Fund	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
REVENUES:				
Property tax	\$ 42,839	\$ -	\$ 4,331	\$ 47,170
Special assessments	-	-	72	72
Sales tax	31,091	-	-	31,091
Utility user tax	15,414	-	-	15,414
Transient occupancy tax	24,937	-	-	24,937
Documentary transfer tax	9,229	-	-	9,229
Other taxes and fines	2,141	-	2,116	4,257
Contributions	-	-	11,733	11,733
Charges for services	26,824	-	11	26,835
Intergovernmental	3,205	1,595	592	5,392
Permits and licenses	8,560	-	4,226	12,786
Investment earnings	(828)	1,016	198	386
Rental income	15,896	-	6	15,902
Other revenue	776	131	5,160	6,067
Total revenues	<u>180,084</u>	<u>2,742</u>	<u>28,445</u>	<u>211,271</u>
EXPENDITURES:				
Current:				
City Council	337	-	-	337
City Manager	2,509	-	-	2,509
City Attorney	2,244	-	-	2,244
City Clerk	819	-	-	819
City Auditor	870	-	-	870
Administrative Services	5,347	-	226	5,573
Human Resources	2,369	-	-	2,369
Public Works	14,569	-	857	15,426
Planning and Community Environment	8,312	-	2,020	10,332
Development Services	11,749	-	-	11,749
Police	40,326	-	68	40,394
Fire	33,522	-	-	33,522
Community Services	27,122	-	2,709	29,831
Library	9,120	-	-	9,120
Non-Departmental	5,973	-	1,606	7,579
Capital outlay	-	40,971	-	40,971
Debt service:				
Principal	416	-	2,545	2,961
Interest and fiscal charges	16	-	2,940	2,956
Total expenditures	<u>165,620</u>	<u>40,971</u>	<u>12,971</u>	<u>219,562</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>14,464</u>	<u>(38,229)</u>	<u>15,474</u>	<u>(8,291)</u>
OTHER FINANCING SOURCES (USES):				
Issuance of debt	-	8,375	595	8,970
Transfers in (Note 4)	20,310	35,844	728	56,882
Transfers out (Note 4)	(29,535)	(116)	(11,434)	(41,085)
Total other financing sources (uses)	<u>(9,225)</u>	<u>44,103</u>	<u>(10,111)</u>	<u>24,767</u>
Change in fund balances	5,239	5,874	5,363	16,476
FUND BALANCES, BEGINNING OF YEAR	<u>63,107</u>	<u>72,036</u>	<u>99,552</u>	<u>234,695</u>
FUND BALANCES, END OF YEAR	<u>\$ 68,346</u>	<u>\$ 77,910</u>	<u>\$ 104,915</u>	<u>\$ 251,171</u>

See accompanying notes to the basic financial statements.

CITY OF PALO ALTO
Reconciliation of the Statement of Revenues, Expenditures and Changes in Fund Balances
of Governmental Funds to the Statement of Activities - Governmental Activities
For the Year Ended June 30, 2018
(Amounts in thousands)

Net change in fund balances - total governmental funds \$ 16,476

Amounts reported for governmental activities in the statement of activities are different from those reported in the governmental funds because of the following:

Governmental funds report capital outlays as expenditures. However, in the statement of activities, the costs of these assets are capitalized and allocated over their estimated useful lives and reported as depreciation expense. Therefore, the activities associated with capital assets are as follows:

Capital outlay added back to fund balance for current year additions	41,586
Depreciation expense is deducted from fund balance (depreciation expense is net of internal service fund depreciation of \$3,074 (Note 6), which has already been allocated through the internal service fund activities below	(15,814)
Disposal of capital assets	(3,659)

Pension and OPEB contribution made subsequent to the measurement date is an expenditure in the governmental funds, but reported as a deferred outflows of resources in the government-wide financial statements	37,915
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Pension and OPEB expenses reported in the statement of activities do not require the use of current financial resources and, therefore, are not reported as expenditures in governmental funds	(50,932)
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Principal payments on long-term liabilities are reported as expenditures in governmental funds when paid. The governmental activities, however, report principal payments as a reduction of long-term debt on the statement of net position. Interest accrued on long-term debt and amortization of premiums do not require the use of current financial resources and therefore are not reported as expenditures in governmental funds. Therefore, the activities associated with long-term debt are as follows:

Principal paid during the year	2,961
Proceeds from debt issuance	(8,970)
Change in interest payable	37
Amortization of bond premium	158

Internal service funds are used by management to charge the costs of activities, such as insurance, equipment acquisition and maintenance, and employees benefits to individual funds. The portion of the net expense of these internal service funds arising out of their transactions with governmental funds is reported with governmental activities.	(510)
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Change in net position of governmental activities	<u>\$ 19,248</u>
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See accompanying notes to the basic financial statements.

CITY OF PALO ALTO
General Fund
Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual
For the Year Ended June 30, 2018
(Amounts in thousands)

	Budgeted Amounts		Actual, Budgetary Basis	Variance with Final Budget Positive (Negative)
	Adopted	Final		
REVENUES:				
Sales tax	\$ 31,458	\$ 30,208	\$ 31,091	\$ 883
Property tax	41,927	42,327	42,839	512
Transient occupancy tax	25,143	24,398	24,937	539
Documentary transfer tax	6,930	6,930	9,229	2,299
Utility user tax	13,867	15,367	15,414	47
Other taxes, fines and penalties	2,060	2,060	2,141	81
Charges for services	26,902	25,125	26,824	1,699
Permits and licenses	8,432	8,432	8,560	128
Investment earnings	1,050	1,050	1,536	486
Rental income	15,502	15,485	15,896	411
From other agencies	1,355	3,074	3,205	131
Other revenues	501	824	776	(48)
	<u>175,127</u>	<u>175,280</u>	<u>182,448</u>	<u>7,168</u>
Charges to other funds and departments	11,076	11,076	11,476	400
Prior year encumbrances	-	8,097	8,097	-
Total revenues	<u>186,203</u>	<u>194,453</u>	<u>202,021</u>	<u>7,568</u>
EXPENDITURES:				
Current:				
City Attorney	3,356	3,825	3,624	201
City Auditor	1,301	1,427	1,276	151
City Clerk	1,374	1,372	1,206	166
City Council	500	524	489	35
City Manager	3,681	4,227	4,031	196
Administrative Services	7,983	8,038	7,849	189
Community Services	27,560	28,756	28,395	361
Police	43,372	43,425	41,923	1,502
Fire	31,774	34,077	34,052	25
Human Resources	3,714	4,044	3,652	392
Library	9,447	9,767	9,357	410
Planning and Community Environment	8,452	10,708	10,446	262
Development Services	12,540	13,187	12,560	627
Public Works	16,975	19,071	18,908	163
Non-Departmental	8,437	8,142	7,149	993
Total expenditures	<u>180,466</u>	<u>190,590</u>	<u>184,917</u>	<u>5,673</u>
EXCESS OF REVENUES OVER EXPENDITURES	<u>5,737</u>	<u>3,863</u>	<u>17,104</u>	<u>13,241</u>
OTHER FINANCING SOURCES (USES):				
Transfers in	20,791	20,310	20,310	-
Transfers out	(29,888)	(29,735)	(29,735)	-
Total other financing sources (uses)	<u>(9,097)</u>	<u>(9,425)</u>	<u>(9,425)</u>	<u>-</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES, BUDGETARY BASIS	<u>\$ (3,360)</u>	<u>\$ (5,562)</u>	<u>7,679</u>	<u>\$ 13,241</u>
Adjustment to Budgetary Basis:				
Unrealized gain/loss on investments			(2,364)	
Changes in advances to other funds			200	
Current year encumbrances and reappropriations			7,821	
Prior year encumbrances and reappropriations			(8,097)	
CHANGE IN FUND BALANCE, GAAP BASIS			<u>5,239</u>	
FUND BALANCE AT BEGINNING OF YEAR, GAAP BASIS			<u>63,107</u>	
FUND BALANCE AT END OF YEAR, GAAP BASIS			<u>\$ 68,346</u>	

See accompanying notes to the basic financial statements.

CITY OF PALO ALTO
Proprietary Funds
Statement of Net Position
June 30, 2018
(Amounts in thousands)

	Business-Type Activities-Enterprise Funds			
	Water	Electric	Fiber Optics	Gas
ASSETS:				
Current assets:				
Cash and investments available for operations (Note 3)	\$ 38,726	\$ 90,470	\$ 28,656	\$ 28,705
Accounts receivable, net of allowance of \$608	5,715	18,727	1,094	2,476
Interest receivable	224	530	161	163
Due from other government agencies	-	-	-	-
Inventory of materials and supplies	-	-	-	-
Restricted cash and investments with fiscal agents and trustees (Note 3)	3,219	-	-	795
Total current assets	<u>47,884</u>	<u>109,727</u>	<u>29,911</u>	<u>32,139</u>
Noncurrent assets:				
Due from other government agencies	-	-	-	-
Deposit	-	35	-	-
Prepaid expense	92	-	-	-
Capital assets (Note 6):				
Nondepreciable	27,555	25,696	2,923	8,366
Depreciable, net	98,964	168,441	5,827	95,701
Total noncurrent assets	<u>126,611</u>	<u>194,172</u>	<u>8,750</u>	<u>104,067</u>
Total assets	<u>174,495</u>	<u>303,899</u>	<u>38,661</u>	<u>136,206</u>
DEFERRED OUTFLOWS OF RESOURCES:				
Unamortized loss from refunding	104	-	-	135
Pension related	2,939	7,403	567	3,153
OPEB related	690	2,246	-	988
Total deferred outflows of resources	<u>3,733</u>	<u>9,649</u>	<u>567</u>	<u>4,276</u>
LIABILITIES:				
Current liabilities:				
Accounts payable and accruals	5,617	8,001	955	3,022
Accrued salaries and benefits	94	241	18	100
Accrued compensated absences (Note 1)	-	-	-	-
Current portion of long term debt (Note 7)	1,636	100	-	619
Accrued claims payable (Note 14)	-	-	-	-
Total current liabilities	<u>7,347</u>	<u>8,342</u>	<u>973</u>	<u>3,741</u>
Noncurrent liabilities:				
Accrued compensated absences (Note 1)	-	-	-	-
Accrued claims payable (Note 14)	-	-	-	-
Advance from other fund (Note 4)	-	-	-	-
Landfill post-closure liability (Note 9)	-	-	-	-
Net pension liabilities (Note 11)	15,180	36,384	2,381	16,202
Net OPEB liabilities (Note 12)	4,958	16,149	-	7,107
Long term debt, net of unamortized discounts/premiums (Note 7)	31,496	278	-	5,370
Total noncurrent liabilities	<u>51,634</u>	<u>52,811</u>	<u>2,381</u>	<u>28,679</u>
Total liabilities	<u>58,981</u>	<u>61,153</u>	<u>3,354</u>	<u>32,420</u>
DEFERRED INFLOWS OF RESOURCES:				
Pension related	213	531	41	228
OPEB related	81	265	-	116
Total deferred inflows of resources	<u>294</u>	<u>796</u>	<u>41</u>	<u>344</u>
NET POSITION (Note 10):				
Net Investment in capital assets	93,491	193,313	8,750	98,213
Restricted for debt service	3,219	-	-	795
Unrestricted (deficit)	22,243	58,286	27,083	8,710
Total net position	<u>\$ 118,953</u>	<u>\$ 251,599</u>	<u>\$ 35,833</u>	<u>\$ 107,718</u>

Some amounts reported for Business-type Activities in the statement of net position are different because certain Internal Service Fund net positions are included with Business-type Activities
Net position reported in Business-type Activities

See accompanying notes to the basic financial statements.

Business-Type Activities-Enterprise Funds						Governmental Activities - Internal Service Funds
Wastewater Collection	Wastewater Treatment	Refuse	Storm Drainage	Airport	Totals	
\$ 8,419	\$ 12,897	\$ 23,703	\$ 5,189	\$ 1,035	\$ 237,800	\$ 78,251
2,165	2,504	3,548	754	2,254	39,237	53
48	83	119	40	5	1,373	463
-	300	-	-	-	300	-
-	-	-	-	-	-	214
-	-	-	-	-	4,014	5,547
10,632	15,784	27,370	5,983	3,294	282,724	84,528
-	3,000	-	-	-	3,000	-
-	-	-	-	-	35	-
-	183	-	-	-	275	-
33,240	26,773	1,952	18,435	13,437	158,377	1,873
54,538	28,717	3,359	22,179	611	478,337	19,905
87,778	58,673	5,311	40,614	14,048	640,024	21,778
98,410	74,457	32,681	46,597	17,342	922,748	106,306
-	-	-	-	-	239	-
1,754	4,739	966	872	305	22,698	3,795
378	1,164	421	184	68	6,139	822
2,132	5,903	1,387	1,056	373	29,076	4,617
572	4,602	2,594	557	2,506	28,426	2,704
58	141	30	27	11	720	103
-	-	-	-	-	-	5,996
94	1,399	-	685	-	4,533	-
-	-	-	-	-	-	5,835
724	6,142	2,624	1,269	2,517	33,679	14,638
-	-	-	-	-	-	6,062
-	-	-	-	-	-	17,913
-	-	-	-	3,115	3,115	-
-	-	6,825	-	-	6,825	-
9,075	22,984	6,009	3,991	775	112,981	16,710
2,717	8,366	3,024	1,320	491	44,132	5,910
551	19,838	-	4,053	-	61,586	-
12,343	51,188	15,858	9,364	4,381	228,639	46,595
13,067	57,330	18,482	10,633	6,898	262,318	61,233
128	340	70	70	23	1,644	286
45	137	50	22	8	724	97
173	477	120	92	31	2,368	383
87,133	37,553	5,311	35,876	14,048	573,688	21,778
-	-	-	-	-	4,014	-
169	(15,000)	10,155	1,052	(3,262)	109,436	27,529
\$ 87,302	\$ 22,553	\$ 15,466	\$ 36,928	\$ 10,786	687,138	\$ 49,307

993
\$ 688,131

See accompanying notes to the basic financial statements.

CITY OF PALO ALTO
Proprietary Funds
Statement of Revenues, Expenses and Changes in Fund Net Position
For the Year Ended June 30, 2018
(Amounts in thousands)

	Business-Type Activities-Enterprise Funds			
	Water	Electric	Fiber Optics	Gas
OPERATING REVENUES:				
Sales to:				
Customers	\$ 40,661	\$ 122,089	\$ 3,380	\$ 33,389
City departments	2,735	4,264	874	1,373
Surplus energy	-	11,792	-	-
Service connection charges and miscellaneous	852	1,766	101	1,079
Charges for services	-	-	-	-
Other	839	14,231	174	1,203
Total operating revenues	<u>45,087</u>	<u>154,142</u>	<u>4,529</u>	<u>37,044</u>
OPERATING EXPENSES:				
Purchase of utilities:				
Retail purchase of utilities	21,958	83,910	-	12,921
Surplus energy	-	10,749	-	-
Administrative and general	5,743	9,762	820	4,767
Engineering (operating)	349	1,776	-	345
Resource management and energy efficiency	911	5,941	-	1,176
Operations and maintenance	5,626	11,384	1,453	4,561
Rent	1,776	5,285	75	602
Depreciation and amortization	2,722	8,095	337	3,152
Claims payments and changes in estimated self-insurance liability	-	-	-	-
Refund of charges for services	-	-	-	-
Employment benefits	-	-	-	-
Total operating expenses	<u>39,085</u>	<u>136,902</u>	<u>2,685</u>	<u>27,524</u>
Operating income (loss)	6,002	17,240	1,844	9,520
NONOPERATING REVENUES (EXPENSES):				
Investment earnings	122	310	40	24
Interest expense	(1,703)	(8,787)	-	(203)
Gain on disposal of capital assets	-	-	-	-
Loss on disposal of capital assets	(117)	(26)	-	(122)
Other nonoperating revenues	501	-	-	-
Total nonoperating revenues (expenses)	<u>(1,197)</u>	<u>(8,503)</u>	<u>40</u>	<u>(301)</u>
Income (loss) before transfers and capital contributions	4,805	8,737	1,884	9,219
Capital contributions	531	-	-	-
Transfers in (Note 4)	512	3,465	-	-
Transfers out (Note 4)	(704)	(13,448)	(135)	(7,677)
Change in net position	<u>5,144</u>	<u>(1,246)</u>	<u>1,749</u>	<u>1,542</u>
NET POSITION (DEFICIT), BEGINNING OF YEAR				
AS PREVIOUSLY STATED	118,331	267,573	34,084	112,658
RESTATEMENT FOR IMPLEMENTATION OF GASB STATEMENT NO. 75	<u>(4,522)</u>	<u>(14,728)</u>	<u>-</u>	<u>(6,482)</u>
NET POSITION (DEFICIT), BEGINNING OF YEAR, AS RESTATED	<u>113,809</u>	<u>252,845</u>	<u>34,084</u>	<u>106,176</u>
NET POSITION (DEFICIT), END OF YEAR	<u>\$ 118,953</u>	<u>\$ 251,599</u>	<u>\$ 35,833</u>	<u>\$ 107,718</u>

Some amounts reported for Business-type Activities in the statement of activities are different because certain Internal Service Fund activities are included with Business-type Activities

Change in net position reported in Business-type Activities

See accompanying notes to the basic financial statements.

Business-Type Activities-Enterprise Funds						Governmental Activities- Internal Service Funds
Wastewater Collection	Wastewater Treatment	Refuse	Storm Drainage	Airport	Totals	
\$ 17,324	\$ 16,775	\$ 30,402	\$ 6,515	\$ 1,760	\$ 272,295	\$ -
95	9,596	804	393	-	20,134	-
-	-	-	-	-	11,792	-
220	-	-	-	-	4,018	-
-	-	-	-	-	-	99,378
351	1,011	3,441	56	622	21,928	121
17,990	27,382	34,647	6,964	2,382	330,167	99,499
9,559	-	15,060	-	-	143,408	-
-	-	-	-	-	10,749	-
1,933	-	1,584	1,274	967	26,850	13,742
303	2,374	320	198	-	5,665	-
-	-	-	922	-	8,950	-
2,683	20,768	8,950	1,352	554	57,331	13,327
310	-	2,272	41	-	10,361	-
2,049	2,882	109	763	21	20,130	3,074
-	-	-	-	-	-	4,705
-	-	-	-	-	-	87
-	-	-	-	-	-	70,547
16,837	26,024	28,295	4,550	1,542	283,444	105,482
1,153	1,358	6,352	2,414	840	46,723	(5,983)
18	35	15	31	1	596	32
(38)	(423)	(156)	(298)	(64)	(11,672)	-
-	-	-	-	-	-	218
(12)	-	-	-	-	(277)	-
-	-	-	-	-	501	42
(32)	(388)	(141)	(267)	(63)	(10,852)	292
1,121	970	6,211	2,147	777	35,871	(5,691)
329	4,000	-	-	9,334	14,194	-
-	-	-	-	-	3,977	5,934
(442)	(210)	(62)	(365)	(11)	(23,054)	(2,654)
1,008	4,760	6,149	1,782	10,100	30,988	(2,411)
88,772	25,423	12,075	36,350	1,134		76,528
(2,478)	(7,630)	(2,758)	(1,204)	(448)		(24,810)
86,294	17,793	9,317	35,146	686		51,718
\$ 87,302	\$ 22,553	\$ 15,466	\$ 36,928	\$ 10,786		\$ 49,307

(1,901)

\$ 29,087

See accompanying notes to the basic financial statements.

CITY OF PALO ALTO
Proprietary Funds
Statement of Cash Flows
For the Year Ended June 30, 2018
(Amounts in thousands)

	Business-Type Activities-Enterprise Funds			
	Water	Electric	Fiber Optics	Gas
Cash flows from operating activities:				
Cash received from customers	\$ 41,851	\$ 135,515	\$ 3,283	\$ 34,363
Cash refunds to customers	-	-	-	-
Cash payments to suppliers for goods and services	(29,786)	(119,238)	(997)	(17,863)
Cash payments to employees	(5,197)	(8,471)	(663)	(4,237)
Internal activity- receipts (payments) from (to) other funds	2,735	4,264	874	1,373
Other receipts	839	14,231	174	1,203
Net cash provided by operating activities	<u>10,442</u>	<u>26,301</u>	<u>2,671</u>	<u>14,839</u>
Cash flows from noncapital financing activities:				
Receipt of loans from other funds	-	-	-	-
Interest subsidy received from Build America Bonds	501	-	-	-
Transfers in	512	3,465	-	-
Transfers out	(704)	(13,448)	(135)	(7,677)
Net cash provided by (used in) noncapital financing activities	<u>309</u>	<u>(9,983)</u>	<u>(135)</u>	<u>(7,677)</u>
Cash flows from capital and related financing activities:				
Acquisition and construction of capital assets	(8,511)	(10,850)	(1,048)	(5,505)
Proceeds from sale of capital assets	-	-	-	-
Capital grants and contributions	531	-	-	-
Proceeds from debt issuance	-	-	-	-
Principal paid on long-term debt	(1,573)	(100)	-	(597)
Interest paid on long-term debt	(1,705)	(8,787)	-	(203)
Net cash used in capital and related financing activities	<u>(11,258)</u>	<u>(19,737)</u>	<u>(1,048)</u>	<u>(6,305)</u>
Cash flows from investing activities:				
Interest received	74	236	2	(14)
Net cash provided by (used in) investing activities	<u>74</u>	<u>236</u>	<u>2</u>	<u>(14)</u>
Net change in cash and cash equivalents	(433)	(3,183)	1,490	843
Cash and cash equivalents, beginning of year	<u>42,378</u>	<u>93,653</u>	<u>27,166</u>	<u>28,657</u>
Cash and cash equivalents, end of year	<u>\$ 41,945</u>	<u>\$ 90,470</u>	<u>\$ 28,656</u>	<u>\$ 29,500</u>
Financial statement presentation:				
Cash and investments available for operations	\$ 38,726	\$ 90,470	\$ 28,656	\$ 28,705
Restricted cash and investments with fiscal agent	3,219	-	-	795
Cash and cash equivalents, end of year	<u>\$ 41,945</u>	<u>\$ 90,470</u>	<u>\$ 28,656</u>	<u>\$ 29,500</u>
Reconciliation of operating income (loss) to net cash provided by operating activities:				
Operating income (loss)	\$ 6,002	\$ 17,240	\$ 1,844	\$ 9,520
Adjustments to reconcile operating income (loss) to net cash provided by operating activities:				
Depreciation and amortization	2,722	8,095	337	3,152
Other	-	-	-	-
Change in assets and liabilities:				
Accounts receivable	338	(132)	(198)	(105)
Inventory of materials and supplies	-	-	-	-
Deposit	8	(20)	-	-
Deferred outflow of resources - pension plans	(442)	(1,047)	(91)	(477)
Deferred outflow of resources - OPEB	(214)	(696)	-	(306)
Accounts payable and accruals	826	(173)	531	1,742
Accrued salaries and benefits	1	(1)	2	5
Accrued compensated absences	-	-	-	-
Landfill closure and post-closure care	-	-	-	-
Accrued claims payable	-	-	-	-
Net Pension liability	1,164	2,931	242	1,260
Net OPEB liability	(40)	(129)	-	(57)
Deferred inflow of resources - pension plans	(4)	(32)	4	(11)
Deferred inflow of resources - OPEB	81	265	-	116
Net cash provided by operating activities	<u>\$ 10,442</u>	<u>\$ 26,301</u>	<u>\$ 2,671</u>	<u>\$ 14,839</u>

See accompanying notes to the basic financial statements.

Business-Type Activities-Enterprise Funds						Governmental Activities- Internal Service Funds
Wastewater Collection	Wastewater Treatment	Refuse	Storm Drainage	Airport	Totals	
\$ 17,438	\$ 19,716	\$ 30,109	\$ 6,508	\$ (283)	\$ 288,500	\$ 99,787
-	-	-	-	-	-	(10)
(13,695)	(21,517)	(26,715)	(2,437)	1,633	(230,615)	(14,463)
(1,592)	(2)	(1,483)	(1,080)	(886)	(23,611)	(79,574)
95	9,596	804	393	-	20,134	(3,837)
351	1,011	3,562	56	622	22,049	42
<u>2,597</u>	<u>8,804</u>	<u>6,277</u>	<u>3,440</u>	<u>1,086</u>	<u>76,457</u>	<u>1,945</u>
-	-	-	-	200	200	-
-	-	-	-	-	501	-
-	-	-	-	-	3,977	5,934
(442)	(210)	(62)	(365)	(11)	(23,054)	(2,654)
<u>(442)</u>	<u>(210)</u>	<u>(62)</u>	<u>(365)</u>	<u>189</u>	<u>(18,376)</u>	<u>3,280</u>
(2,948)	(17,088)	-	(5,610)	(10,370)	(61,930)	(6,275)
-	-	-	-	-	-	248
329	4,300	-	-	9,334	14,494	-
-	7,516	-	-	-	7,516	-
(90)	(5,358)	-	(645)	-	(8,363)	-
(38)	(423)	(155)	(298)	(64)	(11,673)	-
<u>(2,747)</u>	<u>(11,053)</u>	<u>(155)</u>	<u>(6,553)</u>	<u>(1,100)</u>	<u>(59,956)</u>	<u>(6,027)</u>
22	24	(29)	36	(1)	350	(48)
22	24	(29)	36	(1)	350	(48)
(570)	(2,435)	6,031	(3,442)	174	(1,525)	(850)
8,989	15,332	17,672	8,631	861	243,339	84,648
<u>\$ 8,419</u>	<u>\$ 12,897</u>	<u>\$ 23,703</u>	<u>\$ 5,189</u>	<u>\$ 1,035</u>	<u>\$ 241,814</u>	<u>\$ 83,798</u>
\$ 8,419	\$ 12,897	\$ 23,703	\$ 5,189	\$ 1,035	\$ 237,800	\$ 78,251
-	-	-	-	-	4,014	5,547
<u>\$ 8,419</u>	<u>\$ 12,897</u>	<u>\$ 23,703</u>	<u>\$ 5,189</u>	<u>\$ 1,035</u>	<u>\$ 241,814</u>	<u>\$ 83,798</u>
\$ 1,153	\$ 1,358	\$ 6,352	\$ 2,414	\$ 840	\$ 46,723	\$ (5,983)
2,049	2,882	109	763	21	20,130	3,074
-	-	-	-	-	-	42
(106)	2,941	(293)	(7)	(2,043)	395	403
-	-	-	-	-	-	30
-	17	-	-	-	5	-
(291)	(639)	(149)	(247)	(65)	(3,448)	(733)
(117)	(361)	(131)	(57)	(21)	(1,903)	(255)
(840)	697	(113)	76	2,187	4,933	1,687
5	(2)	(2)	6	(1)	13	14
-	-	-	-	-	-	580
-	-	121	-	-	121	-
-	-	-	-	-	-	1,278
728	1,843	367	466	154	9,155	1,709
(22)	(67)	(24)	(11)	(4)	(354)	(48)
(7)	(2)	(10)	15	10	(37)	50
45	137	50	22	8	724	97
<u>\$ 2,597</u>	<u>\$ 8,804</u>	<u>\$ 6,277</u>	<u>\$ 3,440</u>	<u>\$ 1,086</u>	<u>\$ 76,457</u>	<u>\$ 1,945</u>

See accompanying notes to the basic financial statements.

CITY OF PALO ALTO
Agency Funds
Statement of Assets and Liabilities
June 30, 2018
(Amounts in thousands)

	Agency Funds
ASSETS:	
Cash and investments available for operations (Note 3)	\$ 2,522
Restricted cash and investments with fiscal agents (Note 3)	2,594
Account receivable	532
Interest receivable	14
Total assets	\$ 5,662
LIABILITIES:	
Due to bondholders	\$ 4,595
Due to other governments	1,067
Total liabilities	\$ 5,662

See accompanying notes to the basic financial statements.

CITY OF PALO ALTO
Index to the Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

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Notes are essential to present fairly the information contained in the overview level of the basic financial statements. Narrative explanations are intended to communicate information that is not readily apparent or cannot be included in the statements themselves, and to provide additional disclosures as required by the Governmental Accounting Standards Board.

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CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The City of Palo Alto (the City) was incorporated in 1894 and operates as a charter city, having had its first charter granted by the State of California in 1909. The City operates under the Council-Manager form of government and provides the following services: public safety (police and fire), public works, electric, fiber optics, water, gas, wastewater, storm drain, refuse, airport, golf course, planning and zoning, general administration services, library, open space and science, recreational and human services.

(a) Reporting Entity

The City is governed by a nine-member council, elected by City residents. The City is legally separate and fiscally independent, which means it can issue debt, set and modify budgets and fees, and sue or be sued. The accompanying basic financial statements present the financial activities of the City, which is the primary government presented, along with the financial activities of its component unit, which is an entity for which the City is financially accountable. Although a separate legal entity, a blended component unit is, in substance, part of the City's operations and is reported as an integral part of the City's financial statements. The City's component unit described below is blended.

The Palo Alto Public Improvement Corporation (the Corporation) provides financing of public capital improvements for the City through the issuance of Certificates of Participation (COPs), a form of debt that allows investors to participate in a stream of future lease payments. Proceeds from the COPs are used to construct projects that are leased to the City. The lease payments are sufficient in timing and amount to meet the debt service requirements of the COPs. The Board of Directors of the Corporation is composed of the same members as the City Council. The Corporation is controlled by the City, which performs all accounting and administrative functions for the Corporation. The financial activities of the Corporation are included in the Downtown Parking Improvement Debt Service Fund.

Financial statements for the Corporation may be obtained from the City of Palo Alto, Administrative Services Department, 4th Floor, 250 Hamilton Avenue, Palo Alto, CA 94301.

(b) Basis of Presentation

The City's basic financial statements are prepared in conformity with accounting principles generally accepted in the United States of America. The Governmental Accounting Standards Board (GASB) is the acknowledged standard setting body for establishing accounting and financial reporting standards followed by governmental entities in the United States.

These standards require that the financial statements described below be presented:

Government-wide Statements: The Statement of Net Position and the Statement of Activities display information about the primary government and its component unit. These statements include the financial activities of the overall City government, except for fiduciary activities. Eliminations have been made to minimize the double counting of internal activities. However, interfund goods and services transactions have not been eliminated in the consolidation process. These statements distinguish between the governmental and business-type activities of the City.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(b) Basis of Presentation (Continued)

Governmental activities generally are financed through taxes, intergovernmental revenues, and other non-exchange transactions. Business-type activities are financed in whole or in part by fees charged to external parties.

The Statement of Activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the City and for each function of the City's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Program revenues include: (a) charges paid by the recipients for goods and services offered by the programs, (b) grants and contributions that are restricted to meeting the operational needs of a particular program, and (c) fees, grants and contributions that are restricted to financing the acquisition or construction of capital assets. Revenues that are not classified as program revenues, including all taxes, are presented as general revenues.

Fund Financial Statements: The fund financial statements provide information about the City's funds, including fiduciary funds and its blended component unit. Separate statements for each fund category – governmental, proprietary and fiduciary – are presented. The emphasis of fund financial statements is on major individual governmental and enterprise funds, each of which is displayed in a separate column. All remaining governmental and internal service funds are aggregated and reported as non-major funds.

Proprietary fund operating revenues, such as utilities sales and charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investment earnings, result from non-exchange transactions or ancillary activities.

Operating expenses for enterprise funds and internal service funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All expenses not meeting this definition are reported as nonoperating expenses.

(c) Major Funds and Other Funds

The City's major governmental and enterprise funds need to be identified and presented separately in the fund financial statements. All other funds, called non-major funds, are combined and reported in a single column, regardless of their fund type.

Major funds are defined as funds that have assets and deferred outflows of resources, liabilities and deferred inflows of resources, revenues or expenditures/expenses equal to at least 10 percent of their fund type total and at least 5 percent of the grand total. The General Fund is always a major fund. The City may also select other funds it believes should be presented as major funds on a qualitative basis.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(c) Major Funds and Other Funds (Continued)

The City reported the following major governmental funds in the accompanying financial statements:

General Fund – This is the City’s primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

Capital Projects Fund – This fund accounts for resources used for the acquisition and construction of capital facilities by the City, with the exception of those assets financed by proprietary funds.

The City reported the following enterprise funds as major funds in the accompanying financial statements:

Water Services Fund – This fund accounts for all financial transactions relating to the City’s water service. Services are on a user-charge basis to residents and business owners located in the City.

Electric Services Fund – This fund accounts for all financial transactions relating to the City’s electric service. Services are on a user-charge basis to residents and business owners located in the City.

Fiber Optics Fund – This fund accounts for all financial transactions relating to the City’s fiber optics service. Services are on a user-charge basis to licensees located in the City.

Gas Services Fund – This fund accounts for all financial transactions relating to the City’s gas service. Services are on a user-charge basis to residents and business owners located in the City.

Wastewater Collection Services Fund – This fund accounts for all financial transactions relating to the City’s wastewater collection service. Services are on a user-charge basis to residents and business owners located in the City.

Wastewater Treatment Services Fund – This fund accounts for all financial transactions relating to the City’s wastewater treatment. Services are on a user-charge basis to residents and business owners located in the City.

Refuse Services Fund – This fund accounts for all financial transactions relating to the City’s refuse service. Services are on a user-charge basis to residents and business owners located in the City.

Storm Drainage Services Fund – This fund accounts for all financial transactions relating to the City’s storm drainage service. Services are on a user-charge basis to residents and business owners located in the City.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(c) Major Funds and Other Funds (Continued)

The City also reports the following funds:

Airport Fund – This non-major enterprise fund accounts for all financial transactions relating to the Palo Alto Airport (PAO). The City assumed control over operation of PAO from the County of Santa Clara, effective August 11, 2014.

Internal Service Funds – These funds account for fleet replacement and maintenance, technology, central duplicating, printing and mailing services, administration of compensated absences and health benefits, and the City's self-insured workers' compensation and general liability programs, all of which are provided to other departments on a cost-reimbursement basis. Also included is the Retiree Health Benefits Internal Service Fund, which accounts for benefits to retirees.

Vehicle Replacement and Maintenance – This fund accounts for the maintenance and replacement of vehicles and equipment used by all City departments. The source of revenue is from reimbursement of fleet replacement and maintenance costs allocated to each department by usage of vehicle.

Technology – This fund accounts for replacement and upgrade of technology, and covers four primary areas used by all City departments: desktop, infrastructure, applications, and technology research and development. The source of revenue is from reimbursement of costs for support provided to other departments.

Printing and Mailing Services – This fund accounts for central duplicating, printing and mailing services provided to all City departments. The source of revenue for this fund is from reimbursement of costs for services and supplies purchased by other departments.

General Benefits – This fund accounts for the administration of compensated absences and health benefits.

Workers' Compensation Insurance Program – This fund accounts for the administration of the City's self-insured workers' compensation program.

General Liability Insurance Program – This fund accounts for the administration of the City's self-insured general liability program.

Retiree Health Benefits – This fund accounts for retiree health benefits.

Fiduciary Funds – These funds account for assets held by the City, an agent for assessment districts, and members of the Cable Joint Powers Authority. These funds are custodial in nature and do not involve measurement of results of operations. The City maintains two agency funds. The financial activities of these funds are excluded from the government-wide financial statements, but are presented in separate fiduciary fund financial statements. Agency funds apply the accrual basis of accounting but do not have a measurement focus.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(c) Major Funds and Other Funds (Continued)

Cable Joint Powers Authority – This fund accounts for the activities of the cable television system on behalf of the members.

University Avenue Area Off-Street Parking Assessment District – This fund accounts for the receipts and disbursements associated with the 2012 Limited Obligation Refunding Improvement Bonds.

(d) Basis of Accounting

The government-wide and proprietary fund financial statements are reported using the *economic resources* measurement focus and the *full 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.

Governmental funds are reported using the *current financial resources* measurement focus and the *modified accrual* basis of accounting. Under this method, revenues are recognized when *measurable* and *available*. The City considers revenues susceptible to accrual reported in the governmental funds to be available if the revenues are collected within ninety days after year-end, except for property taxes, which are available if collected within sixty days after year-end.

Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures to the extent they have matured. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term debt and acquisitions under capital leases are reported as *other financing sources*.

Revenues susceptible to accrual include taxes, intergovernmental revenues, interest and charges for services.

Grant revenues are recognized in the fiscal year in which all eligibility requirements are met. Under the terms of grant agreements, the City may fund certain programs with a combination of cost-reimbursement grants, categorical block grants, and general revenues. Thus, both restricted and unrestricted net position may be available to finance program expenditures. The City's policy is to first apply restricted grant resources to such programs, followed by general revenues if necessary.

Certain indirect costs are included in program expenses reported for individual functions and activities. Transactions representing the exchange of interfund goods and services have also been included.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(e) Cash and Cash Equivalents

Restricted and unrestricted pooled cash and investments held in the City Treasury, and other unrestricted investments invested by the City Treasurer, are considered cash equivalents for purposes of the statement of cash flows because the City’s cash management pool and funds invested by the City Treasurer possess the characteristics of demand deposit accounts. Other restricted and unrestricted investments with maturities of less than three months at the time of purchase are considered cash equivalents for purposes of the statement of cash flows.

(f) Investments

The City’s investments are carried at fair value, and its fair value measurements are categorized within the fair value hierarchy established by generally accepted accounting principles. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

(g) Inventory of Materials and Supplies

Materials and supplies are held for consumption and are valued at average cost. The consumption method is used to account for inventories. Under the consumption method, inventories are recorded as expenditures at the time inventory items are used, rather than purchased.

(h) Prepaid items

Prepaid items are recorded at cost. Using the consumption method, prepaid items are recorded as expenditures over the period that service is provided.

(i) Compensated Absences

The liability for compensated absences includes the vested portion of vacation, sick leave, and overtime compensation pay. The City’s liability for accrued compensated absences is recorded in the General Benefits Internal Service Fund. The fund is reimbursed through payroll charges to all other funds. Earned but unpaid vacation and overtime compensation pay are recognized as an expense or expenditure in the proprietary and governmental fund types when earned because the City has provided financial resources for the full amount through its budgetary process. Vested accumulated sick pay is paid in the event of termination due to disability and, under certain conditions, is specified in employment agreements.

During the fiscal year ended June 30, 2018, changes to the compensated absences liabilities were as follows (in thousands):

Beginning balance	\$ 11,478
Additions	7,374
Payments	<u>(6,794)</u>
Ending balance	<u>\$ 12,058</u>
Current portion	<u>\$ 5,996</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(j) Property Tax

Santa Clara County (the County) assesses properties and bills, collects, and distributes property taxes to the City. The County remits the entire amount levied and handles all delinquencies, retaining interest and penalties.

The County assesses property values, levies bills and collects taxes as follows:

	<u>Secured</u>	<u>Unsecured</u>
Lien Dates	January 01	January 01
Levy Dates	October 01	July 01
Due Dates	50% on November 01 50% on February 01	Upon receipt of billing
Delinquent after	December 10 (for November) April 10 (for February)	August 31

The term “unsecured” refers to taxes on personal property other than real estate, land and buildings. These taxes are secured by liens on the property being taxed. Property tax revenues are recognized by the City in the fiscal year they are assessed, provided they become available as defined previously within sixty days after year-end.

(k) Deferred Outflows of Resources and Deferred Inflows of Resources

A deferred outflow of resources is the consumption of net position that is applicable to a future reporting period. A deferred inflow of resources is defined as an acquisition of net position applicable to a future reporting period.

(l) Pensions and OPEB

For purposes of measuring the net pension liability and net OPEB liability, deferred outflows/inflows of resources related to pensions and OPEB, and pension and OPEB expense, information about the fiduciary net position of the City’s pension and OPEB plans and additions to/deductions from the plans’ fiduciary net positions have been determined on the same basis as they are reported by the California Public Employees’ Retirement System (CalPERS) and the California Employer’s Retiree Benefit Trust Fund Program (CERBT). For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

(m) Rounding

All amounts included in the basic financial statements and footnotes are presented to the nearest thousand.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(n) Effects of New Pronouncements

As of July 1, 2017, the City implemented the following GASB Statements:

In June 2015, GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. This statement addresses reporting by governments that provide OPEB to their employees and for governments that finance OPEB for employees of other governments. As of July 1, 2017, the City recorded the beginning net OPEB liability of \$154.7 million, the beginning deferred outflows of resources of \$14.7 million related to OPEB contributions made after the beginning measurement date, the removal of the net OPEB asset under the previous standards of \$19.4 million, to arrive at the restatement of \$159.4 million. See Note 12 for detailed information about the impact of the implementation on the City's financial statements.

In March 2016, the GASB issued Statement No. 81, *Irrevocable Split-Interest Agreements*. The statement provides recognition and measurement guidance for situations in which a government is a beneficiary of these agreements. Implementation of this statement did not have a significant impact on the City's financial statements for the fiscal year ended June 30, 2018.

In March 2017, the GASB issued Statement No. 85, *Omnibus 2017*. The objective of the statement is to address practice issues that have been identified during implementation and application of certain GASB Statements. The statement addresses a variety of topics including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits). Implementation of this statement did not have a significant impact on the City's financial statements for the fiscal year ended June 30, 2018.

In May 2017, the GASB issued Statement No. 86, *Certain Debt Extinguishment Issues*. The primary objective of the statement is to improve consistency in accounting and financial reporting for in-substance defeasance of debt by providing guidance for transactions in which cash and other monetary assets acquired with only existing resources - resources other than the proceeds of refunding debt - are placed in an irrevocable trust for the sole purpose of extinguishing debt. Implementation of this statement did not have a significant impact on the City's financial statements for the fiscal year ended June 30, 2018.

The City is currently analyzing its accounting practices to determine the potential impact on the financial statements for the following GASB Statements:

In November 2016, the GASB issued Statement No. 83, *Certain Asset Retirement Obligations*. The statement addresses accounting and financial reporting for certain asset retirement obligations (AROs). An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this statement. The requirements of this statement are effective for the City's fiscal year ending June 30, 2019.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(n) Effects of New Pronouncements (Continued)

In January 2017, the GASB issued Statement No. 84, *Fiduciary Activities*. The statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. Separate criteria are included to identify fiduciary component units and postemployment benefit arrangements that are fiduciary activities. The statement also provides for recognition of a liability to the beneficiaries in a fiduciary fund when an event has occurred that compels the government to disburse fiduciary resources. The requirements of this statement are effective for the City's fiscal year ending June 30, 2020.

In June 2017, the GASB issued Statement No. 87, *Leases*. The objective of this statement is to better meet the information needs of financial statement users by improving accounting and financial reporting for leases by governments. This Statement increases the usefulness of governments' financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract. It establishes a single model for lease accounting based on the foundational principle that leases are financings of the right to use an underlying asset. Under this Statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities. The requirements of this statement are effective for the City's fiscal year ending June 30, 2021.

In March 2018, the GASB issued Statement No. 88, *Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements*. The objective of this statement is to improve the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt. The requirements of this statement are effective for the City's fiscal year ending June 30, 2019.

In June 2018, the GASB issued Statement No. 89, *Accounting for Interest Cost Incurred before the End of a Construction Period*. The objectives of this statement are 1) to enhance the relevance and comparability of information about capital assets and the cost of borrowing for a reporting period, and 2) to simplify accounting for interest cost incurred before the end of a construction period. The requirements of this statement are effective for the City's fiscal year ending June 30, 2021.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

(n) *Effects of New Pronouncements (Continued)*

In August 2018, the GASB issued Statement No. 90, *Majority Equity Interests, an amendment of GASB Statements No.14 and No.61*. The objectives of this statement are to improve the consistency and comparability of reporting a government's majority equity interest in a legally separate organization and to improve the relevance of financial statement information for certain component units. The requirements of this statement are effective for the City's fiscal year ending June 30, 2020.

(o) *Use of Estimates*

The accompanying basic financial statements have been prepared on the modified accrual and accrual basis of accounting in accordance with generally accepted accounting principles. This requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

NOTE 2 – BUDGETS AND BUDGETARY ACCOUNTING

1. The City Manager submits proposed operating and capital budgets to the City Council for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and the means of financing them.
2. Public hearings are conducted to obtain comments on the proposed budgets.
3. The Budget is approved with the adoption of a budget ordinance for all funds except Agency Funds.
4. Per the Palo Alto Municipal Code, only the City Manager is authorized to reallocate funds from contingency accounts maintained in the General Fund. Additional appropriations to departments in the General Fund, or to total appropriations for all other budgeted funds, or transfers of appropriations between funds, require approval by the City Council. Amendments to budgeted revenue and expenditures are added to or subtracted from the Adopted Budget and the resulting totals are reflected as Final Budget amounts.
5. As defined in the Palo Alto Municipal Code, expenditures may not exceed budgeted appropriations at the department level for the General Fund, and at the fund level for Enterprise, Special Revenue and Debt Service Funds.
6. Budgets for governmental funds are adopted on a basis consistent with generally accepted accounting principles (GAAP), except that unrealized gains or losses on investments, changes in advances to other funds and notes receivable are not recognized on a budgetary basis and encumbrances are treated as budgetary expenditures when incurred.
7. Expenditures for the Capital Projects Fund are budgeted and maintained at a project level for the life of the project. Budget to actual comparisons for these expenditures have been excluded from the accompanying financial statements.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 3 – CASH AND INVESTMENTS

The City pools cash from all sources and all funds, except restricted bond proceeds with fiscal agents and Public Agency Retirement Services, and invests its pooled idle cash according to State of California law and the City’s Investment Policy. The basic principles underlying the City’s investment philosophy are to ensure the safety of public funds, ensure that sufficient funds are available to meet current expenditures, and achieve a reasonable rate of return on investments.

Policies

The City invests in individual investments and in investment pools. Individual investments are evidenced by specific identifiable securities instruments, or by an electronic entry registering the owner in the records of the institution issuing the security, called the book entry system. In order to increase security, the City employs the trust department of a bank as the custodian of certain City managed investments.

Classification

Cash and investments are classified in the financial statements as shown below, based on whether or not their use is restricted under the terms of City debt instruments or agreements (in thousands):

	Governmental Activities	Business-Type Activities	Fiduciary Funds	Total
Cash and investments:				
Available for operations	\$ 280,681	\$ 237,800	\$ 2,522	\$ 521,003
Held with fiscal agents and trustees	6,185	4,014	2,594	12,793
Total cash and investments	<u>\$ 286,866</u>	<u>\$ 241,814</u>	<u>\$ 5,116</u>	<u>\$ 533,796</u>

Investments Authorized by the City’s Investment Policy, Debt Agreements and Trust Agreements

The table below summarizes the investment types that are authorized by the California Government Code (Code) and the City’s Investment Policy, and includes the interest rate risk, credit risk and concentration of credit risk as outlined in the Investment Policy. In addition, the table discloses investment of debt proceeds held by bond trustees. These investments are governed by the provisions of each debt agreement of the City, rather than the general provisions of the City’s Investment Policy.

The City must maintain required amounts of cash and investments with trustees under the terms of certain debt issues. These funds are unexpended bond proceeds or are pledged as reserves to be used if the City fails to meet its obligations under these debt issues. The Code requires these funds to be invested in accordance with City ordinance, bond indentures or state statute. All of these funds have been invested as permitted under the Code and the investment policy approved by the City Council.

The City has implemented investment guidelines for its Public Agencies Retirement Services (PARS) Trust which authorizes the investments in U.S. Treasury securities, federal agencies and U.S. guaranteed obligations, corporate notes, certificates of deposit, bankers’ acceptances, equities investments, and mutual funds.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 3 – CASH AND INVESTMENTS (Continued)

Authorized Investment Type	Maximum Maturity	Minimum Credit Quality	Maximum Percentage of Portfolio	Maximum Investment in One Issuer
U.S. Government Securities	10 years (*)	N/A	No Limit	No Limit
U.S. Federal Agency Securities (C)	10 years (*)	N/A	No Limit (A)	No Limit
Certificates of Deposit	10 years (*)	N/A	20%	10% of the par value of portfolio
Bankers Acceptances	180 days (D)	N/A (D)	30%	\$5 million
Commercial Paper	270 days	A-1	15%	\$3 million (B)
Local Agency Investment Fund	N/A	N/A	No Limit	\$50 million per account
Short-Term Repurchase Agreements	1 year	N/A	No Limit	No Limit
City of Palo Alto Bonds	N/A	N/A	No Limit	No Limit
Money Market Mutual Funds	N/A	N/A (E)	No Limit	No Limit
Mutual Funds (F)	N/A	N/A	20%	10%
Negotiable Certificates of Deposit	10 years (*)	N/A	10%	\$5 million
Medium-Term Corporate Notes	5 years	AA	10%	\$5 million
Bonds of State of California	10 years (*)	AA/AA2	20%	No Limit
Municipal Agencies				

(A) Callable and multi-step securities are limited to no more than 25% of the par value of the portfolio, provided that: 1) the potential call dates are known at the time of purchase, 2) the interest rates at which they "step-up" are known at the time of purchase, 3) the entire face value of the security is redeemable at the call date.

(B) The lesser of \$3 million or 10% of outstanding commercial paper of any one institution.

Debt Agreements:

(C) Utility Revenue Bonds 2011 Refunding and 1999 Refunding allow general obligations of states with a minimum credit quality rating of A2/A by Moody's and Standard & Poor's.

(D) Utility Revenue Bonds 2011 Refunding and 1999 Refunding require a minimum credit quality rating of A-1/P-1 by Moody's and Standard & Poor's and maturing after no more than 360 days. Utility Revenue Bonds 1995 Series A limit the maximum maturity to 365 days.

(E) Water Revenue Bonds 2009 Series A, Utility Revenue Bonds 2011 Refunding and 1999 Refunding require a minimum credit quality rating of AAAM or AAAM-G by Standard & Poor's.

(F) Utility Revenue Bonds 2011 Refunding, General Obligation Bonds 2010 and 2013A, and University Avenue Parking Bond 2012 are allowed to invest in the California Asset Management Program.

(*) The maximum maturity is based on the Investment Policy that is approved by the City Council and is less restrictive than the California Government Code.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 3 – CASH AND INVESTMENTS (Continued)

Fair Value Measurements

The City categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure fair value of the assets. Level 1 inputs are quoted prices in an active market for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 inputs are significant unobservable inputs. All of the investments are measured using level 2 inputs, except for investments in money market mutual funds, California Asset Management Program and Local Agency Investment Fund, which are not subject to the fair value hierarchy.

Investment securities classified in Level 2 of the fair value hierarchy are valued using prices determined by the use of matrix pricing techniques maintained by the pricing vendors for these securities. Matrix pricing is used to value securities based on the securities relationship to benchmark quoted prices.

The following is a summary of the fair value measurements of the City as of June 30, 2018 (in thousands):

<u>Type of Investment</u>	<u>June 30, 2018</u>	<u>Level 2</u>
Investments by fair value hierarchy		
U.S. Federal Agency Securities	\$ 316,594	\$ 316,594
U.S. Treasury Notes	19,470	19,470
Local Government Bonds	82,220	82,220
Negotiable Certificates of Deposit	48,556	48,556
Corporate Bonds	20,443	20,443
Total investments by fair value hierarchy	<u>487,283</u>	<u>\$ 487,283</u>
Investment not subject to fair value hierarchy		
Bonds Fund:		
Money Market Mutual Funds	3,005	
U.S Bank Trust Services	4,012	
Equity Mutual Funds (Irrevocable for pension)	5,548	
California Asset Management Program	3,214	
Local Agency Investment Fund	<u>24,647</u>	
Total investments not subject to fair value hierarchy	<u>40,426</u>	
Total investments measured at fair value	<u>\$ 527,709</u>	

Local Agency Investment Fund

The City participates in the Local Agency Investment Fund (LAIF) which, under the oversight of the Treasury of the State of California, is regulated by California Government Code Section 16429. LAIF management calculates the fair value and cost of the entire LAIF pool. The City adjusts its cost basis invested in LAIF to fair value based on this ratio. The fair value of the City's position in the pool is the same as the value of the pool share. The balance available for withdrawal on demand is based on accounting records maintained by LAIF, which are recorded on an amortized cost basis. At June 30, 2018, LAIF had a weighted average maturity of 193 days.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 3 – CASH AND INVESTMENTS (Continued)

Fidelity Institutional Asset Management

Money market mutual funds are available for withdrawal on demand and at June 30, 2018, had a weighted average maturity of 29 days.

California Asset Management Program

The City is a voluntary participant in the California Asset Management Program (CAMP). CAMP is an investment pool offered by the California Asset Management Trust (the Trust). The Trust is a joint powers authority and public agency created by the Declaration of Trust and established under the provisions of the California Joint Exercise of Powers Act (California Government Code Sections 6500 et seq., or the "Act") for the purpose of exercising the common power of its participants to invest certain proceeds of debt issues and surplus funds. The City's investments are limited to investments permitted by subdivisions (a) to (n), inclusive, of Section 53601 of the California Government Code. The City reports its investments in CAMP at the fair value amounts provided by CAMP, which is the same as the value of the pool share. At June 30, 2018, the fair value approximated the City's cost. CAMP had a weighted average maturity of 35 days at June 30, 2018.

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates may adversely affect the fair value of an investment. Normally, the longer the maturity of an investment, the greater the sensitivity its fair value is to changes in market interest rates. As of June 30, 2018, the City's investments consisted of the following (in thousands):

Type of Investment	Maturities				Total
	Less Than One Year	One to Three Years	Three to Five Years	Over Five Years	
U.S. Federal Agency Securities	\$ 43,867	\$ 80,159	\$ 81,637	\$ 110,931	\$ 316,594
U.S. Treasury Notes	6,436	2,951	10,083	-	19,470
Local Government Bonds	251	14,468	34,032	33,469	82,220
Corporate Bonds	2,787	17,558	98	-	20,443
Bond Funds:					
Money Market Mutual Funds	3,005	-	-	-	3,005
U.S Bank Trust Services	4,012	-	-	-	4,012
Equity Mutual Funds (pension trust)	5,548	-	-	-	5,548
Negotiable Certificates of Deposit	6,650	15,935	23,479	2,492	48,556
California Asset Management Program	3,214	-	-	-	3,214
Local Agency Investment Fund	24,647	-	-	-	24,647
Total Investments	<u>\$ 100,417</u>	<u>\$ 131,071</u>	<u>\$ 149,329</u>	<u>\$ 146,892</u>	527,709
Cash in bank and on hand					6,087
Total Cash and Investments					<u>\$ 533,796</u>

Investment with Fair Values Highly Sensitive to Interest Rate Fluctuations

At June 30, 2018, the City's investments (including investments held by bond trustees) include U.S. Federal Agency Callable Securities totaling \$113 million. These investments are highly sensitive to interest rate fluctuations (to a greater degree than already indicated in the information provided above) and are subject to early redemption.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 3 – CASH AND INVESTMENTS (Continued)

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization.

Presented below is the actual rating as provided by Standard & Poor’s, Moody’s and/or Fitch’s investment rating system as of June 30, 2018, for each investment type (in thousands):

Type of Investment	Rating	Total
U.S. Federal Agency Securities	AA+	\$ 167,190
	N/A	149,404
Total U.S Federal Agency Securities		316,594
Corporate Bonds	AAA	10,646
	AA+	8,831
	AA	966
Total Corporate Bonds		20,443
Local Government Bonds	AAA	39,659
	AA+	22,566
	AA	19,995
Total Government Bonds		82,220
Money Market Mutual Funds	AAA	3,005
Total Money Market Mutual Funds		3,005
Total Investments		422,262
Not Applicable:		
U.S. Treasury Notes		19,470
Not Rated:		
Bond Fund: U.S Bank Trust Services		4,012
California Asset Management Program		3,214
Local Agency Investment Fund		24,647
Negotiable Certificates of Deposit		48,556
Equity Mutual Funds		5,548
Cash in bank and on hand		6,087
Total Cash and Investments		\$ 533,796

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 3 – CASH AND INVESTMENTS (Continued)

Concentration of Credit Risk

Investments in any one issuer, other than U.S. Treasury securities, mutual funds, and external investment pools, that represent 5 percent or more of total City portfolio investments are as follows at June 30, 2018 (in thousands):

Investments	Reporting Type	Fair Value at Year-End
Federal Home Loan Bank	U.S. Federal Agency Securities	\$ 99,848
Federal Agricultural Mortgage Corporation	U.S. Federal Agency Securities	109,183
Federal Farm Credit Bank	U.S. Federal Agency Securities	52,623

Custodial Credit Risk

California law requires banks and savings and loan institutions to pledge government securities with a market value of 110 percent of the City’s cash on deposit or first trust deed mortgage notes with a value of 150 percent of the deposit as collateral for these deposits. Under California Law, this collateral is considered held in the City’s name and places the City ahead of general creditors of the institution. The City has waived collateral requirements for the portion of deposits covered by federal deposit insurance.

The custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, the City will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The City’s Investment Policy limits its exposure to custodial credit risk by requiring that all security transactions entered into by the City be conducted on a delivery-versus-payment basis. Securities are to be held by a third-party custodian.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 4 – INTERFUND TRANSACTIONS

Transfers Between Funds

With Council approval, resources may be transferred from one City fund to another. The purpose of the majority of transfers is to subsidize a fund. Less often, a transfer may be made to open or close a fund. Transfers between City funds during FY 2018 were as follows (in thousands):

Fund Receiving Transfer	Fund Making Transfer	Amount Transferred
General Fund	Nonmajor Governmental Funds	\$ 717 A
	Electric Services Fund	12,887 B
	Gas Services Fund	6,699 B
	Capital Projects Fund	7 A
Capital Projects Fund	General Fund	24,800 C
	Nonmajor Governmental Funds	10,696 C
	Water Services Fund	6 C
	Fiber Optics Fund	6 C
	Gas Services Fund	6 C
	Storm Drainage	330 C
Nonmajor Governmental Funds	General Fund	659 A
	Water Services Fund	10 A
	Electric Services Fund	22 A
	Fiber Optics Fund	2 A
	Gas Services Fund	9 A
	Wastewater Collection Fund	5 A
	Internal Service Funds	21 A
Water Services Fund	Gas Services Fund	256 C
	Wastewater Collection Fund	256 C
Electric Services Fund	General Fund	2,486 D
	Water Services Fund	436 C
	Gas Services Fund	436 C
	Fiber Optics Fund	102 C
	Internal Service Funds	5 C
Internal Service Funds	General Fund	1,590 E/F
	Capital Projects Fund	108 E/F
	Nonmajor Governmental Funds	22 E/F
	Water Services Fund	252 E/F
	Electric Services Fund	538 E/F
	Fiber Optics Fund	25 E/F
	Gas Services Fund	271 E/F
	Wastewater Collection Fund	181 E/F
	Wastewater Treatment Fund	210 E/F
	Refuse Services Fund	62 E/F
	Storm Drainage Services Fund	35 E/F
	Airport	11 E/F
	Internal Service Funds	2,629 E/G
Total	<u>\$ 66,793</u>	

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 4 – INTERFUND TRANSACTIONS (Continued)

The reasons for these transfers are set forth below:

- (A) Transfer to fund street maintenance activities, to pay debt service, fund City employee parking, and to return unspent project funds.
- (B) Transfer to fund the return of initial investment made by general fund when utility department was created.
- (C) Allocation of funds to construct, purchase or maintain capital assets.
- (D) Transfer to fund electricity costs associated with City streetlight and traffic signal costs.
- (E) Transfer to fund supplemental pension trust fund.
- (F) Transfer to fund replacement and maintenance of critical desktop, software, infrastructure, vehicles and equipment.
- (G) Transfer to fund an implied subsidy for retiree healthcare.

Long-Term Interfund Advance

On December 6, 2010, the City Council accepted an Airport Business Plan of the Palo Alto Airport (PAO) and approved creation of the Airport Enterprise Fund to facilitate the transition of PAO control from County of Santa Clara to the City. Council approved the following General Fund advances to the Airport Fund:

\$	610,000	Due June 2019
	325,000	Due July 2023
	760,000	Due July 2024
	515,601	Due July 2025
	704,150	Due July 2026
	200,000	Due July 2027

All advances bear interest equal to the average return yield on the City's investment portfolio. As of June 30, 2018, the total outstanding principal amount is \$3.1 million.

Internal Balances

Internal balances represent the net interfund receivables and payables remaining after the elimination of all such balances within governmental and business-type activities.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 5 – NOTES AND LOANS RECEIVABLE

At June 30, 2018, the City’s notes and loans receivable totaled (in thousands):

Palo Alto Housing Corporation:	
Tree House Apartments	\$ 5,344
Emerson Street Project	375
Alma Single Room Occupancy Development	2,222
Barker Hotel	2,111
Sheridan Apartments	2,222
Oak Court Apartments, L.P.	7,834
El Dorado Palace LLC	65
Mid-Peninsula Housing Coalition:	
Palo Alto Gardens Apartments	100
Community Working Group, Inc.	1,280
Opportunity Center Associates, L.P.	750
Home Rehabilitation Loans	46
Executive Relocation Assistance Loans	479
Below Market Rate Assessment Loans	53
Oak Manor Townhouse Water System	114
Lytton Gardens Assisted Living	101
Emergency Housing Consortium	75
Alma Gardens Apartments	1,150
2811-2825 Alma Street Acquisition	1,890
Palo Alto Family Housing, 801 Alma Street	6,422
Palo Alto Senior Housing Project - Stevenson House, LLC	923
MP Palo Alto Garden, LLC	672
Colorado Park Housing Corporation	204
Buena Vista - County of Santa Clara	14,500
	<hr/>
Total Notes and Loans	48,932
Less: Valuation Allowance	(14,637)
	<hr/>
Total Notes and Loans, Net	\$ 34,295
	<hr/> <hr/>

Housing Loans

The City engages in programs designed to encourage construction or improvement in low-to-moderate income housing or other projects. Under these programs, grants or loans are provided under favorable terms to homeowners or developers who agree to spend these funds in accordance with the City’s terms. These loans have been offset by restricted or committed fund balances, as they are not expected to be repaid immediately.

Some of these loans contain forgiveness clauses that provide for the amount loaned to be forgiven if the third party maintains compliance with the terms of the loan and associated regulatory agreements. Since some of these loans are secured by trust deeds that are subordinated to other debt on the associated projects or are only repayable from residual cash receipts on the projects, collectability of some of the outstanding balances may not be realized. As a result of the forgiveness clauses and nature of these housing projects and associated cash flows, a portion of the outstanding balances of the loans has been offset by a valuation allowance.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 5 – NOTES AND LOANS RECEIVABLE (Continued)

Tree House Apartments

In March 2009, the City agreed to loan \$2.8 million to Tree House Apartments, L.P. (THA) for the purchase of the real property located at 488 West Charleston Road. The loan accrues simple interest at the rate of 3 percent per annum. The loan was funded with \$1.8 million of Community Development Block Grant (CDBG) funds and \$1.0 million of residential housing funds. An additional development loan in the amount of \$2.5 million was approved by the City on October 18, 2010. As of June 30, 2018, the outstanding balance for THA in aggregate is \$5.3 million. Principal and interest payments will be deferred, however if the borrower has earned extra income, and if it is acceptable to the other entities providing final permanent sources of funds, payment of interest and principal based on the City's proportionate share of the project's residual receipts from net operating income shall be made by the borrower. In no event shall full payment be made by the borrower later than concurrently with the expiration or earlier termination of the loan agreement, which is December 31, 2067.

Emerson Street Project

On November 8, 1994, the City loaned \$375,000 to Palo Alto Housing Corporation (PAHC) for expenses necessary to acquire an apartment complex for the preservation of rental housing for low and very low income households in the City. This loan is collateralized by a second deed of trust. The loan bears interest at 3 percent.

Alma Single Room Occupancy Development

On December 13, 1996, the City loaned \$2.2 million to Alma Place Associates, L.P. for development of a 107-unit single room occupancy development. This loan bears interest at 3 percent and is collateralized by a subordinated deed of trust. The principal balance is due in 2041.

Barker Hotel

On April 12, 1994, the City loaned a total of \$2.1 million for the preservation, rehabilitation and expansion of a low-income, single occupancy hotel. This loan was funded by three sources: \$400,000 from the Housing In-Lieu Fund, \$1.0 million from HOME Investment Partnership Program Funds, and \$670,000 from CDBG funds. All three notes bear no interest and are collateralized by a deed of trust, which is subordinated to private financing. Loan repayments are deferred until 2035.

In July 2004, the City agreed to loan up to \$41,000 to PAHC to rehabilitate the interior of the Barker Hotel. The loan was funded with CDBG funds and is collateralized by a deed of trust on the property. Annual loan payments are deferred until certain criteria defined in the loan agreement are reached. The loan will be forgiven if the borrower satisfactorily complies with all terms and conditions of the loan agreement.

Sheridan Apartments

On December 8, 1998, the City loaned \$2.2 million to PAHC for the purchase and rehabilitation of a 57-unit apartment complex to be used for senior and low-income housing. The loan was funded with \$1.6 million in CDBG funds, and \$825,000 of Housing In-Lieu funds. The note is collateralized by a second deed of trust and an affordability reserve account held by PAHC. The loan was amended in June 2017. It will not accrue interest between May 1, 2017 and March 1, 2030. The loan will be forgiven on June 30, 2030 if PAHC uses the funds that would otherwise have been due to the City for another affordable housing project.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 5 – NOTES AND LOANS RECEIVABLE (Continued)

Oak Court Apartments, L.P.

On August 18, 2003, the City loaned \$5.9 million to PAHC for the purchase of land. The note bears interest of 5 percent and is secured by a deed of trust. Note payments are due annually after 55 years, or beginning in 2058, unless PAHC elects to extend the note until 2102, as defined in the regulatory agreement. The City also loaned \$1.9 million to Oak Court Apartments, L.P. for the construction of a 53-unit rental apartment complex for low and very low-income households with children, which was completed in April 2005. The note bears no interest until certain criteria defined in the note are satisfied, at which time the note will bear an interest rate not to exceed 3 percent. The note is secured by a subordinate deed of trust. The principal balance is due in 2060.

El Dorado Palace, LLC

On June 22, 2015, the City approved a loan to PAHC Housing Corporation in the amount of \$375,000 to increase the supply of affordable low income housing in the City. The City loaned \$52,000 and \$13,000 in June 2017 and March 2018, respectively. The loan bears three percent (3%) interest, however in the event of default will accrue at the lesser of 8% or the highest rate permitted by law. The term of the loan shall expire 55 years unless the City agree to extend an additional 44 years.

Palo Alto Gardens Apartments

On April 22, 1999, the City loaned \$1.0 million to Mid-Peninsula Housing Coalition (the Coalition) for the purchase and rehabilitation of a 155-unit complex for the continuation of low-income housing. The loan was funded with \$659,000 of CDBG funds and \$341,000 of Housing In-Lieu funds. The two notes bear interest at 3 percent and are secured by second deeds of trust and a City Affordability Reserve Account held by the Coalition. Principal and interest payments began in FY 2008. The principal balance of \$100,000 is due in 2039.

Community Working Group, Inc.

On May 13, 2002, the City loaned \$1.3 million to Community Working Group, Inc. for predevelopment, relocation and acquisition of land for development of an 89-unit complex and homeless service center for very low income households. The loan was funded with \$1.3 million of CDBG funds. The note bears no interest and is secured by a first deed of trust. No repayment is required as long as the borrower complies with all terms and conditions of the agreement. After 89 years of compliance with the regulatory agreement, the City's loan would convert to a grant and its deed of trust would be re-conveyed.

Opportunity Center Associates, L.P.

On July 19, 2004, the City loaned \$750,000 for a 55-year term to Opportunity Center Associates, L.P. for construction of 89 units of rental housing for extremely low-income and very low-income households. The loan was funded with \$750,000 of residential housing funds. The note bears 3 percent interest and is secured by a deed of trust. The loan remains outstanding and becomes due at the end of the 55-year term.

Home Rehabilitation Loans

The City administers a closed housing rehabilitation loan program initially funded with CDBG funds. Under this program, individuals with incomes below a certain level are eligible to receive low interest loans for rehabilitation work on their homes. These loans are secured by deeds of trust, which may be subordinated to subsequent encumbrances upon said real property with the prior written consent of the City. The loan repayments may be amortized over the life of the loans, deferred, or a combination of both.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 5 – NOTES AND LOANS RECEIVABLE (Continued)

Executive Relocation Assistance Loans

The City Council may authorize a mortgage loan as part of a relocation assistance package to executive staff. The loans are secured by first deeds of trust, and interest is adjusted annually based on the rate of return of invested funds of the City for the year ended June 30 plus one-quarter of 1 percent. Principal and interest payments are due bi-weekly. Employees must pay any outstanding balance on their loans within a certain period after ending employment with the City.

As of June 30, 2018, the City had one outstanding home loan from the current City Manager. The original purchase cost for the current City Manager's home was \$1.9 million and the City holds a 75 percent equity share. The loan balance owed as of June 30, 2018 is \$375,000. During FY 2011, the Council authorized a capital improvement loan of \$125,000. Loans for capital improvements are made on a dollar for dollar matching basis, with an equal equity contribution made by the City Manager. The loan balance owed as of June 30, 2018 was \$103,000.

Below Market Rate Assessment Loans

In December 2002, the City loaned \$53,000 to below market rate homeowners with low incomes and/or very limited assets for capital repairs, special assessments and improvements of their properties. The loans bear interest at 3 percent and are secured by a deed of trust on each property. Loan payments are deferred until 2032. In 2018, the City did not receive interest payments.

Oak Manor Townhouse Water System

On May 12, 2003, the City Council approved an allocation of \$114,000 to Palo Alto Housing Corporation Apartments, Inc (PAHCA, Inc) to replace the water pipes. Repayment of the loan will not be required unless the property is sold, the program is terminated or purpose of the program is changed without City's approval prior to July 1, 2033. The loan for this project is subordinated to the existing City loan with PAHCA, Inc dated January 7, 1991 for the acquisition of the project site, which is discussed earlier in this section.

Lytton Gardens Assisted Living

In June 2005, the City loaned \$101,000 to Community Housing, Inc. to upgrade and modernize the existing kitchens at the senior residential facility known as Lytton Gardens Assisted Living. The loan was funded with CDBG funds, and bears simple interest of 3 percent. Principal and interest payments are deferred until July 1, 2035, as long as the borrower continues to comply with all terms and conditions of the agreement.

Emergency Housing Consortium

In November 2005, the City agreed to loan up to \$75,000 to Emergency Housing Consortium to cover architectural expenses that will be incurred in rehabilitating and expanding the property. The loan was funded with CDBG funds, and bears simple interest of 3 percent. Principal and interest payments are deferred until July 1, 2035, as long as the borrower continues to comply with all terms and conditions of the agreement.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 5 – NOTES AND LOANS RECEIVABLE (Continued)

Alma Garden Apartments

In March 2006, the City agreed to loan up to \$1.2 million to Community Working Group, Inc. to acquire a 10-unit multi-family housing complex known as Alma Garden Apartments. The loan was funded with CDBG funds. Principal and interest payments are deferred until July 1, 2061 as long as the borrower complies with all terms and conditions of the agreement.

2811-2825 Alma Street Acquisition

On October 9, 2011, the City agreed to loan \$1.3 million to PAHC to acquire properties on Alma Street for the purpose of developing an affordable rental housing project. On June 29, 2015, the City loaned PAHC an additional \$0.6 million, and entered into an Amended and Restated Acquisition and Development Agreement which combined the two loans for a total loan of \$1.9 million. The loan term expires on December 8, 2066 with an option to extend the term for an additional 44 years. The loan bears simple interest of 3 percent, however in the event of default interest will accrue at the lesser of 8 percent or the highest rate permitted by law. Principal and interest payments are payable during the term of the agreement on a “residual receipt” basis as described in the agreement. All principal and interest is due in the event of an unauthorized transfer, a default or the expiration of the term. As of June 30, 2018, the outstanding balance was \$1.9 million.

Palo Alto Family Housing, 801 Alma Street

On February 14, 2011, the City agreed to loan Palo Alto Family, LP up to \$9.3 million for the purposes of predevelopment expenses and acquiring certain real property for the Alma Street Affordable Multi-Family Rental Housing Project. The loan bears simple interest of 3 percent. Principal and interest are due and payable during the term of the agreement on a “residual receipt” basis as described in the agreement. Except in the case of default, all remaining principal and interest shall be payable on the Restriction Termination Date as defined in the agreement. As of June 30, 2018, the outstanding amount is \$6.4 million.

Palo Alto Senior Housing Project

On October 1, 2015, the City entered into an affordable housing fund loan agreement with PASHPI Stevenson House LP, a California limited partnership, in the principal amount of \$1 million to assist in the rehabilitation of the Stevenson House. The loan bears simple interest of 3 percent. As of June 30, 2018, the loan outstanding balance is \$923,000 and is due at the end of the 55-year term.

MP Palo Alto Garden, LLC

The City loaned \$619,000 and \$53,000 in March 2017 and October 2017, respectively, in CDBG funds for the rehabilitation of the property. The note bears 3% simple interest and shall be deferred until April 24, 2054. If there are no Events of Default prior to the end of the terms, the unpaid principal and interest will be treated as a grant and no repayment will be due to the City.

Colorado Park Housing Corporation

On September 8, 2014, the City entered into an affordable housing fund loan agreement with Colorado Park Housing Corporation (CPHC), a California nonprofit public benefit corporation, in the principal amount of \$204,000. The loan bears no interest except in the event of default. The principal and any accrued interest is due and payable on the earlier of (a) expiration of the term, or (b) a default by CPHC which has not been cured as provided for in the agreement.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 5 – NOTES AND LOANS RECEIVABLE (Continued)

Buena Vista Mobile Home Park – Santa Clara County

In September 2017, the City entered into an agreement with the Santa Clara County Housing Authority (SCCHA) for the acquisition of Buena Vista Mobile Home Park. The City loaned SCCHA \$14.5 million for the acquisition. The City is entitled to twenty six percent of all residual receipts. Interest for the promissory note is 3% simple interest. Principal and interest payments will commence on September 30, 2019 and the note and all interest is payable in full on September 29, 2019. As of June 30, 2018, the loan balance is \$14.5 million.

NOTE 6 – CAPITAL ASSETS

Valuation

Capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Contributed capital assets are recorded at acquisition value at the time received. The City's policy is to capitalize all assets when costs are equal to or exceed \$5,000 and the useful life exceeds one year. Infrastructure assets are capitalized when costs are equal to or exceed \$100,000.

Proprietary fund capital assets are recorded at cost including significant interest costs incurred under restricted tax-exempt borrowings, which finance the construction of capital assets. These interest costs, net of interest earned on investment of proceeds of such borrowings, are capitalized and added to the cost of capital assets during the construction period. Maintenance and repairs are expensed as incurred.

The City has recorded all its public domain capital assets, consisting of roadway and recreation and open space, in its government-wide financial statements. GASB Statement No. 34 requires that all capital assets with limited useful lives be depreciated over their estimated useful lives. Alternatively, the "modified approach" may be used for certain capital assets. Depreciation is not provided under this approach, but all expenditures on these assets are expensed unless they are additions or improvements. The City has elected to use the depreciation method for its capital assets. The purpose of depreciation is to spread the cost of capital assets equitably among all users over the life of those assets. The amount charged to depreciation expense each year represents that year's pro rata share of the cost of capital assets.

Depreciation of capital assets is charged as an expense against operations each year and the total amount of depreciation taken over the years, called accumulated depreciation, is reported on the statement of net position as a reduction in the book value of capital assets.

Depreciation is calculated using the straight line method, which means the cost of the asset is divided by its expected useful life in years, and the result is charged to expense each year until the asset is fully depreciated. The City has assigned the useful lives listed below to capital assets.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 6 – CAPITAL ASSETS (Continued)

Governmental Activities	Years
Buildings and structures	20 - 30
Equipment:	
Computer equipment	3 - 5
Office machinery and equipment	5
Machinery and equipment	5 - 30
Intangible assets - software	5-20
Roadway network:	
Includes pavement, striping and legends, curbs, gutters and sidewalks, parking lots, traffic signage, and bridges	5 - 40
Recreation and open space network:	
Includes major park facilities, park trails, bike paths and medians	25 - 40
Business-type Activities	
Buildings and structures	25 - 60
Vehicles and heavy equipment	3 - 10
Machinery and equipment	10 - 50
Transmission, distribution and treatment systems	10 - 100

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 6 – CAPITAL ASSETS (Continued)

General Capital Assets

Changes in the City’s general capital assets during the year ended June 30, 2018 were (in thousands):

	Balance July 1, 2017	Additions	Retirements	Transfers	Balance June 30, 2018
<i>Governmental activities</i>					
Nondepreciable capital assets:					
Land and improvements	\$ 78,481	\$ -	\$ -	\$ -	\$ 78,481
Street trees	14,893	147	(278)	-	14,762
Intangible assets - Easement	3,567	-	-	-	3,567
Construction in progress	62,661	40,679	(3,334)	(30,663)	69,343
Total nondepreciable capital assets	<u>159,602</u>	<u>40,826</u>	<u>(3,612)</u>	<u>(30,663)</u>	<u>166,153</u>
Depreciable capital assets:					
Buildings and structures	225,414	574	(178)	20,656	246,466
Intangible assets - Software	279	-	-	-	279
Equipment	11,891	186	-	494	12,571
Roadway network	324,817	-	-	9,513	334,330
Recreation and open space network	35,186	-	-	-	35,186
Total depreciable capital assets	<u>597,587</u>	<u>760</u>	<u>(178)</u>	<u>30,663</u>	<u>628,832</u>
Less accumulated depreciation:					
Buildings and structures	(85,247)	(6,418)	131	-	(91,534)
Intangible assets - Software	(274)	(5)	-	-	(279)
Equipment	(7,353)	(507)	-	-	(7,860)
Roadway network	(148,370)	(7,620)	-	-	(155,990)
Recreation and open space network	(12,095)	(1,264)	-	-	(13,359)
Total accumulated depreciation	<u>(253,339)</u>	<u>(15,814)</u>	<u>131</u>	<u>-</u>	<u>(269,022)</u>
Depreciable capital assets, net	<u>344,248</u>	<u>(15,054)</u>	<u>(47)</u>	<u>30,663</u>	<u>359,810</u>
Internal service fund capital assets					
Construction in progress	3,182	6,198	-	(7,507)	1,873
Equipment	56,939	77	(2,954)	7,507	61,569
Less accumulated depreciation	(41,514)	(3,074)	2,924	-	(41,664)
Net internal service fund capital assets	<u>18,607</u>	<u>3,201</u>	<u>(30)</u>	<u>-</u>	<u>21,778</u>
Governmental activities capital assets, net	<u>\$ 522,457</u>	<u>\$ 28,973</u>	<u>\$ (3,689)</u>	<u>\$ -</u>	<u>\$ 547,741</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 6 – CAPITAL ASSETS (Continued)

Business-type Capital Assets

Changes in the City's enterprise fund capital assets during the year ended June 30, 2018 were (in thousands):

	Balance July 1, 2017	Additions	Retirements	Transfers	Balance June 30, 2018
<i>Business-type activities</i>					
Nondepreciable capital assets:					
Land and improvements	\$ 4,973	\$ -	\$ -	\$ -	\$ 4,973
Construction in progress	110,287	61,118	-	(18,001)	153,404
Total nondepreciable capital assets	<u>115,260</u>	<u>61,118</u>	<u>-</u>	<u>(18,001)</u>	<u>158,377</u>
Depreciable capital assets:					
Buildings and structures	56,856	-	-	3,039	59,895
Capital Leases	-	531	-	-	531
Infrastructure	633	-	-	-	633
Transmission, distribution and treatment systems	765,825	280	(1,781)	14,962	779,286
Total depreciable capital assets	<u>823,314</u>	<u>811</u>	<u>(1,781)</u>	<u>18,001</u>	<u>840,345</u>
Less accumulated depreciation:					
Buildings and structures	(12,577)	(1,020)	-	-	(13,597)
Infrastructure	(2)	(21)	-	-	(23)
Transmission, distribution and treatment systems	(330,781)	(19,112)	1,505	-	(348,388)
Total accumulated depreciation	<u>(343,360)</u>	<u>(20,153)</u>	<u>1,505</u>	<u>-</u>	<u>(362,008)</u>
Depreciable capital assets, net	<u>479,954</u>	<u>(19,342)</u>	<u>(276)</u>	<u>18,001</u>	<u>478,337</u>
Business-type activities capital assets, net	<u>\$ 595,214</u>	<u>\$ 41,776</u>	<u>\$ (276)</u>	<u>\$ -</u>	<u>\$ 636,714</u>

Capital Asset Contributions

Some capital assets may be acquired using federal and state grant funds, or they may be contributed by developers or other governments. Generally accepted accounting principles require that these contributions be accounted for as revenues at the time the capital assets are contributed.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 6 – CAPITAL ASSETS (Continued)

Depreciation Allocation

Depreciation expense was charged to functions and programs based on their usage of the related assets. The amount allocated to each function or program is as follows (in thousands):

<i>Governmental Activities</i>		<i>Business-type Activities</i>	
City Manager	\$ 19	Water	\$ 2,747
City Attorney	3	Electric	8,089
City Clerk	4	Fiber Optics	337
City Auditor	1	Gas	3,183
Administrative Services	4	Wastewater Collection	2,049
Community Services	2,523	Wastewater Treatment	2,880
Public Safety	311	Refuse	109
Public Works	10,267	Storm Drainage	738
Planning and Community Environment	333	Airport	21
Library	2,349		<u>\$ 20,153</u>
Internal Service Funds	3,074		
	<u>\$ 18,888</u>		

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 6 – CAPITAL ASSETS (Continued)

Construction In Progress

Construction in progress as of June 30, 2018 is comprised of the following (in thousands):

<u>Governmental Activities</u>	Expended to June 30, 2018
Bicycle Boulevards Implementation Project	\$ 7,917
Highway 101 Pedestrian/Bicycle Overpass	4,406
Fire Station No. 3 Replacement Design	4,109
Lucie Stern Buildings Mech/Electrical Improvements	3,918
Traffic Signal Upgrades	3,593
New Public Safety Building	3,101
Charleston/Arastradero Corridor	2,770
Transportation and Parking Improvements	2,383
Rinconada Park Improvement	2,183
Safe Routes To School	1,647
New California Ave Area Parking Garage	1,634
Park Trails	1,461
CalTrain Corridor Video Management System Installation	1,417
Curb & Gutter Repairs	1,268
Telephone Infrastructure and Network	1,251
Parks Master Plan	1,250
Newell Road Bridge/SFC Bridge Replacement	1,114
Cubberley Roof Replacements	1,103
Baylands Interpretive Center Improvements	1,078
City Facility Parking Lot Maintenance	1,067
Railroad Grade Separation	998
Benches/Signage/Fencing/Walkways	995
New Downtown Parking Garage	976
Baylands Interpretive Center & Boardwalk Improvement	839
Interior Finishes Construction	826
Other Construction In Progress	17,912
Total Governmental Activities Construction In Progress	<u>\$ 71,216</u>
<u>Business-type Activities</u>	Expended to June 30, 2018
Water system extension replacements and improvements	\$ 16,900
Gas system extension replacements and improvements	7,101
Sewer system rehabilitation and extensions	13,271
Electric distribution system improvements	8,097
Water quality control plant equipment replacement and lab facilities	4,063
Storm drainage structural and water quality improvements	9,667
Other electrical improvements projects	2,443
Other construction in progress	91,862
Total Business-type Activities Construction In Progress	<u>\$ 153,404</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 6 – CAPITAL ASSETS (Continued)

Construction In Progress

Allocations of business-type activity administration and general expenses of \$12.2 million have been capitalized and included in amounts expended to June 30, 2018.

Major governmental capital projects that are currently in progress, and the remaining capital commitment of each, are as follows:

- Fire Station Number 3 Replacement – \$5.6 million
- Charleston Arastradero Corridor - \$10.2 million
- Bicycle Boulevards Implementation Project - \$9.3 million

Major business-type capital projects that are currently in progress, and the remaining capital commitment of each, are as follows:

- Water Main Replacement for Water fund - \$4.7 million
- Dewatering & Loadout Facility Project for Wastewater Treatment Fund - \$12.3 million
- Gas Main Replacement for Gas Fund - \$6.8 million

Vehicle Registration Fees (VRF)

In FY 2018, the City received VRF funds from the Santa Clara Valley Transportation Authority and expended the full amount on capital expenditures for the Overlay Resurfacing Project (PE-86070):

Starting VRF balance July 1, 2017	\$	-
VRF revenue		421,874
VRF interest		2,999
VRF expense		(424,873)
Ending VRF balance June 30, 2018	<u>\$</u>	<u>-</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 7 – GENERAL LONG-TERM OBLIGATIONS

Long-Term Obligations

Bond premiums and discounts of long-term debt issues are amortized over the life of the related debt.

The City's long-term debt issues and transactions, other than special assessment debt discussed in Note 8, are as follows (in thousands):

	Original Issue Amount	Balance July 1, 2017	Additions	Retirements	Balance June 30, 2018	Current Portion
Governmental Activities Debt:						
<i>General Long-Term Obligations:</i>						
2002B Downtown Parking Improvements, Certificates of Participation, 6.50%, due 03/01/2022	\$ 3,555	\$ 975	\$ -	\$ 975	\$ -	\$ -
2010 General Obligation Bonds, 3.25% - 5%, due 08/01/2040	55,305	46,980	-	1,170	45,810	1,225
2011 Lease-Purchase Agreement	3,222	842	-	416	426	426
2013A General Obligation Bonds, 2 - 5%, due 08/01/2041	20,695	16,730	-	400	16,330	415
2018 Capital Improvement, Certificates of Participation, 2.2%-4.33%, due 11/1/2047	8,970	-	8,970	-	8,970	35
Add: Unamortized Premium	-	3,768	-	158	3,610	158
Total Governmental Activities Debt	\$ 91,747	\$ 69,295	\$ 8,970	\$ 3,119	\$ 75,146	\$ 2,259
	Original Issue Amount	Balance July 1, 2017	Additions	Retirements	Balance June 30, 2018	Current Portion
Business-type Activities Debt:						
<i>Enterprise Long-Term Obligations:</i>						
Utility Revenue Bonds						
1995 Series A, 5.00-6.25%, due 06/01/2020	\$ 8,640	\$ 1,820	\$ -	\$ 570	\$ 1,250	\$ 605
1999 Refunding, 5.125-5.25%, due 06/01/2024	17,735	8,980	-	735	8,245	775
2009 Series A, 1.80-5.95%, due 06/01/2035	35,015	28,755	-	1,035	27,720	1,080
2011 Refunding, 3-4%, due 06/01/2035	17,225	11,270	-	1,085	10,185	1,125
Add: Unamortized Premium	-	700	-	70	630	-
Energy Tax Credit Bonds						
2007 Series A, 0%, Due 12/15/2021	1,500	500	-	100	400	100
Less: Unamortized Discount	-	(27)	-	(5)	(22)	-
State Water Resources Loans						
2007, 1.02%, due 06/30/2029	9,000	5,400	-	450	4,950	450
2009, 2.6%, due 11/30/2030	8,500	6,452	-	388	6,064	398
2017, 1.8%, due 3/30/2049	29,684	3,181	7,516	4,000	6,697	-
Total Business-type Activities Debt	\$ 127,299	\$ 67,031	\$ 7,516	\$ 8,428	\$ 66,119	\$ 4,533

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 7 – GENERAL LONG-TERM OBLIGATIONS (Continued)

Description of Long-Term Debt Issues

2002B Downtown Parking Improvements Project Certificates of Participation (COPs) – On January 16, 2002, the City issued \$3.6 million of COPs to finance the construction of certain improvements to the non-parking area contained in the City’s Bryant/Florence Garage complex. Due to lower construction costs, \$0.9 million in par bonds were paid off early in January 2005. Principal payments are due annually on March 1 and interest payments semi-annually on March 1 and September 1. Debt service payments are payable from lease revenues received by the Palo Alto Public Improvement Corporation.

As of June 30, 2018, these bonds were refinanced (extinguished) with the issuance of the AA+ rated 2018 (Golf Course Renovation) and refinancing COPs. The present value savings of \$0.3 million included \$0.2 million in reserve funds. The final payment on the defeased 2002B COPs will be in November 2022.

2010 General Obligation Bonds (GO Bonds) – On June 30, 2010, the City issued \$55.3 million of GO Bonds to finance costs for constructing a new Mitchell Park Library and Community Center, and to fund substantial improvements to the Rinconada Library and the Downtown Library. Principal payments are due annually on August 1 and interest payments semi-annually on February 1 and August 1 and are payable from property tax revenues.

On June 28, 2016, the City defeased \$2.3 million of 2010 GO Bonds using funds from bond premiums received at time of issue by depositing the amount in an irrevocable trust account. The trust account assets and the liability for the defeased bonds are not included in the City’s financial statements. The City legally remains the primary obligor on the \$2.3 million of defeased bonds until they are paid on August 1, 2020.

2013A General Obligation Bonds (GO Bonds) – On June 30, 2013, the City issued \$20.7 million of GO Bonds to finance costs for constructing a new Mitchell Park Library and Community Center, as well as making substantial improvements to the Rinconada Library and the Downtown Library. Principal payments are due annually on August 1 and interest payments semi-annually on February 1 and August 1 from 2 percent to 5 percent, and are payable from property tax revenues.

On June 28, 2016, the City defeased \$2.8 million of 2013A GO Bonds using funds remaining at completion of the project by depositing the amount in an irrevocable trust account. The trust account assets and the liability for the defeased bonds are not included in the City’s financial statements. The City legally remains the primary obligor on the \$2.8 million of defeased bonds until they are paid on August 1, 2023.

The City’s 2010 and 2013A GO Bonds are payable from pledged ad valorem property taxes until the final maturity dates of the bonds on August 1, 2040 and August 1, 2041 respectively. For the fiscal year ended June 30, 2018, the City received \$4.3 million in ad valorem property taxes for principal of \$1.5 million and interest of \$2.8 million for both 2010 and 2013A GO Bonds.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 7 – GENERAL LONG-TERM OBLIGATIONS (Continued)

2011 Lease-Purchase Agreement – On August 2, 2011, the City entered into a master lease-purchase agreement with JP Morgan Chase Bank, N.A. to finance redemption of the 1998 Golf Course COPs. The lease is secured by a first priority security interest in twenty-one Fire Department emergency vehicles. Lease proceeds were \$3.2 million. Principal payments are due annually on September 1 and interest payments are due semi-annually on September 1 and March 1 at a rate of 2.49 percent, payable from General Fund revenues.

As of June 30, 2018, there will be \$0.4 million in principal and \$5,302 in interest as the remaining debt service on the bonds with the final payment occurring in September 2018.

2018 Capital Improvement (“Golf Course”) Project and 2002B (“Civic Center Refinancing and Downtown Parking Improvements Project”) Refinancing Certificates of Participation (COPs) – On June 1, 2018, the City issued taxable (Green Bonds) COPs of \$8.4 million for the renovation of the Palo Alto Municipal Golf Course and \$0.6 million to refinance the 2002B COPs. There are two semi-annual debt service payments, consisting of principal payments due annually on November 1 and interest payments due on May 1 and November 1, which are payable solely from and secured by the lease payments to be made by the City’s General Fund to the Public Improvement Corporation pursuant to the Lease Agreement. The leased property is the Palo Alto University Fire Station 1. The 2018 Capital Improvement Project and 2002B refinancing COPs maturity dates and true interest costs are November 2047 and 4.14 percent and November 2022 and 3.11 percent, respectively. The refinancing of the 2002B COPs resulted in present value savings of \$283 thousand and net present savings of \$46 thousand; the higher present value savings was due to utilizing \$0.2 million in the 2002B reserve account cash on hand to reduce the principal amount that was needed to be refinanced. A reserve account is no longer required for a highly rated bond issuer like the City of Palo Alto, so the entire 2018 COPs didn’t have a reserve account.

1995 Utility Revenue Bonds, Series A – The City issued \$8.6 million of Utility Revenue Bonds on February 1, 1995 to finance certain extensions and improvements to the City’s Storm Drainage and Surface Water System. The Bonds are special obligations of the City payable solely from and secured by a pledge of and lien upon the revenues derived by the City from the funds, services and facilities of all Enterprise Funds except the Refuse Services Fund, Fiber Optics Fund and Airport Fund. Principal payments are payable annually on June 1 and interest payments semi-annually on June 1 and December 1. A \$2.9 million at 6.3 percent term bond is due June 1, 2020.

As required by the Indenture, the City established a debt service reserve fund for the Bonds (the “Reserve Account”), with a minimum funding level requirement in the Reserve Account (the “Reserve Requirement”). At the time it issued the Bonds, the City satisfied the Reserve Requirement with a deposit into the Reserve Account of a surety bond (the “Surety Bond”) in the amount of \$685,340 issued by Ambac Indemnity Corporation (renamed to Ambac Assurance Corporation in 1997).

The pledge of future Net Revenues for the above bonds ends upon repayment of the \$1.3 million principal and \$0.1 million interest as the remaining debt service on the bonds, which is scheduled to occur in FY 2020. For FY 2018, Net Revenues, including operating revenues and non-operating interest earnings, amounted to \$289.1 million; operating costs, including operating expenses but not interest, depreciation or amortization, amounted to \$231.3 million. Net Revenues available for debt service amounted to \$57.9 million, which represented coverage of 84.7 times over the \$0.7 million in debt service.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 7 – GENERAL LONG-TERM OBLIGATIONS (Continued)

1999 Utility Revenue and Refunding Bonds – The City issued \$17.7 million of Utility Revenue Bonds on June 1, 1999, to refund the 1990 Utility Revenue Refunding Bonds, Series A and the 1992 Utility Revenue Bonds, Series A, and to finance rehabilitation of two Wastewater Treatment sludge incinerators. The 1990 Utility Revenue Refunding Bonds, Series A and the 1992 Utility Revenue Bonds, Series A, were subsequently retired.

The 1999 Bonds are special obligations of the City payable solely from and secured by a pledge of and lien upon certain net revenues derived by the City’s sewer system and its storm and surface water system (the “Storm Drain System”). As of June 30, 2001, the 1999 Bonds had been allocated to and were repayable from net revenues of the following enterprise funds: Wastewater Collection (10.2 percent), Wastewater Treatment (64.6 percent) and Storm Drainage (25.2 percent). Principal payments are payable annually on June 1 and interest payments semi-annually on June 1 and December 1. A \$3.1 million 5.3 percent term bond and a \$5.1 million 5.3 percent term bond are due June 1, 2021 and 2024, respectively.

As required by the Indenture, the City established a debt service reserve fund for the Bonds (the “Reserve Account”), with a minimum funding level requirement in the Reserve Account (the “Reserve Requirement”). At the time it issued the Bonds, the City satisfied the Reserve Requirement with a deposit into the Reserve Account of a surety bond (the “Surety Bond”) in the amount of \$1,647,300 issued by Ambac Indemnity Corporation (renamed to Ambac Assurance Corporation in 1997).

The pledge of future Net Revenues for the above bonds ends upon repayment of the \$8.2 million principal and \$1.7 million interest as the remaining debt service on the bonds, which is scheduled to occur in FY 2024. For FY 2018, Net Revenues, including operating revenues and non-operating interest earnings, amounted to \$52.4 million; operating costs, including operating expenses but not interest, depreciation or amortization, amounted to \$41.7 million. Net Revenues available for debt service amounted to \$10.7 million, which represents coverage of 8.88 times over the \$1.2 million in debt service.

2007 Electric System Clean Renewable Energy Tax Credit Bonds, Series A – In October 2007, the City issued \$1.5 million of Electric Utility Clean Renewable Energy Tax Credit Bonds (CREBs), 2007 Series A, to finance the City’s photovoltaic solar panel project. The CREBs do not bear interest. In lieu of receiving periodic interest payments, bondholders are allowed annual federal income tax credits in an amount equal to a credit rate for such CREBs multiplied by the outstanding principal amount of the CREBs owned by the bondholders. The CREBs are payable solely from and secured solely by a pledge of the Net Revenues of the Electric system and the other funds pledged under the Indenture.

The pledge of future Electric Fund Net Revenues ends upon repayment of the \$0.4 million remaining debt service on the bonds, which is scheduled to occur in FY 2022. For FY 2018, Net Revenues, including operating revenues and non-operating interest earnings, amounted to \$154.5 million; operating costs, including operating expenses but not interest, depreciation or amortization, amounted to \$128.8 million. Net Revenues available for debt service amounted to \$25.7 million, which represented coverage of 256.4 times over the \$0.1 million in debt service.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 7 – GENERAL LONG-TERM OBLIGATIONS (Continued)

2009 Water Revenue Bonds, Series A – On October 6, 2009, the City issued \$35.0 million of Water Revenue Bonds to finance certain improvements to the City’s water utility system. Principal payments are due annually on June 1, and interest payments are due semi-annually on June 1 and December 1 from 1.80 percent to 5.95 percent. The 2009 Revenue Bonds are secured by net revenues generated by the Water Services Fund. The 2009 Bonds were issued as bonds designated as “Direct Payment Build America Bonds” under the provisions of the American Recovery and Reinvestment Act of 2009 (“Build America Bonds”). The City expects to receive a cash subsidy payment from the United States Treasury equal to 35 percent of the interest payable on the 2009 Bonds. The lien of the 1995 Bonds on the Net Revenues is senior to the lien on Net Revenues securing the 2009 Bonds and the 2011 Bonds. The City received subsidy payments amounting to \$501 thousand, which represents 32.7 percent of the interest payments due on December 1 and June 1.

The pledge of future Net Revenues for the above bonds ends upon repayment of the \$27.7 million principal and \$15.9 million interest as the remaining debt service on the bonds, which is scheduled to occur in FY 2035. For FY 2018, Net Revenues, including operating revenues and non-operating interest earnings, amounted to \$45.2 million; operating costs, including operating expenses but not interest, depreciation or amortization, amounted to \$36.4 million. Net Revenues available for debt service amounted to \$8.8 million, which represented coverage of 3.45 times over the \$2.6 million in debt service.

2011 Utility Revenue Refunding Bonds – On September 8, 2011, the City issued \$17.2 million in Lease Revenue Bonds (2011 Bonds) to refund the outstanding 2002 Series A Utility Revenue Bonds (2002 Bonds) on a current basis. The 2002 Bonds were issued to finance improvement to the City’s municipal water utility system and the natural gas utility system. Principal of the 2011 Bonds is payable annually on June 1, and interest on the 2011 Bonds is payable semi-annually on June 1 and December 1. The 2011 Bonds are secured by net revenues generated by the Water Services and Gas Services Funds.

The pledge of future Net Revenues of the above bonds ends upon repayment of the \$10.2 million principal and \$1.6 million interest as remaining debt service on the bonds, which is scheduled to occur in FY 2035. For FY 2018, Net Revenues, including operating revenues and non-operating interest earnings, amounted to \$82.3 million; operating costs, including operating expenses but not interest, depreciation or amortization, amounted to \$60.7 million. Net Revenues available for debt service amounted to \$21.5 million, which represented coverage of 14.78 times over the \$1.5 million in debt service.

2007 State Water Resources Loan – In October 2007, the City approved a \$9 million loan agreement with State Water Resources Control Board (SWRCB) to finance the City’s Mountain View/Moffett Area reclaimed water pipeline project. Under the terms of the contract, the City has agreed to repay \$9 million to the State in exchange for receiving \$7.5 million in proceeds to be used to fund the Project. The difference of \$1.5 million between the repayment obligation and proceeds represents in-substance interest on the outstanding balance. Principal payments are payable annually on June 30.

Concurrently with the loan, the City entered into various other agreements including a cost sharing arrangement with the City of Mountain View. Pursuant to that agreement, City of Mountain View agreed to finance a portion of the project with a \$6.0 million loan repayable to the City. This loan has been recorded as “Due from other government agencies” in the accompanying financial statements. The balance due to the City at June 30, 2018 was \$3.3 million.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 7 – GENERAL LONG-TERM OBLIGATIONS (Continued)

2009 State Water Resources Loan – In October 2009, the City approved an \$8.5 million loan agreement with SWRCB to finance the City’s Ultraviolet Disinfection project. Principal and interest payments are payable annually on November 30.

2017 State Water Resources Loan - In June 2017, the SWRCB and the City executed agreement for an award up to \$30 million, payable over 30 years to finance the replacement of sewage sludge “bio-solids” incinerators at the City’s Regional Water Quality Control Plant (RWQCP). In September 2017, due to the projected lower project costs, the agreement was amended to a lower loan amount of \$29.7 million. Under the terms of the contract, a portion of the loan amount, \$4.0 million, is federally funded and has been adjusted to reflect the correct long term obligation balance.

The new facility will dewater the bio-solids and allow the material to be loaded onto trucks and taken to a separate facility for further treatment. The RWQCP provides treatment and disposal for wastewater for Palo Alto, Mountain View, Los Altos, Los Altos Hills, East Palo Alto Sanitary District, and Stanford University. Though Palo Alto is the recipient of the loan, the City’s agreement with the partner agencies oblige them to pay their proportionate share of the principal and interest of this loan. Palo Alto’s share of the loan payment is 38.2 percent with the partner agencies paying 61.8 percent.

Debt Service Requirements (in thousands):

Debt service requirements are shown below for all long-term debt.

For the Year Ending June 30	Governmental Activities			Business-Type Activities		
	Principal	Interest	Total	Principal	Interest	Total
2019	\$ 2,101	\$ 3,112	\$ 5,213	\$ 4,533	\$ 2,484	\$ 7,017
2020	1,905	3,068	4,973	5,291	2,651	7,942
2021	1,965	2,991	4,956	5,562	2,523	8,085
2022	2,050	2,909	4,959	5,778	2,359	8,137
2023	2,130	2,826	4,956	5,882	2,158	8,040
2024-2028	12,155	12,624	24,779	21,641	8,063	29,704
2029-2033	15,285	9,405	24,690	12,120	4,861	16,981
2034-2038	18,930	5,677	24,607	4,705	424	5,129
2039-2043	12,665	1,403	14,068	-	-	-
2044-2048	2,350	256	2,606	-	-	-
2048-2052	-	-	-	-	-	-
Total	<u>\$ 71,536</u>	<u>\$ 44,271</u>	<u>\$ 115,807</u>	<u>\$ 65,512</u>	<u>\$ 25,523</u>	<u>\$ 91,035</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 7 – GENERAL LONG-TERM OBLIGATIONS (Continued)

Debt Call Provisions

Long-term debt as of June 30, 2017 is callable on the following terms and conditions:

	<u>Initial Call Date</u>	
<i>Governmental Activities Long-Term Debt</i>		
2010 General Obligation Bonds		
\$6.595 million due 08/01/2032	08/01/31	(2)
\$4.890 million due 08/01/2034	08/01/33	(2)
\$17.725 million due 08/01/2040	08/01/35	(2)
<i>Business-Type Activities Long-Term Debt</i>		
Utility Revenue Bonds		
1999 Refunding	06/01/09	(1)
2011 Refunding	06/01/21	(1)

- (1) Callable in inverse numerical order of maturity at par plus a premium of 2 percent beginning on the initial call date. The call price declines subsequent to the initial date.
- (2) Callable in any order specified by the City at par value plus any accrued interest beginning on the initial call date.

Leasing Arrangements

COPs and Capital Leases are issued for the purpose of financing the construction or acquisition of projects defined in each leasing arrangement. Projects are leased to the City for lease payments which, together with unspent proceeds of the leasing arrangement, will be sufficient to meet the debt service obligations of the leasing arrangement. At the termination of the leasing arrangement, title to the project will pass to the City.

Leasing arrangements are similar to debt in that they allow investors to participate in a share of guaranteed payments made by the City. Because they are similar to debt, the present value of the total payments to be made by the City is recorded as long-term debt. The City's leasing arrangements are included in long-term obligations discussed above.

NOTE 8 – SPECIAL ASSESSMENT DEBT

Special Assessment Debt with no City Commitment

On February 29, 2012, the University Avenue Area Off-Street Parking Assessment District issued Limited Obligation Refunding Improvement Bonds (2012 Bonds), but the City has no legal or moral liability with respect to the payment of this debt, which is secured only by assessments on properties in this District. Therefore, this debt is not included in Governmental Activities long-term debt of the City. At June 30, 2018, the District's outstanding debt amounted to \$22.4 million. The proceeds from the 2012 Bonds, combined with available Assessment Funds, were used to redeem the outstanding University Avenue Area Off-Street Parking Assessment District Series 2001-A and Series 2002-A Bonds. On June 28, 2016, the District defeased \$1.6 million of the 2012 Bonds using funds remaining from completion of the project. The defeased debt will be paid on September 2, 2022.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 9 – LANDFILL POST-CLOSURE MAINTENANCE

The 126 acre Palo Alto Refuse Disposal Site (Palo Alto Landfill) was filled to capacity and stopped accepting waste in July 2011. State and federal laws and regulations require the City to construct a final cover to cap the waste, and to perform certain post-closure maintenance and monitoring activities at the site for a minimum of thirty years after closure. As of November 2015, the Palo Alto Landfill has been fully capped and subsequently converted to a pastoral park (Byxbee Park) that is open to the public. A final post-closure maintenance plan and cost estimate for the thirty year post-closure related activities was approved by state and local regulatory agencies in 2014. This cost estimate is adjusted annually for inflation at a percentage provided by the State. Landfill post-closure liabilities as of June 30, 2018 are \$6.8 million, an increase of \$0.1 million from the previous year. The City is required by state and federal laws and regulations to fund post-closure maintenance activities by pledging future revenue received from Refuse customers through rate fees.

NOTE 10 – NET POSITION AND FUND BALANCES

Net Position

Net Position is the excess of the City's assets and deferred outflows of resources over its liabilities and deferred inflows of resources. Net position is divided into three categories that are described below:

Net Investment in Capital Assets describes the portion of net position, which is represented by current net book value of the City's capital assets, less the outstanding balance of any debt issued to finance these assets.

Restricted describes the portion of net position that is reduced by liabilities related to restricted assets. Generally a liability relates to restricted assets if the asset results from a resource flow that also results in the recognition of a liability or if the liability will be liquidated with the restricted assets reported.

Unrestricted describes the portion of net position which is not restricted as to use.

Fund Balances

As prescribed by GASB Statement No. 54, governmental funds report fund balances in classifications based primarily on the extent to which the City is bound to honor constraints on the specific purposes for which amounts in the funds can be spent. Fund balances for governmental funds are made up of the following:

Nonspendable – This category is comprised of amounts that are: (a) not in spendable form, or (b) legally or contractually required to be maintained intact. The "not in spendable form" criterion includes items that are not expected to be converted to cash, for example: prepaid items. The corpus of the permanent fund is contractually required to be maintained intact.

Restricted – This category is comprised of amounts that can be spent only for the specific purposes stipulated by external resource providers, constitutionally or through enabling legislation. Restrictions may effectively be changed or lifted only with the consent of resource providers.

Committed – This category is comprised of amounts that can only be used for the specific purposes determined by the action that constitutes the most binding constraint (i.e. ordinance) of the City's highest level of decision-making authority, the City Council. Commitments may be changed or lifted only by the City taking the same formal action that imposed the constraint originally.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 10 – NET POSITION AND FUND BALANCES (Continued)

Assigned – This category is comprised of amounts intended to be used by the City for specific purposes that are neither restricted nor committed. Intent is expressed by the City Council or the City Manager, to whom the City Council has delegated the authority to assign amounts to be used for specific purposes.

Unassigned – This category is the residual classification for the General Fund and includes all amounts not contained in the other classifications. Unassigned amounts are technically available for any purpose. Other governmental funds may report negative unassigned fund balance, which occurs when a fund has a residual deficit after allocation of fund balance to the nonspendable, restricted or committed categories.

The fund balances of all governmental funds are presented by the above mentioned categories on the face of the financial statements. In circumstances when an expenditure is made for a purpose for which amounts are available in multiple fund balance categories, fund balance is depleted in the order of restricted, committed, assigned, and unassigned.

The General Fund Budget Stabilization Reserve (BSR) is established by authority of the General Fund Reserve Policy, which is approved by the City Council and included in the City's annual adopted budget. The BSR is maintained in the range of 15 to 20 percent of General Fund expenditures and operating transfers, with a target of 18.5 percent. Any reserve level below 15 percent requires City Council approval. At the discretion of the City Manager, a reserve balance above 18.5 percent may be transferred to the Infrastructure Reserve within the Capital Projects Fund. The purpose of the General Fund BSR is to fund unbudgeted, unanticipated one-time costs. The BSR is not meant to fund ongoing, recurring General Fund expenditures.

As of June 30, 2018 total outstanding encumbrances and reappropriations related to governmental activities were \$7.8 million for the General Fund, \$41.4 million for the Capital Projects Fund, and \$1.0 million for the Special Revenue Funds. General Fund encumbrances are reserved for the following governmental activities: Planning & Community Environment \$1.9 million, Development Services \$0.5 million, Public Works \$0.5 million, Community Services \$0.8 million, Police \$0.9 million, and the remaining City departments \$1.4 million.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 10 – NET POSITION AND FUND BALANCES (Continued)

Enterprise Funds

At June 30, 2018, Enterprise Fund unrestricted net position (in thousands) were as follows:

	Water	Electric	Fiber Optics	Gas	Wastewater Collection	Wastewater Treatment	Refuse	Storm Drainage	Airport	Total
Unrestricted										
Rate stabilization										
Supply	\$ -	\$ 9,011	\$ -	\$ 727	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 9,738
Distribution	4,069	-	26,040	6,363	342	(12,865)	14,748	2,560	(2,926)	38,331
	<u>4,069</u>	<u>9,011</u>	<u>26,040</u>	<u>7,090</u>	<u>342</u>	<u>(12,865)</u>	<u>14,748</u>	<u>2,560</u>	<u>(2,926)</u>	<u>48,069</u>
Operations										
Supply	-	9,537	-	-	-	-	-	-	-	9,537
Distribution	20,927	10,363	-	8,638	7,414	-	-	-	-	47,342
	<u>20,927</u>	<u>19,900</u>	<u>-</u>	<u>8,638</u>	<u>7,414</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>56,879</u>
Emergency plant replacement	-	-	1,000	-	-	1,980	-	-	-	2,980
Electric special projects	-	41,665	-	-	-	-	-	-	-	41,665
Reappropriations	3,614	9,063	1,194	600	506	2,585	-	1,063	-	18,625
Commitments	7,712	8,637	704	8,074	762	18,665	2,165	1,776	588	49,083
Underground loan	-	728	-	-	-	-	-	-	-	728
Notes and loans	-	-	-	-	-	559	-	-	-	559
Landfill corrective action	-	-	-	-	-	-	741	-	-	741
Hydro stabilization reserve	-	11,400	-	-	-	-	-	-	-	11,400
Public benefit program	-	681	-	-	-	-	-	-	-	681
CIP reserve	2,726	880	-	3,820	978	-	-	-	-	8,404
Geng Road reserve	-	-	-	-	-	-	268	-	-	268
GASB 68 Pension reserve	(12,455)	(29,511)	(1,855)	(13,277)	(7,449)	(18,584)	(5,114)	(3,189)	(493)	(91,927)
GASB 75 OPEB reserve	(4,350)	(14,168)	-	(6,235)	(2,384)	(7,340)	(2,653)	(1,158)	(431)	(38,719)
Total	<u>\$ 22,243</u>	<u>\$ 58,286</u>	<u>\$ 27,083</u>	<u>\$ 8,710</u>	<u>\$ 169</u>	<u>\$ (15,000)</u>	<u>\$ 10,155</u>	<u>\$ 1,052</u>	<u>\$ (3,262)</u>	<u>\$ 109,436</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 10 – NET POSITION AND FUND BALANCES (Continued)

The City Council has set aside unrestricted net position for general contingencies, and future capital and debt service expenditures including operating and capital contingencies for unusual or emergency expenditures.

Internal Service Funds

At June 30, 2018, Internal Service Funds unrestricted net position (in thousands) were as follows:

	Vehicle Replacement and Maintenance	Technology	Printing and Mailing Services	General Benefits	Workers' Compensation Insurance Program	General Liabilities Insurance Program	Retiree Health Benefits	Total
Unrestricted net position:								
Commitments	\$ 1,998	\$ 2,030	\$ 61	\$ 302	\$ 40	\$ 19	\$ -	\$ 4,450
Future catastrophic losses	-	-	-	-	1,595	985	-	2,580
Retiree health care	-	-	-	-	-	-	999	999
Capital projects	1,973	2,189	-	-	-	-	-	4,162
GASB68 pension reserve	(2,889)	(9,961)	(306)	-	(43)	-	-	(13,199)
PARS supplemental pension reserve	-	-	-	5,483	-	-	-	5,483
GASB75 OPEB reserve	(1,657)	(3,380)	(148)	-	-	-	-	(5,185)
Available	5,505	18,809	(69)	3,994	-	-	-	28,239
Total	<u>\$ 4,930</u>	<u>\$ 9,687</u>	<u>\$ (462)</u>	<u>\$ 9,779</u>	<u>\$ 1,592</u>	<u>\$ 1,004</u>	<u>\$ 999</u>	<u>\$ 27,529</u>

- **Commitments** represent the portion of net position set aside for open purchase orders.
- **Future catastrophic losses** represent the portion of net position to be used for unforeseen future losses.
- **Retiree health care** represents the portion of net position set aside to defer future costs of retiree health care coverage.
- **Capital projects** represent the portion of net position set aside for adopted capital projects.
- **GASB68 pension reserve** is the portion of net position required to be set aside to meet defined benefit pension obligations.
- **PARS supplemental pension reserve** represents Section 115 irrevocable trust with the PARS to prefund pension obligations.
- **GASB75 OPEB reserve** is the portion of net position required to be set aside to meet OPEB obligations.

Funds with deficits:

At June 30, 2018, the City's Downtown Business Development District special revenue fund had a deficit fund balance of \$32,000. The fund balance will be cured through collection of future special assessments.

At June 30, 2018, the City's Printing and Mailing Services internal service revenue fund had a deficit net position of \$433,000. The deficit is due to the impact from the recording of OPEB items. The deficit is expected to be funded by future internal service charges to other City funds.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 11 – PENSION PLANS

(a) General Information about the Pension Plans

Plan Descriptions - Substantially all permanent City employees are eligible to participate in the City's separate Safety (police and fire) and Miscellaneous (all other) Plans, agent multiple-employer defined benefit pension plans administered by California Public Employees' Retirement System (CalPERS), which acts as a common investment and administrative agent for its participating member employers. Benefits provisions under the Plans are established by State statute and City resolution. CalPERS issues publicly available reports that include a full description of the pension plans including benefits provisions, assumptions and membership information. The reports can be found on the CalPERS website at: <http://www.calpers.ca.gov/index.jsp?bc=/about/forms-pubs/calpers-reports/actuarial-reports/home.xml>

Benefits Provided - CalPERS provides retirement and disability benefits, annual cost of living adjustments and death benefits to Plan members, who must be public employees and beneficiaries. Benefits are based on years of credited service (equal to one year of full-time employment), age at retirement and final compensation. The death benefit is one of the following: the 1959 Survivor Benefit, or the pre-retirement option 2W Death Benefit for local fire members only.

The Plans' provisions and benefits in effect at June 30, 2018, are summarized in the following table. Contribution rates are based on the Actuarial Valuation Report as of June 30, 2015.

	Safety Plan			
	Fire Fighters, Fire Chief Association, Police Officers,	Fire Fighters, Fire Chief Association	Police Officers, Police Management	Fire Fighters, Fire Chief Association, Police Officers,
	Prior to June 8, 2012	On or after June 8, 2012	On or after Dec. 8, 2012	On or after Jan 1, 2013
Hire Date	Prior to June 8, 2012	2012	2012	2013
Benefit formula ¹	3% at 55	3% at 55	3% at 50	2.7% at 57
Benefit vesting schedule	5 years service	5 years service	5 years service	5 years service
Benefit payment	monthly for life	monthly for life	monthly for life	monthly for life
Retirement age	50	55 ¹	55 ¹	57 ¹
Monthly benefit as % of eligible compensatio	3%	3%	3%	2.7%
Actuarially determined contribution rate - EE	9%	9%	9%	11.25%
Actuarially determined contribution rate - ER	49.689%	49.689%	49.689%	49.689%
	Miscellaneous Plan			
	Prior to July 17, 2010	On or after July 17, 2010	On or after Jan 1, 2013	
Hire Date	Prior to July 17, 2010	2010	2013	
Benefit formula	2.7% at 55 ²	2% at 60 ²	2% at 62 ³	
Benefit vesting schedule	5 years service	5 years service	5 years service	
Benefit payments	monthly for life	monthly for life	monthly for life	
Retirement age	55 ²	60 ²	62 ³	
Monthly benefit as % of eligible compensatio	2.70%	2.0% - 2.418%	2%	
Actuarially determined contribution rate - EE	8%	7%	6.25%	
Actuarially determined contribution rate - ER	30.196%	30.196%	30.196%	

¹ Employees can retire at age 50 with reduced benefits of 2.4% - 2.88% if hired before Jan 1, 2013, or 2.0% - 2.6% if hired on or after Jan 1, 2013.

² Employees can retire at age 50 with reduced benefits of 2.0% - 2.56% if hired before July 17, 2010, or 1.092% - 1.874% if hired on or after July 17, 2010.

³ Employees can retire at age 52 with reduced benefits of 1.0% - 1.9%

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 11 – PENSION PLANS (Continued)

Employees Covered – Based on the Actuarial Valuation Report as of June 30, 2017, the following employees were covered by the benefits terms for each Plan:

	Miscellaneous Plan	Safety Plan
Inactive employees or beneficiaries currently receiving benefits	1,098	427
Inactive employees entitled to but not yet receiving benefits	774	103
Active employees	818	172
Total	2,690	702

Contributions –Section 20814(c) of the California Public Employees’ Retirement Law requires that the employer contribution rates for all public employers be determined on an annual basis by the actuary and shall be effective on the July 1 following notice of a change in the rate. Funding contributions for the Plans are determined annually on an actuarial basis as of June 30 by CalPERS. The actuarially determined rate is the estimated amount necessary to finance the costs of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability. The City is required to contribute the difference between the actuarially determined rate and the contribution rate of employees.

Further detail can be found in the Required Supplemental Information Schedule of Contributions.

In April 2017, the City established a Section 115 irrevocable trust with the Public Agency Retirement Services (PARS). The Council approved an initial deposit of \$2.1 million in General Fund proceeds into the General Fund subaccount of the City’s PARS Trust Account. The Trust Account allows more control and flexibility in investment allocations compared to City’s portfolio which is restricted by State regulations to fixed income instruments. As of June 30, 2018, the City reported the account balance of \$5.5 million as restricted cash in the General Benefits, an Internal Service Fund.

(b) Net Pension Liability

The City’s net pension liability for both Plans is measured as the total pension liability, less the plan’s fiduciary net position. Net pension liability is measured as of June 30, 2017 (measurement date), using the Actuarial Valuation Report as of June 30, 2016 rolled forward to June 30, 2017 using standard update procedures. At June 30, 2018, the City reported a net pension liability of \$415.1 million for both plans. A summary of principal assumptions and methods used to determine the net pension liability is as follows:

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 11 – PENSION PLANS (Continued)

Actuarial Assumptions - The total pension liabilities were determined using the following actuarial assumptions in the Accounting Valuation Report:

	Miscellaneous Plan	Safety Plan
Valuation Date	June 30, 2016	June 30, 2016
Measurement Date	June 30, 2017	June 30, 2017
Actuarial Cost Method	Entry Age Normal	Entry Age Normal
Actuarial Assumptions:		
Discount Rate	7.15%	7.15%
Inflation	2.75%	2.75%
Salary Increases	Varies by Entry Age and Service	
Mortality ¹	Derived using CalPERS membership data	
Retirement Age	Probabilities of retirement are based on the 2014 CalPERS Experience Study for the period 1997 to 2011.	

¹ Mortality table used was developed based on CalPERS' specific data. The table includes 20 years of mortality improvements using Society of Actuaries Scale VV. For more details on this table, please refer to the 2014 experience study report.

Further details of the Experience Study can be found on the CalPERS website.

Change in Assumptions – The discount rate reduced from 7.65 percent to 7.15 percent for the June 30, 2017 actuarial valuation.

Discount Rate – The discount rate used to measure the total pension liability was 7.15 percent for each Plan. To determine whether the municipal bond rate should be used in the calculation of a discount rate for each Plan, CalPERS stress tested plans that would most likely result in a discount rate that would be different from the actuarially assumed discount rate. Based on the testing, none of the tested plans ran out of assets. Therefore, the current 7.15 percent discount rate is appropriate and the use of the municipal bond rate calculation is not deemed necessary. The long term expected discount rate of 7.15 percent is applied to all plans in the Public Employees Retirement Fund for the June 30, 2017 measurement date. The stress test results are presented in a detailed report that can be obtained from the CalPERS website under GASB Statement No. 68 section.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 11 – PENSION PLANS (Continued)

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class.

In determining the long-term expected rate of return, CalPERS took into account both short-term and long-term market return expectations as well as the expected pension fund cash flows. Such cash flows were developed assuming that both members and employers will make their required contributions on time and as scheduled in all future years. Using historical returns of all the funds' asset classes, expected compound geometric returns were calculated over the short-term (first ten years) and the long-term (11-60 years) using a building-block approach. Using the expected nominal returns for both short-term and long-term, the present value of benefits was calculated for each fund. The expected rate of return was set by calculating the single equivalent expected return that arrived at the same present value of benefits for cash flows as the one calculated using both short-term and long-term returns. The expected rate of return was then set equivalent to the single equivalent rate calculated above and rounded down to the nearest one quarter of one percent.

The table below reflects the long-term expected real rate of return by asset class for both Miscellaneous and Safety Plans. The rate of return was calculated using the capital market assumptions applied to determine the discount rate and asset allocation. These rates of return are net of administrative expenses.

Asset Class	Current Target Allocation	Real Return Years 1 - 10 ¹	Real Return Years 11+ ²
Global Equity	47.0%	4.90%	5.38%
Global Fixed Income	19.0	0.8	2.27
Inflation Sensitive	6.0	0.6	1.39
Private Equity	12.0	6.6	6.63
Real Estate	11.0	2.80	5.21
Infrastructure and Forestland	3.0	3.90	5.36
Liquidity	2.0	(0.4)	(0.9)

¹ An expected inflation of 2.5% used for this period.

² An expected inflation of 3.0% used for this period.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 11 – PENSION PLANS (Continued)

(c) Changes in the Net Pension Liability

The following table is based on the GASB 68 Accounting Valuation Report and shows the changes in the net pension liability for the Miscellaneous and Safety Plans (in thousands):

	Total Pension Liability	Plan Net Position	Net Pension Liability
Miscellaneous Plan:			
Balances calculated at July 1, 2017	\$ 714,019	\$ 469,782	\$ 244,237
Changes for the year:			
Service cost	14,423	-	14,423
Interest on total pension liability	52,831	-	52,831
Changes in benefit terms	-	-	-
Differences between expected and actual experiences	(6,378)	-	(6,378)
Changes in assumptions	42,239	-	42,239
Contributions from employer	-	20,638	(20,638)
Contributions from employees	-	6,314	(6,314)
Net investment income	-	53,259	(53,259)
Benefit payments, including refunds of employee contributions	(36,405)	(36,405)	-
Administrative expense	-	(694)	694
Other non-investment expenses	-	30	(30)
Net changes	<u>66,710</u>	<u>43,142</u>	<u>23,568</u>
Balances reported at June 30, 2018	<u>780,729</u>	<u>512,924</u>	<u>267,805</u>
Safety Plan:			
Balances calculated at July 1, 2017	\$383,556	\$250,474	\$133,082
Changes for the year:			
Service cost	6,584	-	6,584
Interest on total pension liability	28,272	-	28,272
Change of assumption	22,566	-	22,566
Differences between expected and actual experiences	(2,790)	-	(2,790)
Contributions from employer	-	10,220	(10,220)
Contributions from employees	-	2,475	(2,475)
Net investment income	-	28,112	(28,112)
Benefit payments, including refunds of employee contributions	(22,413)	(22,413)	-
Administrative expense	-	(370)	370
Other non-investment expenses	-	(30)	30
Net changes	<u>32,219</u>	<u>17,994</u>	<u>14,225</u>
Balances reported at June 30, 2018	<u>415,775</u>	<u>268,468</u>	<u>147,307</u>
Total for Miscellaneous & Safety Plans	<u>\$ 1,196,504</u>	<u>\$ 781,392</u>	<u>\$ 415,112</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 11 – PENSION PLANS (Continued)

Sensitivity of the Net Pension Liability to Changes in the Discount Rate - The following table presents the net pension liability of the Plans as of the measurement date, calculated using the discount rate of 7.15 percent, compared to a discount rate that is 1 percentage point lower (6.15 percent) or 1 percentage point higher (8.15 percent). Amounts shown below are in thousands:

	Discount Rate - 1% (6.15%)	Current Discount Rate (7.15%)	Discount Rate + 1% (8.15%)
Miscellaneous Plan:			
Plan's Net Pension Liability/(Asset)	\$ 369,257	\$ 267,805	\$ 183,661
Safety Plan:			
Plan's Net Pension Liability/(Asset)	\$ 201,189	\$ 147,307	\$ 102,861

Plan Fiduciary Net Position – Detailed information about the Plan's fiduciary net position is available in the separately issued CalPERS financial report: Schedule of Changes in Fiduciary Net Position by Rate Plan.

(d) Pension Expenses and Deferred Outflows/Inflows of Resources Related to Pensions

For the year ended June 30, 2018, the City recognized a pension expense of \$38.1 million and \$19.5 million for the Miscellaneous and Safety Plan respectively, for a total of \$57.6 million. At June 30, 2018, the City reported pension related deferred outflows of resources and deferred inflows of resources for the Miscellaneous and Safety Plans from the following sources (in thousands):

	Outflows of Resources	Inflows of Resources
Miscellaneous Plan:		
Pension contributions subsequent to measurement date	\$ 23,225	\$ -
Change of assumptions	27,674	-
Difference between expected and actual experience	235	4,178
Net difference between projected and actual earnings on plan investments	5,949	-
Balance reported at June 30, 2018	<u>57,083</u>	<u>4,178</u>
Safety Plan:		
Pension contributions subsequent to measurement date	11,030	-
Change of assumptions	14,785	744
Difference between expected and actual experience	9	2,366
Net difference between projected and actual earnings on plan investments	3,412	-
Balance reported at June 30, 2018	<u>29,236</u>	<u>\$ 3,110</u>
Total, Miscellaneous & Safety Plans	<u>\$ 86,319</u>	<u>\$ 7,288</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 11 – PENSION PLANS (Continued)

The \$34.2 million reported as deferred outflows of resources relates to contributions paid by the City from July 1, 2017 through June 30, 2018 which is subsequent to the City’s measurement date of June 30, 2017 for both the Miscellaneous and Safety Plans. This amount will be recognized as a reduction of the net pension liability in the year ended June 30, 2019.

The net differences reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in future pension expense as follows (in thousands):

Year Ended June 30,	Miscellaneous Plan	Safety Plan	Total
2019	\$ 12,212	\$ 5,318	\$ 17,530
2020	18,844	10,392	29,236
2021	2,661	1,507	4,168
2022	(4,037)	(2,121)	(6,158)
	<u>\$ 29,680</u>	<u>\$ 15,096</u>	<u>\$ 44,776</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 12 – OTHER POST-EMPLOYMENT BENEFITS (OPEB)

(a) General Information about the OPEB Plan

In addition to providing pension benefits, the City participates in the California Public Employees’ Medical and Health Care Act program to provide certain health care benefits for retired employees. Employees who retire directly from the City are eligible for retiree health benefits if they retire on or after age 50 with 5 years of service and are receiving a monthly pension from CalPERS. Details of benefits to retirees are noted in the following tables:

Unit	Hired Before	Retiree Coverage ¹	Dependent Coverage	Retired on or After	Retiree Contribution
Management & Professional ²	1/1/2004	100%	100%	5/1/2011	Flat rate ⁴
Police Management ²	1/1/2004	100%	100%	6/1/2012	Flat rate ⁴
Fire Fighters ²	1/1/2004	100%	100%	12/1/2011	Flat rate ⁴
Fire Chiefs Association ²	1/1/2004	100%	100%	1/1/2013	Flat rate ⁴
SEIU	1/1/2005	100%	100%	5/1/2011	Flat rate ⁴
Police Officers ³	1/1/2006	100%	100%	4/1/2015	Flat rate ⁴
Utilities Managers & Professional ²	1/1/2004	100%	100%	5/1/2011	10%

¹ 100% of benefits if the employee has five years CalPERS service credit and the employee retired from the City.

² Effective 1/1/2007 plan capped at the second highest CalPERS Bay Area Basic plan premium.

³ Effective 7/1/2014 plan capped at the second highest CalPERS Bay Area Basic plan premium.

⁴ Effective 1/1/2017 City pays \$773 for employee, \$1,544 for employee +1, \$2,008 for family. Effective 1/1/2018 City pays \$804 for employee, \$1,606 for employee +1, \$2,088 for family.

Retiree contributions for units with the following hire dates are determined by Government Code Section 22893, 20 year graduated schedule:

Unit	Hired on or After	Retiree Coverage ¹	Dependent Coverage ²
Management & Professional	1/1/2004	50%-100%	Max. 90%
Police Management	1/1/2004	50%-100%	Max. 90%
Fire Fighters	1/1/2004	50%-100%	Max. 90%
Fire Chiefs Association	1/1/2004	50%-100%	Max. 90%
Utilities Managers & Professional	1/1/2004	50%-100%	Max. 90%
SEIU	1/1/2005	50%-100%	Max. 90%
Police Officers	1/1/2006	50%-100%	Max. 90%

¹ Employees with ten years of CalPERS service, at least five of which are at the City of Palo Alto, receive 50% of the specified employer contribution, with the City portion increasing by 5% for each additional year of service credit.

² The City will contribute an additional 90 percent of the weighted average of the additional premiums required for enrollment of those family members, during the benefit year to which the formula is applied.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 12 – OTHER POST-EMPLOYMENT BENEFITS (OPEB) (Continued)

In FY 2008, the City elected to participate in an irrevocable trust to provide a funding mechanism for retiree health benefits. The Trust, California Employers’ Retirees Benefit Trust (CERBT), is administrated by CalPERS and managed by a separately appointed board, which is not under control of the City Council. This Trust is not considered a component unit of the City.

Employees Covered – Employees covered by the benefit terms as of June 30, 2017 are as follows:

Inactive employees or beneficiaries currently receiving benefits	921
Inactive employees entitled to but not yet receiving benefits	113
Active employees	967
Total	2,001

Contributions – The City’s OPEB funding policy is to prefund these benefits by accumulating assets in the Trust Fund discussed above pursuant to City Council Resolution. For the year ended June 30, 2018, the City’s contributions totaled \$21.3 million.

(b) Net OPEB Liability

The City’s net OPEB liability is measured as the total OPEB liability, less the OPEB plan’s fiduciary net position. The net OPEB liability is measured as of June 30, 2017, using an annual actuarial valuation as of June 30, 2017. A summary of principal assumptions and methods used to determine the net OPEB liability is shown below.

Valuation Date	June 30, 2017
Measurement Date	June 30, 2017
Actuarial Cost Method	Entry-Age, level percentage of payroll
Actuarial Assumptions:	
Discount Rate	6.75%
Inflation	2.75%
Payroll Growth	3.00%
Projected Salary Increase	CalPERS 1997-2015 Experience Study
Investment Rate of Return	6.75% Net of OPEB Plan Investment Expenses, includes Inflation. For medical plan premiums: 6.50% for 2019, decreasing to 4.00% for 2076 and later; For pre-Medicare premiums: 7.50% for 2019, decreasing to 4.00% for 2076 and later
Post Retirement Benefit Increase	CalPERS 1997-2015 Experience Study
Disability, Termination, Retirement	CalPERS 1997-2011 Experience Study, and Society of Actuaries mortality improvement scale MP-17
Mortality	1/2 of Medical Trend, not less than assumed inflation (2.75%)
Increase to Group 3 Flat Dollar Caps	Future retirees: 90%, Based on Plan experience Estimate by 2% load on cash subsidy
Healthcare Participation for Future ACA Excise Tax	

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 12 – OTHER POST-EMPLOYMENT BENEFITS (OPEB) (Continued)

Discount Rate – The discount rate used to measure the total OPEB liability was 6.75%. The projection of cash flows used to determine the discount rate assumed that the City’s contribution will be made equal to the actuarially determined contribution. Based on those assumptions, the OPEB plan’s fiduciary net position was projected to be available to make all projected OPEB payments for current active and inactive employees. Therefore, the long-term expected rate of return on OPEB plan investments applied to all periods of projected benefit payments to determine the total OPEB liability.

The long-term expected rate of return for OPEB plan investments was 6.75%. The asset class target allocation and geometric real rates of return for each major asset class are summarized in the following table.

<u>Asset Class</u>	<u>Current Target Allocation</u>	<u>Expected Real Rate of Return</u>
Global Equity	57.0%	4.82%
Fixed Income	27.0	1.47
TIPS	5.0	1.29
Commodities	3.0	0.84
REITS	8.0	3.76

(a) An expected inflation of 2.50% used for this period

(b) An expected inflation of 3.00% used for this period

(c) Changes in the Net OPEB Liability

The following table shows the changes in the net OPEB liability for the fiscal year ended June 30, 2018.

	Increase (Decrease)		
	Total OPEB Liability	Plan Fiduciary Net Position	Net OPEB Liability
Balance at June 30, 2016	\$ 234,580	\$ 79,843	\$ 154,737
Changes during the measurement period:			
Service cost	6,242	-	6,242
Interest on the total OPEB liability	15,853	-	15,853
Contributions - employer	-	14,739	(14,739)
Investment income	-	8,628	(8,628)
Administrative expenses	-	(44)	44
Benefit payments	(11,916)	(11,916)	-
Net changes	10,179	11,407	(1,228)
Balance at June 30, 2017	\$ 244,759	\$ 91,250	\$ 153,509

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 12 – OTHER POST-EMPLOYMENT BENEFITS (OPEB) (Continued)

Sensitivity of the Net OPEB Liability to Changes in the Discount Rate – The following presents the net OPEB liability of the City as of the measurement date, calculated using the discount rate of 6.75 percent, as well as what the City’s net OPEB liability would be if it were calculated using a discount rate that is 1 percentage-point lower (5.75 percent) or 1 percentage-point higher (7.75 percent) than the current discount rate:

Discount Rate -1% (5.75%)	Current Discount Rate (6.75%)	Discount Rate +1% (7.75%)
\$ 186,295	\$ 153,509	\$ 126,553

Sensitivity of the Net OPEB Liability to Changes in the Healthcare Cost Trend Rate – The following presents the net OPEB liability of the City, as well as what the City’s net OPEB liability would be if it were calculated using healthcare cost trends rates that are 1% lower or 1% higher than the current healthcare cost trend rates.

Healthcare Trend Rate - 1%	Healthcare Trend Current Rate	Healthcare Trend Rate + 1%
\$ 124,392	\$ 153,509	\$ 189,207

OPEB Plan Fiduciary Net Position – Detailed information about the OPEB plan’s fiduciary net position is available in the separately issued CalPERS financial report.

(d) OPEB Expenses and Deferred Outflows/Inflows of Resources Related to OPEB

For the fiscal year ended June 30, 2018, the City recognized an OPEB expense of \$16.0 million for the OPEB plan. At June 30, 2018, the City reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources (dollars in thousands):

	Deferred Outflows of Resources	Deferred Inflows of Resources
OPEB contributions subsequent to measurement date	\$ 21,349	\$ -
Net differences between projected and actual earnings on plan investments	-	(2,516)
Total	\$ 21,349	\$ (2,516)

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 12 – OTHER POST-EMPLOYMENT BENEFITS (OPEB) (Continued)

The \$21.3 million reported as deferred outflows of resources relates to contributions made by the City from July 1, 2017 through June 30, 2018, which is subsequent to the City's measurement date of June 30, 2017. This amount will be recognized as a reduction of the net OPEB liability in the fiscal year ended June 30, 2019. The net difference between projected and actual earnings on plan investments will be recognized in future OPEB expense as follows (dollars in thousands):

<u>Fiscal Year Ending June 30,</u>		
2019	\$	(629)
2020		(629)
2021		(629)
2022		<u>(629)</u>
Total	\$	<u>(2,516)</u>

NOTE 13 – DEFERRED COMPENSATION PLAN

City employees may defer a portion of their compensation under City sponsored Deferred Compensation Plans created in accordance with Internal Revenue Code Section 457. Under these Plans, participants are not taxed on the deferred portion of their compensation until distributed to them. Distributions may be made only at termination, retirement, death or in an emergency as defined by the Plans.

The laws governing deferred compensation plan assets require plan assets to be held by a Trust for the exclusive benefit of plan participants and their beneficiaries. Since the assets held under these plans are not the City's property and are not subject to City control, they have been excluded from these financial statements.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 14 – RISK MANAGEMENT

Coverage

The City provides dental coverage to employees through a City plan, which is administered by a third party service agent. The City is self-insured for dental claims.

The City has a workers' compensation insurance policy with coverage up to the statutory limit set by the State of California. The City retains the risk for the first \$750,000 in losses for each accident and employee under this policy.

The City also has public employee dishonesty insurance with a \$5,000 deductible and coverage up to \$1.0 million per loss. The Interim Director of Administrative Services/CFO and City Manager each have coverage up to \$4.0 million per loss.

The City's property, boiler, and machinery insurance policy has various deductibles and coverage based on the type of property.

The City is a member of the Authority for California Cities Excess Liability (ACCEL), which provides excess general liability insurance coverage, including auto liability, up to \$100 million per occurrence. The City retains the risk for the first \$1.0 million in losses for each occurrence under this policy.

ACCEL was established for the purpose of creating a risk management pool for central California municipalities. ACCEL is governed by a Board of Directors consisting of representatives of its member cities. The board controls the operations of ACCEL, including selection of claims management, general administration and approval of the annual budget.

The City's deposits with ACCEL equal the ratio of the City's payroll to the total payroll of all entities. Actual surpluses or losses are shared according to a formula developed from overall loss costs and spread to member entities on a percentage basis after a retrospective rating.

During the year ended June 30, 2018, the City paid \$0.9 million to ACCEL for current year coverage.

Audited financial statements are available from ACCEL at 100 Pine Street, 11th Floor, San Francisco, California 94110.

Claims Liability

The City provides for the uninsured portion of claims and judgments in the General Liabilities insurance program funds. Claims and judgments, including a provision for claims incurred but not reported, and claim adjustment expenses are recorded when a loss is deemed probable of assertion and the amount of the loss is reasonably determinable. As discussed above, the City has coverage for such claims, but it has retained the risk for the deductible or uninsured portion of these claims.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 14 – RISK MANAGEMENT (Continued)

The City’s liability for uninsured claims is limited to dental, general liability, and workers’ compensation claims, as discussed above. Dental liability is based on a percentage of current year actual expense. General and workers’ compensation liabilities are based on the results of actuarial studies, and include amounts for claims incurred but not reported as follows as of June 30 (in thousands):

	Year Ended June 30	
	2018	2017
Beginning balance	\$ 22,470	\$ 23,379
Claims expense, including claims incurred but not reported (IBNR)	4,705	3,078
Claims paid	(3,427)	(3,987)
Ending balance	\$ 23,748	\$ 22,470
Current portion	\$ 5,835	\$ 5,286

The City has not incurred a claim that has exceeded its insurance coverage limits in any of the last three years, nor have there been any significant reductions in insurance coverage.

NOTE 15 – JOINT VENTURES

General

The City participates in joint ventures through Joint Powers Authorities (JPAs) established under the Joint Exercise of Powers Act of the State of California. As separate legal entities, these JPAs exercise full powers and authorities within the scope of the related Joint Powers Agreement, including the preparation of annual budgets, accountability for all funds, the power to make and execute contracts and the right to sue and be sued. Obligations and liabilities of the JPAs, including the long-term debt in which the City participates in repayment, are not obligations and liabilities of the City, and are not reported on the City’s financial statements.

Each JPA is governed by a board consisting of representatives from each member agency. Each board controls the operations of its respective JPA, including selection of management and approval of operating budgets, independent of any influence by member agencies beyond their representation on the Board.

Northern California Power Agency

The City is a member of Northern California Power Agency (NCPA), a joint powers agency which operates under a joint powers agreement among fifteen public agencies. The purpose of NCPA is to use the combined strength of its members to purchase, generate, sell and interchange electric energy and capacity through the acquisition and use of electrical generation and transmission facilities. Each agency member has agreed to fund a pro rata share of certain assessments by NCPA and enter into take-or-pay power supply contracts with NCPA. While NCPA is governed by its members, none of its obligations are those of its members unless expressly assumed by them.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 15 – JOINT VENTURES (Continued)

During the year ended June 30, 2018, the City incurred expenses totaling \$83.9 million for purchased power and assessments earned by NCPA.

The City's interest in NCPA projects and reserves, as computed by NCPA, was \$7.7 million at June 30, 2018. This amount represents the City's portion of funds, which resulted from the settlement with third parties of issues with financial consequences and reconciliations of several prior years' budgets for programs. It is recognized that all the funds credited to the City are linked to the collection of revenue from the City's ratepayers, or to the settlement of disputes relating to electric power supply and that the money was collected from the City's ratepayers to pay power bills. Additionally, the NCPA Commission identified and approved the funding of specific reserves for working capital, accumulated employees' post-retirement medical benefits, and billed property taxes for the geothermal project. The Commission also identified a number of contingent liabilities that may or may not be realized, the cost of which in most cases is difficult to estimate at this time. One such contingent liability is the steam field depletion, which will require funding to cover debt service and operational costs in excess of the expected value of the electric power. The General Operating Reserve (GOR) is intended to minimize the number and amount of individual reserves needed for each project, protect NCPA's financial condition and maintain its credit worthiness. There are no funds on deposit with NCPA as a reserve against these contingencies identified by NCPA.

Members of NCPA may participate in an individual project of NCPA without obligation for any other project. Member assessments collected for one project may not be used to finance other projects of NCPA without the member's permission.

Geothermal Projects

A purchased power agreement with NCPA obligated the City for 6.2 percent and 6.2 percent, respectively, of the operating costs and debt service of the two NCPA 110-megawatt geothermal steam-powered generating plants, Project Number 2 and Project Number 3.

The City's participation in the Geothermal Project was sold to Turlock Irrigation District in October 1984. Accordingly, the City is liable for payment of outstanding geothermal related debt only in the event that Turlock fails to make specified payments. Total outstanding debt of the NCPA Geothermal Project at June 30, 2018 is \$74.8 million. The City's participation in this project was 6.2 percent, or \$4.6 million.

Calaveras Hydroelectric Project

In July 1981, NCPA agreed with Calaveras County Water District to purchase the output of the North Fork Stanislaus River Hydroelectric Development Project and to finance its construction. Debt service payments to NCPA began in February 1990 when the project was declared substantially complete and power was delivered to the participants. Under its power purchase agreement with NCPA, the City is obligated to pay 22.9 percent of this Project's debt service and operating costs. At June 30, 2018, the book value of this Project's plant, equipment and other assets was \$378 million, while its long-term debt totaled \$309 million and other liabilities totaled \$62.3 million. The City's share of the Project's long-term debt amounted to \$75.9 million at that date.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 15 – JOINT VENTURES (Continued)

Geothermal Public Power Line

In 1983, NCPA, the Sacramento Municipal Utility District, the City of Santa Clara and the Modesto Irrigation District (Joint Owners) initiated studies for a Geothermal Public Power Line (GPPL), which would carry power generated at several existing and planned geothermal plants in The Geysers area to a location where the Joint Owners could receive it for transmission to their load centers. NCPA has an 18.5 percent share of this Project and the City has an 11.1 percent participation in NCPA's share. In 1989, the development of the proposed Geothermal Public Power Line was discontinued because NCPA was able to contract for sufficient transmission capacity to meet its needs in The Geysers.

However, because the project financing provided funding for an ownership interest in a Pacific Gas & Electric (PG&E) transmission line, a central dispatch facility and a performance bond pursuant to the Interconnection Agreement with PG&E, as well as an ownership interest in the proposed GPPL, NCPA issued \$16 million in long-term, fixed-rate revenue bonds in November 1989 to defease the remaining variable rate refunding bonds used to refinance this project. The City is obligated to pay its 11.1 percent share of the related debt service, but debt service costs are covered through NCPA billing mechanisms that allocate the costs to members based on use of the facilities and services.

At June 30, 2018, the book value of this Project's plant, equipment and other assets was zero, and its long-term debt totaled zero.

NCPA's financial statements can be obtained from NCPA, 180 Cirby Way, Roseville, CA 95678.

Transmission Agency of Northern California (TANC)

The City is a member of a joint powers agreement with 14 other entities in Transmission Agency of Northern California (TANC). TANC's purpose is to provide electrical transmission or other facilities for the use of its members. While governed by its members, none of TANC's obligations are those of its members unless expressly assumed by them. The City was obligated to pay 4 percent of TANC's debt-service and operating costs. However, a Resolution was approved authorizing the execution of a Long-Term Layoff Agreement (LTLA) between the Cities of Palo Alto and Roseville. These two agencies desired to "layoff" their entitlement rights to the California-Oregon Transmission Project (COTP) (and Roseville's South of Tesla entitlement rights) for a period of 15 years to those acquiring members (Sacramento Municipal Utility District, Turlock Irrigation District, and Modesto Irrigation District). The effective date of this Agreement was February 1, 2009. As a result, the City is not obligated to pay TANC's debt-service and operating costs starting February 1, 2009, for a period of fifteen years.

TANC's financial statements can be obtained from TANC, P.O. Box 15129, Sacramento, CA 95851.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 15 – JOINT VENTURES (Continued)

Bay Area Water Supply and Conservation Agency (BAWSCA)

The City is a member of a regional water district with 26 other entities, the Bay Area Water Supply and Conservation Agency (BAWSCA). BAWSCA was created on May 27, 2003 to represent the interests of 24 cities and water districts and two private utilities in Alameda, Santa Clara and San Mateo counties that purchase water on a wholesale basis from the San Francisco regional water system. It has the power to issue debt and plan, finance, construct, and operate water supply, transmission, reclamation, and conservation projects on behalf of its members.

In 2013 the City participated in a debt issuance by BAWSCA. The debt was issued to repay certain long-term costs associated with the San Francisco Public Utilities Commission (SFPUC) water supply contract. During the fiscal year, the City paid its share of the annual debt service of \$1.9 million, which will vary based on annual water purchases of the City compared to other BAWSCA agencies.

BAWSCA’s financial statements can be obtained from BAWSCA, 155 Bovet Road, Suite 650, San Mateo, California 94402.

NOTE 16 – COMMITMENTS AND CONTINGENCIES

Palo Alto Unified School District – The City leases 27 acres of the former Cubberley School site and twelve extended day care sites from Palo Alto Unified School District (PAUSD). The lease includes a mechanism for a joint planning process between the City and PAUSD to develop a long-term master plan for the Cubberley site. The City will pay \$1.86 million annually into a separate fund to be used for repairing, renovating and/or improving the infrastructure at the Cubberley site. The previous lease term expired on December 31, 2014, and the City and PAUSD reached an agreement to extend the lease agreement for an additional five (5) years, with a new expiration date of 12/31/2019. The City and PAUSD also agreed to distribute gains or losses of revenue that resulted from the Foothill College departure from Cubberley. The City’s rent and infrastructure payment for the facilities is \$7.3 million per year plus insurance, repairs and maintenance. Lease expenditures for the year ended June 30, 2018 amounted to \$7.6 million. Future minimum annual lease and infrastructure payments are as follows (in thousands):

Year Ending	Payment
June 30	<u> </u>
2019	\$ 7,653
2020	<u>3,922</u>
	<u>\$ 11,575</u>

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 16 – COMMITMENTS AND CONTINGENCIES (Continued)

GreenWaste of Palo Alto – GreenWaste of Palo Alto is the City’s contractor for waste collection, transportation, and processing services. The agreement expires June 30, 2021. The base compensation for GreenWaste is adjusted annually based on CPI indicators stipulated in the contract. In FY 2018 payments to GreenWaste were \$9.3 million.

City of Palo Alto Regional Water Quality Control Plant – The cities of Palo Alto, Mountain View and Los Altos (the Partners) participate jointly in the cost of maintaining and operating the City of Palo Alto Regional Water Quality Control Plant and related system (the Plant). The City is the owner and administrator of the Plant, which provides the transmission, treatment and disposal of sewage for the Partners. The cities of Mountain View and Los Altos are entitled to use a portion of the capacity of the Plant for a specified period of time. Each partner has the right to rent unused capacity from/to the other partners. The expenses of operations and maintenance are paid quarterly by each partner based on its pro rata share of treatment costs. Additionally, joint system revenues are shared by the partners in the same ratio as expenses are paid. The amended agreement has a term of fifty years beginning from the original signing in October 1968, but may be terminated by any partner upon ten years’ notice to the other partners. All sewage treatment property, plant and equipment are included in the Wastewater Treatment Enterprise Fund’s capital assets balance. If the City initiates the termination of the contracts, it is required to pay the other partners their unamortized contribution towards the capital assets.

Solid Waste Materials Recovery and Transfer Station (SMaRT Station) – On June 9, 1992, the City, along with the City of Mountain View, signed a Memorandum of Understanding (MOU) with the City of Sunnyvale (Sunnyvale) to participate in the construction and operation of the SMaRT Station, which recovers recyclable materials from the municipal solid waste delivered from participating cities. Per the MOU, the City has a capacity share of 21.3 percent of this facility and reimburses its proportionate capacity share of design, construction and operation costs to Sunnyvale.

In FY 2008, the members agreed to finance an Equipment Replacement Project from existing reserves and proceeds from the Solid Waste Revenue Bond, Series 2007. The City has committed to repay 27.8 percent of the remaining debt service on the Bonds. The City’s portion of the Bonds amounts to \$0.6 million as of June 30, 2018. During the year ended June 30, 2018, the City paid \$0.2 million as its portion of current debt service.

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 16 – COMMITMENTS AND CONTINGENCIES (Continued)

UTILITIES ENERGY RESOURCE MANAGEMENT

Electric Power Supply Purchase Agreements – The City has numerous power purchase agreements with power producers to purchase capacity and energy to supply a portion of its load requirements. As of June 30, 2018, the approximate minimum obligations for the contracts, assuming the energy is delivered over the next five years, are as follows:

Fiscal Year	Projected Obligation
2019	\$65.6 million
2020	\$63.0 million
2021	\$62.6 million
2022	\$65.2 million
2023	\$63.9 million

Contractual Commitments beyond 2022 (Electricity) – Several of the City’s purchase power and transmission contracts extend beyond the five-year summary presented above. These contracts expire between 2026 and 2051 and provide for power under various terms and conditions. The City estimates that its annual minimum commitments under the contracts, assuming the energy is delivered, ranges between \$67.1 million in 2023 and \$51.7 million in 2034. The City’s largest single purchase power source is the Western Base Resource contract, whereby the City receives 12.31 percent of the amount of energy made available by Western, after meeting Central Valley Project use requirements, in any given year at a 12.31 percent share of their revenue requirement. The Western contract expires on December 31, 2024. The City expects to have the option to extend the Western contract for an additional 30-year period beyond 2024, although likely at a slightly lower share of the total energy output and revenue requirement.

Gas Accord V – The City is a party to the Gas Accord V, a natural gas transportation contract between Pacific Gas and Electric Company (PG&E) and its gas transportation customers. New rates are determined through a proceeding at the California Public Utilities Commission. A final CPUC decision on Pacific Gas and Electric Company’s (PG&E) Gas Transmission and Storage Case was issued June 2016. Although several appeals are underway, Palo Alto’s gas transmission rates increased by 230% and Palo Alto’s local transmission rates increased by \$2 million on August 1, 2016. A processing is underway at the California Public Utilities Commission which will determine new PG&E gas transportation rates to be implemented in 2019.

San Francisco Public Utilities Commission – The City purchases water to deliver to the customers of its water utility from the San Francisco Public Utilities Commission (SFPUC) under a contract terminating in 2034. The City’s wholesale water rate under this contract is determined by a ratemaking process under the authority of the SFPUC, with contractual limitations on the types of costs that may be allocated to wholesale water purchasers like the City. The City is prohibited from purchasing from other water suppliers under this contract, though it is not prohibited from using ground water. The City’s cost of water under this contract is projected to increase by 10% by 2021 as the SFPUC has nearly completed an upgrade to its regional water system facilities under its Water System Improvement Program (WSIP).

CITY OF PALO ALTO
Notes to the Basic Financial Statements
For the Year Ended June 30, 2018

NOTE 16 – COMMITMENTS AND CONTINGENCIES (Continued)

Litigation

The City is subject to litigation arising in the normal course of business. In the opinion of the City Attorney, there is no pending litigation, claims or assessments that are likely to have a materially adverse effect on the City's financial condition.

A class action lawsuit for refund of telephone users tax was filed against the City in August 2015. At this time, the City Attorney is of the opinion that a potential loss is neither probable nor can it be reasonably estimated.

A class action lawsuit for refund of allegedly illegal charges to gas and electrical customers was filed against the City in October 2016. At this time, the City Attorney is of the opinion that a potential loss is neither probable nor can it be reasonably estimated.

Grant Programs

The City participates in Federal and State grant programs. These programs have been audited by the City's independent auditors in accordance with the provisions of the Federal Single Audit Act amendments of 1996 and applicable State requirements. No costs were questioned as a result of these audits; however, these programs are still subject to further examination by the grantors and the amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time. The City expects such amounts, if any, to be immaterial.

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CITY OF PALO ALTO
Required Supplementary Information (Unaudited)
Last 4 Fiscal Years*

I. SCHEDULE OF CHANGES IN NET PENSION LIABILITY AND RELATED RATIOS – MISCELLANEOUS PLAN
(In thousands)

Fiscal year	<u>2017-18</u>	<u>2016-17</u>	<u>2015-16</u>	<u>2014-15</u>
Measurement Period	2016-17	2015-16	2014-15	2013-14
Total pension liability				
Service cost	\$ 14,423	\$ 12,582	\$ 12,183	\$ 12,442
Interest	52,831	51,531	49,345	46,963
Changes of assumptions	42,239	-	(11,552)	-
Difference between expected and actual experience	(6,378)	757	3,507	-
Benefit payments, including refunds of employee contributions	(36,405)	(34,825)	(32,980)	(31,781)
Net change in total pension liability	<u>66,710</u>	<u>30,045</u>	<u>20,503</u>	<u>27,624</u>
Total pension liability - beginning	<u>714,019</u>	<u>683,974</u>	<u>663,471</u>	<u>635,847</u>
Total pension liability - ending (a)	<u>\$ 780,729</u>	<u>\$ 714,019</u>	<u>\$ 683,974</u>	<u>\$ 663,471</u>
Plan fiduciary net position				
Contributions - employer	\$ 20,638	\$ 18,840	\$ 18,610	\$ 17,400
Contributions - employee	6,314	5,812	5,730	6,345
Net investment income	53,259	2,464	10,597	70,989
Benefit payments, including refunds of employee contributions	(36,405)	(34,825)	(32,980)	(31,781)
Administrative expense	(694)	(291)	(538)	-
Other non-investment expenses	30	-	-	-
Net change in fiduciary net position	<u>43,142</u>	<u>(8,000)</u>	<u>1,419</u>	<u>62,953</u>
Plan fiduciary net position - beginning	<u>469,782</u>	<u>477,782</u>	<u>476,363</u>	<u>413,410</u>
Plan fiduciary net position - ending (b)	<u>\$ 512,924</u>	<u>\$ 469,782</u>	<u>\$ 477,782</u>	<u>\$ 476,363</u>
Plan net pension liability/(asset) - Ending (a) - (b)	<u>\$ 267,805</u>	<u>\$ 244,237</u>	<u>\$ 206,192</u>	<u>\$ 187,108</u>
Plan fiduciary net position as a percentage of total pension liability	<u>65.70%</u>	<u>65.79%</u>	<u>69.85%</u>	<u>71.80%</u>
Covered payroll	<u>\$ 77,606</u>	<u>\$ 73,722</u>	<u>\$ 69,837</u>	<u>\$ 66,373</u>
Plan net pension liability/(asset) as a percentage of covered employee pay	<u>345.08%</u>	<u>331.29%</u>	<u>295.25%</u>	<u>281.90%</u>

Notes to Schedule:

Benefit changes - The figures above do not include any liability that may have resulted from plan changes which occurred after the June 30, 2015 valuation date. This applies for voluntary benefit changes as well as any offers of two years additional service credit (Golden Handshake).

Changes in assumptions - The discount rate was changed from 7.5 percent (net of administrative expense) in 2015 to 7.65 percent in 2016. In 2017, the accounting discount rate reduced from 7.65% to 7.15%

* Fiscal year ended June 30, 2015 was the first year of implementation of GASB Statement No. 68, therefore only four years of information is shown.

CITY OF PALO ALTO
Required Supplementary Information (Unaudited)
Last 5 Fiscal Years*

II. SCHEDULE OF PENSION CONTRIBUTIONS— MISCELLANEOUS PLAN
(In thousands)

Fiscal Year	2017-18	2016-17	2015-16	2014-15	2013-14
Contractually required contribution (actuarially determined)	\$ 23,225	\$ 20,638	\$ 18,840	\$ 18,610	\$ 17,400
Actual contribution	(23,225)	(20,638)	(18,840)	(18,611)	(17,400)
Contribution deficiency/(excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (1)</u>	<u>\$ -</u>
Covered payroll	\$ 82,228	\$ 77,606	\$ 73,722	\$ 69,837	\$ 66,373
Contributions as percentage of covered-employee payroll	28.24%	26.59%	25.56%	26.65%	26.22%

Notes to Schedule:

The actuarial methods and assumptions used to set the actuarially determined contributions for fiscal year 2018 contribution rates are as follows:

ADC for fiscal year	June 30, 2018
Actuarial valuation date	June 30, 2015
Actuarial cost method	Entry-Age Normal Cost Method
Asset valuation method	Actuarial value of assets
Inflation	2.75%
Salary increases	Varies by entry age and services
Payroll growth	3.00%
Investment rate of return	7.50%, net of pension plan investment and administrative expenses, includes inflation.
Retirement age	The probabilities of retirement are based on the 2014 CalPERS Experience Study for the period 1997 to 2011.
Mortality	The probabilities of mortality are based on the 2014 CalPERS Experience Study for the period from 1997 to 2011. Pre-retirement and Post-retirement mortality rates include 20 years of projected mortality improvement using Scale BB published by the Society of Actuaries.

* Fiscal year ended June 30, 2015 was the first year of implementation of GASB Statement No. 68, therefore only five years of information is shown.

CITY OF PALO ALTO
Required Supplementary Information (Unaudited)
Last 4 Fiscal Years*

III. SCHEDULE OF CHANGES IN NET PENSION LIABILITY AND RELATED RATIOS – SAFETY PLAN
(In thousands)

Fiscal year	<u>2017-18</u>	<u>2016-17</u>	<u>2015-16</u>	<u>2014-15</u>
Measurement Period	2016-17	2015-16	2014-15	2013-14
Total pension liability				
Service cost	\$ 6,584	\$ 5,916	\$ 5,959	\$ 6,221
Interest	28,272	27,816	27,047	26,113
Changes of assumptions	22,566	-	(6,327)	-
Difference between expected and actual experience	(2,790)	(1,516)	75	-
Benefit payments, including refunds of employee contributions	(22,413)	(21,669)	(21,148)	(19,985)
Net change in total pension liability	32,219	10,547	5,606	12,349
Total pension liability - beginning	383,556	373,009	367,403	355,054
Total pension liability - ending (a)	\$ 415,775	\$ 383,556	\$ 373,009	\$ 367,403
Plan fiduciary net position				
Contributions - employer	\$ 10,220	\$ 9,403	\$ 8,617	\$ 7,616
Contributions - employee	2,475	2,059	2,047	2,762
Net investment income	28,112	1,259	5,774	40,033
Benefit payments, including refunds of employee contributions	(22,413)	(21,669)	(21,148)	(19,985)
Administrative expense	(370)	(157)	(290)	-
Other non-investment expenses	(30)	-	-	-
Net change in fiduciary net position	17,994	(9,105)	(5,000)	30,426
Plan fiduciary net position - beginning	250,474	259,579	264,579	234,153
Plan fiduciary net position - ending (b)	\$ 268,468	\$ 250,474	\$ 259,579	\$ 264,579
Plan net pension liability/(asset) - Ending (a) - (b)	\$ 147,307	\$ 133,082	\$ 113,430	\$ 102,824
Plan fiduciary net position as a percentage of total pension liability	64.57%	65.30%	69.59%	72.01%
Covered payroll	\$ 21,906	\$ 21,822	\$ 21,912	\$ 21,896
Plan net pension liability/(asset) as a percentage of covered employee	672.45%	609.85%	517.66%	469.60%

Notes to Schedule:

Benefit changes - The figures above do not include any liability that may have resulted from plan changes which occurred after the June 30, 2015 valuation date. This applies for voluntary benefit changes as well as any offers of two years additional service credit (Golden Handshake).

Changes in assumptions - The discount rate was changed from 7.5 percent (net of administrative expense) in 2015 to 7.65 percent in 2016. In 2017, the accounting discount rate reduced from 7.65% to 7.15%.

* Fiscal year ended June 30, 2015 was the first year of implementation of GASB Statement No. 68, therefore only four years of information is shown.

CITY OF PALO ALTO
Required Supplementary Information (Unaudited)
Last 5 Fiscal Years*

IV. SCHEDULE OF PENSION CONTRIBUTIONS – SAFETY PLAN
(In thousands)

Fiscal Year	2017-18	2016-17	2015-16	2014-15	2013-14
Contractually required contribution (actuarially determined)	\$ 11,030	\$ 10,220	\$ 9,403	\$ 8,617	\$ 7,616
Actual contribution	(11,030)	(10,220)	(9,403)	(8,617)	(7,616)
Contribution deficiency/(excess)	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Covered payroll	\$ 24,477	\$ 21,906	\$ 21,822	\$ 21,912	\$ 21,896
Contributions as percentage of covered-employee payroll	45.06%	46.65%	43.09%	39.33%	34.78%

Notes to Schedule:

The actuarial methods and assumptions used to set the actuarially determined contributions for fiscal year 2018 contribution rates are as follows:

ADC for fiscal year	June 30, 2018
Actuarial valuation date	June 30, 2015
Actuarial cost method	Entry-Age Normal Cost Method
Asset valuation method	Actuarial value of assets
Inflation	2.75%
Salary increases	Varies by entry age and services
Payroll growth	3.00%
Investment rate of return	7.50%, net of pension plan investment and administrative expenses, includes inflation.
Retirement age	The probabilities of retirement are based on the 2014 CalPERS Experience Study for the period 1997 to 2011.
Mortality	The probabilities of mortality are based on the 2014 CalPERS Experience Study for the period from 1997 to 2011. Pre-retirement and Post-retirement mortality rates include 20 years of projected mortality improvement using Scale BB published by the Society of Actuaries.

* Fiscal year ended June 30, 2015 was the first year of implementation of GASB Statement No. 68, therefore only five years of information is shown.

CITY OF PALO ALTO
Required Supplementary Information (Unaudited)
Last 5 Fiscal Years*

V. SCHEDULE OF CHANGES IN NET OPEB LIABILITY AND RELATED RATIOS
(In thousands)

Fiscal year	<u>2017-18</u>
Measurement Period	2016-17
Total OPEB liability	
Service cost	\$ 6,242
Interest	15,853
Benefit payments, including refunds of employee contributions	<u>(11,916)</u>
Net change in total OPEB liability	10,179
Total OPEB liability - beginning	<u>234,580</u>
Total OPEB liability - ending (a)	<u>\$ 244,759</u>
Plan fiduciary net position	
Contributions - employer	\$ 14,739
Net investment income	8,628
Benefit payments, including refunds of employee contributions	(11,916)
Administrative expense	<u>(44)</u>
Net change in fiduciary net position	11,407
Plan fiduciary net position - beginning	<u>79,843</u>
Plan fiduciary net position - ending (b)	<u>\$ 91,250</u>
Plan net OPEB liability/(asset) - Ending (a) - (b)	<u>\$ 153,509</u>
Plan fiduciary net position as a percentage of total OPEB liability	37.28%
Covered payroll	\$ 118,774
Plan net OPEB liability/(asset) as a percentage of covered employee payroll	129.24%

Notes to Schedule:

Benefit changes - The figures above do not include any liability that may have resulted which occurred after the measurement dates.

Changes in assumptions - There were no changes in assumptions

* Fiscal year ended June 30, 2018 was the first year of implementation of GASB Statement No. 75, therefore only one year of information is shown. The measurement date for GASB Statement No. 75 purposes is June 30, 2017.

CITY OF PALO ALTO
Required Supplementary Information (Unaudited)
Last 5 Fiscal Years*

VI. SCHEDULE OF EMPLOYER OPEB CONTRIBUTIONS
(In thousands)

Fiscal Year	<u>2017-18</u>	<u>2016-17</u>
Contractually required contribution (actuarially determined)	\$ 16,938	\$ 16,365
Actual contribution	<u>(21,349)</u>	<u>(14,739)</u>
Contribution deficiency/(excess)	<u>\$ (4,411)</u>	<u>\$ 1,626</u>
Covered payroll	\$ 119,090	\$ 118,774
Contributions as percentage of covered-employee payroll	17.93%	12.41%

Notes to Schedule:

The actuarial methods and assumptions used to set the actuarially determined contributions for fiscal year 2018 contribution rates are as follows:

ADC for fiscal year	June 30, 2018
Actuarial valuation date	June 30, 2015
Actuarial cost method	Entry-Age, level percentage of payroll
Amortization method	Level percent of payroll over closed 27 year period.
Asset valuation method	Market value, no smoothing
Inflation	3.00%
Payroll growth	3.25%
Investment rate of return	7.25%, net of pension plan investment and administrative expenses, includes inflation.
Other Assumptions	Same as for determining total OPEB liability, except for rates of retirement/mortality/termination, medical trend, medical plan at retirement, waived retiree re-election, and assumed spouse coverage percent.

CITY OF PALO ALTO
Non-major Governmental Funds
Combining Balance Sheet
June 30, 2018
(Amounts in thousands)

	Special Revenue Funds	Debt Service Funds	Permanent Fund	Total Other Governmental Funds
ASSETS:				
Cash and investments:				
Available for operations	\$ 65,621	\$ 3,545	\$ 1,489	\$ 70,655
Receivables, net:				
Accounts	394	5	-	399
Interest	402	21	9	432
Notes	33,816	-	-	33,816
Total assets	<u>\$ 100,233</u>	<u>\$ 3,571</u>	<u>\$ 1,498</u>	<u>\$ 105,302</u>
LIABILITIES AND FUND BALANCES:				
Liabilities:				
Accounts payable and accruals	\$ 358	\$ -	\$ -	\$ 358
Accrued salaries and benefits	16	-	-	16
Interfund payables and advances	13	-	-	13
Total liabilities	<u>387</u>	<u>-</u>	<u>-</u>	<u>387</u>
Fund balances:				
Nonspendable				
Eyerly family	-	-	1,498	1,498
Restricted				
Transportation mitigation	10,511	-	-	10,511
Federal revenue	5,080	-	-	5,080
Street improvement	562	-	-	562
Local law enforcement	322	-	-	322
Debt service	-	3,571	-	3,571
Public benefit	19,633	-	-	19,633
Committed				
Developer impact fee	13,764	-	-	13,764
Housing In-Lieu	44,863	-	-	44,863
Special districts	5,143	-	-	5,143
Unassigned				
Downtown business	(32)	-	-	(32)
Total fund balances	<u>99,846</u>	<u>3,571</u>	<u>1,498</u>	<u>104,915</u>
Total liabilities and fund balances	<u>\$ 100,233</u>	<u>\$ 3,571</u>	<u>\$ 1,498</u>	<u>\$ 105,302</u>

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CITY OF PALO ALTO
Non-major Governmental Funds
Combining Statement of Revenues, Expenditures and Changes in Fund Balances
For the Year Ended June 30, 2018
(Amounts in thousands)

	Special Revenue Funds	Debt Service Funds	Permanent Fund	Total Other Governmental Funds
REVENUES:				
Property tax	\$ -	\$ 4,331	\$ -	\$ 4,331
Special assessments	72	-	-	72
Other taxes and fines	2,116	-	-	2,116
Contributions	11,733	-	-	11,733
Charges for services	11	-	-	11
Intergovernmental:				
Community Development Block Grants	363	-	-	363
State of California	229	-	-	229
Permits and licenses				
University Avenue Parking	3,088	-	-	3,088
California Avenue Parking	556	-	-	556
Other permits and licenses	582	-	-	582
Investment earnings	224	(28)	2	198
Rental income	6	-	-	6
Other:				
Housing In-Lieu - residential	1,145	-	-	1,145
Other fees	4,015	-	-	4,015
Total revenues	<u>24,140</u>	<u>4,303</u>	<u>2</u>	<u>28,445</u>
EXPENDITURES:				
Current:				
Administrative Services	226	-	-	226
Public Works	857	-	-	857
Planning and Community Environment	2,020	-	-	2,020
Police	68	-	-	68
Community Services	2,709	-	-	2,709
Non-Departmental	1,589	14	3	1,606
Debt service:				
Principal retirement	-	2,545	-	2,545
Interest and fiscal charges	-	2,940	-	2,940
Total expenditures	<u>7,469</u>	<u>5,499</u>	<u>3</u>	<u>12,971</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>16,671</u>	<u>(1,196)</u>	<u>(1)</u>	<u>15,474</u>
OTHER FINANCING SOURCES (USES):				
Issuance of debt	-	595	-	595
Transfers in	495	233	-	728
Transfers out	(11,434)	-	-	(11,434)
Total other financing sources (uses)	<u>(10,939)</u>	<u>828</u>	<u>-</u>	<u>(10,111)</u>
Change in fund balances	5,732	(368)	(1)	5,363
FUND BALANCES, BEGINNING OF YEAR	<u>94,114</u>	<u>3,939</u>	<u>1,499</u>	<u>99,552</u>
FUND BALANCES, END OF YEAR	<u>\$ 99,846</u>	<u>\$ 3,571</u>	<u>\$ 1,498</u>	<u>\$ 104,915</u>

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NON-MAJOR GOVERNMENTAL FUNDS

SPECIAL REVENUE FUNDS

Street Improvement

This fund accounts for revenues received from state gas tax. Allocations must be spent on the construction and maintenance of the road network system of the City.

Federal Revenue

This fund accounts for grant funds received under the Community Development Act of 1974 and HOME Investment Grant Programs, for activities approved and subject to federal regulations.

Housing In-Lieu

This fund accounts for revenues from commercial and residential developers to provide housing under the City's Below Market Rate program.

Special Districts

This fund accounts for revenues from parking permits and for maintenance of various parking lots within the City's parking districts.

Transportation Mitigation

This fund accounts for revenues from fees or contributions required for transportation mitigation issues encountered as a result of City development.

Local Law Enforcement

This fund accounts for revenues received in support of City's law enforcement program.

Asset Seizure

This fund accounts for seized property and funds associated with drug trafficking. Under California Assembly Bill No. 4162, the monies are released to the City for specific expenditures related to law enforcement activities.

Developer Impact Fee

This fund accounts for fees imposed on new developments to be used for parks, community centers and libraries.

Downtown Business Development District

The Downtown Business Development District Fund was established to account for the activities of the Palo Alto Downtown Business Development District, which was established to enhance the viability of the downtown business district.

Public Benefit

This fund accounts for the activities of the Stanford University Medical Center (SUMC) Development Agreement (DA) whereby SUMC will enhance and expand their facilities and the City will grant SUMC the right to develop the facilities in accordance with the DA.

CITY OF PALO ALTO
Non-major Special Revenue Funds
Combining Balance Sheet
June 30, 2018
(Amounts in thousands)

	<u>Street Improvement</u>	<u>Federal Revenue</u>	<u>Housing In-Lieu</u>	<u>Special Districts</u>
ASSETS:				
Cash and investments:				
Available for operations	\$ 412	\$ 219	\$ 15,809	\$ 5,292
Receivables:				
Accounts	146	137	-	9
Interest	4	-	129	28
Notes	-	4,831	28,985	-
Total assets	<u>\$ 562</u>	<u>\$ 5,187</u>	<u>\$ 44,923</u>	<u>\$ 5,329</u>
LIABILITIES AND FUND BALANCES:				
Liabilities:				
Accounts payable and accruals	\$ -	\$ 106	\$ 60	\$ 173
Accrued salaries and benefits	-	1	-	13
Interfund payables and advances	-	-	-	-
Total liabilities	<u>-</u>	<u>107</u>	<u>60</u>	<u>186</u>
Fund balances:				
Restricted				
Transportation mitigation	-	-	-	-
Federal revenue	-	5,080	-	-
Street improvement	562	-	-	-
Local law enforcement	-	-	-	-
Public benefit	-	-	-	-
Committed				
Developer impact fee	-	-	-	-
Housing In-Lieu	-	-	44,863	-
Special districts	-	-	-	5,143
Unassigned				
Downtown business	-	-	-	-
Total fund balances	<u>562</u>	<u>5,080</u>	<u>44,863</u>	<u>5,143</u>
Total liabilities and fund balances	<u>\$ 562</u>	<u>\$ 5,187</u>	<u>\$ 44,923</u>	<u>\$ 5,329</u>

Transportation Mitigation	Local Law Enforcement	Asset Seizure	Developer Impact Fee	Downtown Business Development District	Public Benefit	Total Special Revenue Funds
\$ 10,450	\$ 317	\$ 3	\$ 13,581	\$ -	\$ 19,538	\$ 65,621
-	-	-	102	-	-	394
61	2	-	83	-	95	402
-	-	-	-	-	-	33,816
<u>\$ 10,511</u>	<u>\$ 319</u>	<u>\$ 3</u>	<u>\$ 13,766</u>	<u>\$ -</u>	<u>\$ 19,633</u>	<u>\$ 100,233</u>
\$ -	\$ -	\$ -	\$ -	\$ 19	\$ -	\$ 358
-	-	-	2	-	-	16
-	-	-	-	13	-	13
-	-	-	2	32	-	387
10,511	-	-	-	-	-	10,511
-	-	-	-	-	-	5,080
-	-	-	-	-	-	562
-	319	3	-	-	-	322
-	-	-	-	-	19,633	19,633
-	-	-	13,764	-	-	13,764
-	-	-	-	-	-	44,863
-	-	-	-	-	-	5,143
-	-	-	-	(32)	-	(32)
<u>10,511</u>	<u>319</u>	<u>3</u>	<u>13,764</u>	<u>(32)</u>	<u>19,633</u>	<u>99,846</u>
<u>\$ 10,511</u>	<u>\$ 319</u>	<u>\$ 3</u>	<u>\$ 13,766</u>	<u>\$ -</u>	<u>\$ 19,633</u>	<u>\$ 100,233</u>

CITY OF PALO ALTO
Non-major Special Revenue Funds
Combining Statement of Revenues, Expenditures and Changes in Fund Balances
For the Year Ended June 30, 2018
(Amounts in thousands)

	Street Improvement	Federal Revenue	Housing In-Lieu	Special Districts
REVENUES:				
Special assessments	\$ -	\$ -	\$ -	\$ -
Other taxes and fines	1,781	-	-	335
Contributions	-	-	-	-
Charges for services	-	-	-	-
Intergovernmental:				
Community Development Block Grants	-	363	-	-
State of California	78	-	-	-
Permits and licenses				
University Avenue Parking	-	-	-	3,088
California Avenue Parking	-	-	-	556
Other permits and licenses	-	-	-	582
Investment earnings	3	-	70	3
Rental income	-	-	6	-
Other:				
Housing In-Lieu	-	-	1,145	-
Other fees	-	217	106	27
Total revenues	<u>1,862</u>	<u>580</u>	<u>1,327</u>	<u>4,591</u>
EXPENDITURES:				
Current:				
Administrative Services	-	-	-	226
Public Works	-	-	-	857
Planning and Community Environment	-	528	87	1,405
Police	-	-	-	-
Community Services	-	-	-	24
Non-Departmental	-	-	157	303
Total expenditures	<u>-</u>	<u>528</u>	<u>244</u>	<u>2,815</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>1,862</u>	<u>52</u>	<u>1,083</u>	<u>1,776</u>
OTHER FINANCING SOURCES (USES):				
Transfers in	-	-	-	340
Transfers out	<u>(2,166)</u>	<u>-</u>	<u>(1)</u>	<u>(1,237)</u>
Total other financing sources (uses)	<u>(2,166)</u>	<u>-</u>	<u>(1)</u>	<u>(897)</u>
Change in fund balances	(304)	52	1,082	879
FUND BALANCES, BEGINNING OF YEAR	<u>866</u>	<u>5,028</u>	<u>43,781</u>	<u>4,264</u>
FUND BALANCES, END OF YEAR	<u>\$ 562</u>	<u>\$ 5,080</u>	<u>\$ 44,863</u>	<u>\$ 5,143</u>

Transportation Mitigation	Local Law Enforcement	Asset Seizure	Developer Impact Fee	Downtown Business Development District	Public Benefit	Total Special Revenue Funds
\$ -	\$ -	\$ -	\$ -	\$ 72	\$ -	\$ 72
-	-	-	-	-	-	2,116
-	-	-	-	-	11,733	11,733
-	-	-	-	-	11	11
-	-	-	-	-	-	363
-	151	-	-	-	-	229
-	-	-	-	-	-	3,088
-	-	-	-	-	-	556
-	-	-	-	-	-	582
39	-	-	39	-	70	224
-	-	-	-	-	-	6
-	-	-	-	-	-	1,145
2,158	-	-	1,507	-	-	4,015
2,197	151	-	1,546	72	11,814	24,140
-	-	-	-	-	-	226
-	-	-	-	-	-	857
-	-	-	-	-	-	2,020
-	68	-	-	-	-	68
-	-	-	2,685	-	-	2,709
1,000	-	-	-	129	-	1,589
1,000	68	-	2,685	129	-	7,469
1,197	83	-	(1,139)	(57)	11,814	16,671
-	-	-	155	-	-	495
(1,627)	-	-	(653)	-	(5,750)	(11,434)
(1,627)	-	-	(498)	-	(5,750)	(10,939)
(430)	83	-	(1,637)	(57)	6,064	5,732
10,941	236	3	15,401	25	13,569	94,114
\$ 10,511	\$ 319	\$ 3	\$ 13,764	\$ (32)	\$ 19,633	\$ 99,846

CITY OF PALO ALTO
Non-major Special Revenue Funds
Combining Schedule of Revenues, Expenditures and Changes in Fund Balances -
Budget and Actual
For the Year Ended June 30, 2018
(Amounts in thousands)

	Street Improvement			Federal Revenue		
	Budget	Actual, Budgetary Basis	Variance Positive (Negative)	Budget	Actual, Budgetary Basis	Variance Positive (Negative)
REVENUES:						
Special assessments	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Other taxes and fines	1,416	1,781	365	-	-	-
Contributions	-	-	-	-	-	-
Charges for services	-	-	-	-	-	-
Intergovernmental:						
Community Development Block Grants	-	-	-	436	363	(73)
State of California	-	78	78	-	-	-
Permits and licenses						
University Avenue Parking	-	-	-	-	-	-
California Avenue Parking	-	-	-	-	-	-
Other permits and licenses	-	-	-	-	-	-
Investment earnings	13	13	-	-	-	-
Rental income	-	-	-	-	-	-
Other:						
Housing In-Lieu - residential	-	-	-	-	-	-
Loan payoffs	-	-	-	-	-	-
Other fees	-	-	-	136	217	81
Total revenues	<u>1,429</u>	<u>1,872</u>	<u>443</u>	<u>572</u>	<u>580</u>	<u>8</u>
EXPENDITURES:						
Current:						
Administrative Services	-	-	-	-	-	-
Public Works	-	-	-	-	-	-
Planning and Community Environment	-	-	-	977	959	18
Police	-	-	-	-	-	-
Community Services	-	-	-	-	-	-
Non-Departmental	-	-	-	-	-	-
Total expenditures	<u>-</u>	<u>-</u>	<u>-</u>	<u>977</u>	<u>959</u>	<u>18</u>
Excess (deficiency) of revenues over (under) expenditures	<u>1,429</u>	<u>1,872</u>	<u>443</u>	<u>(405)</u>	<u>(379)</u>	<u>26</u>
OTHER FINANCING SOURCES (USES):						
Transfers in	-	-	-	-	-	-
Transfers out	<u>(1,764)</u>	<u>(2,166)</u>	<u>(402)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total other financing sources (uses)	<u>(1,764)</u>	<u>(2,166)</u>	<u>(402)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Change in fund balances, budgetary basis	<u>\$ (335)</u>	<u>(294)</u>	<u>\$ 41</u>	<u>\$ (405)</u>	<u>(379)</u>	<u>\$ 26</u>
Adjustment to Budgetary Basis:						
Unrealized gain/loss on investments		(10)			-	
Changes in notes receivable		-			52	
Current year encumbrances/reappropriations		-			379	
CHANGE IN FUND BALANCE, GAAP BASIS		<u>(304)</u>			<u>52</u>	
FUND BALANCES, BEGINNING OF YEAR, GAAP BASIS		<u>866</u>			<u>5,028</u>	
FUND BALANCES, END OF YEAR, GAAP BASIS		<u>\$ 562</u>			<u>\$ 5,080</u>	

Housing In-Lieu			Special Districts			Transportation Mitigation		
Budget	Actual, Budgetary Basis	Variance Positive (Negative)	Budget	Actual, Budgetary Basis	Variance Positive (Negative)	Budget	Actual, Budgetary Basis	Variance Positive (Negative)
\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
-	-	-	180	335	155	-	-	-
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
-	-	-	2,717	3,088	371	-	-	-
-	-	-	441	556	115	-	-	-
-	-	-	1,069	582	(487)	-	-	-
427	478	51	27	100	73	204	240	36
9	6	(3)	-	-	-	-	-	-
2,150	1,145	(1,005)	-	-	-	-	-	-
25	77	52	-	-	-	-	-	-
170	106	(64)	-	27	27	467	2,158	1,691
<u>2,781</u>	<u>1,812</u>	<u>(969)</u>	<u>4,434</u>	<u>4,688</u>	<u>254</u>	<u>671</u>	<u>2,398</u>	<u>1,727</u>
-	-	-	231	226	5	-	-	-
-	-	-	1,224	857	367	-	-	-
573	440	133	2,021	2,176	(155)	-	-	-
-	-	-	-	-	-	-	-	-
-	-	-	26	24	2	-	-	-
14,765	14,670	95	683	303	380	1,000	1,000	-
<u>15,338</u>	<u>15,110</u>	<u>228</u>	<u>4,185</u>	<u>3,586</u>	<u>599</u>	<u>1,000</u>	<u>1,000</u>	<u>-</u>
<u>(12,557)</u>	<u>(13,298)</u>	<u>(741)</u>	<u>249</u>	<u>1,102</u>	<u>853</u>	<u>(329)</u>	<u>1,398</u>	<u>1,727</u>
-	-	-	340	340	-	-	-	-
-	(1)	(1)	(1,237)	(1,237)	-	(1,627)	(1,627)	-
-	(1)	(1)	(897)	(897)	-	(1,627)	(1,627)	-
<u>\$ (12,557)</u>	<u>(13,299)</u>	<u>\$ (742)</u>	<u>\$ (648)</u>	<u>205</u>	<u>\$ 853</u>	<u>\$ (1,956)</u>	<u>(229)</u>	<u>\$ 1,727</u>
	(408)			(97)			(201)	
	14,436			-			-	
	353			771			-	
	1,082			879			(430)	
	43,781			4,264			10,941	
	<u>\$ 44,863</u>			<u>\$ 5,143</u>			<u>\$ 10,511</u>	

CITY OF PALO ALTO
Non-major Special Revenue Funds
Combining Schedule of Revenues, Expenditures and Changes in Fund Balances -
Budget and Actual
For the Year Ended June 30, 2018
(Amounts in Thousands)

	Local Law Enforcement			Asset Seizure		
	Budget	Actual, Budgetary Basis	Variance Positive (Negative)	Budget	Actual, Budgetary Basis	Variance Positive (Negative)
REVENUES:						
Special assessments	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Other taxes and fines	-	-	-	-	-	-
Contributions	-	-	-	-	-	-
Charges for services	-	-	-	-	-	-
Intergovernmental:						
Community Development Block Grants	-	-	-	-	-	-
State of California	-	151	151	-	-	-
Permits and licenses						
University Avenue Parking	-	-	-	-	-	-
California Avenue Parking	-	-	-	-	-	-
Other permits and licenses	-	-	-	-	-	-
Investment earnings	2	6	4	-	-	-
Rental income	-	-	-	-	-	-
Other:						
Housing In-Lieu - residential	-	-	-	-	-	-
Loan payoffs	-	-	-	-	-	-
Other fees	-	-	-	-	-	-
Total revenues	2	157	155	-	-	-
EXPENDITURES:						
Current:						
Administrative Services	-	-	-	-	-	-
Public Works	-	-	-	-	-	-
Planning and Community Environment	-	-	-	-	-	-
Police	1	68	(67)	-	-	-
Community Services	-	-	-	-	-	-
Non-Departmental	-	-	-	-	-	-
Total expenditures	1	68	(67)	-	-	-
Excess (deficiency) of revenues over (under) expenditures	1	89	88	-	-	-
OTHER FINANCING SOURCES (USES):						
Transfers in	-	-	-	-	-	-
Transfers out	-	-	-	-	-	-
Total other financing sources (uses)	-	-	-	-	-	-
Change in fund balances, Budgetary basis	\$ 1	89	\$ 88	\$ -	-	\$ -
Adjustment to Budgetary Basis:						
Unrealized gain/loss on investments		(6)			-	
Changes in notes receivable		-			-	
Current year encumbrances/reappropriations		-			-	
CHANGE IN FUND BALANCE, GAAP BASIS		83			-	
FUND BALANCES, BEGINNING OF YEAR, GAAP BASIS		236			3	
FUND BALANCES, END OF YEAR, GAAP BASIS		\$ 319			\$ 3	

Developer Impact Fee			Downtown Business Improvement District			Public Benefit		
Budget	Actual, Budgetary Basis	Variance Positive (Negative)	Budget	Actual, Budgetary Basis	Variance Positive (Negative)	Budget	Actual, Budgetary Basis	Variance Positive (Negative)
\$ -	\$ -	\$ -	\$ 140	\$ 72	\$ (68)	\$ -	\$ -	\$ -
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	11,734	11,733	(1)
-	-	-	-	-	-	11	11	-
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
215	314	99	2	1	(1)	211	374	163
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
1,599	1,507	(92)	-	-	-	-	-	-
1,814	1,821	7	142	73	(69)	11,956	12,118	162
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
-	-	-	-	-	-	-	-	-
2,682	2,685	(3)	-	-	-	35	45	(10)
-	-	-	152	150	2	-	-	-
2,682	2,685	(3)	152	150	2	35	45	(10)
(868)	(864)	4	(10)	(77)	(67)	11,921	12,073	152
155	155	-	-	-	-	-	-	-
(653)	(653)	-	-	-	-	(5,750)	(5,750)	-
(498)	(498)	-	-	-	-	(5,750)	(5,750)	-
<u>\$ (1,366)</u>	<u>(1,362)</u>	<u>\$ 4</u>	<u>\$ (10)</u>	<u>(77)</u>	<u>\$ (67)</u>	<u>\$ 6,171</u>	<u>6,323</u>	<u>\$ 152</u>
	(275)			(1)			(304)	
	-			-			-	
	-			21			45	
	(1,637)			(57)			6,064	
	15,401			25			13,569	
	<u>\$ 13,764</u>			<u>\$ (32)</u>			<u>\$ 19,633</u>	

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NON-MAJOR GOVERNMENTAL FUNDS

DEBT SERVICE FUNDS

Downtown Parking Improvement

This fund accounts for revenues received from the General Fund to provide payment of principal and interest associated with the 2002B Downtown Parking Improvement Certificates of Participation as they become due.

Library Projects

This fund accounts for revenues received from property taxes to provide payment of principal and interest associated with the 2010 and 2013A General Obligation Bonds as they become due.

CITY OF PALO ALTO
Non-major Debt Service Funds
Combining Balance Sheet
June 30, 2018
(Amounts in thousands)

	<u>Downtown Parking Improvement</u>	<u>Library Projects</u>	<u>Total Debt Service Funds</u>
ASSETS:			
Cash and investments:			
Available for operations	\$ 15	\$ 3,530	\$ 3,545
Receivables:			
Accounts	-	5	5
Interest	-	21	21
Total assets	<u>\$ 15</u>	<u>\$ 3,556</u>	<u>\$ 3,571</u>
FUND BALANCES:			
Debt service	<u>\$ 15</u>	<u>\$ 3,556</u>	<u>\$ 3,571</u>

CITY OF PALO ALTO
Non-major Debt Service Funds
Combining Statement of Revenues, Expenditures and Changes in Fund Balances
For the Year Ended June 30, 2018
(Amounts in thousands)

	Downtown Parking Improvement	Library Projects	Total Debt Service Funds
REVENUES:			
Property tax	\$ -	\$ 4,331	\$ 4,331
Investment earnings	2	(30)	(28)
Total revenues	<u>2</u>	<u>4,301</u>	<u>4,303</u>
EXPENDITURES:			
Current:			
Non-Departmental	14	-	14
Debt service:			
Principal retirement	975	1,570	2,545
Interest and fiscal charges	77	2,863	2,940
Total expenditures	<u>1,066</u>	<u>4,433</u>	<u>5,499</u>
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	<u>(1,064)</u>	<u>(132)</u>	<u>(1,196)</u>
OTHER FINANCING SOURCES (USES):			
Issuance of debt	595	-	595
Transfers in	233	-	233
Total other financing sources (uses)	<u>828</u>	<u>-</u>	<u>828</u>
Change in fund balances	(236)	(132)	(368)
FUND BALANCES, BEGINNING OF YEAR	<u>251</u>	<u>3,688</u>	<u>3,939</u>
FUND BALANCES, END OF YEAR	<u>\$ 15</u>	<u>\$ 3,556</u>	<u>\$ 3,571</u>

CITY OF PALO ALTO
Non-major Debt Service Funds
Combining Schedule of Revenues, Expenditures and Changes in Fund Balances -
Budget and Actual
For the Year Ended June 30, 2018
(Amounts in thousands)

	Downtown Parking Improvement			Library Projects		
	Budget	Actual, plus Encumbrances	Variance Positive (Negative)	Budget	Actual, plus Encumbrances	Variance Positive (Negative)
REVENUES:						
Special assessments	\$ -	\$ -	\$ -	\$ 4,433	\$ 4,331	\$ (102)
Investment earnings	-	2	2	-	38	38
Total revenues	<u>-</u>	<u>2</u>	<u>2</u>	<u>4,433</u>	<u>4,369</u>	<u>(64)</u>
EXPENDITURES:						
Current:						
Debt service:						
Principal retirement	170	975	(805)	1,570	1,570	-
Interest and fiscal charges	63	77	(14)	2,863	2,863	-
Total expenditures	<u>233</u>	<u>1,052</u>	<u>(819)</u>	<u>4,433</u>	<u>4,433</u>	<u>-</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(233)</u>	<u>(1,050)</u>	<u>(817)</u>	<u>-</u>	<u>(64)</u>	<u>(64)</u>
OTHER FINANCING SOURCES (USES):						
Issuance of debt	-	595	595	-	-	-
Payment to bond refunding escrow	-	(14)	(14)	-	-	-
Transfers in	233	233	-	-	-	-
Total other financing sources (uses)	<u>233</u>	<u>814</u>	<u>581</u>	<u>-</u>	<u>-</u>	<u>-</u>
Change in fund balances, Budgetary basis	<u>\$ -</u>	<u>(236)</u>	<u>\$ (236)</u>	<u>\$ -</u>	<u>(64)</u>	<u>\$ (64)</u>
Adjustment to Budgetary Basis:						
Unrealized gain/loss on investments					(68)	
CHANGE IN FUND BALANCE, GAAP BASIS		(236)			(132)	
FUND BALANCES, BEGINNING OF YEAR		<u>251</u>			<u>3,688</u>	
FUND BALANCES, END OF YEAR		<u>\$ 15</u>			<u>\$ 3,556</u>	

NON-MAJOR GOVERNMENTAL FUNDS

PERMANENT FUND

Eyerly Family

This fund accounts for the revenues received from assets donated by Mr. and Mrs. Fred Eyerly for the City and or its citizenry.

CITY OF PALO ALTO
Non-major Permanent Fund
Schedule of Revenues, Expenditures and Changes in Fund Balance -
Budget and Actual
For the Year Ended June 30, 2018
(Amounts in thousands)

	Eyerly Family Permanent Fund		
	Budget	Actual, plus Encumbrances	Variance Positive (Negative)
REVENUES:			
Investment earnings	\$ 27	\$ 31	\$ 4
Total revenues	27	31	4
EXPENDITURES:			
Current:			
Non-Departmental	-	3	(3)
Total expenditures	-	3	(3)
Excess (deficiency) of revenues over (under) expenditures	27	28	1
Change in fund balance	\$ 27	28	\$ 1
Adjustment to Budgetary Basis:			
Unrealized gain/loss on investments		(29)	
CHANGE IN FUND BALANCE, GAAP BASIS		(1)	
FUND BALANCE, BEGINNING OF YEAR		1,499	
FUND BALANCE, END OF YEAR		\$ 1,498	

INTERNAL SERVICE FUNDS

INTRODUCTION

Internal Service Funds are used to finance and account for special activities and services performed by a designated department for other departments in the City on a cost reimbursement basis.

Vehicle Replacement and Maintenance

This fund accounts for the maintenance and replacement of vehicles and equipment used by all City departments. The source of revenue is from reimbursement of fleet replacement and maintenance costs allocated to each department by usage of vehicle.

Technology

This fund accounts for replacement and upgrade of technology, and covers four primary areas used by all City departments: desktop, infrastructure, applications, and technology research and development. The source of revenue is from reimbursement of costs for support provided to other departments.

Printing and Mailing Services

This fund accounts for central duplicating, printing and mailing services provided to all City departments. Source of revenue for this fund is from reimbursement of costs for services and supplies purchased by other departments.

General Benefits

This fund accounts for the administration of compensated absences and health benefits.

Workers' Compensation Insurance Program

This fund accounts for the administration of the City's self-insured workers' compensation programs.

General Liabilities Insurance Program

This fund accounts for the administration of the City's self-insured general liability programs.

Retiree Health Benefits

This fund accounts for the retiree health benefits contributions.

CITY OF PALO ALTO
Internal Service Funds
Combining Statement of Fund Net Position
June 30, 2018
(Amounts in thousands)

	Vehicle Replacement and Maintenance	Technology	Printing and Mailing Services	General Benefits	Workers' Compensation Insurance Program	General Liabilities Insurance Program	Retiree Health Benefits	Total Internal Services Funds
ASSETS:								
Current Assets:								
Cash and investments:								
Available for operations	\$ 9,614	\$ 23,419	\$ 188	\$ 17,304	\$ 19,805	\$ 6,289	\$ 1,632	\$ 78,251
Restricted investments with trustees	-	-	-	5,547	-	-	-	5,547
Accounts receivable, net	4	-	-	32	17	-	-	53
Interest receivable	57	136	1	96	116	37	20	463
Inventory of materials and supplies	214	-	-	-	-	-	-	214
Total current assets	9,889	23,555	189	22,979	19,938	6,326	1,652	84,528
Noncurrent Assets:								
Capital assets:								
Nondepreciable	622	1,251	-	-	-	-	-	1,873
Depreciable, net	17,720	2,156	29	-	-	-	-	19,905
Total noncurrent assets	18,342	3,407	29	-	-	-	-	21,778
Total assets	28,231	26,962	218	22,979	19,938	6,326	1,652	106,306
DEFERRED OUTFLOWS OF RESOURCES:								
Pension related	878	2,776	64	-	77	-	-	3,795
OPEB related	263	536	23	-	-	-	-	822
Total deferred outflows of resources	1,141	3,312	87	-	77	-	-	4,617
LIABILITIES:								
Current Liabilities:								
Accounts payable and accruals	386	435	193	1,002	35	-	653	2,704
Accrued salaries and benefits	23	76	2	-	2	-	-	103
Accrued compensated absences	4	16	-	5,976	-	-	-	5,996
Accrued claims payable - current	-	-	-	160	3,231	2,444	-	5,835
Total current liabilities	413	527	195	7,138	3,268	2,444	653	14,638
Noncurrent liabilities:								
Accrued compensated absences	-	-	-	6,062	-	-	-	6,062
Accrued claims payable	-	-	-	-	15,035	2,878	-	17,913
Net pension liabilities	3,704	12,526	366	-	114	-	-	16,710
Net OPEB liabilities	1,888	3,853	169	-	-	-	-	5,910
Total noncurrent liabilities	5,592	16,379	535	6,062	15,149	2,878	-	46,595
Total liabilities	6,005	16,906	730	13,200	18,417	5,322	653	61,233
DEFERRED INFLOWS OF RESOURCES:								
Pension related	64	211	5	-	6	-	-	286
OPEB related	31	63	3	-	-	-	-	97
Total deferred inflows of resources	95	274	8	-	6	-	-	383
NET POSITION:								
Net Investment in capital assets	18,342	3,407	29	-	-	-	-	21,778
Unrestricted	4,930	9,687	(462)	9,779	1,592	1,004	999	27,529
Total net position	\$ 23,272	\$ 13,094	\$ (433)	\$ 9,779	\$ 1,592	\$ 1,004	\$ 999	\$ 49,307

CITY OF PALO ALTO
Internal Service Funds
Combining Statement of Revenues, Expenses and Changes in Fund Net Position
For the Year Ended June 30, 2018
(Amounts in thousands)

	Vehicle Replacement and Maintenance	Technology	Printing and Mailing Services	General Benefits	Workers' Compensation Insurance Program	General Liabilities Insurance Program	Retiree Health Benefits	Total Internal Services Funds
OPERATING REVENUES:								
Charges for services	\$ 9,361	\$ 13,775	\$ 1,646	\$ 56,429	\$ 1,827	\$ 1,813	\$ 14,527	\$ 99,378
Other	-	-	-	1	114	6	-	121
Total operating revenues	9,361	13,775	1,646	56,430	1,941	1,819	14,527	99,499
OPERATING EXPENSES:								
Administrative and general	1,420	7,994	1,218	177	740	2,150	43	13,742
Operations and maintenance	3,994	7,770	432	926	205	-	-	13,327
Depreciation and amortization	2,601	469	4	-	-	-	-	3,074
Claim payments and change in estimated self-insured liability	-	-	-	1,613	2,594	498	-	4,705
Refund of charges for services	77	10	-	-	-	-	-	87
Employment benefits	-	-	-	49,231	-	-	21,316	70,547
Total operating expenses	8,092	16,243	1,654	51,947	3,539	2,648	21,359	105,482
Operating income (loss)	1,269	(2,468)	(8)	4,483	(1,598)	(829)	(6,832)	(5,983)
NONOPERATING REVENUES (EXPENSES):								
Investment earnings	17	37	(5)	(64)	34	5	8	32
Gain on disposal of capital assets	218	-	-	-	-	-	-	218
Other nonoperating revenues	42	-	-	-	-	-	-	42
Total nonoperating revenues (expenses)	277	37	(5)	(64)	34	5	8	292
Income (loss) before transfers	1,546	(2,431)	(13)	4,419	(1,564)	(824)	(6,824)	(5,691)
Transfers in	26	2,032	-	1,427	-	5	2,444	5,934
Transfers out	(42)	(162)	(3)	(2,444)	(3)	-	-	(2,654)
Change in net position	1,530	(561)	(16)	3,402	(1,567)	(819)	(4,380)	(2,411)
NET POSITION (DEFICIT), BEGINNING OF YEAR AS PREVIOUSLY STATED	23,464	17,170	(263)	6,377	3,159	1,823	24,798	76,528
RESTATEMENT FOR IMPLEMENTATION OF GASB STATEMENT NO. 75	(1,722)	(3,515)	(154)	-	-	-	(19,419)	(24,810)
NET POSITION, BEGINNING OF YEAR, AS RESTATED	21,742	13,655	(417)	6,377	3,159	1,823	5,379	51,718
NET POSITION, END OF YEAR	\$ 23,272	\$ 13,094	\$ (433)	\$ 9,779	\$ 1,592	\$ 1,004	\$ 999	\$ 49,307

CITY OF PALO ALTO
Internal Service Funds
Combining Statement of Cash Flows
For the Year Ended June 30, 2018
(Amounts in thousands)

	Vehicle Replacement and Maintenance	Technology	Printing and Mailing Services	General Benefits	Workers' Compensation Insurance Program	General Liabilities Insurance Program	Retiree Health Benefits	Total Internal Services Funds
Cash flows from operating activities:								
Cash received from customers	\$ 9,369	\$ 13,775	\$ 1,646	\$ 56,410	\$ 2,241	\$ 1,819	\$ 14,527	\$ 99,787
Cash refunds to customers	-	(10)	-	-	-	-	-	(10)
Cash payments to suppliers for goods and services	(2,782)	(7,964)	(1,227)	(1,255)	(211)	(1,677)	653	(14,463)
Cash payments to employees	(2,211)	(7,069)	(257)	(47,967)	(711)	-	(21,359)	(79,574)
Cash payments for judgments and claims	-	-	-	(1,598)	(1,714)	(525)	-	(3,837)
Other cash receipts	42	-	-	-	-	-	-	42
Net cash flows provided by (used in) operating activities	4,418	(1,268)	162	5,590	(395)	(383)	(6,179)	1,945
Cash flows from noncapital financing activities:								
Transfers in	26	2,032	-	1,427	-	5	2,444	5,934
Transfers out	(42)	(162)	(3)	(2,444)	(3)	-	-	(2,654)
Net cash flows provided by (used in) noncapital financing activities	(16)	1,870	(3)	(1,017)	(3)	5	2,444	3,280
Cash flows from capital and related financing activities:								
Acquisition of capital assets	(5,359)	(916)	-	-	-	-	-	(6,275)
Proceeds from sale of capital assets	248	-	-	-	-	-	-	248
Net cash flows (used in) capital and related financing activities	(5,111)	(916)	-	-	-	-	-	(6,027)
Cash flows from investing activities:								
Interest received (charged)	10	9	(6)	(90)	16	3	10	(48)
Net change in cash and cash equivalents	(699)	(305)	153	4,483	(382)	(375)	(3,725)	(850)
Cash and cash equivalents, beginning of year	10,313	23,724	35	18,368	20,187	6,664	5,357	84,648
Cash and cash equivalents, end of year	\$ 9,614	\$ 23,419	\$ 188	\$ 22,851	\$ 19,805	\$ 6,289	\$ 1,632	\$ 83,798
Reconciliation of operating income (loss) to net cash flows provided by (used in) operating activities:								
Operating income (loss)	\$ 1,269	\$ (2,468)	\$ (8)	\$ 4,483	\$ (1,598)	\$ (829)	\$ (6,832)	\$ (5,983)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:								
Depreciation	2,601	469	4	-	-	-	-	3,074
Other	42	-	-	-	-	-	-	42
Change in assets and liabilities:								
Accounts receivable	8	-	-	(19)	414	-	-	403
Inventory of materials and supplies	30	-	-	-	-	-	-	30
Net OPEB asset	-	-	-	-	-	-	-	-
Deferred outflows of resources - pension plan	(126)	(580)	(16)	-	(11)	-	-	(733)
Deferred outflows of resources - OPEB	(82)	(166)	(7)	-	-	-	-	(255)
Accounts payable and accruals	292	112	155	533	(6)	(52)	653	1,687
Accrued salaries and benefits	2	12	-	-	-	-	-	14
Accrued compensated absences	-	1	-	579	-	-	-	580
Accrued claims payable	-	-	-	14	766	498	-	1,278
Net pension liability	360	1,283	32	-	34	-	-	1,709
Net OPEB liability	(15)	(32)	(1)	-	-	-	-	(48)
Deferred inflows of resources - pension plans	6	38	-	-	6	-	-	50
Deferred inflows of resources - OPEB	31	63	3	-	-	-	-	97
Net cash flows provided by (used in) operating activities	\$ 4,418	\$ (1,268)	\$ 162	\$ 5,590	\$ (395)	\$ (383)	\$ (6,179)	\$ 1,945

FIDUCIARY FUNDS

INTRODUCTION

Fiduciary Funds are used to account for assets held by the City acting in a fiduciary capacity for other entities and individuals. The funds are operated to carry out the specific actions required by the trust agreements, ordinances and other governing regulations.

Fiduciary Funds are presented separately from the Citywide and Fund financial statements.

Agency Funds are custodial in nature and do not involve measurement of results of operations. The City maintains three agency funds, as follows:

Cable Joint Powers Authority

The fund was established to account for the activities of the cable television system on behalf of the members.

University Avenue Area Off-Street Parking Assessment District

The fund accounts for the receipts and disbursements associated with the Series 2012 Limited Obligation Refunding Improvement Bonds.

CITY OF PALO ALTO
All Agency Funds
Statement of Changes in Assets and Liabilities
For the Year Ended June 30, 2018
(Amounts in thousands)

	Balance June 30, 2017	Additions	Deletions	Balance June 30, 2018
<u>Cable Joint Powers Authority</u>				
ASSETS:				
Cash and investments available for operations	\$ 473	\$ 76	\$ -	\$ 549
Accounts receivable	515	-	-	515
Interest receivable	3	-	-	3
Total assets	<u>\$ 991</u>	<u>\$ 76</u>	<u>\$ -</u>	<u>\$ 1,067</u>
LIABILITIES:				
Due to other governments	<u>\$ 991</u>	<u>\$ 76</u>	<u>\$ -</u>	<u>\$ 1,067</u>
<u>University Avenue Area</u>				
<u>Off-Street Parking Assessment District</u>				
ASSETS:				
Cash and investments available for operations	\$ 1,935	\$ 38	\$ -	\$ 1,973
Cash and investments with fiscal agents	2,556	38	-	2,594
Accounts receivable	64	-	47	17
Interest receivable	9	2	-	11
Total assets	<u>\$ 4,564</u>	<u>\$ 78</u>	<u>\$ 47</u>	<u>\$ 4,595</u>
LIABILITIES:				
Due to bondholders	<u>\$ 4,564</u>	<u>\$ 31</u>	<u>\$ -</u>	<u>\$ 4,595</u>
<u>Total Agency Funds</u>				
ASSETS:				
Cash and investments available for operations	\$ 2,408	\$ 114	\$ -	\$ 2,522
Cash and investments with fiscal agents	2,556	38	-	2,594
Accounts receivable	579	-	47	532
Interest receivable	12	2	-	14
Total assets	<u>\$ 5,555</u>	<u>\$ 154</u>	<u>\$ 47</u>	<u>\$ 5,662</u>
LIABILITIES:				
Due to bondholders	\$ 4,564	\$ 31	\$ -	\$ 4,595
Due to other governments	991	76	-	1,067
Total liabilities	<u>\$ 5,555</u>	<u>\$ 107</u>	<u>\$ -</u>	<u>\$ 5,662</u>

STATISTICAL SECTION

The statistical section contains comprehensive statistical data, which relates to physical, economic, social and political characteristics of the City. It is intended to provide users with a broader and more complete understanding of the City and its financial affairs than is possible from the financial statements and supporting schedules included in the financial section.

In this section, readers will find comparative information related to the City's revenue sources, expenditures, property tax valuations, levies and collections, general obligation bonded debt, utility revenue debt service, and demographics. Where available, the comparative information is presented for the last ten fiscal years.

In addition, this section presents information related to the City's legal debt margin computation, principal taxpayers, notary and security bond coverages, and other miscellaneous statistics pertaining to services provided by the City.

In contrast to the financial section, the statistical section information is not usually subject to independent audit.

Financial Trends

These schedules contain trend information to help the reader understand how the City's financial performance and well-being have changed over time:

- Net Position by Component
- Changes in Net Position
- Fund Balances of Governmental Funds
- Changes in Fund Balances of Governmental Funds

Revenue Capacity

These schedules contain information to help the reader assess the City's most significant local revenue sources, property tax and electric charges:

- Electric Operating Revenue by Source
- Supplemental Disclosure for Water Utilities
- Supplemental Disclosure for Gas Utilities
- Assessed Value of Taxable Property
- Property Tax Rates, All Overlapping Governments
- Property Tax Levies and Collections
- Principal Property Taxpayers
- Assessed Valuation and Parcels by Land Use
- Per Parcel Assessed Valuation of Single Family Residential

Debt Capacity

These schedules present information to help the reader assess the affordability of the City's current levels of outstanding debt and the City's ability to issue additional debt in the future:

- Ratio of Outstanding Debt by Type
- Computation of Direct and Overlapping Debt
- Computation of Legal Bonded Debt Margin
- Revenue Bond Coverage

STATISTICAL SECTION

Demographic and Economic Information

These schedules offer demographic and economic indicators to help the reader understand the environment within which the City's financial activities take place:

- Taxable Transactions by Type of Business
- Demographic and Economic Statistics
- Principal Employers

Operating Information

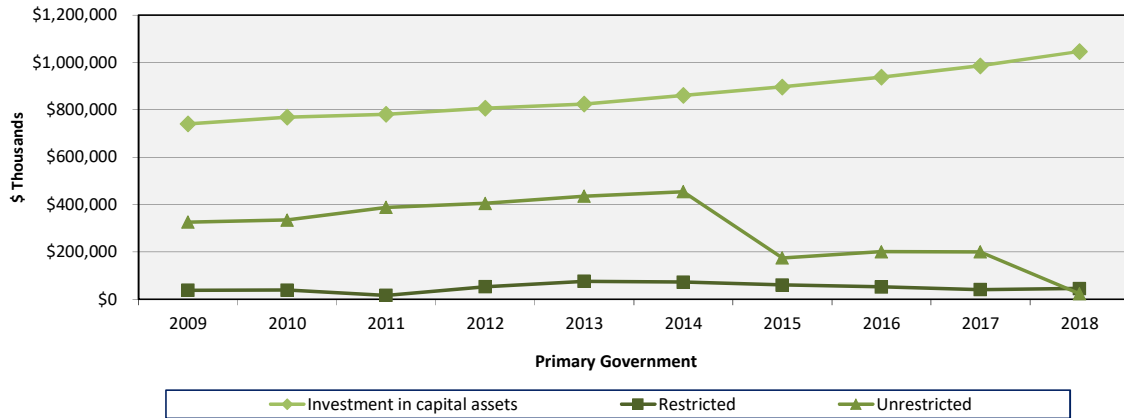
These schedules contain service and infrastructure data to help the reader understand how the information in the City's financial report relates to the services the City provides and the activities it performs:

- Operating Indicators by Function/Program
- Capital Asset Statistics by Function/Program
- Full-Time Equivalent City Government Employees by Function

Sources

Unless otherwise noted, the information in these schedules is derived from the Comprehensive Annual Financial Reports for the relevant year.

CITY OF PALO ALTO
Net Position by Component
Last Ten Fiscal Years
(Accrual basis of accounting)
(Amounts in thousands)



	Fiscal Year Ended June 30									
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Governmental Activities										
Investment in capital assets	\$ 356,657	\$ 369,499	\$ 364,747	\$ 370,111	\$ 378,047	\$ 386,696	\$ 405,921	\$ 425,179	\$ 453,878	\$ 473,233
Restricted	36,632	34,323	16,437	52,934	71,717	68,331	55,963	47,907	36,081	41,177
Unrestricted	118,133	102,199	134,722	142,102	165,810	187,386	1,972	37,905	37,330	(87,040)
Total Governmental Activities Net Position	\$ 511,422	\$ 506,021	\$ 515,906	\$ 565,147	\$ 615,574	\$ 642,413	\$ 463,856	\$ 510,991	\$ 527,289	\$ 427,370
Business-type Activities										
Investment in capital assets	\$ 384,313	\$ 399,317	\$ 416,418	\$ 437,151	\$ 446,597	\$ 473,795	\$ 490,874	\$ 512,918	\$ 532,063	\$ 573,688
Restricted	1,732	4,300	-	-	4,060	4,166	4,142	4,115	4,073	4,014
Unrestricted	208,025	232,420	253,740	262,602	269,926	266,794	172,802	162,806	163,158	110,429
Total Business-type Activities Net Position	\$ 594,070	\$ 636,037	\$ 670,158	\$ 699,753	\$ 720,583	\$ 744,755	\$ 667,818	\$ 679,839	\$ 699,294	\$ 688,131
Primary Government										
Investment in capital assets	\$ 740,970	\$ 768,816	\$ 781,165	\$ 807,262	\$ 824,644	\$ 860,491	\$ 896,795	\$ 938,097	\$ 985,941	\$ 1,046,921
Restricted	38,364	38,623	16,437	52,934	75,777	72,497	60,105	52,022	40,154	45,191
Unrestricted	326,158	334,619	388,462	404,704	435,736	454,180	174,774	200,711	200,488	23,389
Total Primary Government Net Position	\$ 1,105,492	\$ 1,142,058	\$ 1,186,064	\$ 1,264,900	\$ 1,336,157	\$ 1,387,168	\$ 1,131,674	\$ 1,190,830	\$ 1,226,583	\$ 1,115,501

Notes: The City implemented GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, effective July 1, 2014, and GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pension*, effective July 1, 2017. The City's unrestricted net position decreased in FY 2015 and again in FY 2018 as a result.

Source: Annual Financial Statements, Statement of Net Position

CITY OF PALO ALTO
Changes in Net Position
Last Ten Fiscal Years
(Accrual basis of accounting)
(Amounts in thousands)

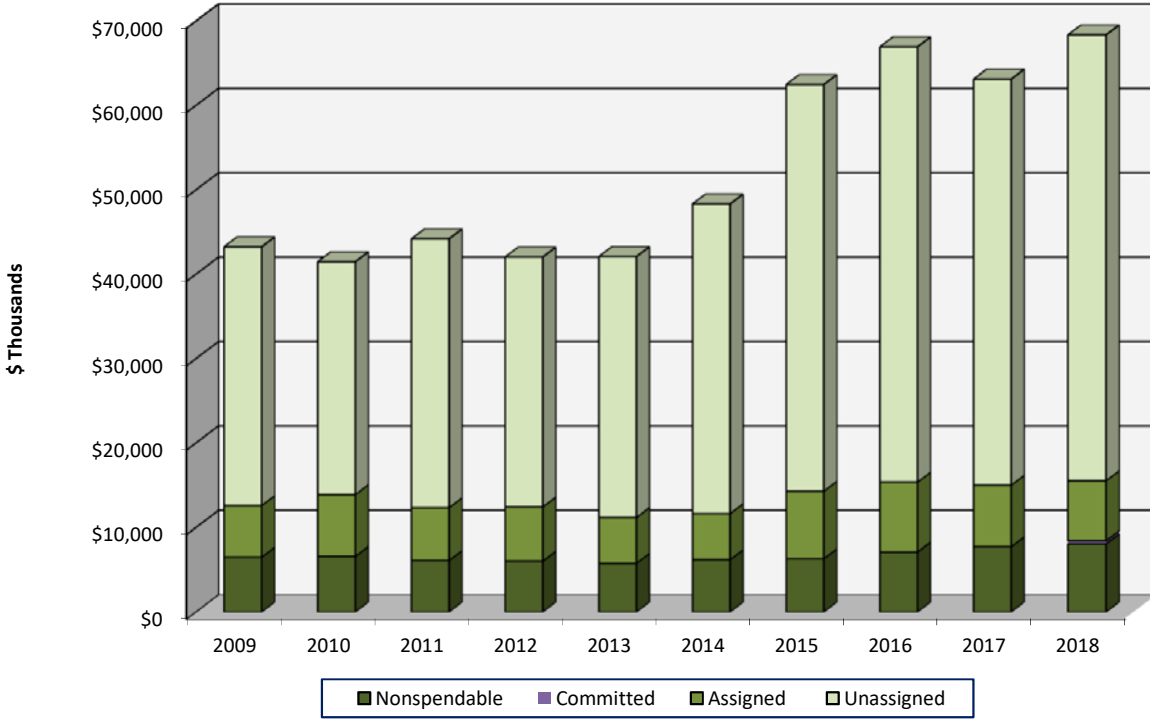
	Fiscal Year Ended June 30									
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
PROGRAM REVENUES										
Governmental Activities										
Charges for services										
City Council	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
City Manager	-	-	-	-	-	-	-	-	-	-
City Attorney	12.00	53.00	-	-	-	-	-	-	-	-
City Clerk	-	-	-	-	-	-	-	-	-	-
City Auditor	-	-	-	-	-	-	-	-	-	-
Administrative Services	726	984	2,889	1,647	15,629	4,055	5,460	9,444	5,242	6,536
Human Resources	-	-	-	-	-	-	-	-	-	-
Public Works	1,169	1,258	2,419	1,008	1,314	1,093	1,209	599	878	781
Planning & Community Environment	4,704	4,813	7,237	31,491	28,768	12,896	8,090	9,071	6,067	5,119
Development Services ¹	-	-	-	-	-	-	12,019	12,570	11,768	16,000
Public Safety	14,670	14,337	15,274	15,658	16,139	14,902	15,726	13,945	12,670	13,507
Community Services	8,522	8,729	7,724	11,365	13,808	20,882	20,912	21,551	20,472	21,285
Library	177	199	480	1,600	187	166	137	198	139	145
Operating grants and contributions	3,599	4,829	2,884	3,441	5,038	5,360	5,300	2,164	1,990	14,054
Capital grants and contributions	3,810	1,280	1,903	1,064	515	917	619	344	1,929	1,534
Total Governmental Activities										
Program Revenues	37,389	36,482	40,810	67,274	81,398	60,271	69,472	69,886	61,155	78,961
Business-type Activities										
Charges for services										
Water	27,120	26,259	26,624	31,467	37,746	40,291	35,847	37,588	42,678	45,087
Electric	119,320	121,900	122,109	118,886	121,805	121,916	120,842	120,743	137,543	154,142
Fiber Optics	3,336	3,105	3,322	3,662	4,382	4,485	4,627	4,505	4,553	4,529
Gas	47,838	44,450	43,584	41,774	34,633	35,737	30,751	30,212	36,431	37,044
Wastewater Collection	14,486	15,136	15,094	14,942	16,077	15,599	16,182	16,496	17,748	17,990
Wastewater Treatment	28,425	16,915	18,830	22,200	21,528	18,460	24,120	23,825	23,649	27,382
Refuse	29,101	28,568	30,469	30,645	30,583	30,297	31,576	32,169	33,918	34,647
Storm Drainage	5,505	5,647	5,796	5,892	6,053	6,183	6,281	6,520	6,693	6,964
Airport	-	-	-	-	-	-	683	826	1,286	2,382
External Services	-	-	-	-	-	-	-	-	-	-
Operating grants and contributions	-	361	610	605	572	549	534	744	512	501
Capital grants and contributions	639	475	3,004	1,526	2,224	2,005	2,080	1,061	4,265	14,194
Total Business-type Activities										
Program Revenues	275,770	262,816	269,442	271,599	275,603	275,522	273,523	274,689	309,276	344,862
Total Primary Government										
Program Revenues	\$ 313,159	\$ 299,298	\$ 310,252	\$ 338,873	\$ 357,001	\$ 335,793	\$ 342,995	\$ 344,575	\$ 370,431	\$ 423,823
EXPENSES										
Governmental Activities										
City Council	\$ 394	\$ 455	\$ 15	\$ 345	\$ 94	\$ 387	\$ 271	\$ 352	\$ 329	\$ 345
City Manager	2,085	2,399	1,842	1,960	1,237	2,180	2,155	2,662	1,975	2,757
City Attorney	2,575	2,621	953	1,656	1,642	1,797	1,759	2,472	2,140	2,511
City Clerk	1,098	1,369	803	908	330	641	680	582	762	931
City Auditor	2,053	2,601	138	235	464	489	362	414	847	994
Administrative Services	17,784	17,893	9,888	10,100	7,614	11,388	9,980	10,637	11,887	13,949
Human Resources	3,448	3,707	1,346	1,071	1,420	1,346	1,464	2,224	2,272	2,674
Public Works	21,270	18,658	19,357	14,568	20,816	24,577	21,075	24,613	25,539	30,349
Planning & Community Environment	12,940	12,114	15,031	12,074	13,549	14,926	8,423	10,208	10,918	11,357
Development Services ¹	-	-	-	-	-	-	10,449	11,158	11,102	12,664
Public Safety	52,487	55,799	58,996	62,817	59,452	62,883	58,660	56,653	73,320	83,923
Community Services	19,862	17,171	22,845	21,915	22,705	23,822	24,688	28,547	27,866	33,709
Library	6,244	6,143	6,920	7,323	7,319	7,758	7,721	10,825	11,437	12,208
Interest on long term debt	404	370	2,742	2,575	2,562	3,367	3,658	3,552	2,846	2,761
Total Governmental										
Activities Expenses	142,644	141,300	140,876	137,547	139,204	155,561	151,345	164,899	183,240	211,132
Business-type Activities										
Water	20,271	21,037	24,268	29,093	30,707	31,593	33,205	35,120	37,535	40,836
Electric	122,268	107,910	100,130	102,030	106,438	113,004	122,499	120,319	128,603	146,033
Fiber Optics	1,284	1,407	1,561	1,489	1,437	1,661	1,891	2,107	2,159	2,653
Gas	34,603	32,498	32,051	28,878	26,749	26,869	23,525	20,879	26,783	27,930
Wastewater Collection	14,875	10,696	12,275	14,825	14,313	13,235	14,595	15,199	16,405	16,801
Wastewater Treatment	36,896	13,466	19,731	20,712	20,635	21,018	21,553	22,546	23,498	27,518
Refuse	37,217	28,119	30,684	31,900	28,542	28,413	27,974	30,370	30,665	28,808
Storm Drainage	2,943	2,491	3,229	3,103	3,703	3,644	3,721	3,735	4,106	5,059
Airport	-	-	31	153	246	466	1,004	970	1,274	1,656
Total Business-type										
Activities Expenses	270,357	217,624	223,960	232,183	232,770	239,903	249,967	251,245	271,028	297,294
Total Primary										
Government Expenses	\$ 413,001	\$ 358,924	\$ 364,836	\$ 369,730	\$ 371,974	\$ 395,464	\$ 401,312	\$ 416,144	\$ 454,268	\$ 508,426

	Fiscal Year Ended June 30									
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
NET (EXPENSE)/REVENUE										
Governmental Activities	\$ (105,255)	\$ (104,818)	\$ (100,066)	\$ (70,273)	\$ (57,806)	\$ (95,290)	\$ (81,873)	\$ (95,013)	\$ (122,085)	\$ (132,171)
Business-type Activities	5,413	45,192	45,482	39,416	42,833	35,619	23,556	23,444	38,248	47,568
Total Primary Government										
Net (Expense)/Revenue	<u>\$ (99,842)</u>	<u>\$ (59,626)</u>	<u>\$ (54,584)</u>	<u>\$ (30,857)</u>	<u>\$ (14,973)</u>	<u>\$ (59,671)</u>	<u>\$ (58,317)</u>	<u>\$ (71,569)</u>	<u>\$ (83,837)</u>	<u>\$ (84,603)</u>
GENERAL REVENUES AND OTHER CHANGES IN NET POSITION										
Governmental Activities										
Taxes										
Property tax	\$ 25,432	\$ 25,981	\$ 29,156	\$ 30,104	\$ 31,929	\$ 35,299	\$ 38,750	\$ 41,189	\$ 43,953	\$ 47,170
Sales tax	20,089	17,991	20,746	22,132	25,606	29,424	29,675	30,018	29,923	31,091
Utility user tax	11,030	11,295	10,851	10,834	10,861	11,008	10,861	12,469	14,240	15,414
Transient occupancy tax	7,111	6,858	8,082	9,664	10,794	12,255	16,699	22,366	23,477	24,937
Other taxes	3,364	4,055	8,156	8,173	10,504	9,660	11,867	7,868	8,989	11,337
Investment earnings	8,525	6,514	3,500	6,238	(1,228)	5,859	5,010	8,639	(711)	420
Miscellaneous	15,682	12,729	12,377	14,943	518	2,575	3,428	894	168	1,973
Transfers	24,020	13,994	17,083	17,426	19,249	17,103	16,405	18,705	18,344	19,077
Total Governmental Activities	<u>115,253</u>	<u>99,417</u>	<u>109,951</u>	<u>119,514</u>	<u>108,233</u>	<u>123,183</u>	<u>132,695</u>	<u>142,148</u>	<u>138,383</u>	<u>151,419</u>
Business-type Activities										
Investment earnings	14,103	10,769	5,722	7,605	(2,754)	6,379	4,857	7,282	(449)	596
Transfers	(24,020)	(13,994)	(17,083)	(17,426)	(19,249)	(17,103)	(16,405)	(18,705)	(18,344)	(19,077)
Total Business-type Activities	<u>(9,917)</u>	<u>(3,225)</u>	<u>(11,361)</u>	<u>(9,821)</u>	<u>(22,003)</u>	<u>(10,724)</u>	<u>(11,548)</u>	<u>(11,423)</u>	<u>(18,793)</u>	<u>(18,481)</u>
Total Primary Government	<u>\$ 105,336</u>	<u>\$ 96,192</u>	<u>\$ 98,590</u>	<u>\$ 109,693</u>	<u>\$ 86,230</u>	<u>\$ 112,459</u>	<u>\$ 121,147</u>	<u>\$ 130,725</u>	<u>\$ 119,590</u>	<u>\$ 132,938</u>
CHANGE IN NET POSITION										
Governmental Activities	\$ 9,998	\$ (5,401)	\$ 9,885	\$ 49,241	\$ 50,427	\$ 27,893	\$ 50,822	\$ 47,135	\$ 16,298	\$ 19,248
Business-type Activities	(4,504)	41,967	34,121	29,595	20,830	24,895	12,008	12,021	19,455	29,087
Total Primary Government										
Change in Net Position	<u>\$ 5,494</u>	<u>\$ 36,566</u>	<u>\$ 44,006</u>	<u>\$ 78,836</u>	<u>\$ 71,257</u>	<u>\$ 52,788</u>	<u>\$ 62,830</u>	<u>\$ 59,156</u>	<u>\$ 35,753</u>	<u>\$ 48,335</u>

Notes: ¹The Development Services Department was formed in FY15.

Source: Annual Financial Statements, Statement of Activities

CITY OF PALO ALTO
Fund Balances of Governmental Funds (General Fund)
Last Ten Fiscal Years
(Modified accrual basis of accounting)
(Amounts in thousands)

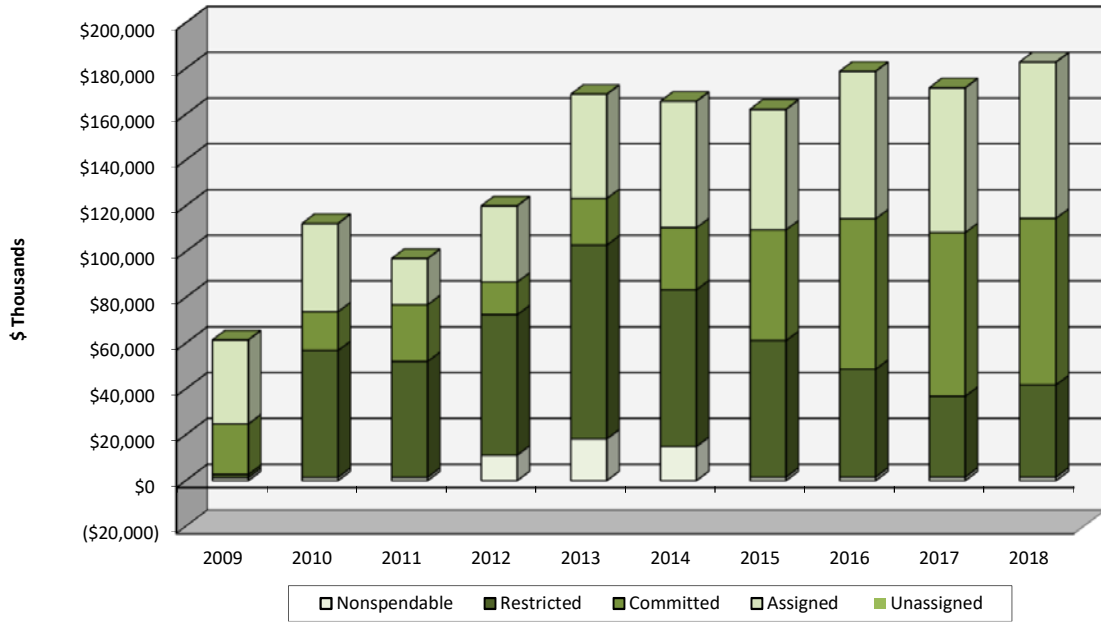


Fiscal Year Ended June 30

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
General Fund										
Nonspendable	\$ 6,476	\$ 6,581	\$ 6,085	\$ 6,007	\$ 5,749	\$ 6,188	\$ 6,296	\$ 7,088	\$ 7,709	\$ 8,049
Committed	-	-	-	-	-	-	-	-	-	\$ 373
Assigned	6,100	7,295	6,235	6,400	5,415	5,432	7,976	8,261	7,280	7,098
Unassigned	30,648	27,581	31,859	29,616	30,913	36,690	48,198	51,582	48,118	52,826
Total General Fund	<u>\$ 43,224</u>	<u>\$ 41,457</u>	<u>\$ 44,179</u>	<u>\$ 42,023</u>	<u>\$ 42,077</u>	<u>\$ 48,310</u>	<u>\$ 62,470</u>	<u>\$ 66,931</u>	<u>\$ 63,107</u>	<u>\$ 68,346</u>

Source: Annual Financial Statements, Balance Sheet

CITY OF PALO ALTO
Fund Balances of Governmental Funds (All Other Governmental Funds)
Last Ten Fiscal Years
(Modified accrual basis of accounting)
(Amounts in thousands)



	Fiscal Year Ended June 30									
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
All Other Governmental Funds										
Nonspendable	\$ 1,308	\$ 1,402	\$ 1,422	\$ 11,112	\$ 18,189	\$ 14,869	\$ 1,468	\$ 1,505	\$ 1,499	\$ 1,498
Restricted	1,412	55,400	50,646	61,324	84,688	68,468	59,650	47,113	35,298	40,317
Committed	22,043	16,962	24,775	14,284	20,400	27,145	48,434	65,745	71,566	72,781
Assigned	36,629	38,538	20,114	33,264	45,514	55,211	52,627	64,411	63,225	68,261
Unassigned	-	-	-	-	-	-	-	-	-	(32)
Total All Other Governmental Funds										
Governmental Funds	<u>\$ 61,392</u>	<u>\$ 112,302</u>	<u>\$ 96,957</u>	<u>\$ 119,984</u>	<u>\$ 168,791</u>	<u>\$ 165,693</u>	<u>\$ 162,179</u>	<u>\$ 178,774</u>	<u>\$ 171,588</u>	<u>\$ 182,825</u>

Source: Annual Financial Statements, Balance Sheet

CITY OF PALO ALTO
Changes in Fund Balances of Governmental Funds
Last Ten Fiscal Years
(Modified accrual basis of accounting)
(Amounts in thousands)

	Fiscal Year Ended June 30									
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenues										
Property tax	\$ 25,432	\$ 25,981	\$ 29,248	\$ 30,216	\$ 32,040	\$ 35,393	\$ 38,836	\$ 41,289	\$ 44,050	\$ 47,242
Sales tax	20,089	17,991	20,746	22,132	25,606	29,424	29,675	30,018	29,923	31,091
Other taxes and fines	24,843	25,063	27,890	29,231	32,141	35,305	41,576	44,909	48,875	53,837
Contributions ³	-	-	-	-	-	-	-	-	-	11,733
Charges for services	19,837	19,775	22,311	46,273	38,976	23,962	25,973	23,910	22,267	26,835
From other agencies	5,984	3,035	1,614	1,116	4,109	5,700	7,727	4,417	5,443	5,392
Permits and licenses	4,033	4,408	5,433	7,136	8,218	8,990	9,179	11,228	10,523	12,786
Interest and rentals	19,183	19,045	16,553	18,583	12,136	18,445	18,658	22,269	15,348	16,288
Other revenue	6,223	4,724	8,624	12,739	17,570	7,471	12,837	13,827	4,985	6,067
Total Revenues	125,624	120,022	132,419	167,426	170,796	164,690	184,461	191,867	181,414	211,271
Expenditures										
Administration ¹	16,002	17,353	8,351	9,412	8,291	9,961	10,806	11,501	13,192	14,721
Public Works	10,064	9,787	11,317	11,304	11,489	12,439	12,276	13,112	14,485	15,426
Planning and Community Environment	10,462	9,480	10,309	11,966	13,474	14,761	8,628	9,722	10,568	10,332
Development Services ²	-	-	-	-	-	-	11,152	10,643	10,908	11,749
Public Safety	48,957	51,022	58,874	62,418	59,537	62,028	61,447	63,784	71,164	73,916
Community Services	17,451	16,451	20,029	20,860	21,661	22,644	23,553	25,511	25,408	29,831
Library	5,985	5,900	6,509	7,072	6,902	7,340	7,980	7,960	8,953	9,120
Non-departmental	10,765	10,149	7,352	6,819	4,567	8,135	6,180	8,068	6,566	7,579
Special revenue and capital projects	21,485	22,006	35,486	29,154	29,542	37,035	41,754	24,457	39,643	40,971
Debt service - principal payments	800	840	870	1,743	1,489	1,524	1,948	7,130	2,066	2,961
Debt service -interest and fiscal fees	416	382	1,815	2,757	2,659	3,196	3,404	4,266	3,032	2,956
Payment to bond refunding escrow	-	-	-	586	540	-	-	-	-	-
Total Expenditures	142,387	143,370	160,912	164,091	160,151	179,063	189,128	186,154	205,985	219,562
Excess (Deficiency) of Revenues										
Over (Under) Expenditures	(16,763)	(23,348)	(28,493)	3,335	10,645	(14,373)	(4,667)	5,713	(24,571)	(8,291)
Other Financing Sources (Uses)										
Issuance of Debt	-	-	-	-	-	-	-	-	-	8,970
Transfers in	39,903	34,835	30,323	47,200	50,343	41,683	45,137	61,835	58,331	56,882
Transfers out	(22,399)	(21,415)	(14,352)	(29,782)	(33,833)	(24,175)	(29,824)	(46,492)	(44,770)	(41,085)
Other	-	-	(101)	-	-	-	-	-	-	-
Proceeds from long term debt	-	59,071	-	3,222	21,706	-	-	-	-	-
Payments to refund bond escrow	-	-	-	(3,104)	-	-	-	-	-	-
Total Other Financing Sources (Uses)	17,504	72,491	15,870	17,536	38,216	17,508	15,313	15,343	13,561	24,767
Net Change in Fund Balances	\$ 741	\$ 49,143	\$ (12,623)	\$ 20,871	\$ 48,861	\$ 3,135	\$ 10,646	\$ 21,056	\$ (11,010)	\$ 16,476
Debt Service as a Percentage of										
Non-Capital Expenditures	1.0%	1.0%	2.2%	3.5%	3.2%	3.3%	3.7%	7.1%	3.1%	3.3%

Notes:

¹Comprised of the following departments: City Council, City Manager, City Attorney, City Clerk, City Auditor, Administrative Services and Human Resources.

²The Development Services Department was formed in FY15.

³Contributions from the Stanford University Medical Center.

Source: Annual Financial Statements, Governmental Funds, Statement of Revenues, Expenditures and Changes in Fund Balances

CITY OF PALO ALTO
Electric Operating Revenue by Source *
Last Ten Fiscal Years
(Amounts in thousands)

Fiscal Year	Residential	Commercial & Industrial	City of Palo Alto	Total
2009	17,939	83,710	2,823	104,472
2010	19,898	89,315	2,890	112,103
2011	19,848	88,076	2,991	110,915
2012	20,328	85,895	3,352	109,575
2013	19,951	86,998	3,265	110,214
2014	18,744	88,419	3,225	110,388
2015	17,404	88,257	3,234	108,895
2016	18,191	86,715	3,127	108,033
2017	20,269	90,635	3,780	114,684
2018	22,764	100,200	4,264	127,228

* The electric operating revenues include sales to customers and city departments, and excludes the sale of surplus energy, utility billing discounts, and bad debt expense.

Top Ten Electric Customers by Revenue¹

Customer (alphabetical order)	Type of Business
529 Bryant Street LLC	Technology
City of Palo Alto	Municipal
Communications & Power Industries (CPI)	Research
Hewlett-Packard Company	Computer
Hewlett-Packard Enterprise	Computer
Space Systems/Loral, LLC	Satellite & Satellite Systems
Stanford Hospital & Clinics	Hospital
Varian Medical Systems, Inc.	Manufacturing
Veterans Administration Hospital	Hospital
VMware, Inc.	Computer

¹The top ten customers accounted for approximately 35.2% of total kWh consumption (317,136,608 kWh) and 31.0% of revenue (\$40,521,589). The largest customer accounted for 8.1% of total kWh consumption and 6.9% of revenue. The smallest customer accounted for 1.9% of total kWh consumption and 1.6% of revenue. Revenue used to determine top ten electric customers includes metered and non-metered charges, adjustments, surcharges and discounts. Revenue does not include Utility Users Tax (UUT) and deposits.

	Number of Customers	Kilowatt-hour Sales (kWh)	Revenue²
Residential	25,502	150,064,098	\$ 22,764
Commercial	3,788	588,217,628	82,299
Industrial	79	141,387,345	17,901
CPA	144	29,780,348	4,264
Total	29,513	909,449,419	\$ 127,228

City of Palo Alto Power Purchase

Western Area Power Administration Hydroelectric	39.3%
Forward Market Purchases	-9.4%
Wind Energy	9.6%
Landfill Gas Energy	11.4%
Solar Energy	36.3%
Northern California Power Agency Hydroelectric	12.4%
Short-Term Market	0.4%

²Revenue includes metered and non-metered charges and revenue adjustments. Revenue does not include California Energy Commission (CEC) surcharges, Utility Users Tax (UUT), Primary Voltage and Rate Assistance (RAP) discounts and deposits. Parts of this schedule are provided as required by the Continuing Disclosure Agreement for the City's Utility Revenue Bond and are not required by Governmental Accounting Standards Board (GASB).

Source: City of Palo Alto, Utilities and Accounting Departments

CITY OF PALO ALTO
Supplemental Disclosure for Water Utilities
Fiscal Year 2018

Top Ten Largest Water Utility Customers (alphabetical order)

City of Palo Alto
Oak Creek Apartments
Palo Alto Hills Golf & Country Club
Palo Alto Unified School District
Simon Property Group
Stanford Hospital & Clinics
Stanford West Management
Veterans Administration Hospital
Vi at Palo Alto
VMware Inc.

The top ten customers total consumption is 867,488 CCF with revenue of \$8,116,799. This amount accounts for approximately 19% of total consumption and 17.6% of total revenue. The largest customer (other than the City of Palo Alto) accounted for 2.4% of consumption and 2.1% of revenue. The smallest customer accounted for 0.8% of consumption and 0.7% of revenue. Revenue used to determine top ten water utility customers includes metered and non-metered charges, adjustments, surcharges and discounts. Revenue does not include Utility Users Tax (UUT) and deposits.

Note: This schedule is provided as required by the Continuing Disclosure Agreement for the City's Utility Revenue Bond and is not required by Governmental Accounting Standards Board (GASB).

Source: City of Palo Alto, Utilities Department

CITY OF PALO ALTO
Supplemental Disclosure for Gas Utilities
Fiscal Year 2018

Top Ten Largest Gas Utility Customers (alphabetical order)

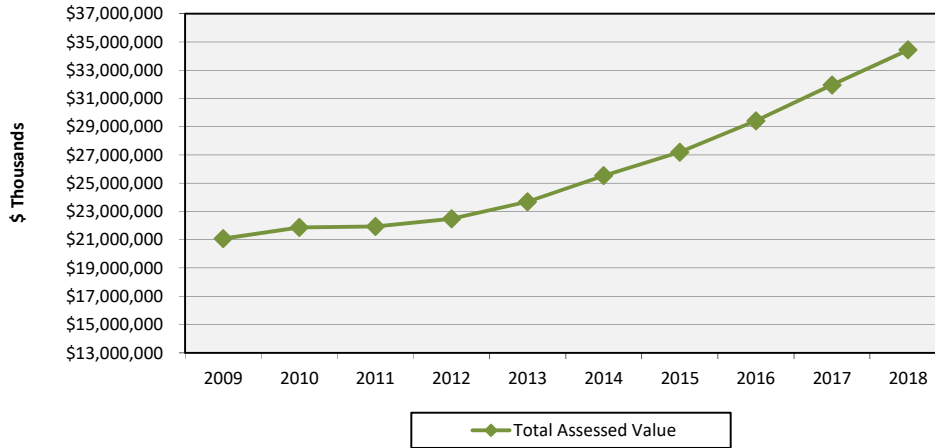
City of Palo Alto
Communications & Power Industries (CPI)
Hewlett Packard
Palo Alto Unified School District
Space Systems/Loral, LLC
Stanford Hospital & Clinics
Stanford School of Medicine
Stanford University
Veterans Administration Hospital
VMware Inc.

The top ten customers total consumption is 6,972,852 THM with revenue of \$7,608,768. This amount accounts for approximately 24.5% of total consumption and 21% of total revenue. The largest customer (other than the City of Palo Alto) accounted for 6.2% of consumption and 5.2% of revenue. The smallest customer accounted for 1.1% of consumption and 1% of revenue.

Note: This schedule is provided as required by the Continuing Disclosure Agreement for the City's Utility Revenue Bond and is not required by Governmental Accounting Standards Board (GASB).

Source: City of Palo Alto, Utilities Department

CITY OF PALO ALTO
Assessed Value of Taxable Property
Last Ten Fiscal Years
(Amounts in thousands)

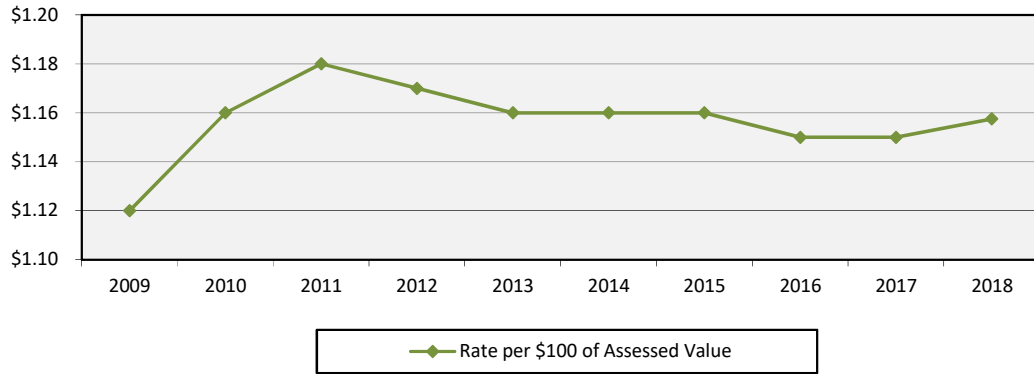


	Fiscal Year Ended June 30									
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Net Local Secured Roll										
Land	\$ 10,420,139	\$ 11,007,650	\$ 11,011,160	\$ 11,352,993	\$ 12,255,515	\$ 13,357,851	\$ 14,409,837	\$ 15,718,665	\$ 17,333,969	\$ 18,770,642
Improvements	10,527,617	10,752,671	10,962,928	11,703,597	12,381,306	12,984,735	13,633,986	14,998,502	16,752,295	18,642,970
Personal property	303,688	288,148	241,280	257,436	287,296	307,499	290,590	310,929	306,576	300,352
	<u>21,251,444</u>	<u>22,048,469</u>	<u>22,215,368</u>	<u>23,314,026</u>	<u>24,924,117</u>	<u>26,650,085</u>	<u>28,334,413</u>	<u>31,028,096</u>	<u>34,392,840</u>	<u>37,713,964</u>
Less:										
Exemptions net of state aid	<u>(1,871,292)</u>	<u>(1,809,119)</u>	<u>(1,757,241)</u>	<u>(2,346,728)</u>	<u>(2,589,653)</u>	<u>(2,610,521)</u>	<u>(2,761,495)</u>	<u>(3,409,836)</u>	<u>(4,244,500)</u>	<u>(5,203,968)</u>
Total Net Local Secured Roll	<u>19,380,152</u>	<u>20,239,350</u>	<u>20,458,127</u>	<u>20,967,298</u>	<u>22,334,464</u>	<u>24,039,564</u>	<u>25,572,918</u>	<u>27,618,260</u>	<u>30,148,340</u>	<u>32,509,996</u>
Public utilities	2,573	2,573	2,573	2,573	2,573	2,573	2,573	2,573	2,573	2,573
Unsecured property	<u>1,702,884</u>	<u>1,638,436</u>	<u>1,495,574</u>	<u>1,516,837</u>	<u>1,355,970</u>	<u>1,493,922</u>	<u>1,622,636</u>	<u>1,794,921</u>	<u>1,803,468</u>	<u>1,922,170</u>
Total Assessed Value	<u>\$ 21,085,609</u>	<u>\$ 21,880,359</u>	<u>\$ 21,956,274</u>	<u>\$ 22,486,708</u>	<u>\$ 23,693,007</u>	<u>\$ 25,536,059</u>	<u>\$ 27,198,127</u>	<u>\$ 29,415,754</u>	<u>\$ 31,954,381</u>	<u>\$ 34,434,739</u>
Total Direct Tax Rate	1%	1%	1%	1%	1%	1%	1%	1%	1%	1%

Note: The State Constitution requires property to be assessed at 100% of the most recent purchase price, plus an increment of no more than 2% annually, plus any local over-rides. These values are considered to be full market values.

Source: County of Santa Clara Assessor's Office

**CITY OF PALO ALTO
Property Tax Rates
All Overlapping Governments
Last Ten Fiscal Years**



Fiscal Year	Basic County Wide Levy	County Retirement Levy	County Hospital G.O. Bond (Measure A) ¹	City Library G.O. Bond (Measure N) ²	Santa Clara Valley Water District	School District	Community College	Midpeninsula Open Space ³	County Affordable Housing Bond (Measure A) ⁴	Total Direct and Overlapping Rates
2009	1.00	0.0388	-	-	0.0061	0.0674	0.0123			1.12
2010	1.00	0.0388	0.0122	-	0.0074	0.0686	0.0322			1.16
2011	1.00	0.0388	0.0095	0.0171	0.0072	0.0751	0.0326			1.18
2012	1.00	0.0388	0.0047	0.0155	0.0064	0.0742	0.0297			1.17
2013	1.00	0.0388	0.0051	0.0129	0.0069	0.0718	0.0287			1.16
2014	1.00	0.0388	0.0035	0.0177	0.0070	0.0655	0.0290			1.16
2015	1.00	0.0388	0.0091	0.0159	0.0065	0.0657	0.0276			1.16
2016	1.00	0.0388	0.0088	0.0148	0.0057	0.0604	0.0240	0.0008		1.15
2017	1.00	0.0388	0.0086	0.0129	0.0086	0.0591	0.0234	0.0006		1.15
2018	1.00	0.0388	0.0082	0.0118	0.0062	0.0570	0.0220	0.0009	0.0127	1.16

Notes: ¹The County General Obligation Bond (Measure A) was passed in 2008 to fund the seismic upgrade of the Santa Clara Valley Medical Center. Rates were first levied for the 2009-10 fiscal year.

²The City of Palo Alto General Obligation Bond (Measure N) was passed in 2008 to fund the construction and renovation of three of the City's libraries. Rates were first levied for the 2010-11 fiscal year.

³The Midpeninsula Regional Open Space District Bond Issue and Property Tax, Measure AA, passed in 2014.

⁴The Santa Clara County Affordable Housing Bond - Measure A 2016 passed on November 8, 2016.

Source: County of Santa Clara, Tax Rates and Information

CITY OF PALO ALTO
Property Tax Levies and Collections
Last Ten Fiscal Years
(Amounts in thousands)

Fiscal Year Ended June 30	Total Tax Levy ¹ for FY	Collected within the Fiscal Year of the Levy		Collections in Subsequent Years ²	Total Collections to Date	
		Amount	Percentage of Levy		Amount	Percentage of Levy
2009	25,432	25,432	100%	-	25,432	100%
2010	25,981	25,981	100%	-	25,981	100%
2011	25,688	25,688	100%	-	25,688	100%
2012	26,494	26,494	100%	-	26,494	100%
2013	28,742	28,742	100%	-	28,742	100%
2014	30,587	30,587	100%	-	30,587	100%
2015	34,117	34,117	100%	-	34,117	100%
2016	36,607	36,607	100%	-	36,607	100%
2017	39,381	39,381	100%	-	39,381	100%
2018	42,839	42,839	100%	-	42,839	100%

Notes: ¹During fiscal year 1995, the County of Santa Clara began providing the City 100% of its tax levy under an agreement which allows the county to keep all interest and delinquency charges collected.

²Effective fiscal year 1994, the City is on the Teeter Plan, under which the County of Santa Clara pays the full tax levy due. All prior delinquent taxes were also received in that fiscal year.

Source: Annual Financial Statements, Government Funds, Statement of Revenues, Expenditures and Changes in Fund Balances.

CITY OF PALO ALTO
Principal Property Taxpayers
Current Year and Nine Years Ago
(Amounts in thousands)

Taxpayer	Fiscal Year 2018			Fiscal Year 2009		
	Taxable Assessed Value	Rank	Percentage of Total Taxable Assessed Value	Taxable Assessed Value	Rank	Percentage of Total Taxable Assessed Value
Leland Stanford Jr. University	\$ 5,119,879	1	14.9%	\$ 3,288,925	1	15.6%
Loral Space & Communications	235,175	2	0.7%	182,172	2	0.9%
Google Inc.	209,211	3	0.6%			
EOSII Palo Alto Technology Center LLC	126,019	4	0.4%			
395 Page Mill LLC	115,984	5	0.3%			
Hudson Embarcadero Place LLC	112,328	6	0.3%			
Hohbach Realty Co. LP	92,081	7	0.3%			
SI 45 LLC	79,554	8	0.2%			
BVK Hamilton Ave LLC	71,754	9	0.2%			
LVBL Ventures LLC	69,744	10	0.2%			
Arden Realty Limited Partnership				109,703	3	0.5%
Whisman Ventures, LLC				102,479	4	0.5%
ECI 2 Bayshore LLC/ECI Hamilton LLC				66,421	5	0.3%
Blackhawk Parent LLC				48,960	6	0.2%
Pacific Hotel Dev Venture LP				42,829	7	0.2%
300 / 400 Hamilton Associates				40,413	8	0.2%
505 Hamilton Avenue Partners LLC				39,355	9	0.2%
Ronald & Ann Williams Charitable Foundation				39,189	10	0.2%
Total	\$ 6,231,729		18.1%	\$ 3,960,446		18.8%

Total City Taxable Assessed Value:

FY 2018	\$ 34,434,739
FY 2009	\$ 21,085,609

Source: California Municipal Statistics, Inc.

CITY OF PALO ALTO
Assessed Valuation and Parcels by Land Use
As of June 30, 2018

	2017-2018					
	Assessed	% of	No. of	% of	No. of	% of
	Valuation¹	Total	Parcels	Total	Taxable	Total
	Valuation¹		Parcels		Parcels	
Non-Residential:						
Agricultural/forest	\$ 32,699,093	0.10 %	49	0.24 %	31	0.15 %
Commercial	1,919,466,847	5.90	458	2.21	455	2.23
Professional/office	4,829,648,560	14.86	550	2.65	530	2.60
Industrial/research & development	2,014,536,745	6.20	232	1.12	231	1.13
Recreational	45,199,508	0.14	14	0.07	12	0.06
Government/social/institutional	81,684,346	0.25	111	0.53	46	0.23
Miscellaneous	<u>7,539,575</u>	<u>0.02</u>	<u>18</u>	<u>0.09</u>	<u>17</u>	<u>0.08</u>
Subtotal Non-Residential	\$ 8,930,774,674	27.47 %	1,432	6.90 %	1,322	6.48 %
Residential:						
Single family residence	\$ 19,059,115,051	58.63 %	15,066	72.54 %	15,019	73.66 %
Condominium/townhouse	2,429,099,115	7.47	3,033	14.60	3,029	14.86
Mobile Home	72,701	0.00	7	0.03	7	0.03
2-4 Residential units	486,523,359	1.50	502	2.42	502	2.46
5+ Residential units	<u>1,426,234,104</u>	<u>4.39</u>	<u>341</u>	<u>1.64</u>	<u>326</u>	<u>1.60</u>
Subtotal Residential	\$ 23,401,044,330	71.98 %	18,949	91.24 %	18,883	92.61 %
Vacant Parcels	\$ 178,176,982	0.55 %	387	1.86 %	184	0.90 %
Total	\$ 32,509,995,986	100 %	20,768	100 %	20,389	100 %

Notes: This schedule is provided as required by the Continuing Disclosure Agreement for the City's General Obligation 2010 and 2013A Bonds and is not required by Governmental Accounting Standards Board (GASB). Therefore, ten years of comparison data is not presented.

¹Local secured assessed valuation, excluding tax-exempt property.

Source: California Municipal Statistics, Inc.

CITY OF PALO ALTO
Per Parcel Assessed Valuation of Single Family Residential
As of June 30, 2018

	No. of Taxable Parcels ¹	2017-2018 Assessed Valuation	Average Assessed Valuation	Median Assessed Valuation
Single Family Residential	15,019	\$19,059,115,051	\$1,269,000	\$923,460

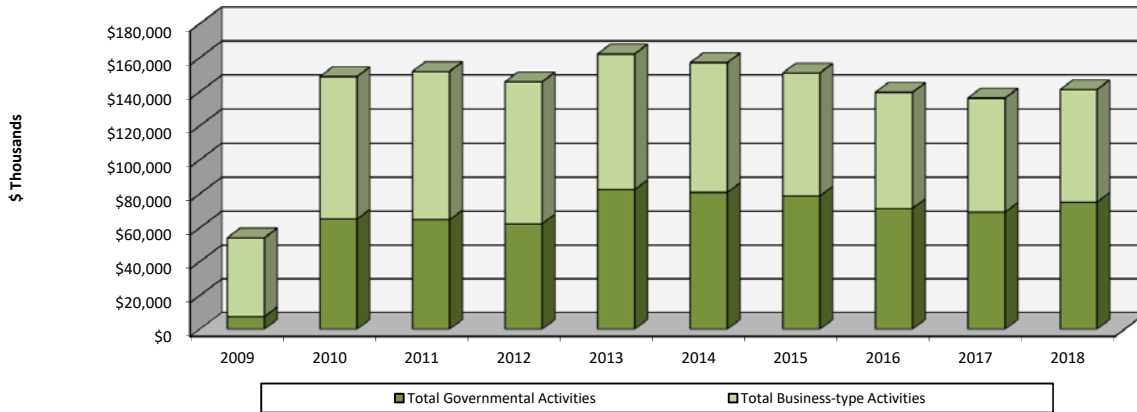
2017-2018 Assessed Valuation	No. of Taxable Parcels ¹	% of Total Parcels	Cumulative % of Total Parcels	Total Valuation	% of Total Valuation	Cumulative % of Total Valuation
\$0-99,999	1,104	7.35	7.35	\$ 88,330,950	0.46	0.46
\$100,000-199,999	1,724	11.48	18.83	239,011,366	1.25	1.72
\$200,000-299,999	788	5.25	24.08	194,789,586	1.02	2.74
\$300,000-399,999	700	4.66	28.74	242,034,889	1.27	4.01
\$400,000-499,999	628	4.18	32.92	282,502,458	1.48	5.49
\$500,000-599,999	678	4.51	37.43	373,803,650	1.96	7.45
\$600,000-699,999	638	4.25	41.68	413,101,443	2.17	9.62
\$700,000-799,999	581	3.87	45.55	434,768,134	2.28	11.90
\$800,000-899,999	529	3.52	49.07	451,055,602	2.37	14.27
\$900,000-999,999	615	4.09	53.17	584,609,797	3.07	17.34
\$1,000,000-1,099,999	557	3.71	56.87	585,596,977	3.07	20.41
\$1,100,000-1,199,999	528	3.52	60.39	606,426,223	3.18	23.59
\$1,200,000-1,299,999	414	2.76	63.15	517,138,530	2.71	26.30
\$1,300,000-1,399,999	440	2.93	66.08	592,647,993	3.11	29.41
\$1,400,000-1,499,999	419	2.79	68.87	607,508,258	3.19	32.60
\$1,500,000-1,599,999	376	2.50	71.37	582,467,595	3.06	35.66
\$1,600,000-1,699,999	390	2.60	73.97	643,233,203	3.37	39.03
\$1,700,000-1,799,999	318	2.12	76.08	556,202,247	2.92	41.95
\$1,800,000-1,899,999	315	2.10	78.18	582,513,341	3.06	45.01
\$1,900,000-1,999,999	264	1.76	79.94	513,482,644	2.69	47.70
\$2,000,000 and greater	3,013	20.06	100.00	9,967,890,165	52.30	100.00
Total	15,019	100.00		\$ 19,059,115,051	100.00	

Notes: This schedule is provided as required by the Continuing Disclosure Agreement for the City's General Obligation 2010 and 2013A Bonds and is not required by Governmental Accounting Standards Board (GASB). Therefore, ten years of comparison data is not presented.

¹Improved single family residential parcels. Excludes condominiums and parcels with multiple family units.

Source: California Municipal Statistics, Inc.

CITY OF PALO ALTO
Ratio of Outstanding Debt by Type
Last Ten Fiscal Years
(Amounts in thousands)



	Fiscal Year Ended June 30									
	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
<u>Governmental Activities</u>										
Certificates of Participation	\$ 7,605	\$ 6,765	\$ 5,895	\$ 1,685	\$ 1,560	\$ 1,430	\$ 1,285	\$ 1,135	\$ 975	\$ 8,970
General Obligation Bonds	-	55,305	55,305	54,540	74,235	73,215	71,795	65,210	63,710	62,140
2011 Lease-Purchase Agreement	-	-	-	2,764	2,400	2,026	1,643	1,248	842	426
Add: unamortized premium	-	3,766	3,640	3,514	4,400	4,242	4,084	3,926	3,768	3,610
Less: unamortized discount/ issuance costs	-	(571)	-	-	-	-	-	-	-	-
Total Governmental Activities	7,605	65,265	64,840	62,503	82,595	80,913	78,807	71,519	69,295	75,146
<u>Business-type Activities</u>										
Utility Revenue Bonds	38,744	72,104	69,551	65,879	63,104	60,224	57,224	54,095	50,825	47,400
Energy Tax Credits	1,300	1,200	1,100	1,000	900	800	700	600	500	400
State Water Resources Loan	9,000	13,080	16,696	15,900	15,109	14,309	13,500	12,681	15,034	17,711
Less: unamortized discount/ issuance costs	(2,479)	(2,737)	(229)	580	543	867	803	737	673	608
Total Business-type Activities	46,565	83,647	87,118	83,359	79,656	76,200	72,227	68,113	67,032	66,119
Total Primary Government Outstanding Debt	\$ 54,170	\$ 148,912	\$ 151,958	\$ 145,862	\$ 162,251	\$ 157,113	\$ 151,034	\$ 139,632	\$ 136,327	\$ 141,265
Percentage of Personal Income ¹	1.53%	4.51%	3.86%	3.36%	3.36%	3.24%	2.94%	2.52%	2.38%	2.33%
Population	64,484	65,408	64,417	65,544	66,368	66,861	66,029	66,968	66,478	66,649
Debt Per Capita	\$ 0.84	\$ 2.28	\$ 2.36	\$ 2.23	\$ 2.44	\$ 2.35	\$ 2.29	\$ 2.09	\$ 2.05	\$ 2.12

Notes: ¹See the schedule of Demographic and Economic Statistics for personal income data. Per capita personal income is only available for Santa Clara County, therefore personal income is the product of the countywide per capita amount and the City's population.

Sources: County of Santa Clara (assessed valuation)
2018 Official City Data Set (population)
California Department of Transportation Long-Term Socio-Economic Forecasts (personal income)
Annual Financial Statements and Note 7 General Long-Term Obligations

CITY OF PALO ALTO
Computation of Direct and Overlapping Debt
As of June 30, 2018

2017-2018 Assessed Valuation

\$ 34,434,739,002

	Total Debt Outstanding	Percentage Applicable to City of Palo Alto¹	Amount Applicable to City of Palo Alto
<u>Direct and Overlapping Tax and Assessment Debt</u>			
Santa Clara County	\$ 1,012,400,000	7.66%	\$ 77,509,344
Foothill-DeAnza Community College District	633,997,978	22.10%	140,145,253
Palo Alto Unified School District	298,433,689	90.08%	268,841,004
Fremont Union High School District	433,280,088	0.01%	43,328
Los Gatos-Saratoga Joint Union High School District	105,845,000	0.01%	12,701
Mountain View-Los Altos Union High School District	52,243,375	0.96%	502,059
Cupertino Union School District	270,528,688	0.02%	45,990
Los Altos School District	57,145,000	1.21%	692,026
Mountain View-Whisman School District	185,455,000	0.75%	1,381,640
Saratoga Union School District	25,833,901	0.03%	6,717
Whisman School District	15,293,173	1.96%	299,593
City of Palo Alto	62,140,000	100%	62,140,000
El Camino Hospital District	127,800,000	0.08%	102,240
Midpeninsula Regional Open Space District	93,350,000	12.97%	12,107,495
City of Palo Alto Special Assessment Bonds	22,370,000	100%	22,370,000
Santa Clara Valley Water District Benefit Assessment District	82,285,000	7.66%	6,299,740
Total Direct and Overlapping Tax and Assessment Debt			<u>592,499,130</u>

Direct and Overlapping General Fund Debt

Santa Clara County General Fund Obligations	590,242,965	7.66%	45,189,001
Santa Clara County Pension Obligations	357,547,175	7.66%	27,373,812
Santa Clara County Board of Education Certificates of Participation	4,985,000	7.66%	381,652
Foothill-DeAnza Community College District Certificates of Participation	28,803,859	22.10%	6,367,093
Los Gatos-Saratoga Joint Union High School District Certificates of Participation	4,424,000	0.01%	531
Mountain View-Los Altos Union High School District Certificates of Participation	1,845,000	0.96%	17,730
Mountain View-Whisman School District Certificates of Participation	32,850,000	0.75%	244,733
Saratoga Union High School District Certificates of Participation	3,905,000	0.03%	1,015
Los Altos School District Certificates of Participation	2,616,389	1.21%	31,684
City of Palo Alto General Fund Obligations	9,395,852	100%	9,395,852
Santa Clara County Vector Control District Certificates of Participation	2,470,000	7.66%	189,103
Midpeninsula Regional Open Space Park District General Fund Obligations	123,040,600	12.97%	15,958,366
Total Gross Direct and Overlapping General Fund Debt			<u>\$ 105,150,572</u>
Less: Santa Clara County supported obligations			<u>31,151,167</u>
Total Net Direct and Overlapping General Fund Debt			<u>\$ 73,999,405</u>
Total Combined Debt			<u>\$ 666,498,535</u>

	Ratio to Assessed Valuation	
Total Direct Debt	0.21%	\$ 71,535,852 ³
Total Overlapping Debt	1.73%	<u>594,962,683</u>
Total Direct and Overlapping Debt	1.94%	<u>\$ 666,498,535</u> ²

Notes: Overlapping debt is the financial obligations of one political jurisdiction that also falls partly on a nearby jurisdiction. The amount of debt of each unit applicable to the reporting unit is arrived at by 1) determining what percentage of the total assessed value of the overlapping jurisdiction lies within the limits of the reporting unit, and 2) applying this percentage to the total debt of the overlapping jurisdiction.

¹Percentage of overlapping agency's assessed valuation located within boundaries of the city.

²Excludes tax and revenue anticipation notes, enterprise revenue, mortgage revenue and tax allocation bonds and non-bonded capital lease obligations.

³Total direct debt excludes any premiums, discounts or other amortization amounts.

Source: California Municipal Statistics, Inc.

CITY OF PALO ALTO
Computation of Legal Bonded Debt Margin
As of June 30, 2018
(Amounts in thousands)

Assessed Valuation:		
Secured property assessed value, net of exempt real property	<u>\$ 34,434,739</u>	
Bonded Debt Limit (3.75% of Assessed Value)¹		<u>1,291,303</u>
Direct Debt:		
Certificates of Participation	8,970	
Lease Purchase Agreement	426	
General Obligation bonds	<u>62,140</u>	
Total Direct Debt³		<u>71,536</u>
Less: Amount of Debt Not Subject to Limit²		<u>9,396</u>
Total Net Debt Applicable to Limit		<u>62,140</u>
Legal Bonded Debt Margin		<u>\$ 1,229,163</u>

Fiscal Year	Total Assessed Value (AV)	Bonded Debt Limit (3.75% of AV)	Total Net Debt Applicable to Limit	Legal Bonded Debt Margin	Population	Total Net Debt Applicable to the Debt as a %	Ratio of Net Debt to Assessed Value	General Bonded Debt Per Capita
2009	21,085,609	790,710	-	790,710	64,484	0.00%	-	0.00
2010	21,880,359	820,513	55,305	765,208	65,408	6.74%	0.0025	0.85
2011	21,956,274	823,360	55,305	768,055	64,417	6.72%	0.0025	0.86
2012	22,486,708	843,252	54,540	788,712	65,544	6.47%	0.0024	0.83
2013	23,693,007	888,488	74,235	814,253	66,368	8.36%	0.0031	1.12
2014	25,536,058	957,602	73,215	884,387	66,861	7.65%	0.0029	1.10
2015	27,198,127	1,019,930	71,795	948,135	66,029	7.04%	0.0026	1.09
2016	29,415,754	1,103,091	65,210	1,037,881	66,968	5.91%	0.0022	0.97
2017	31,954,381	1,198,289	63,710	1,134,579	66,478	5.32%	0.0020	0.96
2018	34,434,739	1,291,303	62,140	1,229,163	66,649	4.81%	0.0018	0.93

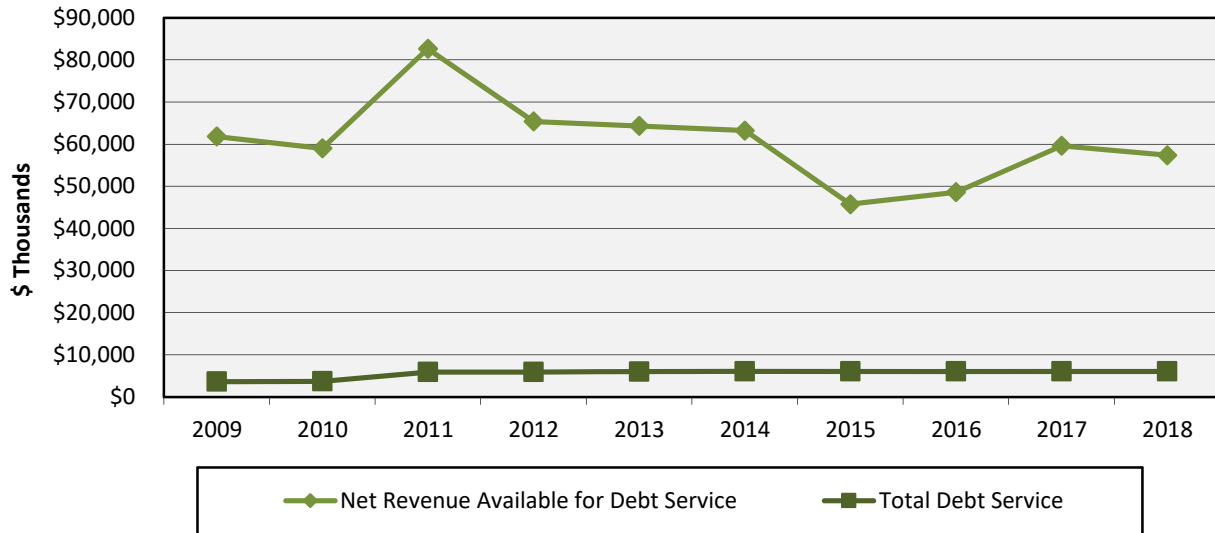
Notes: ¹California Government Code, Section 43605 sets the debt limit at 15% of the assessed value of all real and personal property of the City. Because this Code section was enacted when assessed value was 25% of market value, the limit is calculated at one-fourth, or 3.75%. This legal debt margin applies to General Obligation debt. Prior year limits have been adjusted to conform to the current year methodology.

²In accordance with California Government Code Section 43605, only the City's General Obligation bonds are subject to the legal debt limit of 15%. Enterprise Fund debt is not subject to legal debt margin.

³Total direct debt excludes any premiums, discounts or other amortization amounts.

Source: Annual Financial Statements, Assessed Value of Taxable Property and Note 7 General Long-Term Obligations

CITY OF PALO ALTO
Revenue Bond Coverage
Business-type Activities¹
Last Ten Fiscal Years
(Amounts in thousands)



Fiscal Year	Gross Revenue	Less: Direct Operating Expenses ²	Net Revenue Available for Debt Service	Debt Service			Coverage Ratio
				Principal	Interest ³	Total	
2009	242,693	180,880	61,813	1,590	2,024	3,614	17.10
2010	230,308	171,320	58,988	1,755	1,954	3,709	15.90
2011	234,278	151,641	82,637	2,655	3,261	5,916	13.97
2012	235,160	169,777	65,383	2,945	2,959	5,904	11.07
2013	237,842	173,510	64,332	2,875	3,167	6,042	10.65
2014	239,948	176,718	63,230	2,980	3,073	6,053	10.45
2015	234,025	188,276	45,749	3,100	2,954	6,054	7.56
2016	235,386	186,793	48,593	3,230	2,823	6,053	8.03
2017	264,734	205,102	59,632	3,370	2,678	6,048	9.86
2018	288,610	231,255	57,355	3,525	2,524	6,049	9.48

Notes: ¹Airport, Refuse and Fiber Optics funds have no debt and are therefore excluded from this schedule.

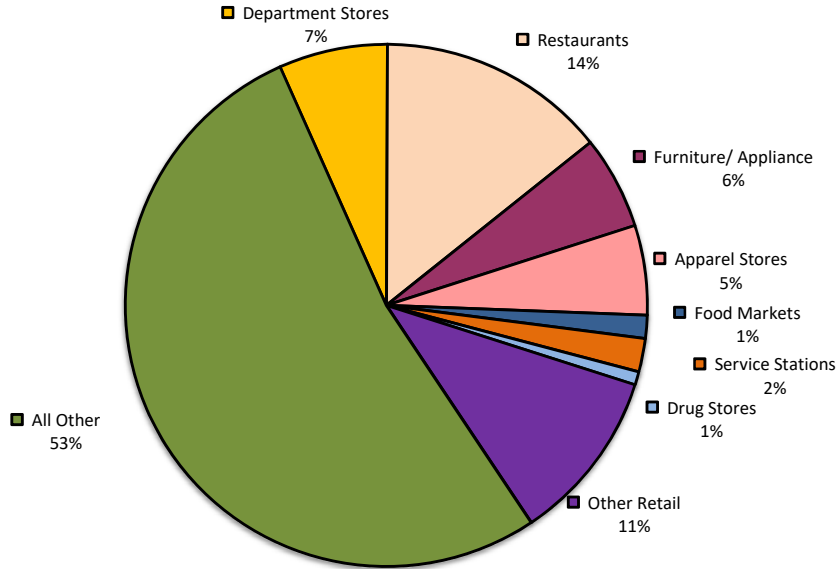
²Excludes depreciation and amortization expense.

³Excludes joint venture debt service and federal interest subsidy.

Source: City of Palo Alto, Accounting Department

**CITY OF PALO ALTO
Taxable Transactions by Type of Business
Last Ten Fiscal Years
(Amounts in thousands)**

Fiscal Year 2018



ECONOMIC SEGMENT

Fiscal Year	Department Stores		Furniture/ Appliance	Apparel Stores	Food Markets	Service Stations	Drug Stores	Other Retail	All Other	Total
	Stores	Restaurants								
2009	2,251	2,443	1,431	1,258	315	493	214	4,284	6,635	19,324
2010	2,215	2,418	1,402	1,254	343	549	219	4,458	5,556	18,414
2011	2,374	2,621	1,564	1,292	381	630	242	4,873	6,322	20,299
2012	2,445	2,937	1,590	1,492	387	722	257	5,049	7,034	21,913
2013	2,478	3,160	1,465	1,656	424	765	259	4,056	13,729	27,992
2014	2,097	3,541	1,555	2,041	392	772	444	4,845	9,890	25,577
2015	2,398	3,894	1,672	1,708	435	699	265	3,674	11,253	25,998
2016	2,250	4,134	1,410	1,694	448	582	257	4,949	12,423	28,147
2017	2,036	4,079	1,513	1,794	542	502	259	3,810	14,325	28,860
2018	2,001	4,224	1,716	1,647	428	614	243	3,184	15,663	29,720

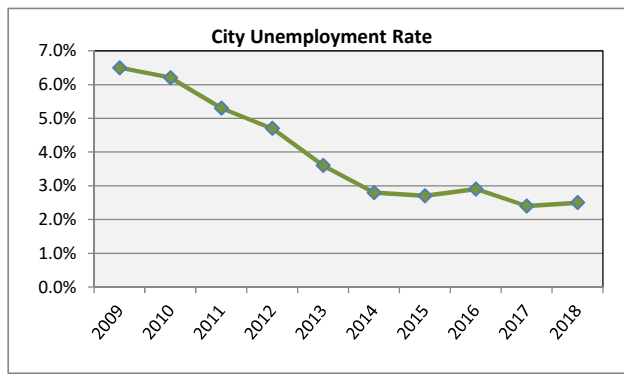
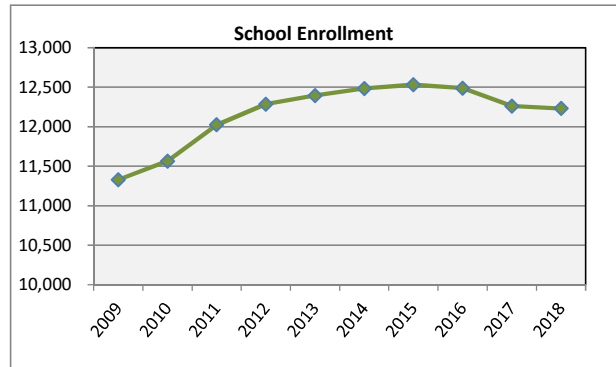
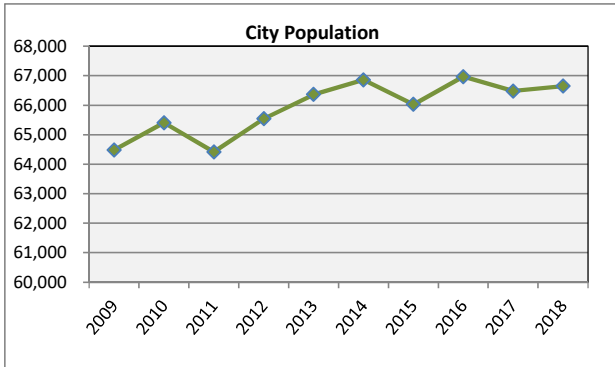
Source: California State Board of Equalization, compiled by MuniServices LLC

Sales Tax Rates for the Fiscal Year ended June 30, 2018

State Rate:	7.25%
Special District Tax Rates:	
Santa Clara County Transit District (SCCT)	0.50%
Santa Clara County Valley Transportation Authority (SCVT)	0.50%
Santa Clara VTA BART Operating and Maintenance Transactions and Use Tax (SVTB)	0.125%
Santa Clara Retail Transactions and Use Tax (SCCR)	0.125%
Santa Clara County Valley Transportation Authority (SCVT)	0.50%
Total Sales and Use Tax Rate:	9.000%

Source: California State Board of Equalization

CITY OF PALO ALTO
Demographic and Economic Statistics
Last Ten Fiscal Years



Fiscal Year	City of Palo Alto Population	City of Palo Alto Unemployment Rate	City of Palo Alto School Enrollment	Santa Clara County Population	City Population as a Percentage of County Population	Santa Clara County Total Personal Income (in thousands)	Santa Clara County Per Capita Personal Income (in thousands)
2009	64,484	6.5%	11,329	1,857,621	3.47%	101,800,000	54,801
2010	65,408	6.2%	11,565	1,880,876	3.48%	95,000,000	50,508
2011	64,417	5.3%	12,024	1,786,443	3.61%	109,300,000 *	61,183 *
2012	65,544	4.7%	12,286	1,813,860	3.61%	120,100,000 *	66,212 *
2013	66,368	3.6%	12,396	1,840,218	3.61%	134,000,000 *	72,817 *
2014	66,861	2.8%	12,483	1,866,208	3.58%	135,200,000 *	72,446 *
2015	66,029	2.7%	12,532	1,890,929	3.49%	147,300,000 *	77,898 *
2016	66,968	2.9%	12,488	1,915,102	3.50%	158,700,000 *	82,868 *
2017	66,478	2.4%	12,261	1,930,215	3.44%	166,600,000	86,312
2018	66,649	2.5%	12,230	1,948,176	3.42%	177,600,000	91,162

Note: Data on personal income and per capita personal income is only available for Santa Clara County.

Source: Beginning in 2015 population is sourced from the US Census Bureau Community Survey (via the City of Palo Alto's Official City Data Set).
 State of California Employment Development Office (unemployment rate)
 Palo Alto Unified School District (school enrollment)

* California Department of Transportation Long-Term Socio-Economic Forecasts (personal income). Forecasts from prior years are updated annually.

CITY OF PALO ALTO
Principal Employers
Current Year and Nine Years Ago

Employer	FY 2018¹			FY 2009		
	Number of Employees	Rank	Percentage of Total City Employment	Number of Employees	Rank	Percentage of Total City Employment
Stanford Health Care	5,500	1	4.2%	5,025	2	7.8%
Lucile Packard Children's Hospital	5,400	2	4.1%	3,326	4	5.2%
Stanford University ²	4,300	3	3.3%	9,821	1	15.2%
Veteran's Affairs Palo Alto Health Care System	3,900	4	3.0%	3,500	3	5.4%
VMware Inc.	3,500	5	2.7%			
SAP Labs Inc.	3,500	6	2.7%			
Space Systems/Loral	2,800	7	2.1%	1,700	7	2.6%
Hewlett-Packard Company	2,500	8	1.9%	2,001	5	3.1%
Palo Alto Medical Foundation	2,200	9	1.7%	2,000	6	3.1%
Varian Medical Systems	1,400	10	1.1%			
Wilson Sonsini Goodrich & Rosati				1,500	8	2.3%
Palo Alto Unified School District				1,304	9	2.0%
City of Palo Alto				1,100	10	1.7%
Total	35,000		26.8%	31,277		48.5%

Estimated Total City Day Population:

FY 2018	130,443
FY 2008	64,484

Notes: ¹Available data sources are limited and may be unreliable. The City does not affirm the validity of this data. 2018 numbers are rounded. Figures may include employees not located within City limits.

²Stanford University number of employees was provided by the Stanford Office of Planning in FY17 and includes only employees located in Palo Alto.

Source: 2018 Official City Data Set (total City day population); AtoZ databases; Stanford website, Stanford Planning Office.

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CITY OF PALO ALTO
Operating Indicators by Function/Program
Last Ten Fiscal Years¹

FUNCTIONS/PROGRAMS	Fiscal Year Ended June 30			
	2008	2009	2010	2011
<u>Governmental activities</u>				
Community Services				
Number of theater performances	166	159	174	175
Total hours of athletic field usage ²	63,212	45,762	41,705	42,687
Number of rounds of golf	74,630	72,170	69,791	67,381
Enrollment in recreation classes (includes summer camps)	13,851	13,091	12,880	12,310
Planning and Community Environment				
Planning applications completed	257	273	226	238
Building permits issued	3,046	2,543	2,847	3,559
Caltrain average weekday boarding ³	4,589	4,407	4,359	4,923
Police				
Calls for service	58,742	53,275	55,860	52,159
Total arrests	3,253	2,612	2,451	2,288
Parking citations issued	50,706	49,996	42,591	40,426
Animal Services				
Number of service calls	3,059	2,873	2,692	2,804
Number of animals handled	3,532	3,422	3,147	3,323
Fire				
Calls for service	7,723	7,549	7,468	7,555
Number of fire incidents	192	239	182	165
Number of fire inspections ⁴	1,277	1,028	1,526	1,807
Library				
Total number of cardholders	53,740	54,878	51,969	53,246
Total number of items in collection	279,403	293,735	298,667	314,101
Total checkouts	1,542,116	1,633,955	1,624,785	1,476,648
Public Works				
Street resurfacing (lane miles)	27	23	32	29
Number of potholes repaired	1,977	3,727	3,149	2,986
Sq. ft. of sidewalk replaced or permanently repaired	83,827	56,909	54,602	71,174
Number of trees planted	188	250	201	150
Tons of materials recycled or composted	52,196	49,911	48,811	56,586
<u>Business-type activities</u>				
Electric				
Number of customer accounts	29,024	28,527	29,430	29,708
Residential MWH consumed	162,680	159,899	163,098	160,318
Gas				
Number of customer accounts	23,502	23,090	23,724	23,816
Residential therms consumed	11,969,151	11,003,088	11,394,712	11,476,609
Water				
Number of customer accounts	19,942	19,422	20,134	20,248
Residential water consumption (CCF)	2,746,980	2,566,962	2,415,467	2,442,415
Wastewater collection				
Number of customer accounts	21,970	22,210	22,231	22,320
Millions of gallons processed	8,510	7,958	8,184	8,652

Notes: ¹Ten most recent years available.

²According to the department, this measure was not accurately tracked during FY13 or FY14.

³Prior-year data has been updated based on annual counts revised by Caltrain. Beginning 2015, data source is Official City Data Set.

⁴The method for calculating the number of fire inspections changed in FY17. The department now uses a more detailed feature which categorizes inspections by type and location.

Source: City of Palo Alto Performance Report (formerly the Service Efforts and Accomplishments Report); 2017 Official City Data Set (Caltrain)

Fiscal Year Ended June 30

2012	2013	2014	2015	2016	2017
175	184	108	172	161	171
44,226	-	-	47,504	65,723	82,526
65,653	60,153	46,527	42,048	42,573	-
11,703	11,598	11,997	12,586	12,974	11,649
204	307	310	335	383	365
3,320	3,682	3,624	3,844	3,492	2,970
5,730	6,763	7,564	8,294	9,622	9,994
51,086	54,628	58,559	59,795	53,870	53,901
2,212	2,274	2,589	3,273	2,988	2,745
41,875	43,877	36,551	41,412	37,624	33,661
3,051	2,909	2,398	2,013	2,421	2,399
3,379	2,675	2,480	2,143	2,184	2,211
7,796	7,904	7,829	8,548	8,882	9,056
186	150	150	135	150	155
1,654	2,069	1,741	1,964	2,806	5,476
60,283	51,007	46,950	51,792	57,307	54,676
306,160	277,749	361,103	429,460	461,292	427,548
1,559,932	1,512,975	1,364,872	1,499,406	1,400,926	1,524,614
40	36	36	31	39	39
3,047	2,726	3,418	2,487	3,435	3,449
72,787	82,118	74,051	120,776	115,293	17,275
143	245	148	305	387	319
51,725	47,941	49,594	50,546	56,438	60,582
29,545	29,299	29,338	29,065	29,304	29,616
160,604	156,411	153,190	145,284	150,112	148,986
23,915	23,659	23,592	23,461	23,467	23,637
11,522,999	10,834,793	10,253,776	8,537,754	9,535,377	10,233,669
20,317	20,043	20,037	20,061	19,994	20,213
2,513,595	2,521,930	2,496,549	2,052,176	1,696,383	1,856,879
22,421	22,152	22,105	21,990	22,016	22,216
8,130	7,546	7,186	6,512	6,387	7,176

CITY OF PALO ALTO
Capital Asset Statistics by Function/Program
Last Ten Fiscal Years

FUNCTION/PROGRAM	Fiscal Year Ended June 30				
	2009	2010	2011	2012	2013
Public Safety					
Fire:					
Fire Stations Operated	8	8	8	7	7
Police:					
Police Stations	1	1	1	1	1
Police Patrol Vehicles	30	30	30	30	30
Community Services					
Acres - Downtown/Urban Parks ²	157	157	157	157	157
Acres - Open Space ²	3,744	3,744	3,744	3,744	3,744
Acres - Parks and Preserves ²	-	-	-	-	-
Acres - Open Space ²	-	-	-	-	-
Acres - Municipal Golf Course ²	-	-	-	-	-
Parks and Preserves	36	36	36	36	36
Golf Course (see above for acreage)	1	1	1	1	1
Tennis Courts	51	51	51	51	51
Athletic Center	4	4	4	4	4
Community Centers	4	4	4	4	4
Theaters	3	3	3	3	3
Cultural Center/Art Center	1	1	1	1	1
Junior Museum and Zoo	1	1	1	1	1
Swimming Pools	1	1	1	1	1
Nature Center	3	3	3	3	3
Libraries					
Libraries	5	5	5	5	5
Public Works:					
Number of Trees Maintained ³	32,007	32,007	31,993	31,890	31,923
Electric Utility¹					
Miles of Overhead Lines	193	193	193	223	222
Miles of Underground Lines	253	253	253	245	246
Water Utility					
Miles of Water Mains	214	214	214	234	233
Gas Utility					
Miles of Gas Mains	207	205	205	210	210
Waste Water					
Miles of Sanitary Sewer Lines	207	207	207	217	217

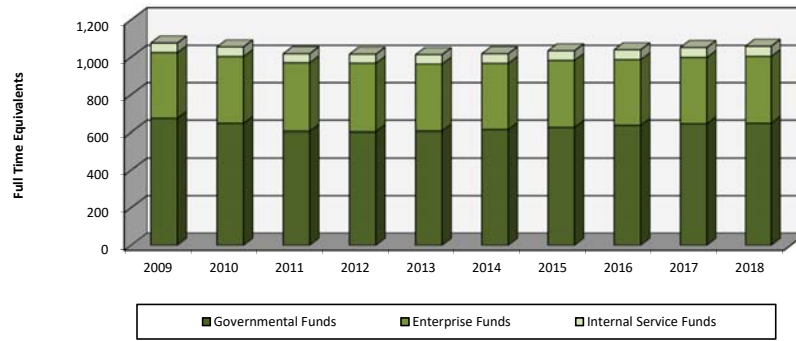
Note: ¹The City of Palo Alto Utilities Department recently completed the conversion of its electric system maps to a GIS mapping system database. Therefore, the distances reported for FY 11/12 and forward are more accurate than the distances reported in previous years.
²Beginning in 2016 park acreage is sourced from the Official City Data Set. The discrepancy between FY16 and FY17 is because FY16 numbers were derived off GIS parcels identified as parks or zoned in the Open Space Zoning District. For FY17, Council approved Parks Master Plan numbers were used.
³Due to an error in the beginning balance, the number of trees maintained was adjusted for all prior years in FY18.

Source: City of Palo Alto

Fiscal Year Ended June 30

2014	2015	2016	2017	2018
7	7	7	7	7
1	1	1	1	1
30	30	30	30	30
157	157	-	-	-
3,744	3,752	-	-	-
-	-	3,921	174	174
-	-	4,489	4,030	4,030
-	-	-	181	181
36	36	36	36	36
1	1	1	1	1
51	51	51	51	51
4	4	4	4	4
4	4	4	4	4
3	3	3	3	3
1	1	1	1	1
1	1	1	1	1
1	1	1	1	1
3	3	3	3	3
5	5	5	5	5
31,757	31,652	31,699	31,712	31,849
223	223	222	223	222
249	262	268	264	272
236	236	235	236	236
214	211	209	210	210
217	217	216	216	216

CITY OF PALO ALTO
Full-Time Equivalent City Government Employees by Function
Last Ten Fiscal Years



Full Time Equivalent Employees as of June 30

	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	
Governmental Funds											
General Fund:											
Administrative		98	89	83	83	85	83	84	86	87	89
Community Services		97	94	74	74	74	74	76	77	78	79
Development Services ⁶		-	-	-	-	-	-	38	38	36	36
Fire		127	123	121	122	119	116	107	107	109	109
Library		44	42	41	41	41	42	44	48	48	48
Office of Emergency Services ⁵		-	-	-	-	-	3	3	3	3	3
Planning and Community Environment ⁶		53	49	44	43	48	49	28	31	32	30
Police		164	161	157	157	154	155	155	155	155	155
Public Works ¹		69	64	59	56	57	56	53	54	56	55
Subtotal General Fund		652	622	579	576	578	578	588	599	604	604
All Other Funds:											
Capital Projects Fund		21	24	24	24	26	27	27	28	31	34
Special Revenue Fund		1	1	2	2	2	9	10	9	10	9
Total Governmental Funds		674	647	605	602	606	614	625	636	645	647
Enterprise Funds											
Public Works ²		113	115	115	115	104	99	100	95	99	101
Utilities ³		238	242	251	251	254	255	258	256	255	257
External Services ⁴		-	-	-	-	-	-	-	-	-	-
Total Enterprise Funds		351	357	366	366	358	354	358	351	354	358
Internal Service Funds											
Printing and Mailing		4	4	2	2	2	2	2	2	2	2
Technology		31	31	30	30	31	32	32	34	35	36
Vehicle Replacement		16	16	16	16	17	17	17	17	16	16
Total Internal Service Funds		51	51	48	48	50	51	51	53	53	54
Total		1,076	1,055	1,019	1,016	1,014	1,019	1,034	1,040	1,052	1,059

Notes: ¹Fleet and Facilities Management

²Refuse, Storm Drainage, Wastewater Treatment

³Electric, Gas, Wastewater Collection, Water

⁴In 2009, External Services was dissolved. 5 FTEs were eliminated and 1 FTE was transferred to the Technology Fund.

⁵In 2014, emergency services and disaster preparation activities have been removed from the Fire Department and are now shown in newly created Office of Emergency Services.

⁶In FY15, staff was moved from Planning and Community Environment (PC&E), Public Works and Fire to create Development Services.

Numbers adjusted for rounding purposes.

Source: City of Palo Alto - Fiscal Year 2017 Adopted Operating Budget

CITY OF PALO ALTO
Index to the Single Audit Report
For the Year Ended June 30, 2018

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**Independent Auditor's Report on Internal Control Over Financial Reporting
and on Compliance and Other Matters Based on an Audit of Financial
Statements Performed in Accordance With *Government Auditing Standards***

Honorable Mayor and the Members
of the City Council of the City of Palo Alto
Palo Alto, California

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Palo Alto, California (City), as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the City's basic financial statements and have issued our report thereon dated November 15, 2018.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the City's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control. Accordingly, we do not express an opinion on the effectiveness of the City's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. 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.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify a certain deficiency in internal control, described in the accompanying schedule of findings and questioned costs as item 2018-001 that we consider to be a significant deficiency.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

City's Response to Finding

The City's response to the finding identified in our audit is described in the accompanying schedule of findings and questioned costs. The City's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Macias Gini & O'Connell LLP

Walnut Creek, California
November 19, 2018



Independent Auditor’s Report on Compliance for Each Major Federal Program and on Internal Control Over Compliance Required by the Uniform Guidance

Honorable Mayor and the Members
of the City Council of the City of Palo Alto
Palo Alto, California

Report on Compliance for Each Major Federal Program

We have audited the City of Palo Alto’s, California (City) compliance with the types of compliance requirements described in the *OMB Compliance Supplement* that could have a direct and material effect on the City’s major federal program for the year ended June 30, 2018. The City’s major federal program is identified in the summary of auditor’s results section of the accompanying schedule of findings and questioned costs.

Management’s Responsibility

Management is responsible for compliance with federal statutes, regulations, and the terms and conditions of its federal awards applicable to its federal programs.

Auditor’s Responsibility

Our responsibility is to express an opinion on compliance for the City’s major federal program based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and the audit requirements of Title 2 U.S. *Code of Federal Regulations* Part 200, *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards* (Uniform Guidance). Those standards and the Uniform Guidance require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City’s compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for the major federal program. However, our audit does not provide a legal determination of the City’s compliance.

Opinion on Each Major Federal Program

In our opinion, the City of Palo Alto, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2018.

Report on Internal Control Over Compliance

Management of the City is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the City's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with the Uniform Guidance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of the Uniform Guidance. Accordingly, this report is not suitable for any other purpose.

Macias Gini & O'Connell LLP

Walnut Creek, California
November 19, 2018

CITY OF PALO ALTO
Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2018

Grantor/Pass-Through Grantor/Program Title	Grantor Identifying Number	Federal CFDA Number	Expenditures	Subrecipients Expenditures
U.S. Department of Housing and Urban Development				
<i>Direct</i>				
CDBG - Entitlement Grants Cluster	B-14-MC-06-0020			
Community Development Block Grants/Entitlement Grants	B-15-MC-06-0020			
	B-16-MC-06-0020	14.218	\$ 579,856	\$ 497,396
U.S. Department of Justice				
<i>Direct</i>				
Bulletproof Vest Partnership	n/a	16.607	12,391	-
U.S. Department of Transportation				
<i>Direct</i>				
Public Transportation Research, Technical Assistance and Training	CA-2017-020-00	20.514	42,374	-
Airport Improvement Program	3-06-0182-010-2015 3-06-0182-011-2016, 3-06-0182-012-2016, 3-06-0182-013-2017	20.106	9,340,267	-
<i>Subtotal - Direct Awards</i>			<u>9,382,641</u>	<u>-</u>
<i>Pass-through from State of California Department of Transportation</i>				
Highway Planning and Construction	BRLS-5100(017)	20.205	132,623	-
Total U.S. Department of Transportation			<u>9,515,264</u>	<u>-</u>
National Endowment for the Humanities				
<i>Pass-through from California State Library</i>				
Museums for America	MA-10-17-0327-17	45.301	10,937	
	MA-11-15-0104-15	45.301	8,324	-
Total National Endowment for the Humanities			<u>19,261</u>	<u>-</u>
U.S. Department of Homeland Security				
<i>Pass-through from State of California Department of Transportation</i>				
Emergency Management Performance Grants	085-00000-2017-0007	97.042	2,600	-
TOTAL FEDERAL FINANCIAL AWARDS			<u>\$ 10,129,372</u>	<u>\$ 497,396</u>

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CITY OF PALO ALTO
Notes to the Schedule of Expenditures of Federal Awards
For the Year Ended June 30, 2018

NOTE 1 – REPORTING ENTITY

The schedule of expenditures of federal awards (the Schedule) includes expenditures of federal awards for the City of Palo Alto, California (City), and its component unit as disclosed in the notes to the basic financial statements.

NOTE 2 – BASIS OF ACCOUNTING

Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of measurement focus applied. All governmental funds are accounted for using the modified accrual basis of accounting. All proprietary funds are accounted for using the accrual basis of accounting. Expenditures of federal awards reported in the Schedule are recognized when incurred and all eligibility requirements have been met. Such expenditures are recognized following the cost principles contained in 2 CFR 200, Subpart E (Cost Principles), wherein certain types of expenditures are not allowable or are limited as to reimbursement. The City did not elect to use the 10% de minimis cost rate as covered in 2 CFR 200.414(F&A) costs.

NOTE 3 – DIRECT AND INDIRECT (PASS-THROUGH) FEDERAL AWARDS

Federal awards may be granted directly to the City by a federal granting agency or may be granted to other government agencies which pass-through federal awards to the City. The Schedule includes both of these types of federal award programs when they occur.

NOTE 4 – RELATIONSHIP TO FEDERAL FINANCIAL REPORTS

Amounts reported in the Schedule agree to or can be reconciled with the amounts reported in the related federal financial reports.

NOTE 5 – RELATIONSHIP TO BASIC FINANCIAL STATEMENTS

Federal awards and expenditures agree to or can be reconciled with the amounts reported in the City's basic financial statements.

CITY OF PALO ALTO

Schedule of Findings and Questioned Costs

For the Year Ended June 30, 2018

Section I - Summary of Auditor's Results

Financial Statements

Type of auditor's report issued on the basic financial statements of the City:	Unmodified
Internal control over financial reporting:	
◆ Material weakness(es) identified?	No
◆ Significant deficiency(ies) identified?	Yes
Noncompliance material to the financial statements noted?	No

Federal Awards

Internal control over major programs:	
◆ Material weakness(es) identified?	No
◆ Significant deficiency(ies) identified?	None reported
Type of auditor's report issued on compliance for major programs:	Unmodified
Any audit findings disclosed that are required to be reported in accordance with Uniform Guidance?	No
Identification of Major Programs:	CFDA No. 20.106 - Airport Improvement Program
Dollar threshold used to distinguish between type A and type B programs:	\$750,000
Auditee qualified as a low-risk auditee?	No

CITY OF PALO ALTO

Schedule of Findings and Questioned Costs

For the Year Ended June 30, 2018

Section II – Financial Statements Findings

**Item 2018-001 Significant Deficiency
Internal Controls over Financial Reporting**

Effective March 20, 2017, the City and the State Water Resources Control Board (SWRCB) entered into an agreement to award the City up to \$30 million from its Clean Water State Revolving Fund for the Sludge Dewatering and Loadout Facility project. The SWRCB loan is to be repaid over 30 years at a rate of 1.8%, with the first annual installment due on May 31, 2020. In September 2017, due to the projected lower project costs, the agreement was amended to reduce the SWRCB loan amount to \$29.7 million. Under the terms of the agreement, \$4 million of the SWRCB loan is a federal pass through grant from the U.S. Environmental Protection Agency under its Capitalization Grants for Clean Water State Revolving Funds program.

On August 4, 2018, the City received a letter from the SWRCB explaining the status of the SWRCB loan and the federal pass through grant. The letter clarified the funding sources and summarized the project draws through the date of the letter. Based on the information provided in the SWRCB letter, we observed the following two issues:

1. The SWRCB letter on August 4, 2018 clarified that the project costs included in the first two draws submitted to SWRCB were applied to the federal awards first, before applying them to State funding sources. Therefore, an adjustment of \$4,000,000 was necessary to reduce the SWRCB loan balance and recognize grant revenue for the year ended June 30, 2018.
2. The City incurred eligible project costs of \$4,964,775 during the year ended June 30, 2018 and submitted the loan draws subsequent to year end. Accordingly, the City accrued draws made in July and August as a receivable from the SWRCB and as an obligation for SWRCB loan payable. The draws for the \$4,964,775 were not made by June 30, 2018, therefore City does not owe that amount to SWRCB as of year-end and overstated its obligation for the SWRCB loan. An audit adjustment of \$4,964,775 was necessary to reduce the SWRCB loan balance at June 30, 2018 and reduce receivables from the SWRCB to properly account for the loan.

We recommend the City document the important terms and conditions of the SWRCB loan, to ensure proper internal controls over the financial reporting and compliance. The City's Finance department should also collaborate with other departments that have material or complex transactions to strengthen internal controls over financial reporting and compliance.

Management Response

The City concurs with the finding and recommendation. City Staff will update the year-end closing processes and procedures to ensure that all material transactions and balances are properly reflected in the financial statements in conformance with Generally Accepted Accounting Principles (GAAP) and the terms and conditions of the loan.

Section III - Federal Award Findings and Questioned Costs

No current year findings are reported.



ADMINISTRATIVE SERVICES

CITY OF
**PALO
ALTO**

250 Hamilton Avenue, 4th Floor
Palo Alto, CA 94301
650.329.2692

**CITY OF PALO ALTO
Schedule of Prior Year Finding and Questioned Costs
For the Year Ended June 30, 2018**

Reference Number:	2017-001
Federal Agency:	U.S. Department of Transportation
Federal Program Title:	Highway Planning and Construction
Federal Catalog Number:	20.205
Pass-through Agency:	State of California Department of Transportation
Federal Grant Number and Year:	BRLS-5100-017 and 2015
Category of Finding:	Procurement, Suspension and Debarment
Classification of Findings:	Significant Deficiency in Internal Control over Compliance

Audit Finding: During the testing of contracts for procurement, suspension and debarment for the HPC program for the period of July 1, 2016 to June 30, 2017, a contract was selected where the City did not verify the suspension and debarment status of the contractor before entering into the contract. As a result, the City is at risk that federal funds could be remitted to a vendor that is suspended or debarred.

Recommendation: It was recommended that the City's Public Works department evaluate its existing procedures and policies in place to ensure it includes all compliance requirements from federal statutes, regulations and terms and conditions of the grants, including verification that contractors paid with federal funds are not suspended or debarred.

Status: Corrective action plan has been implemented.



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ADMINISTRATIVE SERVICES

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CITY OF PALO ALTO
Schedule of Prior Year Finding and Questioned Costs
For the Year Ended June 30, 2018

Reference Number: 2017-002
Federal Agency: U.S. Department of Transportation
Federal Program Title: Highway Planning and Construction
Federal Catalog Number: 20.205
Pass-through Agency: State of California Department of Transportation
Federal Grant Number and Year: STPL-5100-022 and 2017
Category of Finding: Wage Rate Requirements
Classification of Findings: Material Weakness in Internal Control over Compliance
Material Noncompliance

Audit Finding: During the testing of the City's compliance with the wage rate requirements of the HPC program for the period of July 1, 2016 to June 30, 2017, a statistically valid sample of four certified payrolls in a population of twelve certified payrolls was selected and no exceptions were noted. However, it was noted that the City only obtained certified payrolls for the month of July 2016, while the project's duration for construction activities occurred from May 23, 2016 through November 30, 2016. As a result, the City is at risk that federal funds could be remitted to a contractor or subcontractor that does not comply with the wage rate requirements.

Recommendation: It was recommended that the City's Public Works department establish internal control procedures ensuring the City develop a mechanism to ensure that all certified payrolls/statements of non-performance are received and reviewed by the City before release of payment to contractors occurs. This will ensure that federally-funded disbursements were made for allowable activities throughout the service period.

Status: Corrective action plan has been implemented.





ADMINISTRATIVE SERVICES

**CITY OF
PALO
ALTO**

250 Hamilton Avenue, 4th Floor
Palo Alto, CA 94301
650 329 2692

**CITY OF PALO ALTO
Schedule of Prior Year Finding and Questioned Costs
For the Year Ended June 30, 2018**

Reference Number: 2017-003
Federal Agency: Environmental Protection Agency
Federal Program Title: Capitalization Grants for Clean Water State Revolving Funds
Federal Catalog Number: 66.458
Pass-through Agency: California State Water Resources Control Board
Federal Grant Number and Year: D16-01034 and 2017
Category of Finding: Wage Rate Requirements
Classification of Findings: Significant Deficiency in Internal Control over Compliance

Program Identification: United States Environmental Protection Agency
Passed Through California State Water Resources Control Board
CFDA No. 66.458 – Capitalization Grants for Clean Water State
Revolving Funds

Audit Finding: During the testing of the City’s compliance with the wage rate requirements of the City’s Capitalization Grants for Clean Water State Revolving Funds program for the period of July 1, 2016 to June 30, 2017, a statistically valid sample of four certified payrolls in a population of seven certified payrolls was selected and it was noted that the City did not have procedures in place to obtain documentation from the construction management company that all certified payrolls were collected and reviewed. The City occasionally checks the California State Department of Industrial Relations website to ensure that the certified payrolls were submitted. However, no record was maintained. As a result, the City is at risk that federal funds could be remitted to a contractor or subcontractor that does not comply with the wage rate requirements.

Recommendation: It was recommended that the City modify the existing procedures to obtain documentation from the construction management company and retain record of the verification of certified payroll to the California State Department of Industrial Relations, to substantiate the compliance of the contractors and subcontractors before release of payment to contractors occurs.

Status: Corrective action plan has been implemented.



CityOfPaloAlto.org

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Americans with Disabilities Act Statement



IN COMPLIANCE WITH
AMERICANS WITH DISABILITIES ACT (ADA) OF 1990,
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For information contact:
ADA Coordinator
City of Palo Alto
250 Hamilton Ave
(650) 329-2550
ADA@cityofpaloalto.org

Spanish explorers named the area for the tall, twin-trunked redwood tree they camped beneath in 1769. Palo Alto incorporated in 1894 and the State of California granted its first charter in 1909. The City has long been known for its innovative people and its exploration of ideas that have changed the world. In Palo Alto, our history has always been about the future.

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APPENDIX C
INVESTMENT POLICY OF THE CITY

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CITY OF PALO ALTO
Investment Policy
Fiscal Year 2018-19
(Adopted November 6, 2018)

INTRODUCTION

The City of Palo Alto invests its pooled idle cash according to State of California law and the charter of the City of Palo Alto. In particular, the City follows “The Prudent Investor Standard” cited in the State Government Code (Section 53600.3). Under this standard, all governing bodies of local agencies or persons authorized to make investment decisions on behalf of the City are trustees and therefore fiduciaries subject to the prudent investor standard. When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency.

INVESTMENT PHILOSOPHY

The basic principles underlying Palo Alto's investment philosophy is to ensure the safety of public funds; provide that sufficient money is always available to meet current expenditures; and achieve a reasonable rate of return on its investments.

The City's preferred and chief practice is to buy securities and to hold them to their date of maturity rather than to trade or sell securities prior to maturity. The City may, however, elect to sell a security prior to its maturity should there be a significant financial need. If securities are purchased and held to their maturity date, then any changes in the market value of those securities during their life will have no effect on their principal value. Under a buy and hold philosophy, the City is able to protect its invested principal. The economy, the money markets, and various financial institutions (such as the Federal Reserve System) are monitored carefully to make prudent investments and to assess the condition of the City's portfolio.

INVESTMENT OBJECTIVES

The primary objectives, in priority order, of investment activities shall be safety, liquidity, and yield:

1. **Safety:** Safety of principal is the foremost objective of the investment program. Investments shall be undertaken in a manner that seeks to ensure the preservation of capital in the overall portfolio. The objective will be to mitigate credit risk and interest rate risk.

- a) Credit risk is the risk that an obligation will not be paid and a loss will result. The City will seek to minimize this risk by:
- Limiting investment to the safest types of securities as listed in the “Authorized Investment” section
 - Diversifying its investments among the types of securities that are authorized under this investment policy
- b) Interest rate risk is the risk that changes in interest rates will adversely affect the value of an investor’s portfolio. For example, an investor with large holdings in long-term bonds has assumed significant interest rate risk because the value of the bonds will fall if interest rates rise. The City can minimize this risk by:
- Buying and holding its securities until maturity
 - Structuring the investment portfolio so that securities mature to meet cash flow requirements

To further achieve the objective of safety, the amount that can be invested in all investment categories, excluding obligations of the U.S. Government and its agencies, is limited either as a percentage of the portfolio or by a specific dollar amount. These limits are defined under the “Authorized Investments” section.

2. **Liquidity:** Liquidity is the second most important objective of the investment program. The investment portfolio shall remain sufficiently liquid to meet all operating requirements that may be reasonably anticipated. This is accomplished by maintaining a portion of the portfolio in liquid money market mutual funds or local government investment pools. In addition, the City will maintain one month’s cash needs in short term investments and at least \$50 million shall be maintained in securities maturing in less than two years. Since all possible cash demands cannot be anticipated, however, the portfolio will consist of securities with active secondary or resale markets should the need to sell a security prior to maturity arises.
3. **Yield:** Yield on the City’s portfolio is last in priority among investment objectives. The investment portfolio shall be designed to obtain a market rate of return that reflects the authorized investments, risk constraints, and liquidity needs outlined in the City’s investment policy. Compared to similar sized cities, the City of Palo Alto should be able to take advantage of its relatively large reserve balances to achieve higher yields through long-term investments. In addition, the City will strive to maintain the level of investment of idle funds as close to 100 percent as possible.

ENVIRONMENTAL, SOCIAL AND GOVERNANCE (ESG) RESPONSIBILITIES

In addition to and subordinate to the above investment objectives (e.g. Safety, Liquidity, & Yield), the City has a desire to encourage investments that support sound environmental, social and governance (ESG) investing. While the portfolio may not be classified as an ESG portfolio, investments in entities that support community well-being through safe and environmentally

sound practices and fair labor practices and equality of rights regardless of sex, race, age, disability, or sexual orientation is encouraged. Direct investments are discouraged in entities that manufacture tobacco products, firearms, and engage in direct production or drilling of fossil fuels.

This section applies to new investments only and does not require divestment of existing investments. Investments in Certificates of Deposit (CDs) and Negotiable Certificates of Deposit are exempt from the ESG investing requirement.

SCOPE

- A. This investment policy shall apply to all financial assets of the City of Palo Alto as accounted for in the Comprehensive Annual Financial Report (CAFR), including but not limited to the following funds:
 - 1. General Fund
 - 2. Special Revenue Funds
 - 3. Debt Service Funds
 - 4. Capital Project Fund
 - 5. Enterprise Funds
 - 6. Internal Service Funds
 - 7. Trust and Agency Funds
- B. The policy does not cover funds held by the California Public Employees Retirement System (CalPERS), Deferred Compensation programs (e.g. ICMA, Hartford), and Public Agency Retirement Services (PARS) section 115 irrevocable trust.
- C. Investments of bond proceeds shall be governed by the provisions of the related bond indentures.

GENERAL INVESTMENT GUIDELINES

- 1. The maximum stated final maturity of individual securities in the portfolio should be ten years.
- 2. A maximum of 30 percent of the par value of the portfolio shall be invested in securities with maturities beyond five years.
- 3. The City shall maintain a minimum of one month's cash needs in short term investments.
- 4. At least \$50 million shall be maintained in securities maturing in less than 2 years.
- 5. Should the ratio of the market value of the portfolio to the book value of the portfolio fall below 95 percent, the Administrative Services Department will report this fact to the City Council within a reasonable time frame and evaluate whether there is any risk

of holding any of the securities to maturity.

6. Commitments to purchase securities newly introduced on the market shall be made no more than three (3) working days before pricing.
7. Whenever possible, the City will obtain three or more quotations on the purchase or sale of comparable securities and take the higher yield on purchase or higher price on sale. This rule will not apply to new issues, which are purchased at market no more than three (3) working days before pricing, as well as to LAIF, City of Palo Alto bonds, money market accounts and mutual funds, all of which shall be evaluated separately.
8. Where the Investment Policy specifies a percentage limitation for a particular category of investment, that percentage is applicable only at the date of purchase. A later increase or decrease in a percentage resulting from a change in the portfolio's assets or values shall not constitute a violation of that restriction. As soon as possible, percentage limitations will be restored as investments mature in each category.

AUTHORIZED INVESTMENTS

The California Government Code (Sections 53600 et seq.) governs investment of City funds. The following investments are authorized:

1. **U.S. Government Securities** (e.g. Treasury notes, bonds and bills) Securities that are backed by the full faith and credit of the United States
 - a) There is no limit on purchase of these securities.
 - b) Securities will not exceed 10 years maturity.
 - c) All purchased securities must have an explicit or a de facto backing of the full faith and credit of the U.S. Government.
2. **U.S. Government Agency Securities** – Obligations issued by the Federal Government agencies (e.g. Federal National Mortgage Association).
 - a. There is no limit on purchase of these securities except for:
 - Callable and Multi-step-up securities provided that:
 - The potential call dates are known at the time of purchase
 - The interest rates at which they “step-up” are known at the time of purchase
 - The entire face value of the security is redeemed at the call date
 - No more than 25 percent of the par value of the portfolio
 - b. Securities will not exceed 10 years maturity.

3. **California State, California Local Government Agencies, and other United States State Bonds**
 - a) Having at time of investment a minimum Double A (AA/Aa2) rating as provided by a nationally recognized rating service (e.g. Moody's, Fitch, and/or Standard and Poor's).
 - b) May not exceed 20 percent of the par value of the portfolio.
 - c) Investments include:
 - i) Registered state warrants or treasury notes or bonds of the State of California and bonds, notes, warrants, or other evidences of indebtedness of any local agency within California, including bonds payable solely out of the revenues from a revenue producing property owned, controlled, or operated by the state or local agency or by a department, board, agency, or authority of the state or local agency.
 - ii) Registered treasury notes or bond of any of the 49 United States in addition to the State of California, including bonds payable solely out of the revenues from a revenue-producing property owned, controlled, or operated by a state or by a department, board, agency or authority of any of the other 49 United States, in addition to the State of California.
4. **Certificates of Deposit (CD)** - A debt instrument issued by a bank for a specified period of time at a specified rate of interest.
 - a) May not exceed 20 percent of the par value of the portfolio.
 - b) No more than 10 percent of the par value of the portfolio in collateralized CDs in any institution.
 - c) Purchase collateralized deposits only from federally insured large banks that are rated by a nationally recognized rating service (e.g. Moody's, Fitch, and/or Standard and Poor's).
 - d) For non-rated banks, deposit should be limited to amounts federally insured (FDIC). – See Appendix C
 - e) Rollovers are not permitted without specific instruction from authorized City staff.
5. **Banker's Acceptance Notes (BA)** – Bills of exchange or time drafts drawn on and

accepted by commercial banks. Purchase of banker's acceptances are limited to:

- a) No more than 30 percent of the par value of the portfolio.
 - b) Not to exceed 180 days maturity.
 - c) No more than \$5 million with any one institution.
6. **Commercial Paper** - Short-term unsecured obligations issued by banks, corporations, and other borrowers. Purchases of commercial paper are limited to:
- a) Having highest letter or numerical rating as provided for by a nationally recognized rating service (e.g. Moody's, Fitch, and/or Standard and Poor's).
 - b) No more than 15 percent of the par value of the portfolio.
 - c) Not to exceed 270 days maturity.
 - d) No more than \$3 million or 10 percent of the outstanding commercial paper of any one institution, whichever is lesser.
7. **Local Agency Investment Fund (LAIF)** – A State of California managed investment pool may be used up to the maximum permitted by California State Law.
8. **Short-Term Repurchase Agreements (REPO)** – A contractual agreement between a seller and a buyer, usually of U.S. government securities, whereby the seller agrees to repurchase the securities at an agreed upon price and, usually, at a stated time.
- a) Not to exceed 1 year.
 - b) Market value of securities that underlay a repurchase agreement shall be valued at 102 percent or greater of the funds borrowed against those securities.
 - c) A Master Repurchase agreement must be signed with the bank or dealer.
9. **Money Market Deposit Accounts** – Liquid bank accounts which seek to maintain a net asset value of \$1.00.
10. **Mutual Funds** which seek to maintain a net asset value of \$1.00 and which are limited essentially to the above investments and further defined in note 9 of Appendix A
- a) No more than 20 percent of the par value of the portfolio.
 - b) No more than 10 percent of the par value with any one institution.

11. **Negotiable Certificates of Deposit (NCD)** issued by nationally or state chartered banks and state or federal savings institutions and further defined in note 11 of Appendix A. Purchases of negotiable certificates of deposit:
 - a) May not exceed 20 percent of the par value of the portfolio.
 - b) No more than \$5 million in any one institution.

12. **Medium-Term Corporate Notes** – Issued by corporation organized and operating within the United States or by depository institutions licensed by the United States or any state and operating with the United States.
 - a) Not to exceed 5 years maturity.
 - b) Securities eligible for investment shall have a minimum rating of AA or Aa2 from a nationally recognized rating service (e.g. Moody’s, Fitch, and/or Standard & Poor’s).
 - c) No more than 10 percent of the par value of the portfolio.
 - d) No more than \$5 million of the par value may be invested in securities of any single issuer, other than the U.S. Government, its agencies and instrumentality.
 - e) If securities owned by the City are downgraded by Moody’s, Fitch, or Standard & Poors to a level below AA or Aa2, it shall be the City’s policy to review the credit situation and make a determination as to whether to sell or retain such securities in the portfolio.

13. **Supranational Organizations Securities** – Supranational organizations refer to International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC) and Inter-American Development Bank (IADB).
 - a. Securities will not exceed 10 years maturity.
 - b. No more than 20 percent of the par value of the portfolio.
 - c. No more than 10 percent of the par value with any one institution.
 - d. Securities eligible for investment shall have a minimum rating of AA or Aa2 from a nationally recognized rating service (e.g. Moody’s, Fitch, and/or Standard & Poor’s).
 - e. Limited to United States dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by IBRD, IFC, and IADB.

Appendix A provides a more detailed description of each investment vehicle and its security and liquidity features. Most of the City's short-term investments will be in securities which pay principal

upon maturity, while long-term investments may be in securities that periodically repay principal, as well as interest. Most of the City's investments will be at a fixed rate. However, some of the investments may be at a variable rate, so long as that rate changes on specified dates in pre-determined increments.

PROHIBITED INVESTMENTS:

Includes all investments not specified above, and in particular:

1. Reverse repurchase agreements
2. Derivatives, as defined in Appendix B

Appendix B provides a more detailed description of each investment, which is prohibited, for City investment.

AUTHORIZED INVESTMENT PERSONNEL

Idle cash management and investment transactions are the responsibility of the Administrative Services Department. The Administrative Services Department is under the control of the Director of Administrative Services (Director), as treasurer, who is subject to the direction and supervision of the City Manager.

The Assistant Directors of Administrative Services, who reports to the Director, are authorized to make all investment transactions allowed by the Statement of Investment Policy. He or she may authorize the Manager of Treasury, Debt & Investments and/or Senior Management Analyst (Manager and/or Analyst) to enter into investments within clearly specified parameters.

The Investment function is under the supervision of the Assistant Director of Administrative Services (Assistant). The Assistant is charged with the responsibility to manage the investment program (portfolio), which includes developing and monitoring the City's cash flow model and developing long-term revenue and financing strategies and forecasts.

The Manager and/or Analyst are subject to the direction and supervision of the Assistant. The Manager and/or Analyst assist the Assistant, in the purchase and sale of securities. The Manager and/or Analyst also prepare the quarterly report, and record daily all investment transactions as to the type of investment, amount, yield, and maturity. Cash flow projections are prepared as needed.

In all circumstances, approval from the Director of Administrative Services is required before selling securities from the City's portfolio. The Manager and/or Analyst may also transfer no more than a total of \$10 million a day from the City's general account to any one financial institution, without the prior approval of the Assistant Director of Administrative Services.

No other person has authority to make investment transactions without the written authority of the Director or Assistant Director of Administrative Services.

USE OF BROKERS AND DEALERS

The Administrative Services Department maintains a list of acceptable dealers. A dealer acts as a principal in security transactions, selling securities from and buying securities for their own position. A dealer must have

- a) At least three years experience operating with California municipalities;
- b) Maintain an inventory of trading securities of at least \$10 million; and
- c) Be approved by the Assistant Administrative Services Director before being added to the City's list of approved dealers. In addition, individual traders or agents representing a dealer:

A dealer will be removed from the list should there develop a history of problems to include: failure to deliver securities as promised, failure to honor transactions as quoted, or failure to provide accurate information.

SAFEKEEPING AND CUSTODY

All securities shall be delivered to the City's safekeeping custodian and held in the name of the City of Palo Alto, with the exception of the following investments:

- a) Certificates of deposit, which may be held by the City itself.
- b) City shares in pooled investment funds, under contract.
- c) Mutual funds
- d) Local Agency Investment Fund (LAIF)

POLICY REVIEW AND REPORTING ON INVESTMENTS

Monthly, the Administrative Services Department will review performance in relation to-Council-adopted Policy. Quarterly, the Department will report to Council on: its performance in comparison to policy, explain any variances from policy, provide any recommendations for policy changes, and discuss overall compliance with the City's Investment Policy. In addition, the Department will provide Council with:

- a) A detailed list of all securities, investments and monies held by the City, and
- b) Report on the City's ability to meet expenditure requirements over the next six months.

Annually, the Administrative Services Department will present a Proposed Statement of Investment Policy, to include the delegation of investment authority, to the City Council for review during the annual budget process. All proposed changes in policy must be approved by the Council prior to implementation.

Adopted by City Council October 22, 1984	Amended by City Council June 19, 2000
Monthly reporting effective January 1985	Amended by City Council June 11, 2001
Amended and Adopted by City Council June 24, 1985	Amended by City Council June 17, 2002
Amended by City Council December 2, 1985	Amended by City Council June 17, 2003
Amended by City Council June 23, 1986	Amended by City Council June 28, 2004
Amended by City Council June 22, 1987	Amended by City Council June 20, 2005
Amended by City Council August 8, 1988	Amended by City Council June 12, 2006
Amended by City Council November 28, 1988	Amended by City Council June 11, 2007
Amended by City Council June 26, 1989	Amended by City Council June 09, 2008
Amended by City Council May 14, 1990	Amended by City Council June 15, 2009
Amended by City Council June 24, 1991	Amended by City Council June 28, 2010
Amended by City Council June 22, 1992	Amended by City Council June 20, 2011
Amended by City Council June 23, 1993	Amended by City Council June 18, 2012
Amended by City Council June 20, 1994	Amended by City Council June 03, 2013
Amended by City Council June 19, 1995	Amended by City Council June 16, 2014
Amended by City Council June 24, 1996	Amended by City Council June 15, 2015
Amended by City Council June 23, 1997	Amended by City Council June 13, 2016
Amended by City Council January 26, 1998	Amended by City Council June 27, 2017
Amended by City Council June 22, 1998	Amended by City Council November 5, 2018
Amended by City Council June 28, 1999	

APPENDIX A

EXPLANATION OF PERMITTED INVESTMENTS

1. **U.S. Government Securities** – United States Treasury notes, bonds, bills, or certificates of indebtedness or those for which the faith and credit of the United States are pledged for the payment of principal and interest.
2. **U.S. Government Agency Securities** - U.S. Government Agency Obligations include the securities of the Federal National Mortgage Association (FNMA), Federal Land Banks (FLB), Federal Intermediate Credit Banks (FICB), banks for cooperatives, Federal Home Loan Banks (FHLB), Government National Mortgage Association (GNMA), Federal Home Loan Mortgage Corporation (FHLMC), Student Loan Marketing Association (SLMA), Small Business Administration (SBA), Federal Farm Credit (FFC), and Federal Agricultural Mortgage Corporation (FAMC or FMAC).. Federal Agency securities are debt obligations that essentially result from lending programs of the Government. Federal agency securities differ from other types of securities, as well as among themselves. Their characteristics depend on the issuing agency. It is possible to distinguish three types of issues: (A) participation certificates (pooled securities), (B) Certificates of interest (pooled loans), (C) notes, bonds, and debentures. The securities of a few agencies are explicitly backed by the full faith and credit of the U.S. Government. All other issues purchased by the City have the de facto backing from the federal government, and it is highly unlikely that the government would let any agency default on its obligations.
3. **Certificates of Deposit** - A certificate of deposit (CDs) is a receipt for funds deposited in a bank, savings bank, or savings and loan association for a specified period of time at a specified rate of interest. Denominations are \$250,000 and up. The first \$250,000 of a certificate of deposit is guaranteed by the Federal Deposit Insurance Corporation (FDIC), if the deposit is with a bank or savings bank, or the Savings Association Insurance Fund (SAIF), if the deposit is with a savings and loan. CDs with a face value in excess of \$250,000 can be collateralized by U.S. Government Agency and Treasury Department securities or first mortgage loans. Government securities must be at least 110 percent of the face value of the CD collateralized in excess of the first \$250,000. The value of first mortgages must be at least 150 percent of the face value of the CD balance insured in excess of the first \$250,000. Generally, CDs are issued for more than 30 days and the maturity can be selected by the purchaser.
4. **Bankers' Acceptance** - A Banker's acceptance (BA) is a negotiable time draft or bill of exchange drawn on and accepted by a commercial bank. Acceptance of the draft irrevocably obligates the bank to pay the bearer the face amount of the draft at maturity. BAs are usually created to finance the import and export of goods, the shipment of goods within the United States and storage of readily marketable staple commodities. In over 70 years of usage in the United States, there has been no known instance of principal loss to any investor in BAs. In addition to the guarantee by the accepting bank, the transaction is identified with a specific commodity. Warehouse receipts verify that the pledged commodities exist, and, by definition, these commodities are readily marketable. The sale of the underlying goods generates the

necessary funds to liquidate the indebtedness.

BAs enjoy marketability since the Federal Reserve Bank is authorized to buy and sell prime BAs with maturities of up to nine months. The Federal Reserve Bank enters into repurchase agreements in the normal course of open market operations with BA dealers.

As are sold at a discount from par. An acceptance is tied to a specific loan transaction; therefore, the amount and maturity of the acceptance is fixed.

5. **Commercial Paper** - Commercial paper notes are unsecured promissory notes of industrial corporations, utilities, and bank holding companies. Interest is discounted from par and calculated using actual number of days on a 360-day year. The notes are in bearer form, with maturities up to 270 days selected by the purchaser, and denominations generally start at \$100,000. There is a small secondary market for commercial paper notes and an investor may sell a note prior to maturity.

Commercial paper notes are backed by unused lines of credit from major banks. Some issuer's notes are insured, while some are backed by irrevocable letters of credit from major banks. State law limits a City to investments in United States corporations having assets in excess of five hundred million dollars with an "A" or higher rating by a nationally recognized rating service for the issuer's debentures. Cities may not invest more than 25 percent of idle cash in commercial paper.

6. **Local Agency Investment Fund Demand Deposit** - The Local Agency Investment Fund (LAIF) was established by the State to enable treasurers to place funds in a pool for investments. The City is limited to an investment of the amount allowed by LAIF (currently \$40 million). LAIF has been particularly beneficial to those jurisdictions with small portfolios. Palo Alto uses this fund for short-term investment, liquidity, and yield.
7. **Repurchase Agreements** - A Repurchase Agreement (REPOS) is not a security, but a contractual arrangement between a financial institution or dealer and an investor. The agreement normally can run for one or more days. The investor puts up funds for a certain number of days at a stated yield. In return, the investor takes title to a given block of securities as collateral. At maturity, the securities are repurchased and the funds repaid, plus interest. Usually, amounts are \$500,000 or more, but some REPOS can be smaller.
8. **Money Market Deposit Accounts** - Money Market Deposit Accounts are market-sensitive bank accounts, which are available to depositors at any time, without penalty. The interest rate is generally comparable to rates on money market mutual funds, though any individual bank's rate may be higher or lower. These accounts are insured by the Federal Deposit Insurance Corporation or the Savings Association Insurance Fund.

9. **Mutual Funds** - Mutual funds are shares of beneficial interest issued by diversified management companies, as defined by section 23701 M of the Revenue and Taxation Code. To be eligible for investment, these funds must:
- a) Attain the highest ranking in the highest letter and numerical rating provided by not less than two of the three largest nationally recognized rating services; or
 - b) Have an investment advisor registered with the Securities and Exchange Commission with not less than five years' experience investing in the securities and obligations, as authorized by subdivisions (a) to (n), inclusive, of Section 53601 of the California Government Code, and with assets under management in excess of five hundred million dollars; and
 - c) Invest solely in those securities and obligations authorized by Sections 53601 and 53635 of the California Government Code. Where the Investment Policy of the City of Palo Alto may be more restrictive than the State Code, the Policy authorizes investments in mutual funds that shall have minimal investment in securities otherwise restricted by the City's Policy. Minimal investment is defined as less than 5 percent of the mutual fund portfolio; and
 - d) The purchase price of shares of beneficial interest purchased shall not include any commission that these companies may charge.
 - e) Have a net asset value of \$1.00.
10. **Callable Securities and Multi-Step-ups:** Callable securities are defined as fixed interest rate government agency securities that give the issuing agency the option of returning the invested funds at a specific point in time to the purchaser. Multi-step-ups are government agency securities in which the interest rate increases ("steps-up") at preset intervals, and which also have a callable option that allows the issuing agency to return the invested funds at a preset interval. Callable and multi-step-ups are permitted, provided that:
- the potential call dates are known at the time of purchase;
 - the interest rates at which they "step-up" are known at the time of purchase; and
 - the entire face value of the security is redeemed at the call date.

11. **Negotiable Certificates of Deposit (NCD).** NCDs are large-dollar-amount, short-term certificate of deposit. Such certificates are issued by large banks and bought mainly by corporations and institutional investors. They are payable either to the bearer or to the order of the depositor, and, being negotiable, they enjoy an active secondary market, where they trade in round lots of \$5 million. Although they can be issued in any denomination from \$100,000 up, the typical amount is \$1 million. Also called a Jumbo Certificate of Deposit.

State law prohibits the investment of local agency funds in negotiable certificates of deposit issued by a state or federal credit union if a member of the legislative body of the local agency, or any person with investment decision making authority in the administrative, manager's, budget, auditor-controller's, or treasurer's offices of the local agency also serves on the board of directors, other credit committee or the supervisory committee of the state or federal credit union issuing the negotiable certificate of deposit.

12. **Medium-Term Corporate Notes:** Notes of a maximum of five years maturity issued by corporations organized and operating with the United States or by depository institutions licensed by the United States or any state and operating with the United States. According to California Code Section 53601, "Notes eligible for investment under this subdivision shall be rated in the rating category of "Double A" or its equivalent or better by a nationally recognized rating service. Purchase of medium-term notes may not exceed 30 percent of the agency's surplus money which may be invested pursuant to this section."

13. **Supranational Securities:** California Government Code (CGC 53601) defines allowable supranational securities as United States dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development, the International Finance Corporation, and Inter-American Development Bank. Supranationals are well capitalized and in most cases have strong credit support from contingent capital calls from their member countries. CGC 53601 was amended effective January 1, 2015 to allow local agencies to invest in the senior debt obligations of these three supranational issuers which are eligible for purchase and resale within the United States. These entities were established with the purpose of ending poverty and raising the standard of living around the world through sustainable economic growth.

- a) The supranationals are international organization owned by member countries. Again, these are:

- **International Bank for Reconstruction and Development (IBRD or World Bank)**, a member of the World Bank Group, provides direct loans and guarantees to sovereigns and government-backed projects
- **International Finance Corporation (IFC)**, a member of the World Bank Group, supports the creation and growth of private companies through direct lending and equity investment, attracting third party capital, and providing advisory services
- **Inter-American Development Bank (IADB)**, a member of the Inter-American Development Bank Group, provides loans, grants, and guarantees to sovereigns in Latin America and the Caribbean

- b) Additional characteristics shared by the IBRD, IFC, and IADB include:
- Headquartered in Washington, D.C. with the United States as the largest shareholder of each organization
 - Rated AAA/Aaa by S&P and Moody's

APPENDIX B

EXPLANATION OF PROHIBITED INVESTMENTS

1. **Reverse Repurchase Agreements:** A Reverse Repurchase Agreement (Reverse REPO) is a contractual agreement by the investor (e.g. local agency) to post a security it owns as collateral, and a bank or dealer temporarily exchanges cash for this collateral, for a specific period of time, at an agreed-upon interest rate. During the period of the agreement, the local agency may use this cash for any purpose. At maturity, the securities are repurchased from the bank or dealer, plus interest.

California law contains a number of restrictions on the use of Reverse REPOS by local agencies.

2. **Derivatives:** A derivative is a financial instrument created from, or whose value depends on (is derived from), the value of one or more underlying assets or indices. The term "derivative" refers to instruments or features, such as collateralized mortgage obligations, forwards, futures, currency and interest rate swaps, options, caps and floors. Except for those callable and multi-step-up securities as described under Permitted Investments, derivatives are prohibited.

Certain derivative products have characteristics which could include high price volatility, liquid markets, products that are not market-tested, products that are highly leveraged, products requiring a high degree of sophistication to manage, and products that are difficult to value.

According to California law, a local agency shall not invest any funds in inverse floaters, range notes, or interest-only strips that are derived from a pool of mortgages.

APPENDIX C GLOSSARY OF INVESTMENT TERMS

AGENCIES: Federal agency and instrumentality securities.

ASKED: The price at which securities are offered.

BID: The price offered by a buyer of securities (when one sells securities, one asks for a bid). See “*Offer*”.

BROKER: A broker brings buyers and sellers together so that he can earn a commission.

COLLATERAL: Securities, evidence of deposit, or other property, which a borrower pledges to secure repayment of a loan. Also refers to securities pledged by a bank to secure deposits of public monies.

COMPREHENSIVE ANNUAL FINANCIAL REPORT (“CAFR”): The official annual report for the City of Palo Alto. It includes combined financial statements for each individual fund and account group prepared in conformity with GAAP. It also includes supporting schedules that are necessary to demonstrate compliance with finance-related legal and contractual provisions, extensive introductory material, and a detailed statistical section.

COUPON: (a) The annual rate of interest that a bond’s issuer promises to pay the bondholder on the bond’s face value. (b) A certificate attached to a bond evidencing interest due on a payment date.

DEALER: A dealer, as opposed to a broker, acts as a principal in all transactions, buying and selling for his own account.

DEBENTURE: A bond secured only by the general credit of the issuer.

DELIVERY VERSUS PAYMENT: There are two methods of delivery of securities: (1) delivery versus payment (DVP); and (2) delivery versus receipt (DVR). DVP is delivery of securities with an exchange of money for the securities. DVR is delivery of securities with an exchange of a signed receipt for the securities.

DISCOUNT: The difference between the acquisition cost of a security and its value at maturity when quoted at lower than face value. A security that sells below original offering price shortly after sale, is also is considered to be at a discount.

DISCOUNT SECURITIES: Non-interest bearing money market instruments that are issued a discount and that are redeemed at maturity for full face value (e.g., U.S. Treasury Bills).

DIVERSIFICATION: Dividing investment funds among a variety of securities that offer

independent returns.

FEDERAL AGRICULTURAL MORTGAGE CORPORATION (“FAMC” or “FMAC”): A federal agency established in 1988 to provide a secondary market for farm mortgage loans. Informally called *Farmer Mac*.

FEDERAL CREDIT AGENCIES: Agencies of the Federal Government that were established to supply credit to various classes of institutions and individuals (e.g., S&Ls, small business firms, students, farmers, farm cooperatives, and exporters).

FEDERAL DEPOSIT INSURANCE CORPORATION (“FDIC”): A federal agency that insures all types of deposits received at an insured bank, including deposits in a checking account, negotiable order of withdrawal (NOW) account, savings account, money market deposit account (MMDA) or time deposit such as a certificate of deposit (CD). FDIC insurance covers depositors' accounts at each insured bank, dollar-for-dollar, including principal and any accrued interest through the date of the insured bank's closing, up to the insurance limit.

The FDIC does not insure money invested in stocks, bonds, mutual funds, life insurance policies, annuities or municipal securities, even if these investments are purchased at an insured bank. The FDIC does not insure U.S. Treasury bills, bonds or notes, but these investments are backed by the full faith and credit of the United States government.

The standard maximum deposit insurance amount is described as the “SMDIA” in FDIC regulations. The SMDIA is \$250,000 per depositor, per insured bank.

FEDERAL FUNDS RATE: The rate of interest at which Fed funds are traded. This rate is currently pegged by the Federal Reserve through open-market operations.

FEDERAL HOME LOAN BANKS (“FHLB”): Government-sponsored wholesale banks (currently 12 regional banks) which lend funds and provide correspondent banking services to member commercial banks, thrift institutions, credit unions, and insurance companies. The mission of the FHLBs is to liquefy the housing-related assets of its members, who must purchase stock in their District Bank.

FEDERAL NATIONAL MORTGAGE ASSOCIATION (“FNMA”): FNMA, like GNMA, was chartered under the Federal National Mortgage Association Act in 1938. FNMA is a federal corporation working under the auspices of the Department of Housing and Urban Development (HUD). It is the largest single provider of residential mortgage funds in the United States. Fannie Mae, as the corporation is called, is a private stockholder-owned corporation. The corporation's purchases include a variety of adjustable mortgages and second loans, in addition to fixed-rate mortgages. FNMA's securities are also highly liquid and are widely accepted. FNMA assumes and guarantees that all security holders will receive timely payment of principal and interest.

FEDERAL OPEN MARKET COMMITTEE (“FOMC”): The FOMC consists of seven members of the Federal Reserve Board and five of the 12 Federal Reserve Bank Presidents. The

President of the New York Federal Reserve Bank is a permanent member, while the other Presidents serve on a rotating basis. The Committee periodically meets to set Federal Reserve guidelines regarding purchases and sales of government securities in the open market, as a means of influencing the volume of bank credit and money.

FEDERAL RESERVE SYSTEM: The central bank of the United States created by Congress and consisting of a seven-member Board of Governors in Washington, D.C., 12 regional banks, and about 5,700 commercial banks that are members of the system.

GOVERNMENT NATIONAL MORTGAGE ASSOCIATION (“GNMA” or “Ginnie Mae”): Securities that influence the volume of bank credit that is guaranteed by GNMA and issued by mortgage bankers, commercial banks, savings and loan associations, and other institutions. A security holder is protected by the full faith and credit of the U.S. Government. Ginnie Mae securities are backed by the FHA, VA, or FMHM mortgages. The term “pass-throughs” is often used to describe Ginnie Maes.

LIQUIDITY: A liquid asset is one that can be converted easily and rapidly into cash without a substantial loss of value. In the money market, a security is said to be liquid if the spread between bid and asked prices is narrow, and reasonable amount can be done at those quotes.

LOCAL GOVERNMENT AGENCY: A local government agency is any city, county, city and county, district, or other local governmental body or corporation, including the California State Universities (CSU) and University of California (UC) systems, K-12 schools and community colleges empowered to expend public funds.

LOCAL GOVERNMENT INVESTMENT FUND (“LAIF”): Monies from local governmental units may be remitted to the California State Treasurer for deposit in this special fund for the purpose of investment.

MARKET VALUE: The price at which a security is trading and could presumably be purchased or sold.

MASTER REPURCHASE AGREEMENT: A written contract covering all future transactions between the parties to repurchase-reverse repurchase agreements that establish each party’s rights in the transactions. A master agreement will often specify, among other things, the right of the buyer (lender) to liquidate the underlying securities in the event of default by the seller (borrower).

MATURITY: The date upon which the principal or stated value of an investment becomes due and payable.

MONEY MARKET: The market in which short-term debt instruments (e.g., bills, commercial paper, and bankers’ acceptances) are issued and traded.

OFFER: The price asked by a seller of securities (when one buys securities, one asks for an offer). See “*Asked*” and “*Bid*”.

OPEN MARKET OPERATIONS: Purchases and sales of government and certain other securities in the open market by the New York Federal Reserve Bank, as directed by the FOMC in order to influence the volume of money and credit in the economy. Purchases inject reserves into the bank system and stimulate growth of money and credit; sales have the opposite effect. Open market operations are the Federal Reserve's most important and most flexible monetary policy tool.

PORTFOLIO: A collection of securities that an investor holds.

PRIMARY DEALER: A group of government securities dealers that submit daily reports of market activity and positions, and monthly financial statements to the Federal Reserve Bank of New York, and are subject to its informal oversight. Primary dealers include Securities and Exchange Commission (SEC) -- registered securities broker-dealers, banks, and a few unregulated firms.

PRUDENT INVESTOR RULE: An investment standard cited in the California Government Code (CGC) Section 53600 et seq. Under this standard, all governing bodies of local agencies or persons authorized to make investment decisions on behalf of the City are trustees and therefore fiduciaries subject to the prudent investor standard. When investing, reinvesting, purchasing, acquiring, exchanging, selling, or managing public funds, a trustee shall act with care, skill, prudence, and diligence under the circumstances then prevailing, including, but not limited to the general economic conditions and the anticipated needs of the agency, that a prudent person acting in a like capacity and familiarity with those matters would use in the conduct of funds of a like character and with like aims, to safeguard the principal and maintain the liquidity needs of the agency.

QUALIFIED PUBLIC DEPOSITORIES: A financial institution that: (1) does not claim exemption from the payment of any sales, compensating use, or ad valorem taxes under the laws of this state; (2) has segregated for the benefit of the commission eligible collateral having a value of not less than its maximum liability; and (3) has been approved by the Public Deposit Protection Commission to hold public deposits.

RATE OF RETURN: The yield obtainable on a security based on its purchase price or its current market price.

SAFEKEEPING: A service to customers rendered by banks for a fee whereby securities and valuables of all types and descriptions are held in the bank's vaults for protection.

SECONDARY MARKET: A market made for the purchase and sale of outstanding issues following the initial distribution.

SECURITIES AND EXCHANGE COMMISSION: An agency created by Congress to administer securities legislation for the purpose of protecting investors in securities transactions.

STRUCTURED NOTES: Notes issued by instrumentalities (e.g., FHLB, FNMA, SLMA) and by corporations, that have imbedded options (e.g., call features, step-up coupons, floating rate coupons, derivative-based returns) in their debt structure. The market performance of structured notes is affected by fluctuating interest rates; the volatility of imbedded options; and shifts in the yield curve.

SUPRANATIONALS: International institutions that provide development financing, advisory services and/or financial services to their member countries to achieve the overall goal of improving living standards through sustainable economic growth. The California Government Code (CGC 53601) allows local agencies to purchase the United States dollar denominated senior unsecured unsubordinated obligations issued or unconditionally guaranteed by the International Bank for Reconstruction and Development (IBRD), International Finance Corporation (IFC), or Inter-American Development Bank (IADB).

TIME CERTIFICATE OF DEPOSIT: A non-negotiable certificate of deposit, which cannot be sold prior to maturity.

TREASURY BILLS: A non-interest bearing discount security that is issued by the U.S. Treasury to finance the national debt. Most T-bills are issued to mature in three months, six months, or one year.

TREASURY BONDS: Long-term, coupon-bearing U.S. Treasury securities that are issued as direct obligations of the U.S. Government, and having initial maturities of more than 10 years.

TREASURY NOTES: Medium-term, coupon-bearing U.S. Treasury securities that are issued as direct obligations of the U.S. Government, and having initial maturities of two to 10 years.

YIELD: The rate of annual income return on an investment, expressed as a percentage.

YIELD-TO-CALL (YTC): The rate of return an investor earns from a bond assuming the bond is redeemed (called) prior to its nominal maturity date.

YIELD-TO-MATURITY: The current income yield minus any premium above par or plus any discount from par in purchase price, with the adjustment spread over the period from the date of purchase to the date of maturity.

ZERO-COUPON SECURITIES: Security that is issued at a discount and makes no periodic interest payments. The rate of return consists of a gradual accretion of the principal of the security and is payable at par upon maturity.

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APPENDIX D

FORM OF SPECIAL COUNSEL OPINION

[Closing Date]

City Council
City of Palo Alto
250 Hamilton Avenue
Palo Alto, California 94301

OPINION: \$26,785,000 City of Palo Alto 2019 Certificates of Participation, Series A
(California Avenue Parking Garage) (Tax-Exempt)

\$10,585,000 City of Palo Alto 2019 Certificates of Participation, Series B
(California Avenue Parking Garage) (Federally Taxable)

Members of the City Council:

We have acted as special counsel to the City of Palo Alto (the “City”) in connection with the delivery by the City of the Lease Agreement dated as of March 1, 2019 (the “Lease Agreement”) between the Palo Alto Public Improvement Corporation (the “Corporation”) as lessor and the City as lessee. Under the Trust Agreement dated as of March 1, 2019 (the “Trust Agreement”) among the City, the Corporation and U.S. Bank National Association, as trustee (the “Trustee”), the Trustee has executed and delivered the above-captioned certificates of participation dated the date hereof (the “Series A Certificates” and the “Series B Certificates”; together, the “Certificates”). In such capacity, we have examined such law and such certified proceedings, certifications and other documents as we have deemed necessary to render this opinion.

The Certificates evidence the direct, undivided fractional interests of the owners thereof in two streams of lease payments to be made by the City under the Lease Agreement (the “Tax-Exempt Lease Payments” and the “Taxable Lease Payments”; together, the “Lease Payments”), which have been assigned by the Corporation to the Trustee. The City authorized execution and delivery of the Lease Agreement, the Trust Agreement and the Certificates pursuant to a resolution of the city council of the City adopted on October 15, 2018 (the “Resolution”).

Regarding questions of fact material to our opinion, we have relied on representations of the City contained in the Lease Agreement and the Trust Agreement, and in the certified proceedings and other certifications of public officials furnished to us, without undertaking to verify the same by independent investigation.

Based on the foregoing, we are of the opinion that, under existing law:

1. The City is a duly created and validly existing municipal corporation and charter city with the power to adopt the Resolution, enter into the Lease Agreement and the Trust Agreement, and perform the agreements on its part contained therein.

2. The Lease Agreement and the Trust Agreement have been duly authorized, executed and delivered by the City, and constitute the valid and binding obligations of the City, enforceable against the City.

3. The Certificates have been validly executed and delivered by the Trustee under the Trust Agreement and, by virtue of the assignment made by the Corporation, the owners of the Certificates are entitled to the benefits of the Lease Agreement.

4. The portion of the Tax-Exempt Lease Payments designated as and comprising interest and received by the owners of the Series A Certificates is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the federal alternative minimum tax. The opinions set forth in the preceding sentence are subject to the condition that the City comply with all requirements of the Internal Revenue Code of 1986, as amended, that must be satisfied subsequent to the execution and delivery of the Lease Agreement in order that the portion of the Tax-Exempt Lease Payments designated as and comprising interest be, and continue to be, excludable from gross income for federal income tax purposes. The City has made certain representations and covenants in order to comply with each such requirement. Inaccuracy of those representations, or failure to comply with certain of those covenants, may cause the inclusion of such interest in gross income for federal income tax purposes, which may be retroactive to the date of delivery of the Lease Agreement.

5. The portion of the Lease Payments designated as and comprising interest and received by the owners of the Certificates is exempt from personal income taxation imposed by the State of California.

We express no opinion regarding any other tax consequences arising with respect to the ownership, sale or disposition of, or the amount, accrual or receipt of interest on, the Lease Agreement or the Certificates.

The rights of the owners of the Certificates and the enforceability of the Lease Agreement and the Trust Agreement are limited by bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting creditors' rights generally, and by equitable principles, whether considered at law or in equity.

This opinion is given as of the date hereof, and we assume no obligation to revise or supplement this opinion to reflect any facts or circumstances that may hereafter come to our attention, or any changes in law that may hereafter occur. Our engagement with respect to this matter has terminated as of the date hereof.

Respectfully submitted,

A Professional Law Corporation

APPENDIX E

SUMMARY OF THE PRINCIPAL LEGAL DOCUMENTS

The following are brief summaries of the provisions of the principal legal documents. These summaries are not intended to be definitive. Reference is made to the actual documents (copies of which are available from the City) for the complete terms thereof.

DEFINED TERMS

“2019A Certificates” means the \$26,785,000 aggregate principal amount of City of Palo Alto 2019 Certificates of Participation, Series A (California Avenue Parking Garage) (Tax-Exempt).

“2019B Certificates” means the \$10,585,000 aggregate principal amount of City of Palo Alto 2019 Certificates of Participation, Series B (California Avenue Parking Garage) (Federally Taxable).

“Assignment Agreement” means the Assignment Agreement, dated as of March 1, 2019, by and between the Corporation and the Trustee, together with any duly authorized and executed amendments thereto.

“Bond Counsel” means any attorney or firm of attorneys of nationally recognized expertise with respect to legal matters relating to obligations the interest on which is exempt from federal income taxation pursuant to Section 103 of the Code.

“Business Day” means a day of the week on which the Trustee is not required or authorized to remain closed and on which the New York Stock Exchange is open.

“California Avenue Parking Garage” means the parking garage to be located at 350 Sherman Avenue.

“Certificates” means the 2019A Certificates and the 2019B Certificates, to be executed and delivered pursuant to the Trust Agreement.

“City” means the City of Palo Alto, a chartered municipal corporation duly organized and existing under the Constitution and the laws of the State.

“City Representative” means the City Manager, the Assistant City Manager or the Director of Administrative Services of the City or any other person authorized by resolution of the City Council to act on behalf of the City under or with respect to the Trust Agreement and the Lease Agreement.

“Closing Date” means the date upon which there is an exchange of the Certificates for the proceeds representing the purchase of the Certificates by the Original Purchaser.

“Code” means the Internal Revenue Code of 1986 as in effect on the date of delivery of the Lease Agreement or (except as otherwise referenced in the Lease Agreement) as it may be amended to apply to obligations issued on the date of delivery of the Lease Agreement, together with applicable temporary and final regulations promulgated, and applicable official public guidance published, under the Code.

“Corporation” means the Palo Alto Public Improvement Corporation, a nonprofit public benefit corporation duly formed, organized, operating and existing under the laws of the State, and its successors and assigns.

“Corporation Representative” means the President or Vice President of the Corporation, or any other person authorized by resolution of the Corporation to act on behalf of the Corporation under or with respect to the Trust Agreement and the Lease Agreement.

“Corporate Trust Office” means the corporate trust office of the Trustee in San Francisco, California, or such other or additional offices as the Trustee may designate in writing to the Corporation from time to time as the corporate trust office for purposes of the Trust Agreement, except that with respect to presentation of Certificates for payment or for registration of transfer and exchange thereof, such term shall mean the office or agency of the Trustee at which, at any particular time, its corporate trust agency business shall be conducted, initially in Saint Paul, Minnesota.

“Costs of Issuance” means all items of expense directly or indirectly payable by or reimbursable to the City or the Corporation relating to the execution, sale and delivery of the Certificates, including but not limited to settlement costs, printing costs, reproduction and binding costs, initial fees and charges of the Trustee, financing discounts, legal fees and charges, bond insurance or title, insurance fees and charges, financial and other professional consultant fees, costs of rating agencies for credit ratings, fees for execution, transportation and safekeeping of the Certificates and charges and fees in connection with the foregoing.

“Costs of Issuance Fund” means the fund by that name established and held by the Trustee pursuant to the Trust Agreement.

“Counsel” means any attorney at law or law firm (who or which may be counsel for the City, the Trustee or the Corporation).

“Event of Default” means an event of default under the Lease Agreement.

“Fair Market Value” means the price at which a willing buyer would purchase the investment from a willing seller in a bona fide, arm's length transaction (determined as of the date the contract to purchase or sell the investment becomes binding) if the investment is traded on an established securities market (within the meaning of section 1273 of the Code) and, otherwise, the term “Fair Market Value” means the acquisition price in a bona fide arm's length transaction (as referenced above) if (i) the investment is a certificate of deposit that is acquired in accordance with applicable regulations under the Code, (ii) the investment is an agreement with specifically negotiated withdrawal or reinvestment provisions and a specifically negotiated interest rate (for example, a guaranteed investment contract, a forward supply contract or other investment agreement) that is acquired in accordance with applicable regulations under the Code, (iii) the investment is a United States Treasury Security--State and Local Government Series that is acquired in accordance with applicable regulations of the United States Bureau of Public Debt, or (iv) any commingled investment fund in which the City and related parties do not own more than a ten percent (10%) beneficial interest therein if the return paid by the fund is without regard to the source of the investment.

“Federal Securities” means any of the following which at the time of investment are legal investments under the laws of the State for the moneys proposed to be invested therein:

- (a) 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); and
- (b) obligations of any department, agency or instrumentality of the United States of America the timely payment of principal of and interest on which are unconditionally and fully guaranteed by the United States of America.

“Final Completion” means, with respect to the acquisition and construction of the California Avenue Parking Garage with the proceeds of the Certificates, the substantial readiness of the California Avenue Parking Garage for use and occupancy by the City, as evidenced by the delivery to the Trustee of a certificate of completion.

“Fiscal Year” means each twelve-month period beginning on July 1 of any year and ending on June 30 of the succeeding year, or any other twelve-month period hereafter adopted by the City as its official fiscal year period.

“Independent Counsel” means an attorney duly admitted to the practice of law before the highest court of the state in which such attorney maintains an office and who is not an employee of the Corporation, the Trustee or the City.

“Insurance and Condemnation Fund” means the fund by that name established and held by the Trustee pursuant to the Trust Agreement.

“Investment Securities” means any of the following which at the time of investment are legal investments under the laws of the State of California for trust funds held by the Trustee (the Trustee is entitled to rely upon any investment direction of the City as a certification that such investment constitutes an Investment Security):

1. Direct and general obligations of the United States of America, or obligations that are unconditionally guaranteed as to payments of principal and interest by the United States of America, including (in the case of direct and general obligations of the United States of America) evidences of direct ownership of proportionate interests in future interest or principal payments of such obligations. Investments in such proportionate interests must be limited to circumstances wherein (a) a bank or trust company acts as custodian and holds the underlying United States obligations; (b) the owner of the investment is the real party in interest and has the right to proceed directly and individually against the obligor of the underlying United States obligations; and (c) the underlying United States obligations are held in safekeeping in a special account, segregated from the custodian's general assets, and are not available to satisfy any claim of the custodian, any person claiming through the custodian, or any person to whom the custodian may be obligated. The obligations described in this paragraph are hereinafter called “United States Obligations”.

2. Obligations issued or guaranteed by the following instrumentalities or agencies:

- (a) Federal Home Loan Banks;
- (b) Government National Mortgage Association;
- (c) Farmers Home Administration;
- (d) Federal Home Loan Mortgage Corporation;
- (e) Federal Housing Administration; and
- (f) Federal National Mortgage Association.

3. Direct and general long-term obligations of any state or commonwealth of the United States, to the payment of which the full faith and credit of the state or commonwealth is pledged and that are rated “Aaa” by Moody's and “AAA” by S&P.

4. Direct and general short-term obligations of any state or commonwealth, to the payment of which the full faith and credit of the state or commonwealth is pledged and that are rated in the highest rating category by Moody's and S&P.

5. Interest-bearing demand or time deposits issued by state banks or trust companies or national banking associations that are members of the Federal Deposit Insurance Corporation (FDIC). These deposits must be continuously and fully insured by FDIC and be with banks whose debt is rated at least P-1 or Aa by Moody's and at least A-1+ or AA by S&P.

6. Repurchase agreements, the maturities of which are 30 days or less, or are due on demand, entered into with financial institutions such as banks or trust companies organized under state law or national banking associations, insurance companies, or government bond dealers reporting to, trading with,

and recognized as a primary dealer by, the Federal Reserve Bank of New York and a member of the Security Investors Protection Corporation or with a dealer or parent holding company, in each such case the debt of which is rated at least "A" or "P-1" by Moody's and S&P. Such repurchase agreements shall be in respect of United States Obligations and (except repurchase agreements with institutions whose debt or commercial paper is rated "Aaa" or "P-1" by Moody's and S&P) shall be collateralized by United States Obligations, and the provisions of the repurchase agreement shall meet the following additional criteria:

(i) the Trustee (who shall not be the provider of the collateral) or a third party acting solely as agent for the Trustee has possession of the United States Obligations;

(ii) failure to maintain the requisite collateral levels will require the Trustee to liquidate the United States Obligations immediately;

(iii) the Trustee has a perfected, first priority security interest in the United States Obligations; and

(iv) the United States Obligations are free and clear of third-party liens, and in the case of an SIPC broker, were not acquired pursuant to a repurchase or reverse repurchase agreement.

7. Pre-refunded municipal obligations meeting the following conditions:

(a) the municipal obligations are (i) not to be redeemed prior to maturity or the Trustee has been given irrevocable instructions concerning their calling and redemption and (ii) the issuer has covenanted not to redeem such municipal obligations other than as set forth in such instructions;

(b) the municipal obligations are secured by cash or United States Obligations that may be applied only to interest, principal, and premium payments of such municipal obligations;

(c) the principal of and interest on the United States Obligations (plus any cash in the escrow fund) are sufficient to meet the liabilities on the municipal obligations;

(d) the United States Obligations serving as security for the municipal obligations are held by an escrow agent or trustee; and

(e) the United States Obligations (plus any cash in the escrow fund) are not available to satisfy any other claims, including those against the trustee or escrow agent.

8. Prime commercial paper of a United States corporation, finance company or banking institution if such commercial paper is rated at least "P1" by Moody's and at least "A-1+" by S&P and if such commercial paper is stated to mature in not more than 270 days.

9. Shares of a diversified open-end management investment company (as defined in the Investment Company Act of 1940) or shares in a regulated investment company (as defined in Section 851 (a) of the Internal Revenue Code of 1986, as amended) that is a money market fund that has been rated in the highest rating category by S&P.

10. The Local Agency Investment Fund maintained by the Treasurer of the State ("LAIF") to the extent deposits and withdrawals may be made by the Trustee in its own name.

11. Banker's acceptances drawn on and accepted by commercial banks (including the Trustee and any affiliate of the Trustee) having a combined unencumbered capital, surplus and retained earnings of not

less than \$30,000,000 and whose notes or commercial paper are rated in the highest rating category by Moody's (if the Certificates are then rated by Moody's) and S&P (if the Certificates are then rated by S&P).

12. Money market funds restricted to obligations issued or guaranteed as to payment of principal and interest by the full faith and credit of the United States of America, including such funds for which the Trustee or an affiliate acts as investment advisor or provides other services, which are rated in the highest rating category by S&P.

13. Investment Agreements which are approved in writing by Moody's and S&P.

14. Shares in a California common law trust established pursuant to Title 1, Division 7, Chapter 5 of the California Government Code which invests exclusively in investments permitted by Section 53635 of Title 5, Division 2, Chapter 4 of the California Government Code, as it may be amended; i.e., the California Arbitrage Management Program (CAMP).

"Lease Agreement" means the Lease Agreement, dated as of March 1, 2019, by and between the Corporation as lessor and the City as lessee, together with any duly authorized and executed amendments thereto.

"Lease Default Event" means any of the events specified in the Lease Agreement.

"Lease Payments" means the aggregate of the Tax-Exempt Lease Payments and the Taxable Lease Payments required to be paid by the City pursuant to the Lease Agreement, including any prepayment thereof pursuant to the Lease Agreement.

"Lease Payment Date" means April 15 and October 15 of each year during the term of the Lease Agreement, commencing October 15, 2019.

"Lease Payment Fund" means the fund by that name established and held by the Trustee pursuant to the Trust Agreement.

"Leased Property" means, initially, the Rinconada Library, as more particularly described in Exhibit A of the Property Lease.

"Lease Term" means the period during which the Lease is in effect as specified in the Lease Agreement.

"Moody's" means Moody's Investors Service, of New York, New York, or its successors.

"Net Proceeds" means any insurance proceeds or condemnation award in excess of \$50,000, paid with respect to the Leased Property, to the extent remaining after payment therefrom of all expenses incurred in the collection thereof.

"Original Purchaser" means Stifel, Nicolaus & Company, Incorporated, as original purchaser of the Certificates upon their delivery by the Trustee on the Closing Date.

"Outstanding", when used as of any particular time with reference to Certificates, means (subject to the provisions the Trust Agreement) all Certificates theretofore, or thereupon being, executed and delivered by the Trustee under the Trust Agreement except (1) Certificates theretofore cancelled by the Trustee or surrendered to the Trustee for cancellation; (2) Certificates with respect to which all liability of the City shall have been discharged in accordance with the Trust Agreement, including Certificates (or portions of Certificates) referred to the Trust Agreement; and (3) Certificates for the transfer or exchange of or in lieu of or in substitution for which other Certificates shall have been executed and delivered by the Trustee pursuant to the Trust Agreement.

“Owner” or **“Certificate Owner”**, when used with respect to a Certificate means the person in whose name the ownership of such Certificate shall be registered.

“Parking Garage Costs” means all costs of payment of, or reimbursement for, design, acquisition, construction, installation and equipping of the California Avenue Parking Garage, including but not limited to, architect and engineering fees, construction contractor payments, costs of feasibility and other reports, inspection costs, performance bond premiums and permit fees, and includes Costs of Issuance not paid out of the Costs of Issuance Fund.

“Parking Garage Construction Fund” means the fund by that name established and held by the Trustee pursuant to the Trust Agreement.

“Payment Date” means (i) with respect to the interest component of the Lease Payments payable to the Owners of the Certificates, November 1, 2019, and the first day of each May and November thereafter so long as any Certificates are Outstanding under the Trust Agreement, and (ii) with respect to the principal of the Certificates, November 1, 2019 and each November 1 thereafter so long as the Certificates are Outstanding, terminating November 1, 2048.

“Permitted Encumbrances” means, as of any particular time: (i) liens for general ad valorem taxes and assessments, if any, not then delinquent; (ii) the Assignment Agreement; (iii) the Property Lease and the Lease Agreement; (iv) the Trust Agreement; (v) any right or claim of any mechanic, laborer, materialman, supplier or vendor not filed or perfected in the manner prescribed by law; (vi) easements, rights of way, mineral rights, drilling rights and other rights, reservations, covenants, conditions or restrictions which exist of record as of the date on which the Certificates are delivered to the purchasers thereof and which the City certifies in writing will not materially impair the use of the Leased Property; (vii) easements, rights of way, mineral rights, drilling rights and other rights, reservations, covenants, conditions or restrictions established following the date of recordation of the Property Lease and to which the Corporation and the City consent in writing and (viii) any items listed in the title report issued by Stewart Title Guaranty on the date of execution and delivery of the Certificates.

“Principal Amount” means the total unpaid principal component of the Lease Payments due under the Lease Agreement.

“Pro Rata” means, with respect to the 2019A Certificates and the 2019B Certificates, 71.68% for the 2019A Certificates, and 28.32% for the 2019B Certificates.

“Property Lease” means the Property Lease, dated as of March 1, 2019, recorded concurrently with the Lease Agreement, by and between the City, as lessor, and the Corporation, as lessee, together with any duly authorized and executed amendments thereto.

“Property Lease Payment” means the payment required to be paid by the Corporation on the Closing Date pursuant to the Property Lease.

“Rating Category” means any generic rating category of Moody's or S&P, without regard to any refinement of such category by plus or minus sign or by numerical or other qualifying designation.

“Record Date” means the close of business on the fifteenth day of the month preceding each Payment Date, whether or not such fifteenth day is a Business Day.

“Registration Books” means the records maintained by the Trustee pursuant to the Trust Agreement for registration and transfer of ownership of the Certificates.

“Regulations” means temporary and permanent regulations promulgated under the Code.

“Rental Period” means each twelve-month period during the term of the Lease Agreement commencing on November 2 in any year and ending on the next succeeding November 1, except that the first rental period shall commence on the Closing Date.

“S&P” means S&P Global Ratings, of New York, New York, or its successors.

“State” means the State of California.

“Tax-Exempt Construction Account” means the account by that name established within the Parking Garage Construction Fund pursuant to the Trust Agreement.

“Tax-Exempt Lease Payment Account” means the account by that name established within the Lease Payment Fund pursuant to the Trust Agreement.

“Tax-Exempt Lease Payments” means the Lease Payments shown on Exhibit A-1 of the Lease Agreement.

“Taxable Construction Account” means the account by that name established within the Parking Garage Construction Fund pursuant to the Trust Agreement.

“Taxable Lease Payment Account” means the account by that name established within the Lease Payment Fund pursuant to the Trust Agreement.

“Taxable Lease Payments” means the Lease Payments shown on Exhibit A-2 of the Lease Agreement.

“Term of the Lease Agreement” means the time during which the Lease Agreement is in effect, as provided in the Lease Agreement.

“Trust Agreement” means the Trust Agreement dated as of March 1, 2019 by and among Trustee, the Corporation and the City, relating to the Certificates.

“Trustee” means U.S. Bank National Association, and its successors and assigns.

“Written Request of the Corporation” means an instrument in writing signed by the Corporation Representative.

“Written Request of the City” means an instrument in writing signed by the City Representative.

PROPERTY LEASE

Under the Property Lease (the “Property Lease”), the City initially leases the Rinconada Library (the “Leased Property”) to the Corporation, to enable the Corporation to sublease the Leased Property back to the City under the Lease Agreement.

Term

The term of the Property Lease will commence on the Closing Date and will end on November 1, 2049, unless such term is extended as provided in the Property Lease. If on November 1, 2049, the Trust Agreement will not be discharged by its terms, then the term of the Property Lease will be extended until the Trust Agreement will be discharged by its terms (but in no event beyond November 1, 2059). If prior to November 1, 2049, the Trust Agreement will be discharged by its terms, the term of the Property Lease will thereupon end.

Property Lease Payment

Under the Property Lease, the Corporation agrees to pay to the City, as rental for the use and occupancy of the Leased Property during the term of the Property Lease, the amount of \$37,370,000, which will be due and payable on the Closing Date, and which will be deemed to have been paid when the proceeds of the Certificates are deposited with the Trustee. No further amounts will be due and payable by the Corporation to the City under the Property Lease.

Title

Title to the Leased Property will reside in the City, and during the term of the Property Lease, the City will hold title to the Leased Property and any and all additions which comprise fixtures, repairs, replacements or modifications to the Leased Property, including those fixtures, repairs, replacements or modifications which are added to the Leased Property by the City at its own expense and which may be removed without damaging the Leased Property and including any items added to the Leased Property by the City pursuant to the Lease Agreement.

Eminent Domain

If all of the Leased Property will be 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 Property Lease will cease as of the day possession will be so taken. If less than all of the Leased Property will be taken permanently, or if all of the Leased Property or any part thereof will be taken temporarily, under the power of eminent domain, the Property Lease will continue in full force and effect and will not be terminated by virtue of such taking and the parties to the Property Lease waive the benefit of any law to the contrary.

Application of Net Proceeds

The Net Proceeds of any insurance award resulting from any damage to or destruction of the Leased Property or any improvements thereon by fire or other casualty, and the Net Proceeds of any eminent domain award resulting from any event described in the Property Lease, will be applied as set forth in the Lease Agreement. All such Net Proceeds will be paid to the City or the Trustee as their interests may appear under the Lease Agreement, and the Corporation waives any and all right, title and interest which it may have in and to any such Net Proceeds by virtue of its estate in the Leased Property under the Property Lease.

LEASE AGREEMENT

Agreement to Lease; Term

The Corporation subleases the Leased Property to the City, and the City subleases the Leased Property from the Corporation, upon the terms and conditions set forth in the Lease Agreement.

The term of the Lease Agreement is coterminous with the term of the Property Lease. The term of the Lease Agreement will commence on the Closing Date and will end on November 1, 2049, unless such term is extended as provided in the Lease Agreement. If on November 1, 2049, the Trust Agreement will not be discharged by its terms, then the term of the Lease Agreement will be extended until the Trust Agreement will be discharged by its terms (but in no event beyond November 1, 2059). If prior to November 1, 2049, the Trust Agreement will be discharged by its terms, the term of the Lease Agreement will thereupon end. The foregoing provisions are subject to the provisions of the Lease Agreement relating to the taking in eminent domain of the Leased Property or any portion thereof.

Acquisition and Construction of the California Avenue Parking Garage

The Corporation has appointed the City as its agent for the purposes of acquisition, construction, installation and equipping of the California Avenue Parking Garage. The City, as agent of the Corporation, shall cause the acquisition, construction, installation and equipping of the California Avenue Parking Garage to be performed diligently.

Abatement of Lease Payments in the Event of Damage or Destruction.

The Lease Payments shall be abated under the Lease Agreement during any period in which due to damage or destruction of the Leased Property in whole or in part, or due to taking in eminent domain proceedings of the Leased Property in whole or in part, there is substantial interference with the City's use and occupancy of all or any portion of the Leased Property. The amount of such abatement shall be an amount agreed upon by the City and the Corporation such that the resulting Lease Payments represent fair consideration for the use and occupancy of the portions of the Leased Property not damaged or destroyed. Such abatement shall 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, the Lease Agreement shall continue in full force and effect and the City waives any right to terminate the Lease Agreement by virtue of any such damage and destruction. However, there shall be no abatement of Lease Payments under the Lease Agreement to the extent that the proceeds of an eminent domain or insurance award are available to pay Lease Payments, or to the extent that moneys are available in the Lease Payment Fund, it being declared that such proceeds and amounts constitute special funds for the payment of the Lease Payments.

Quiet Enjoyment

The Corporation will provide the City with quiet use and enjoyment of the Leased Property, and the City will, for the term of the Lease Agreement, peaceably and quietly have and hold and enjoy the Leased Property, without suit, trouble or hindrance from the Corporation, except as expressly set forth in the Lease Agreement. The Corporation will, at the request of the City and at the City's cost, join in any legal action in which the City asserts its right to such possession and enjoyment to the extent the Corporation may lawfully do so. Notwithstanding the foregoing, the Corporation shall have the right to inspect the Leased Property as provided in the Lease Agreement.

Title

During the term of the Lease Agreement, the City will hold title to the Leased Property and any and all additions which comprise fixtures, repairs, replacements or modifications to the Leased Property, including those fixtures, repairs, replacements or modifications which are added to the Leased Property by the City at its own expense and which may be removed without damaging the Leased Property and including any items added to the Leased Property by the City pursuant to the Lease Agreement. Such title will be governed by the provisions of the Property Lease during the term of the Property Lease.

If the City prepays the Lease Payments in full pursuant to the Lease Agreement or makes the security deposit permitted by the Lease Agreement or pays all Lease Payments during the term of the Lease Agreement as the same become due and payable, all right, title and interest of the Corporation under the Property Lease in and to the Leased Property will be terminated. The Corporation agrees to take any and all steps and execute and record any and all documents reasonably required by the City to consummate any such termination of leasehold estate.

Maintenance, Utilities, Taxes and Assessments

Throughout the term of the Lease Agreement, as part of the consideration for the rental of the Leased Property, all improvement, repair and maintenance of the Leased Property shall be the responsibility of the City, and the City shall pay for or otherwise arrange for the payment of all utility services supplied to the Leased Property, which may include, without limitation, janitor service, security, power, gas, telephone, light, heating, water and all

other utility services, and shall pay for or otherwise arrange for the payment of the cost of the repair and replacement of the Leased Property resulting from ordinary wear and tear or want of care on the part of the City or any assignee or lessee thereof. In exchange for the Lease Payments, the Corporation agrees to provide only the Leased Property. The City waives the benefits of Section 1942 of the California Civil Code and waives the right to make repairs at the expense of the Corporation or in lieu thereof, vacate under Section 1942 of the California Civil Code, and all similar rights under the statutes of similar effect, but such waiver shall not limit any of the rights of the City under the terms of the Lease Agreement.

The City shall also pay or cause to be paid all taxes and assessments of any type or nature, if any, charged to the Corporation or the City affecting the Leased Property or the interests or estates therein; provided that with respect to special assessments or other governmental charges that may lawfully be paid in installments over a period of years, the City shall be obligated to pay only such installments as are required to be paid during the term of the Lease Agreement as and when the same become due.

The City may, at the City's expense and in its name, in good faith contest any such taxes, assessments, utility and other charges and, in the event of any such contest, may permit the taxes, assessments or other charges so contested to remain unpaid during the period of such contest and any appeal therefrom unless the Corporation shall notify the City that, in the opinion of Independent Counsel, by nonpayment of any such items, the interest of the Corporation in the Leased Property will be materially endangered or any part thereof will be subject to loss or forfeiture, in which event the City shall promptly pay such taxes, assessments or charges or provide the Corporation with full security against any loss which may result from nonpayment, in form satisfactory to the Corporation and the Trustee.

Modification of Leased Property

The City shall, at its own expense, have the right to remodel the Leased Property or to make additions, modifications and improvements to the Leased Property. All additions, modifications and improvements shall thereafter comprise part of the Leased Property and be subject to the provisions of the Lease Agreement. Such additions, modifications and improvements shall not in any way damage the Leased Property or cause it 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, shall be of a value which is not substantially less than the value of the Leased Property 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; provided that if any such lien is established and the City shall first notify or cause to be notified the Corporation 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 shall provide the Corporation with full security against any loss or forfeiture which might arise from the nonpayment of any such item, in form satisfactory to the Corporation. The Corporation will cooperate fully in any such contest, upon the request and at the expense of the City.

Insurance

The Lease Agreement requires the City to maintain or cause to be maintained the following insurance against risk of physical damage to the Leased Property and other risks for the protection of the Certificate Owners, the Corporation and the Trustee.

Public Liability and Property Damage Insurance

The City shall maintain or cause to be maintained, throughout the term of the Lease Agreement, a standard comprehensive general insurance policy or policies in protection of the Corporation, City, and their respective members, officers, agents and employees. 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. Said policy or policies shall provide coverage in the minimum liability limits of \$1,000,000 for personal injury or death of each person and \$3,000,000 for personal injury or deaths of two or more persons in each accident or event, and in a minimum amount of \$150,000 (subject to a deductible clause of not to exceed \$250,000, or such higher amount as the City shall determine, provided that such higher deductible shall be considered a self-insured retention) for damage to property resulting from each accident or event. Such public liability and property damage insurance may, however, be in the form of a single limit policy in the amount of \$3,000,000 per occurrence covering all such risks. Such liability insurance may be maintained as part of or in conjunction with any other liability insurance coverage carried by the City. The proceeds of such liability insurance shall be applied toward extinguishment or satisfaction of the liability with respect to which the proceeds of such insurance shall have been paid.

Fire and Extended Coverage Insurance; Title Insurance

The City shall procure and maintain, or cause to be procured and maintained, throughout the term of the Lease Agreement, insurance against loss or damage to any structures constituting any part of the Leased Property by fire and lightning, with extended coverage and vandalism and malicious mischief insurance. Said extended coverage insurance shall, 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. The City shall have no obligation to obtain earthquake insurance. Such insurance shall be in an amount at least equal to the lesser of (i) 100% of the replacement cost (without deducting for depreciation) of the Leased Property and (ii) the aggregate principal amount of Certificates at the time outstanding. Such insurance may be subject to deductible clauses of not to exceed \$100,000 for any one loss. Such insurance may be maintained as part of or in conjunction with any other fire and extended coverage carried by the City. 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 authority or other program providing pooled insurance. The City assigns to the Corporation all right of the City to collect and receive Net Proceeds under any of said policies, which right has been assigned by the Corporation to the Trustee pursuant to the Assignment Agreement. The Net Proceeds of such insurance shall be applied as provided in the Lease Agreement.

The City shall procure, and deliver to the Trustee on the Closing Date, a title insurance policy which insures the leasehold estate created under the Lease Agreement, subject only to Permitted Encumbrances, in an amount equal to the principal amount of the Certificates.

Rental Interruption Insurance.

The City shall procure and maintain, or cause to be procured and maintained, throughout the term of the Lease Agreement, rental interruption or use and occupancy insurance to cover loss, total or partial, of the use of the buildings, facilities and other improvements constituting any part of the Leased Property and the California Avenue Parking Garage, as a result of any of the hazards covered in the insurance required by the Lease Agreement, in an amount at least equal to the maximum Lease Payments coming due and payable during any two consecutive Fiscal Years during the remaining term of the Lease Agreement. 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 authority 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, shall be paid to the Trustee and deposited in the Tax-Exempt Lease Payment Account and the Taxable Lease Payment Account on a Pro Rata basis, and shall be credited towards the payment of the Lease Payments allocable to the insured improvements as the same become due and payable.

Liens

The City shall not, directly or indirectly, create, incur, assume or suffer to exist any mortgage, pledge, lien, charge, encumbrance or claim on or with respect to the Leased Property, other than the respective rights of the

Corporation and the City as provided in the Lease Agreement and Permitted Encumbrances. Except as expressly provided, the City shall promptly, at its own expense, take such action as may be necessary to duly discharge or remove any such mortgage, pledge, lien, charge, encumbrance or claim, for which it is responsible, if the same shall arise at any time. The City shall reimburse the Corporation for any expense incurred by it in order to discharge or remove any such mortgage, pledge, lien, charge, encumbrance or claim.

Security Deposit

The City may on any date secure the payment of Lease Payments by a deposit with the Trustee of: (i) an amount of cash which, together with amounts on deposit in the Lease Payment Fund and the Insurance and Condemnation Fund, is sufficient to pay all unpaid Lease Payments, including the principal and interest components thereof, in accordance with the Lease Agreement, or (ii) Federal Securities together with cash, if required, in such amount as will, in the opinion of an independent certified public accountant, together with interest to accrue thereon and, if required, all or a portion of moneys or Federal Securities then on deposit in the Lease Payment Fund and the Insurance and Condemnation Fund, be fully sufficient to pay all unpaid Lease Payments on their respective Lease Payment Dates or on any purchase option date as set forth in the Lease Agreement, as the City shall instruct at the time of said deposit. In the event of a security deposit, all obligations of the City under the Lease Agreement, and all security provided by the Lease Agreement for said obligations, shall cease and terminate, excepting only the obligation of the City to make, or cause to be made, Lease Payments from such security deposit, and title to the Leased Property shall be affected thereby as described in the Lease Agreement. Said security deposit shall be deemed to be and shall constitute a special fund for the payment of Lease Payments in accordance with the provisions of the Lease Agreement.

Prepayment; Purchase Option

The City may exercise its option to prepay the principal component of the Lease Payments, in whole or in part, on any date on or after October 15, 2028, by paying a prepayment price equal to the aggregate or a portion of the unpaid principal components of the remaining Lease Payments, together with the interest component of the Lease Payment required to be paid on such date, and premium due in connection with the prepayment of the Certificates, if any. The City shall notify the Corporation and the Trustee as to which of the Tax-Exempt Lease Payments and Taxable Lease Payments it wishes to prepay. Such prepayment price shall be deposited by the Trustee in the applicable account within the Lease Payment Fund to be applied to the prepayment of the Certificates pursuant to the Trust Agreement. The City shall give the Trustee notice of its intention to exercise its option not less than forty-five (45) days in advance of the date of exercise. In the event the Lease Payments have been fully paid, and the City prepays the entire unpaid principal component of the Lease Payments in whole, the City will be deemed to have purchased the Leased Property and title to the Leased Property shall thereupon vest in the City, free and clear of any encumbrance created by the Lease Agreement.

Tax Covenants

Private Activity Bond Limitation. The City will assure that the proceeds of the 2019A Certificates are not so used as to cause the obligations of the City under the Lease Agreement to satisfy the private business tests of section 141(b) of the Code or the private loan financing test of section 141(c) of the Code.

Federal Guarantee Prohibition. The City will not take any action or permit or suffer any action to be taken if the result of such action would be to cause any of the obligations of the City under the Lease Agreement to be “federally guaranteed” within the meaning of section 149(b) of the Code.

Rebate Requirement. The City will take any and all actions necessary to assure compliance with section 148(f) of the Code, relating to the rebate of excess investment earnings, if any, to the federal government, to the extent that such section is applicable to the 2019A Certificates and the Lease Agreement.

No Arbitrage. The City will not take, or permit or suffer to be taken by the Trustee or otherwise, any action with respect to the proceeds of the 2019A Certificates which, if such action had been reasonably expected to have been taken, or had been deliberately and intentionally taken, on the date of delivery of the Lease Agreement would have caused any of the obligations of the City under the Lease Agreement to be “arbitrage bonds” within the meaning of section 148 of the Code.

Maintenance of Tax-Exemption. The City will take all actions necessary to assure the exclusion of interest with respect to the 2019A Certificates from the gross income of the Owners of the 2019A Certificates to the same extent as such interest is permitted to be excluded from gross income under the Code as in effect on the date of delivery of the Lease Agreement.

Record Retention. The City will retain its records of all accounting and monitoring it carries out with respect to the 2019A Certificates for at least 3 years after the 2019A Certificates mature or are redeemed (whichever is earlier); however, if the 2019A Certificates are redeemed and refunded, the City will retain its records of accounting and monitoring at least 3 years after the earlier of the maturity or redemption of the last obligation in the series of obligations that refunded the 2019A Certificates.

Compliance with Tax Certificate. The City will comply with the provisions of the tax certificate and the use of proceeds certificate to be delivered with respect to the 2019A Certificates.

Assignment; Subleases

The Corporation has assigned certain of its rights under the Lease Agreement to the Trustee pursuant to the Assignment Agreement. The City may not assign the Lease Agreement. The City may lease all or a portion of the Leased Property only with the prior written consent of the Corporation, and subject to the following conditions: (1) the Lease Agreement and the obligation of the City to make Lease Payments thereunder shall remain obligations of the City, (2) the City will, within thirty (30) days after the delivery thereof, furnish or cause to be furnished to the Corporation and the Trustee a true and complete copy of such lease, (3) such lease shall not cause the City to violate any of its tax covenants in the Lease Agreement, (4) no such lease by the City will cause the Leased Property to be used for a purpose other than as may be authorized under the provisions of the Constitution and laws of the State and (5) the City shall furnish the Corporation and the Trustee with a written opinion of bond counsel stating that such lease does not cause the interest components of the Tax-Exempt Lease Payments to become subject to federal or State personal income taxes.

Notwithstanding the foregoing, the City may sublease a portion of the rooftop of the California Avenue Parking Garage in connection with the installation of distributed renewable energy systems without complying with the preceding clause (2).

Amendment

Except as provided below, without the prior written consent of the Trustee, the City will not alter, modify or cancel, or agree or consent to alter, modify or cancel the Lease Agreement, excepting only such alteration or modification as may be permitted by the Trust Agreement.

In addition, the Lease Agreement may be amended to obligate the City to pay additional amounts of rental thereunder for the use and occupancy of the Leased Property or any portion thereof, but only if (a) such additional amounts of rental do not cause the total rental payments made by the City under the Lease Agreement to exceed the fair rental value of the Leased Property, (b) the City shall have obtained and filed with the Trustee and the Corporation a written certificate to the effect that the estimated fair market value thereof is not less than the aggregate unpaid principal components of such additional amount of rental plus the existing aggregate unpaid principal components of the Lease Payments, (c) such additional amounts of rental shall be pledged or assigned for the payment of any bonds, notes, leases or other obligations the proceeds of which shall be applied to finance the

completion of public facilities and (d) the City shall send notification of the additional financing to the rating agency then rating the Certificates.

TRUST AGREEMENT

Trustee

The Trustee is appointed pursuant to the Trust Agreement and is authorized to prepare, execute and deliver the Certificates thereunder, and to act as a depository of amounts held thereunder. The Trustee is required to make deposits into and withdrawals from funds, and invest amounts held under the Trust Agreement in accordance with the City's instructions.

Funds

The Trust Agreement creates the Lease Payment Fund, including the Tax-Exempt Lease Payment Account and the Taxable Lease Payment Account, the Parking Garage Construction Fund, including the Tax-Exempt Construction Account and the Taxable Construction Account, the Costs of Issuance Fund and the Insurance and Condemnation Fund to be held in trust by the Trustee.

Lease Payment Fund. The Trustee shall establish a special fund designated as the "Lease Payment Fund", and within such fund the "Tax-Exempt Lease Payment Account" and the "Taxable Lease Payment Account". All moneys at any time deposited by the Trustee in the Lease Payment Fund shall be held by the Trustee in trust for the benefit of the Owners of the Certificates. So long as any Certificates are Outstanding, neither the City nor the Corporation shall have any beneficial right or interest in the Lease Payment Fund or the moneys deposited therein, except only as provided in the Trust Agreement, and such moneys shall be used and applied by the Trustee as set forth in the Trust Agreement.

There shall be deposited in the Tax-Exempt Lease Payment Account all Tax-Exempt Lease Payments received by the Trustee, including any moneys required to be deposited therein pursuant to the Lease Agreement or pursuant to the Trust Agreement, and including any other moneys required to be credited towards payment of the Tax-Exempt Lease Payments.

There shall be deposited in the Taxable Lease Payment Account all Taxable Lease Payments received by the Trustee, including any moneys required to be deposited therein pursuant to the Lease Agreement or pursuant to the Trust Agreement, and including any other moneys required to be credited towards payment of the Taxable Lease Payments.

All amounts in the Lease Payment Fund shall be used and withdrawn by the Trustee solely for the purpose of paying the principal, interest and prepayment premiums (if any) with respect to the Certificates as the same shall become due and payable, in accordance with the Trust Agreement; except that all amounts in the Tax-Exempt Lease Payment Account shall be used and withdrawn by the Trustee solely for the purpose of paying the principal, interest and prepayment premiums (if any) with respect to the 2019A Certificates, and all amounts in the Taxable Lease Payment Account shall be used and withdrawn by the Trustee solely for the purpose of paying the principal, interest and prepayment premiums (if any) with respect to the 2019B Certificates.

Any surplus remaining in the Lease Payment Fund, after prepayment and payment of all Certificates, including premiums and accrued interest (if any) and payment of any applicable fees to the Trustee or provision for such prepayment or payment having been made to the satisfaction of the Trustee, shall be withdrawn by the Trustee and remitted to the City.

Parking Garage Construction Fund. The Trustee shall establish and maintain a separate fund to be known as the "Parking Garage Construction Fund", and within the Parking Garage Construction Fund, the "Tax-Exempt

Construction Account” and the “Taxable Construction Account”. The Trustee shall disburse moneys in the Parking Garage Construction Fund from time to time, for the purpose of paying the Parking Garage Costs. Each such disbursement shall be documented by a requisition which shall: (a) identify the total amount of such costs to be paid pursuant to such requisition, including all items of cost in such detail as may be available to the City; and (b) state with respect to such disbursement (i) the requisition number, in sequential order, (ii) the amount to be disbursed for payment of such costs, (iii) whether such amounts are to be paid from the Tax-Exempt Construction Account or the Taxable Construction Account and (iv) that each item of cost identified therein has been properly incurred, constitutes payment of a Parking Garage Cost and has not been the basis of any previous disbursement. Upon completion of the California Avenue Parking Garage and following payment of all Parking Garage Costs, the Parking Garage Construction Fund and the accounts therein shall be closed and transferred to the Lease Payment Fund.

Costs of Issuance Fund. The Trustee shall establish a special fund designated as the “Costs of Issuance Fund”; shall keep such fund separate and apart from all other funds and moneys held by it; and shall administer such fund as provided in the Trust Agreement. There shall be deposited in the Costs of Issuance Fund the proceeds of the Certificates deposited therein pursuant to the Trust Agreement, and any other funds from time to time deposited by the Trustee. The moneys in the Costs of Issuance Fund shall be disbursed to pay the Costs of Issuance from time to time upon the receipt of Written Requests of the City setting forth the amounts to be disbursed for payment or reimbursement of Costs of Issuance and the name and address of the person or persons to whom said amounts are to be disbursed, stating that the amounts to be disbursed are for Costs of Issuance properly chargeable to the Costs of Issuance Fund. Any amounts remaining in the Costs of Issuance Fund on the date one hundred and twenty (120) days after the Closing Date shall be withdrawn therefrom by the Trustee and transferred to the Lease Payment Fund.

Insurance and Condemnation Fund; Application of Net Proceeds of Insurance Award

Any Net Proceeds of insurance against accident to or destruction of any structure constituting any part of the Leased Property collected by the City in the event of any such accident or destruction shall be paid to the Trustee by the City pursuant to the Lease Agreement and deposited by the Trustee promptly upon receipt thereof in a special fund to be established and held by the Trustee, designated as the “Insurance and Condemnation Fund”. If the City determines and notifies the Trustee in writing of its determination, within ninety (90) days following the date of such deposit, that the replacement, repair, restoration, modification or improvement of the Leased Property is not economically feasible or in the best interest of the City, then such Net Proceeds shall be promptly transferred by the Trustee to the Lease Payment Fund and the accounts in the Lease Payment Fund, on a Pro Rata basis, and applied to the prepayment of Lease Payments pursuant to the Trust Agreement; provided, that such transfer shall only be made if the amount transferred is sufficient to prepay the principal amount of Certificates attributable to the portion of the Leased Property damaged or destroyed, determined on the basis of the ratio resulting from dividing the cost of the portion of the Leased Property so damaged or destroyed by the total cost of the Leased Property. All Net Proceeds deposited in the Insurance and Condemnation Fund and not so transferred to the Lease Payment Fund shall be applied to the prompt replacement, repair, restoration, modification or improvement of the damaged or destroyed portions of the Leased Property by the City.

Application of Net Proceeds of Eminent Domain Award

If all or any part of the Leased Property shall be taken by eminent domain proceedings (or sold to a government threatening to exercise the power of eminent domain) the Net Proceeds therefrom shall be deposited with the Trustee in the Insurance and Condemnation Fund pursuant to the Lease Agreement and shall be applied and disbursed by the Trustee as follows: (a) if all of the Leased Property shall have been taken in such eminent domain proceedings or sold to a government threatening the use of eminent domain powers, or if the City has given written notice to the Trustee of its determination that such proceeds are not needed for repair or rehabilitation of the Leased Property, the Trustee shall transfer such proceeds to the accounts within the Lease Payment Fund on a Pro Rata basis to be credited towards the prepayments of the Lease Payments required to be paid pursuant to the Lease Agreement and applied to the prepayment of Certificates and (b) if less than all of the Leased Property shall have been taken in such eminent domain proceedings or sold to a government threatening the use of eminent domain powers, and if the City has given written notice to the Trustee of its determination that such proceeds are needed for

repair, rehabilitation or replacement of the Leased Property, the Trustee shall pay to the City, or to its order, from said proceeds such amounts as the City may expend for such repair or rehabilitation.

Investment of Funds

All moneys in any of the funds and accounts established pursuant to the Trust Agreement shall be invested by the Trustee, upon Written Request of the City, solely in Investment Securities. Investment Securities shall be purchased at Fair Market Value, provided the Trustee shall not be responsible to determine Fair Market Value. Moneys in all funds and accounts shall be invested in Investment Securities maturing not later than five (5) years from the date said investment is made. Any income, profit or loss on such investments in any of the funds and accounts shall be deposited in or charged to the respective funds and accounts from which such investments were made.

Remedies Upon Event of Default

If an Event of Default shall happen, then and in each and every such case during the continuance of such Event of Default, the Trustee may, and upon request of the Owners as provided in the Lease Agreement shall, exercise any and all remedies available pursuant to law or granted pursuant to the Lease Agreement; provided, however, that notwithstanding anything in the Trust Agreement or in the Lease Agreement to the contrary, there shall be no right under any circumstances to accelerate the maturities of the Certificates or otherwise to declare any Lease Payment not then in default to be immediately due and payable.

All moneys received by the Trustee pursuant to any right given or action taken under the provisions of the Trust Agreement or the Lease Agreement shall be applied by the Trustee first, to the payment of the costs and expenses of the Trustee and of the Certificate Owners in declaring such Event of Default, including reasonable compensation to its or their agents, attorneys and advisors and second, to the payment of the whole amount then owing and unpaid with respect to the Certificates for principal and interest, with interest on the overdue principal and installments of interest, and in case such moneys shall be insufficient to pay in full the whole amount so owing and unpaid with respect to the Certificates, then to the payment of such principal and interest without preference or priority of principal over interest, or of interest over principal, or of any installment of interest over any other installment of interest, ratably to the aggregate of such principal and interest.

Amendment of Trust Agreement or Lease Agreement

The Trust Agreement or the Lease Agreement may be modified or amended at any time with the written consent of the Owners of at least sixty percent (60%) in aggregate principal amount of the Certificates then Outstanding. No such modification or amendment shall (1) extend or have the effect of extending the fixed maturity of any Certificate or reducing the interest rate with respect thereto or extending the time of payment of interest, or reducing the amount of principal thereof or reducing any premium payable upon the prepayment thereof, without the express consent of the Owner of such Certificate, or (2) reduce or have the effect of reducing the percentage of Certificates required for the affirmative vote or written consent to an amendment or modification of the Lease Agreement, or (3) modify any of the rights or obligations of the Trustee without its written assent thereto.

The Trust Agreement or the Lease Agreement may be modified or amended at any time without the consent of any such Owners, but only to the extent permitted by law and only (1) to add to the covenants and agreements of any party, other covenants to be observed, or to surrender any right or power reserved to the City, (2) to cure, correct or supplement any ambiguous or defective provision, (3) to make such additions, deletions or modifications as may be necessary or desirable to assure exemption from federal income taxation of the portion of Tax-Exempt Lease Payments designated as and comprising interest and received by Owners of the 2019A Certificates, (4) in regard to questions arising under the Trust Agreement or the Lease Agreement, as the parties to the Trust Agreement or the Lease Agreement may deem necessary or desirable and which shall not adversely affect the interests of the Owners of the Certificates or (5) to correct any incorrect property description.

Defeasance

The Certificates may be paid by the City in any of the following ways, provided that the City also pays or causes to be paid any other sums payable under the Trust Agreement by the City: (a) by paying or causing to be paid the Principal Amount relating to the Certificates, together with interest thereon, as and when the same become due and payable; (b) by depositing with the Trustee, in trust, at or before maturity, money or securities in the necessary amount to pay or prepay all Certificates then Outstanding or (c) by delivering to the Trustee, for cancellation by it, all of the Certificates then Outstanding. If the City shall also pay or cause to be paid all other sums payable by the City under the Trust Agreement, then and in that case, at the election of the City, and notwithstanding that any Certificates shall not have been surrendered for payment, the Trust Agreement and the pledge of Lease Payments and other assets made under the Trust Agreement and all covenants, agreements and other obligations of the City under the Trust Agreement shall cease, terminate, become void and be completely discharged and satisfied.

ASSIGNMENT AGREEMENT

The Corporation and the Trustee will enter into the Assignment Agreement under which the Corporation assigns and sets over to the Trustee, for the benefit of the Owners of the Certificates, all of the Corporation's rights under the Property Lease and the Lease Agreement (subject to certain exceptions), including the right of the Corporation to receive and collect Lease Payments, its right to receive and collect proceeds of any insurance maintained with respect to the Leased Property, or any eminent domain award paid with respect to the Leased Property and the right to exercise rights and remedies of the Corporation in the Lease Agreement to enforce payments of amounts thereunder. The Trustee accepts such assignment for the purpose of securing such payments due to and rights of the Owners of the Certificates, subject to the provisions of the Trust Agreement.

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APPENDIX F

DTC'S BOOK-ENTRY ONLY SYSTEM

The information in this Appendix F, concerning The Depository Trust Company, New York, New York ("DTC"), and DTC's book-entry system, has been furnished by DTC for use in official statements and the City takes no responsibility for the completeness or accuracy thereof. The City cannot and does not give any assurances that DTC, DTC Participants or Indirect Participants will distribute to the Beneficial Owners (a) payments of interest or principal with respect to the Certificates, (b) certificates representing ownership interest in or other confirmation of ownership interest in the Certificates, or (c) redemption or other notices sent to DTC or Cede & Co., its nominee, as the registered owner of the Certificates, 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 F. 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. Information Furnished by DTC Regarding its Book-Entry Only System

1. The Depository Trust Company ("DTC"), New York, NY, will act as securities depository for the Certificates (as used in this Appendix E, 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 maturity of the Securities, 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 is rated AA+ by Standard & Poor's. 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.

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 affect 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 the 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 the Securities unless authorized by a Direct Participant in accordance with DTC's MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the City 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 the 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 the City or the paying agent or bond trustee, 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 nor its nominee, the paying agent or bond trustee, or the City, 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 the City or the paying agent or bond trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

9. DTC may discontinue providing its services as depository with respect to the Securities at any time by giving reasonable notice to the City or the paying agent or bond trustee. Under such circumstances, in the event that a successor depository is not obtained, Security certificates are required to be printed and delivered.

10. The City may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, Security certificates will be printed and delivered to DTC.

11. The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that the City believes to be reliable, but the City takes no responsibility for the accuracy thereof.

APPENDIX G

FORMS OF CONTINUING DISCLOSURE CERTIFICATES

2019A CERTIFICATES

This CONTINUING DISCLOSURE CERTIFICATE (the “Disclosure Certificate”) is executed and delivered by the CITY OF PALO ALTO (the “City”) in connection with the execution and delivery of \$26,785,000 City of Palo Alto 2019 Certificates of Participation, Series A (California Avenue Parking Garage) (Tax-Exempt) (the “2019A Certificates”). The 2019A Certificates are being executed and delivered pursuant to a Trust Agreement, dated as of March 1, 2019, by and among U.S. Bank National Association, as trustee (the “Trustee”), the City and the Palo Alto Public Improvement Corporation (the “Trust Agreement”). Pursuant to Section 10.11 of the Trust Agreement, the City covenants and agree as follows:

Section 1. Definitions. In addition to the definitions set forth above and in the Trust Agreement, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section 1, the following capitalized terms shall have the following meanings:

“*Annual Report*” means any Annual Report provided by the City pursuant to, and as described in, Sections 3 and 4 of this Disclosure Certificate.

“*Annual Report Date*” means the March 31 after the end of the City’s Fiscal Year.

“*Dissemination Agent*” shall mean, initially, the City, or any successor Dissemination Agent designed in writing by the City and which has been filed with the then current Dissemination Agent a written acceptance of such designation.

“*Fiscal Year*” means any twelve-month period beginning on July 1 in any year and extending to the next succeeding June 30, both dates inclusive, or any other twelve-month period selected and designated by the City as its official fiscal year period under a Certificate of the City filed with the Trustee.

“*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, or any other repository of disclosure information that may be designated by the Securities and Exchange Commission as such for purposes of the Rule in the future.

“*Official Statement*” means the final official statement executed by the City in connection with the issuance of the 2019A Certificates.

“*Participating Underwriter*” means Stifel, Nicolaus & Company, Incorporated, as the original underwriter of the 2019A Certificates.

“*Rule*” means Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as it may be amended from time to time.

“*Significant Events*” means any of the events listed in Section 5(a) of this Disclosure Certificate.

Section 2. 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 2019A Certificates and in order to assist the Participating Underwriter in complying with S.E.C. Rule 15c2- 12(b)(5).

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 March 31, 2019, with the report for fiscal year 2018-19 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; *provided, however*, that the first Annual Report shall consist solely of the Official Statement. 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 Significant Event under Section 5(c). 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 in a timely manner 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. 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 prior to the annual filing deadline for Annual Reports provided for in Section 3 above, financial information and operating data with respect to the City for preceding fiscal year, substantially similar to that provided in the following tables in the Official Statement:

- (i) Table 2—General Fund Statement of Revenue, Expenditures and Changes in Fund Balances;
- (ii) Table 4—Tax Revenues by Source;
- (iii) Table 5—Assessed Valuations;
- (iv) Table 6—Largest Local Secured Property Tax Payers;
- (v) Table 7—Current Sales Tax Rates; and
- (vi) Table 8—Property Tax In-Lieu of VLF.

(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 Significant Events with respect to the 2019A Certificates:

(i) Principal and interest payment delinquencies;

(ii) Non-payment related defaults, if material;

(iii) Unscheduled draws on debt service reserves reflecting financial difficulties;

(iv) Unscheduled draws on credit enhancements reflecting financial difficulties;

(v) Substitution of credit or liquidity providers, or their failure to perform;

(vi) 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;

(vii) Modifications to rights of security holders, if material;

(viii) Bond calls, if material, and tender offers;

(ix) Defeasances;

(x) Release, substitution, or sale of property securing repayment of the securities, if material;

(xi) Rating changes;

(xii) Bankruptcy, insolvency, receivership or similar event of the City or other obligated person;

(xiii) 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;

(xiv) Appointment of a successor or additional trustee or the change of name of a trustee, if material;

(xv) The incurrence of a financial obligation of the City or other obligated person, if material, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the City or other obligated person, any of which affect security holders, if material; or

(xvi) A default, event of acceleration, termination event, modification of terms, or other similar events under the terms of a financial obligation of the City or other obligated person, any of which reflect financial difficulties.

(b) Whenever the City obtains knowledge of the occurrence of a Significant 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 Significant Event. Notwithstanding the foregoing, notice of Significant Events described in subsection (a)(viii) 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 2019A Certificates under the Trust Agreement.

(c) The City acknowledges that the events described in subparagraphs (a)(ii), (a)(vii), (a)(viii) (if the event is a bond call), (a)(x), (a)(xiii), (a)(xiv) and (a)(xv) 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. The City intends that the words used in paragraphs (xv) and (xvi) and the definition of “financial obligation” to have the meanings ascribed thereto in SEC Release No. 34-83885 (August 20, 2018).

(d) For purposes of this Disclosure Certificate, any event described in paragraph (a)(xii) 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.

Section 6. Identifying Information for Filings with the MSRB. All documents provided to the MSRB under this 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 2019A Certificates. If such termination occurs prior to the final maturity of the 2019A Certificates, the City shall give notice of such termination in the same manner as for a Significant 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 2019A Certificates, 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 2019A Certificates, 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 2019A Certificates in the manner provided in the Trust Agreement for amendments to the Trust Agreement with the consent of holders, or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the holders or beneficial owners of the 2019A Certificates.

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.

The Dissemination Agent shall not be obligated to enter into any amendment increasing or affecting its duties or obligations hereunder.

A notice of any amendment made pursuant to this Section 9 shall be filed in the same manner as for a Significant 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 Significant 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 Significant 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 Significant 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 2019A Certificates 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 Trust Agreement, and the sole remedy under this Disclosure Certificate in the event of any failure of the City to comply with this Disclosure Certificate shall be an action to compel performance.

Section 12. Duties, Immunities and Liabilities of Dissemination Agent.

(a) Article VIII of the Trust Agreement is hereby made applicable to this Disclosure Certificate as if this Disclosure Certificate were (solely for this purpose) contained in the Trust Agreement. The Dissemination Agent shall be entitled to the protections and limitations from liability afforded to the Trustee thereunder. The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Certificate, and the

City agrees to indemnify and save the Dissemination Agent, its officers, directors, employees and agents, harmless against any loss, expense and liabilities which they may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys' fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's negligence or willful misconduct. The Dissemination Agent shall have no duty or obligation to review any information provided to it by the City hereunder and shall not be deemed to be acting in any fiduciary capacity for the City, the 2019A Certificate 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 2019A Certificates.

(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. Beneficiaries. This Disclosure Certificate shall inure solely to the benefit of the City, the Dissemination Agent, the Participating Underwriter and the holders and beneficial owners from time to time of the 2019A Certificates and shall create no rights in any other person or entity.

Section 14. 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: [Closing Date]

CITY OF PALO ALTO

By _____
Authorized Officer

EXHIBIT A

NOTICE TO MSRB OF FAILURE TO FILE ANNUAL REPORT

Name of Issuer: City of Palo Alto, California
Name of Issue: CITY OF PALO ALTO
2019 Certificates of Participation, Series A
(California Avenue Parking Garage)
(Tax-Exempt)
Date of Issuance: [Closing Date]

NOTICE IS HEREBY GIVEN that the City has not provided an Annual Report with respect to the above-named Issue as required by the Continuing Disclosure Certificate, dated [Closing Date], furnished by the City in connection with the Issue. The City anticipates that the Annual Report will be filed by _____.

Date: _____

CITY OF PALO ALTO, as Dissemination Agent

By _____
Authorized Officer

2019B CERTIFICATES

This CONTINUING DISCLOSURE CERTIFICATE (the “Disclosure Certificate”) is executed and delivered by the CITY OF PALO ALTO (the “City”) in connection with the execution and delivery of \$10,585,000 City of Palo Alto 2019 Certificates of Participation, Series B (California Avenue Parking Garage) (Federally Taxable) (the “2019B Certificates”). The 2019B Certificates are being executed and delivered pursuant to a Trust Agreement, dated as of March 1, 2019, by and among U.S. Bank National Association, as trustee (the “Trustee”), the City and the Palo Alto Public Improvement Corporation (the “Trust Agreement”). Pursuant to Section 10.11 of the Trust Agreement, the City covenants and agree as follows:

Section 1. Definitions. In addition to the definitions set forth above and in the Trust Agreement, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section 1, the following capitalized terms shall have the following meanings:

“*Annual Report*” means any Annual Report provided by the City pursuant to, and as described in, Sections 3 and 4 of this Disclosure Certificate.

“*Annual Report Date*” means the March 31 after the end of the City’s Fiscal Year.

“*Dissemination Agent*” shall mean, initially, the City, or any successor Dissemination Agent designed in writing by the City and which has been filed with the then current Dissemination Agent a written acceptance of such designation.

“*Fiscal Year*” means any twelve-month period beginning on July 1 in any year and extending to the next succeeding June 30, both dates inclusive, or any other twelve-month period selected and designated by the City as its official fiscal year period under a Certificate of the City filed with the Trustee.

“*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, or any other repository of disclosure information that may be designated by the Securities and Exchange Commission as such for purposes of the Rule in the future.

“*Official Statement*” means the final official statement executed by the City in connection with the issuance of the 2019B Certificates.

“*Participating Underwriter*” means Stifel, Nicolaus & Company, Incorporated, as the original underwriter of the 2019B Certificates.

“*Rule*” means Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as it may be amended from time to time.

“*Significant Events*” means any of the events listed in Section 5(a) of this Disclosure Certificate.

Section 2. 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 2019B Certificates and in order to assist the Participating Underwriter in complying with S.E.C. Rule 15c2- 12(b)(5).

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 March 31, 2019, with the report for fiscal year 2018-19 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; *provided, however*, that the first Annual Report shall consist solely of the Official Statement. 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 Significant Event under Section 5(c). 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 in a timely manner 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. 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 prior to the annual filing deadline for Annual Reports provided for in Section 3 above, financial information and operating data with respect to the City for preceding fiscal year, substantially similar to that provided in the following tables in the Official Statement:

- (i) Table 2—General Fund Statement of Revenue, Expenditures and Changes in Fund Balances;
- (ii) Table 4—Tax Revenues by Source;
- (iii) Table 5—Assessed Valuations;
- (iv) Table 6—Largest Local Secured Property Tax Payers;
- (v) Table 7—Current Sales Tax Rates; and
- (vi) Table 8—Property Tax In-Lieu of VLF.

(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 Significant Events with respect to the 2019B Certificates:

- (i) Principal and interest payment delinquencies;
- (ii) Non-payment related defaults, if material;
- (iii) Unscheduled draws on debt service reserves reflecting financial difficulties;
- (iv) Unscheduled draws on credit enhancements reflecting financial difficulties;
- (v) Substitution of credit or liquidity providers, or their failure to perform;
- (vi) 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;
- (vii) Modifications to rights of security holders, if material;
- (viii) Bond calls, if material, and tender offers;
- (ix) Defeasances;
- (x) Release, substitution, or sale of property securing repayment of the securities, if material;
- (xi) Rating changes;
- (xii) Bankruptcy, insolvency, receivership or similar event of the City or other obligated person;
- (xiii) 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;
- (xiv) Appointment of a successor or additional trustee or the change of name of a trustee, if material;
- (xv) The incurrence of a financial obligation of the City or other obligated person, if material, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the City or other obligated person, any of which affect security holders, if material; or
- (xvi) A default, event of acceleration, termination event, modification of terms, or other similar events under the terms of a financial obligation of the City or other obligated person, any of which reflect financial difficulties.

(b) Whenever the City obtains knowledge of the occurrence of a Significant 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 Significant Event. Notwithstanding the foregoing, notice of Significant Events described in subsection (a)(viii) 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 2019B Certificates under the Trust Agreement.

(c) The City acknowledges that the events described in subparagraphs (a)(ii), (a)(vii), (a)(viii) (if the event is a bond call), (a)(x), (a)(xiii), (a)(xiv) and (a)(xv) 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. The City intends that the words used in paragraphs (xv) and (xvi) and the definition of “financial obligation” to have the meanings ascribed thereto in SEC Release No. 34-83885 (August 20, 2018).

(d) For purposes of this Disclosure Certificate, any event described in paragraph (a)(xii) 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.

Section 6. Identifying Information for Filings with the MSRB. All documents provided to the MSRB under this 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 2019B Certificates. If such termination occurs prior to the final maturity of the 2019B Certificates, the City shall give notice of such termination in the same manner as for a Significant 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 2019B Certificates, 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 2019B Certificates, 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 2019B Certificates in the manner provided in the Trust Agreement for amendments to the Trust Agreement with the consent of holders, or

(ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the holders or beneficial owners of the 2019B Certificates.

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.

The Dissemination Agent shall not be obligated to enter into any amendment increasing or affecting its duties or obligations hereunder.

A notice of any amendment made pursuant to this Section 9 shall be filed in the same manner as for a Significant 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 Significant 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 Significant 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 Significant 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 2019B Certificates 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 Trust Agreement, and the sole remedy under this Disclosure Certificate in the event of any failure of the City to comply with this Disclosure Certificate shall be an action to compel performance.

Section 12. Duties, Immunities and Liabilities of Dissemination Agent.

(a) Article VIII of the Trust Agreement is hereby made applicable to this Disclosure Certificate as if this Disclosure Certificate were (solely for this purpose) contained in the Trust Agreement. The Dissemination Agent shall be entitled to the protections and limitations from liability afforded to the Trustee thereunder. The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Certificate, and the City agrees to indemnify and save the Dissemination Agent, its officers, directors, employees and agents, harmless against any loss, expense and liabilities which they may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys' fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's negligence or willful misconduct. The Dissemination Agent shall have no duty or obligation to review any information provided to it by the City hereunder and shall not be deemed to be acting in any fiduciary capacity for the City, the 2019B Certificate 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 2019B Certificates.

(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. Beneficiaries. This Disclosure Certificate shall inure solely to the benefit of the City, the Dissemination Agent, the Participating Underwriter and the holders and beneficial owners from time to time of the 2019B Certificates and shall create no rights in any other person or entity.

Section 14. 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: [Closing Date]

CITY OF PALO ALTO

By _____
Authorized Officer

EXHIBIT A

NOTICE TO MSRB OF FAILURE TO FILE ANNUAL REPORT

Name of Issuer: City of Palo Alto, California
Name of Issue: CITY OF PALO ALTO
2019 Certificates of Participation, Series B
(California Avenue Parking Garage)
(Federally Taxable)
Date of Issuance: [Closing Date]

NOTICE IS HEREBY GIVEN that the City has not provided an Annual Report with respect to the above-named Issue as required by the Continuing Disclosure Certificate, dated [Closing Date], furnished by the City in connection with the Issue. The City anticipates that the Annual Report will be filed by _____.

Date: _____

CITY OF PALO ALTO, as Dissemination Agent

By _____
Authorized Officer

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