CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY
10th Largest U.S. City

# 2005

California

# Comprehensive Annual Debt Report

City Hall

Year Ended June 30, 2005

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

**City of San José**
**California**

# $14^{th}$ Comprehensive Annual Debt Report

Fiscal Year Ended June 30, 2005

Prepared by
Finance Department
Treasury & Risk Management Division

Scott P. Johnson
Director of Finance

**14th Comprehensive Annual Debt Report**
**City of San José**
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**Special Assistance – Departments and Offices**


City Attorney's Office
City Manager's Office
Environmental Services Department
Fire Department
Housing Department
Library Department
Norman Y. Mineta San José International Airport
Parks, Recreation & Neighborhood Services Department
Police Department
Public Works Department
Redevelopment Agency
Transportation Department

# CITY OF SAN JOSE
# FISCAL YEAR 2004-05
# COMPREHENSIVE ANNUAL DEBT REPORT

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CITY OF SAN JOSE

CAPITAL OF SILICON VALLEY

October 13, 2005

HONORABLE MAYOR AND CITY COUNCIL

**THE COMPREHENSIVE ANNUAL DEBT REPORT OF THE CITY OF SAN JOSE**

I am pleased to present the 14th Comprehensive Annual Debt Report for the City of San José (the "Annual Report") for the fiscal year ended June 30, 2005. The Annual Report is submitted for review and approval by the Making Government Work Better Committee and the City Council in accordance with the City's Debt Management Policy which was approved by the City Council on May 21, 2002. This Annual Report covers Fiscal Year 2004-05 and discusses the activities undertaken and managed by the Debt Management Program, a section of the Treasury and Risk Management Division within the Finance Department. The major sections in the Annual Report include:

- Overview of the City's Debt Management Program
- Summary of Recent Debt Issuance Activity
- Discussion of Key Debt Administration Tasks
- Review of the City's Outstanding Debt Portfolio

The discussions of debt management activities in the Annual Report only pertain to those activities managed by the City's Debt Management Program, while the section of the Annual Report reviewing the City's outstanding debt portfolio includes all debt issued by the City of San José, its Redevelopment Agency and various other financing authorities of which the City is a member.

The Debt Management Program is responsible for managing the debt issuance process for all City borrowings including the issuance and management of tax increment debt for the Housing Department's Expanded Housing Program. It should be noted that debt issued by the Redevelopment Agency is administered separately by Redevelopment Agency staff.

In addition to the activities and programs described above, the Annual Report also includes a review of Debt Management Policies, rating agency relations and credit maintenance issues, and a discussion of legislative and regulatory issues.

## DEBT MANAGEMENT ACTIVITIES

As illustrated on the graph on page 1, Fiscal Year 2004-05 was an active year for debt issuance with a total of eleven series of bonds for seven projects totaling over $507 million. In addition to providing these services, Debt Management staff were also involved in a number of projects during Fiscal Year 2004-05 including financial analysis related to the Evergreen East Hills Vision Strategy, vehicle license fee receivables financing program, alternative financing approaches for affordable housing and confirmation of the City's outstanding long-term ratings of Aa1/AA+/AA+ in June 2005.

The debt calendar for Fiscal Year 2005-06 anticipates continued opportunities and challenges for the City with an estimated seven series of bonds to be issued during the year totaling approximately $456 million and an estimated $17 million expansion of the lease revenue commercial paper program. As of October 2005, four of these series of bonds have already closed with an aggregate par amount of approximately $301.2 million. This activity is in addition to an outstanding debt portfolio of over $4.3 billion as of June 30, 2005, with 119 series of bonds outstanding for the City, Redevelopment Agency, and related entities.

In addition to the seven series of bonds anticipated during Fiscal Year 2005-06, other projects underway include: Airport financing analysis; development and implementation of a website for the City's continuing disclosure requirements; continued use of the newly-established Disclosure USA website to transmit various annual continuing disclosure reports; and preparation of several requests for qualification (RFQs) for financial advisory and debt underwriting services for financing pools.

## DECADE OF INVESTMENT

Despite the continuing economic challenges in the local economy, the City's commitment to the "Decade of Investment" continued in 2004-05 in which significant facilities were added in the City for the benefit of its residents and business community. The 2005-06 through 2009-10 Five-Year Capital Improvement Program (the "CIP") totals $1.9 billion. A significant reduction from last year's CIP primarily due to the rephasing of the Airport Master Plan projects. By continuing the City's commitment to the "Decade of Investment," the City's facilities infrastructure will be transformed. The major investments continue to be in facilities most often used by the public – parks, community centers, and libraries with added emphasis on public safety and airport-related improvements – primarily as a result of the funding available from voter-approved bond measures.

Approximately 40% of the source of funding for projects identified in the CIP (excluding beginning fund balance) is bond proceeds. In addition to providing funds for CIP projects, the City also provides financing to support an aggressive affordable housing program. The Finance Department Debt Management staff continues to be a key partner with the Housing Department in providing viable financing plans to facilitate delivery of these necessary housing units to the community.

## ACKNOWLEDGMENTS

The preparation of this Report represents the culmination of a concerted team effort by Debt Management staff of the Finance Department as well as special assistance and support from key departments and offices throughout the City. Of particular note is the special assistance the Finance Department's Debt Management Program receives on a continuous basis from the City Attorney's Office, especially the dedication of Danielle Kenealey and Ed Moran. Special recognition goes to Julia Cooper, Deputy Director of Finance, Debt and Risk Management, and David Persselin, Debt Administrator, who demonstrated personal determination to produce this exemplary document, and for their continued dedication in managing the daily operations of the Debt Management Program.

In addition, City departments who have participated in partnership with the Debt Management Program should be recognized for responding so positively to the requests for detailed information that are required for every debt issue, as well as for the information they provide to the Debt Management staff for the on-going management and monitoring required of the City's outstanding debt portfolio. The role of the City's Financial Advisors and Bond Counsels should also be acknowledged as a significant contribution to the City's success in its Debt Management Program, especially for the role they have played in helping to secure and maintain the City's excellent bond ratings.

On a personal note, as Director of Finance for the City of San José, there are a number of achievements over this past year related to the City's debt management program that I am particularly proud of. First, the professionalism, dedication and commitment of our Financing Team during the most active debt management period in the City's history. Second, the completion and occupancy of the City's new City Hall, and Debt Management's role in the success of this historical City facility being the City's largest capital improvement project to date. Third, the City's ability to maintain its excellent credit ratings as the highest rated large city in the State of California during a difficult economic climate through the sound fiscal policies approved by the City Council and proactively implemented through conservative fiscal measures by the Administration. Fourth, the City's attainment as the 10th largest City in the United States, as being included in this elite group puts the City and its finances on a higher platform to implement services to the community of San Jose.

Finally, I wish to express my sincere appreciation to the Mayor, City Council, and the City Manager, for providing leadership, policy direction and support in guiding the City to a secure, strong financial condition. Their leadership assures that financial resources are available through the City's Debt Management Program to provide capital facilities and affordable housing to the community.

Respectfully submitted,

Scott P. Johnson

SCOTT P. JOHNSON
Director of Finance

# I. OVERVIEW

The Overview section of the Annual Debt Report includes a discussion of the Debt Management Program, Review of Debt Management Policies, Rating Agency Relations and Credit Maintenance, and Legislative and Regulatory Issues.

## A. Debt Management Program

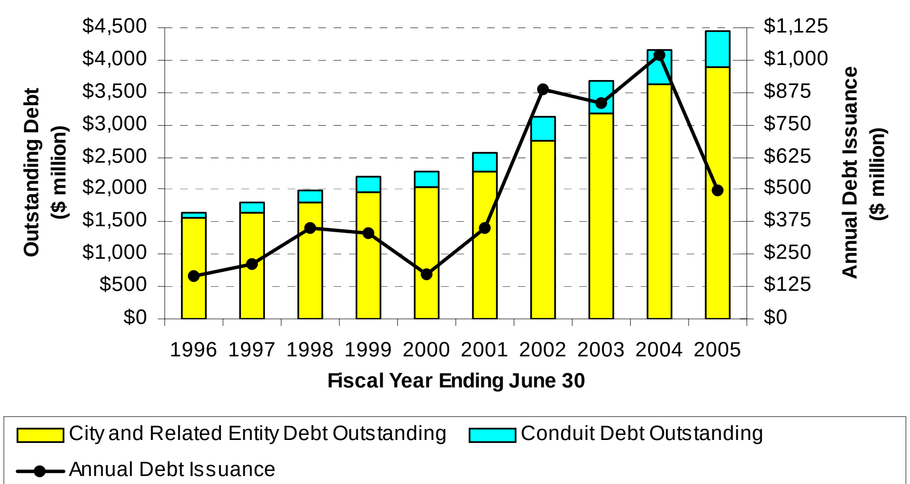
This section of the report provides an overview of debt issuance, debt administration and debt management projects for Fiscal Year 2004-05, including those debt management projects completed, currently underway or planned for Fiscal Year 2005-06.

### 1. Debt Issuance

The Debt Management Program, part of the Treasury and Risk Management Division within the Finance Department, is responsible for managing the debt issuance process for all City borrowings. Fiscal Year 2004-05 was an active year for City and Redevelopment Agency debt issuance, with a total of eleven series of bonds for seven projects totaling over $507 million, including execution of a $25.8 million HUD Section 108 Loan commitment. The debt calendar for Fiscal Year 2005-06 projects an estimated seven series of bonds totaling approximately $456 million and an estimated $17 million expansion of the lease revenue commercial paper program. Through October 2005, four of these series have closed with an aggregate par amount of approximately $301 million.

The graph below illustrates the size of the City's debt portfolio and the dollar volume of debt issued in each of the last ten years.

**City Debt Portfolio and Debt Issuance History**
*Fiscal Year 1995-96 through Fiscal Year 2004-05*



## 2. Debt Administration

After debt has been issued, the Debt Management Program is responsible for managing and administering the debt portfolio. As part of the City's statutory compliance program, the Special Tax Annual Report has been incorporated into this Annual Debt Report as Appendix E. Section III of this report, Debt Administration, provides a detailed discussion of debt administration tasks performed by Debt Management staff.

## 3. Debt Management Projects

In addition to debt issuance and administration, the Debt Management Program serves in a financial advisory role to other City departments, and works on other projects as necessary.

### *a. Projects Completed During Fiscal Year 2004-05*

<u>Investment Broker/Advisor Pool for Investment of Bond Proceeds:</u> To facilitate and expedite the investment of bond proceeds derived from new bond financings, Debt Management staff circulated a Request for Qualifications and established an Investment Broker/Advisor pool. In addition to establishing a pool of advisors, the selection process included selection and assignment of an advisor who assisted with investment of the 2004 Airport Revenue Bond proceeds.

<u>Evergreen-East Hills Vision Strategy</u>: In July 2004, Debt Management held the first monthly Developer Support meeting. These meetings were established to bring a subset of the Technical Advisory Committee consisting of City staff and developer consultants together to encourage sharing of data among the respective consultants. It is anticipated that Developer Support meetings will continue throughout the life of the potential financing project. Debt Management staff also conducted an RFP process to select an appraiser who, under the CDIAC guidelines for land-secured financings, will conduct a preliminary appraisal of the properties involved in the project to estimate bonding capacity.

<u>Vehicle License Fee (VLF) Receivables Financing Program</u>: In early 2005, the City Council chose to participate in a program sponsored by the California Statewide Communities Development Authority (CSCDA) to finance VLF receivables owed by the State to municipalities. On March 17, 2005, the CSCDA note issue closed and $14.8 million of City net proceeds was deposited with the Issuing and Paying Agent for the City of San Jose Financing Authority's Lease Revenue Commercial Paper Program. On July 1, 2005, those VLF Gap Loan Receivable sale proceeds were used to redeem maturing commercial paper notes attributable to the Civic Center offsite parking garage. As a result of this redemption the principal amount of bonds that will need to be issued to redeem CP Notes issued to finance the construction of the offsite garage will be reduced, saving the City approximately $1 million per year in avoided interest costs beginning in FY 2006-07 for the parking garage bonds.

Alternative Financing Approaches for Affordable Housing: Debt Management staff worked with the California Debt Limit Allocation Committee (CDLAC), the Housing Department, and the Housing Department's general financial advisor to develop a program whereby the City/Redevelopment Agency, along with other issuers in the state, can apply for a tax-exempt CDLAC private activity allocation for the issuance of tax allocation bonds to fund loans for multifamily housing projects. The program was approved by CDLAC on July 21, 2004, and in December 2004, the Agency was awarded an allocation of $75.315 million. On June 30, 2005, the Agency issued $66.150 million of bonds, Series 2005C and 2005D. These were the first bonds issued in the State under the new program. The use of tax-exempt, rather than more costly taxable, bond proceeds for these loans resulted in the ability to fund approximately 120 additional affordable housing units in the City of San José.

Housing Department Bonding Capacity Analysis: During the first quarter of Fiscal Year 2004-05, Debt Management assisted the Housing Department in evaluating the impact of recent reductions in redevelopment tax increment revenue on the ability of the City to achieve its affordable housing goals. The analysis resulted in identification of a level of housing set-aside tax allocation bond issuance that would maximize near-term housing production while preventing over-extension of the Housing Department's bonding capacity.

Housing Department Line of Credit: Debt Management staff worked with the Bank of New York to extend the Housing Department's Line of Credit for an additional year. The Housing Department uses the line of credit to fund loans to developers, which are later taken out by the issuance of Housing Set-Aside Tax Allocation Bonds.

IRS Audits of Multifamily Housing Revenue Bonds: In October 2003, the City received notification from the IRS with respect to an audit of the 1999A Multifamily Housing Revenue Bonds (The Gardens Apartments) for tax compliance. Debt Management staff worked closely with the developer, bond counsel, tax counsel, the City Attorney's Office and the Housing Department to gather all requested information and to prepare an appropriate response to additional questions from the IRS. On March 17, 2005, the IRS notified the City that it had completed its examination of the project and reaffirmed that interest on the bonds is tax-exempt.

Affordable Housing Project Ongoing Administration: In Fiscal Year 2004-05, Debt Management assisted the Housing Department and affordable housing developers in activities related to the ongoing administration of affordable housing projects financed with multifamily housing revenue bonds.

*Fairway Glen Transfer of Ownership* – The Fairway Glen Apartments project, financed in part with Multifamily Housing Revenue Bonds, Series 1985A, was sold by Toyon Road San Jose Partners, L.P. (a partnership involving Avalon Bay Communities) to Fairfield Affordable Housing LLC. This required Fairfield to assume the existing bonds secured by the property. As the bond issuer, the City of

San José was required to approve the acquisition and the assumption of the bond obligations. This transaction closed on December 14, 2004.

*Timberwood Letter of Credit Extension* – The Timberwood Apartments bonds were secured by a letter of credit with an expiration date of February 15, 2005. Debt Management staff worked with Housing and the City Attorney's Office to extend the term of the letter of credit. No Council action was necessary as the extension required no amendments to the documents and did not impact the affordability restrictions on the property.

*Betty Anne Gardens & El Paseo Studios General Partner substitution* – The City assisted the developer for these two projects with a General Partner substitution. In both cases the withdrawing General Partner was First Community Housing. It was replaced by Betty Anne Gardens, Inc. for the Betty Anne Gardens project and by El Paseo Apartments, Inc. for the El Paseo project. Both corporations are California non-profit public benefit corporations. No action on behalf of the City was needed because the new General Partners are entities wholly controlled by the same or similar members of the original general partner.

*Somerset Park Apartments* – The City originally issued bonds on this project in 1987 and the bonds were remarketed in 2003. The developer, Somerset Park Investors, LP, contacted the City in May 2005 asking to prepay the bonds and, in so doing, end the Qualified Project Period. City staff worked with the developer and bond counsel to facilitate this request and the transaction closed on June 30, 2005. In accordance with the amended regulatory agreement, the City received a fee of $25,000 representing the net present value of all future annual administrative fees through the end of the original bond term (2017).

*Villagio and Villa Torre 2 Conversions* – Debt Management staff facilitated the process to convert two multi-family housing projects to permanent financing. The City issued two series of multi-family revenue bonds in August 2001; Villagio (formerly known as Villages Parkway) and Villa Torre 2 (formerly known as 6th & Martha), both developed by JSM. A total of $536,000 of the Villagio bonds and $373,000 of the Villa Torre 2 bonds were redeemed. The redeemed bonds were paid by a supplemental loan to the projects from Jim Morley, one of the members of the JSM partnership. Conversion occurred on March 10, 2005.

<u>Affordable Housing Project TEFRA Hearings</u>: The Tax Equity and Fiscal Responsibility Act (TEFRA) of 1982 requires a published notice, public hearing and approval by elected officials for issuance of qualified private activity bonds such as multifamily housing revenue bonds. The City's Policy for the Issuance of Multifamily Housing Revenue Bonds, adopted by Council in June 2002, and San José Municipal Code Chapter 5.06 specify that the TEFRA hearing for multifamily housing projects be held before the Director of Finance. In Fiscal Year 2004-05, the Finance Department held hearings for five projects:

**Finance Director's TEFRA Hearings for Multifamily Housing Projects**
*Fiscal Year 2004-05*

| Date | Project | Amount | Issuer |
|---|---|---|---|
| 07/29/2004 | Story Road Family Apartments (formerly Sunny Apartments) | $ 4,000,000 | CA Statewide Communities Dev't. Authority (CSCDA) |
| 09/27/2004 | Curtner Gardens Apartments | 9,000,000 | City of San José |
| 10/18/2004 | Raintree Apartments (formerly Shadowbrook Gardens) | 24,000,000 | City of San José |
| 10/18/2004 | Tax Allocation Bonds, Series 2005 | 125,000,000 | The Redevelopment Agency of the City of San José |
| 05/23/2005 | Tax Allocation Bonds, Series 2005[1] | 207,315,000 | The Redevelopment Agency of the City of San José |
| 06/01/2005 | Capitol Park Apartments | 25,000,000 | Association of Bay Area Governments (ABAG) |

[1] Some of the projects in the first hearing were deemed ineligible for tax-exempt bond proceeds. A second hearing was held to include new projects in order to utilize as much of the CDLAC allocation as possible.

Debt Policies: During Fiscal Year 2004-05, staff collected background information on derivative debt instruments and exemplar policies from other municipal issuers as an initial step in developing a City derivatives policy.

### *b. Projects for Fiscal Year 2005-06*

Optional Redemption of Series 1994B Reassessment Revenue Bonds: Debt Management worked with Public Works Department and Attorney's Office staff to conduct an analysis of the funds that might be available for optional redemption of the Series 1994B Reassessment Revenue Bonds. The accounting structure for that financing included both City- and trustee-held funds, portions of which were allocable to property-owners and portions of which were available for repayment of the bonds. After staff confirmed that sufficient amounts were available, the Series 1994B Bonds were redeemed on September 2, 2005.

Evergreen-East Hills Vision Strategy: In June 2005, the City Council directed staff to prepare an analysis illustrating how different policy choices in the areas of housing density, affordable housing, and conversion of industrial zoning to residential would impact bonding capacity in the proposed community facilities district. Debt Management staff is working with the City's special tax consultant in preparing that trade-off analysis.

Affordable Housing Project Ongoing Administration: In Fiscal Year 2005-06, Debt Management is assisting the Housing Department and affordable housing developers in activities related to the ongoing administration of affordable housing projects financed with multifamily housing revenue bonds.

*Timberwood Apartments Bond Redemption* – The City issued bonds for the Timberwood Apartments project in 1990. On June 28, 2005 City Council approved the subordination of the City's existing Bond Regulatory Agreement and Declaration of Restrictive Covenants to the new Bond Deed of Trust and the Letter of Credit Bank Deed of Trust in order to facilitate the issuance of new bonds by the Housing Authority of the County of Santa Clara ("HACSC") and 4% low-income tax credits to pay off the existing bonds and fund improvements to the project. The affordability period required under federal law (15 years) has expired and the new regulatory agreement places even more restrictive affordability requirements on the Project. This will result in affordability restrictions being extended for an additional 40 years (to 2060) and will provide 228 newly restricted units to San José's housing stock.

Mid Peninsula Housing Coalition ("Mid-Pen") requested that HACSC issue and sell bonds to provide financing for the rehabilitation of Timberwood Apartments. Bonds were issued in an amount sufficient to pay off the City's outstanding bonds and the Housing Department loan, plus pay for additional rehabilitation costs. This is an exception to the City's policy but was granted because the loan was paid off in full, the City received a lump-sum payment representing the present value of the annual administration fees; it increased the affordable housing units from 20% to 100% of the units; and the affordability restrictions were increased to 55 years from the issuance of the new bonds. The transaction with HACSC closed on July 15, 2005.

*Oaks of Almaden Conversion to Permanent Financing* – Debt Management staff worked with the developer, the Housing Department and the City Attorney's Office to coordinate the conversion of this project from construction to permanent financing. The conversion was completed on October 3, 2005.

*The Enclave, formerly known as Siena at Renaissance Square* – In July 2005, the developer informed the City that it intends to sell this project before the end of the year. The City will have to do an assumption agreement and formally consent to the ownership transfer. It is expected that this transaction will be completed by December 2005.

*Villa Solera Partial Bond Redemption* – In August 2005, the developer, JSM Properties, contacted the City to request a work-out for this project, formerly known as Kennedy Apartments, due to cash flow difficulties during initial lease up period. The developer would like to income-restrict more units to increase tax credit funds, which in turn will necessitate partial redemption of the bonds, thereby resulting in a lower loan amount and allowing the project to meet the debt service coverage requirement for conversion. City Council approved the increased affordability restrictions on September 13, 2005. Discussions are in progress with the tax credit investor.

*Ohlone-Chynoweth Credit Enhancement Substitution* – The Ohlone-Chynoweth Apartments Multifamily Housing Revenue Bonds Series 1999A and taxable 1999B were issued in 1999 to provide financing for the development of a 195-unit housing project. In July 2003, the developer was informed that the current letter of credit bank (Bay View Bank, N.A.) intended to dissolve on September 30, 2003. The letter of credit was assumed by Bay View Capital Corporation ("BVCC") effective October 1, 2003. Since BVCC wishes to exit the letter of credit business, staff anticipates moving forward with a credit enhancement substitution in mid-2006.

Affordable Housing Project TEFRA Hearings: To date, in the current fiscal year, the Finance Department has held hearings for the following projects:

**Finance Director's TEFRA Hearings for Multifamily Housing Projects**
*Fiscal Year 2005-06 through September 2005*

| Date | Project | Amount | Issuer |
|---|---|---|---|
| 07/18/2005 | Paseo Senter I | $ 32,000,000 | City of San José |
| 07/18/2005 | Paseo Senter II | 28,000,000 | City of San José |

Debt Policies: During Fiscal Year 2005-06, work is anticipated to continue on program-specific policies for land secured financings and for the use of derivative debt instruments, to the extent workload and staffing levels permit. These policies will be brought forward to the City Council as they are developed.

Technology Projects: In Fiscal Year 2005-06, Debt Management will continue to pursue its investor relations and disclosure website, Debt Management database, and electronic document storage projects, subject to resource and staff availability. Debt Management will also continue to make use of the newly-established Disclosure USA website to transmit annual reports required under various continuing disclosure agreements.

## B. Review of Debt Management Policies

On May 21, 2002, City Council adopted by Resolution #70977 a Debt Management Policy which establishes the following equally important objectives:

- Minimize debt service and issuance costs;
- Maintain access to cost-effective borrowing;
- Achieve the highest practical credit rating;
- Full and timely repayment of debt;
- Maintain full and complete financial disclosure and reporting; and
- Ensure compliance with applicable State and Federal laws.

The general Debt Management Policy establishes parameters for when and how the City may enter into debt obligations, but permits sufficient flexibility to allow the City to take advantage of opportunities that may arise. As outlined in the Debt Management Policy, it is to be reviewed annually by the Finance Department to ensure its consistency with respect to the City's debt management objectives. The annual review has been conducted and no amendments or changes to the Debt Management Policy (Appendix A) are recommended at this time.

In addition, the Council approved by Resolution #71023 on June 11, 2002, a supplemental Policy for the Issuance of Multifamily Housing Revenue Bonds (Appendix B). Among its other provisions, the Policy specifies that the bonds for any project that utilizes City funds must be issued by the City.

In Fiscal Year 2004-05, the City granted the following four exceptions to the Multifamily Housing Revenue Bonds Policy.

> *Story Road Apartments* – This project does not have City loans or grants. The developer, Simpson Housing Solutions, LLC, worked with the California State Community Development Authority (CSCDA) on another, simultaneous, transaction and requested that CSCDA serve as the issuer for this project in order to take advantage of economies of scale by maintaining the same financing team.
>
> *Capitol Park Apartments* – This project does not have City loans or grants. The developer, Hudson Jones Commercial Real Estate, requested to work with the Association of Bay Area Governments (ABAG) in issuing the debt since its issuance fees are lower than those charged by the City.
>
> *First & Gish Apartments* – This project has a funding commitment from the City of $2,275,000, but the bonds will be issued by CalHFA (which also held the TEFRA hearing). By issuing the bonds through CalHFA, the developer can take advantage of CalHFA's low-interest program for special needs housing. Of the 35 units in the complex, 13 will be dedicated to serving developmentally disabled tenants. The project will also include 3,800 square feet of commercial space to be financed separately by CalHFA.
>
> *Timberwood Apartments* – This exception was granted because the reissuance of bonds through the Housing Authority of the County of Santa Clara (HACSC) allowed the City's loan to be paid off in full, increased the number of affordable housing units in the City, and extended the affordability period on those units. HACSC held the TEFRA hearing.

## C. Rating Agency Relations and Credit Maintenance

### 1. Credit Analysis Process

Municipal bond ratings provide investors with a simple way to compare the relative investment quality of different bonds. Bond ratings express the opinions of the rating agencies as to the issuers' ability and willingness to pay debt service when it is due. In general, the credit rating analysis includes the evaluation of the relative strengths and weaknesses of the following four factors as they affect an issuer's ability to pay debt service:

### *a. Fiscal Factors*

Financial results have the most significant impact on the rating process. This review involves an examination of results of operations, including a review of the actual fiscal performance versus planned budget performance, with deviations from the plan to be explained. The general fund financial statement is examined with emphasis on current financial position and fund balances, as well as three- to five-year trends in planning and budgeting procedures. Pension liabilities are also important in the analysis process. The early production of the City's Comprehensive Annual Financial Report is a positive step in providing meaningful, valuable and timely information to the rating agencies.

### *b. Economic Factors*

The overall economic strength of the City is heavily weighted in the evaluation of the City's creditworthiness by diversity of both the economic base and tax base. The diversity of the City's industries reflects its ability to weather industry-specific downturns as well as general economic recession. In either scenario, stronger surviving industries carry the ailing industries through the period of downturn. In a truly diverse economy, it is rare that all industries will deteriorate to the same level at the same time.

The strength of the City's tax base is equally crucial. The City relies on taxes on its residents and businesses for the majority of its revenues. The ability of the City to continue to receive those revenues is directly related to the ability of its taxpayers to pay their taxes. Property values, employment, unemployment, income levels, costs of living, and other factors impacting the wealth of the taxpayers provide an indication of the strength of the City's tax base.

### *c. Debt Factors*

The City's overall debt burden is considered in the credit analysis process. In addition to government regulated debt ceilings, the City's ability to maintain manageable debt levels and debt service coverage is evaluated. Other positive indicators are proper management of existing debt, proactive efforts in identifying and executing financially prudent refunding opportunities, and closely matching capital financing structures to the funding needs of the project.

### *d. Administrative/Management Factors*

These factors include the examination of the form of government and assessment of the City's ability to implement plans as well as to fulfill legal requirements. The focus is on the capabilities of the management staff within the City, which is seen as a vital ingredient in assessing its credit quality. Managerial and legislative willingness to make difficult decisions, development of financial policies, and the reliability and continuity of regularly-updated accounting and financial information are key. Management that maintains regular contact with the rating agencies is well-regarded.

As part of the credit analysis process, the rating agencies look at several quantitative indicators. The table below provides a summary of San José's key debt indicators in comparison with corresponding medians for California cities with AA-category general obligation bond ratings. The California city medians are derived from Fiscal Year 2002-03 data reported by Moody's Investors Service, the most recent year for which Moody's has published medians. The City of San José ratios are based on non-self-supporting debt with recourse to the City's General Fund as of June 30, 2005.

**Comparison of Rating Agency Medians to City of San José Debt Ratios**

| | Rating Agency Median[1] | City of San José[2] |
|---|---|---|
| **Net Direct Debt** | | |
| Per Capita ($) | $391 | $511.90 |
| As a % of Assessed Value | 0.3% | 0.5% |
| **Net Lease Burden** | | |
| 5-Year Average of Annual Lease Payments as a % of Current General Fund Revenue | 3.3% | 4.29% |

[1] Comparison to AA-category California cities.
[2] Lease burden ratio net of debt service payments made from capitalized interest.
*Source: Medians for California Cities: Fiscal 2003, Moody's Investors Service, February 2005.*

As illustrated in the table, the City is above the AA-category California city medians for all categories. Note that capitalized interest for the City of San José Financing Authority Lease Revenue Bonds, Series 2002 (Civic Center Project), ends in April 2006, as a result the City is showing a higher net lease burden than in previous years. The terms used in the table are defined below.

Net Direct Debt: Tax-supported debt, net of self-supporting and revenue anticipation debt. Includes the City's non-self-sustaining lease revenue debt. Excludes the City's general obligation and special assessment/tax bonds, which are paid from voter-approved special assessments or taxes, lease revenue bonds paid from non-general fund sources, and the airport, parking and sewer revenue bonds, which are limited obligations of those enterprise funds. Also excludes redevelopment tax allocation debt.

Net Lease Burden: Average scheduled annual payment in the five years following the audit year for all outstanding lease obligations (excluding leases which are self-supporting from non-general fund sources) combined, divided by total general fund revenues and other sources of funds for the audit year.

## 2. Rating Summary

The four factors described above were instrumental in the City receiving its general obligation bond ratings from the three major rating agencies: Aa1 from Moody's; AA+ from Standard & Poor's; and AA+ from Fitch. These ratings, initially assigned in February 2001 and reconfirmed in June 2005, place San José in the second highest rating category (only one "notch" below Aaa/AAA/AAA), ranking it higher than the State of California and the County of Santa Clara, and making it the highest-rated large city in California. The ratings for the City's general obligation, lease revenue, and enterprise debt are summarized in Appendix C.

### 3. Legal Debt Margins

Section 1216 of the San José City Charter limits outstanding general obligation bonds of the City to 15% of the total assessed value of all real and personal property within the City limits. General obligation debt is debt secured by the City's property tax revenues. As of June 30, 2005, the total assessed value on the City's 2004-2005 tax roll was $95.3 billion, which results in a total debt capacity of approximately $14.3 billion. As of June 30, 2005, the City had approximately $337.2 million in general obligation debt outstanding, representing 0.35% of the assessed value of taxable property; therefore the City's debt margin was $13.959 billion (debt limit less outstanding general obligation debt).

## D. Legislative and Regulatory Issues

Debt Management reviews legislative referrals at the request of the Office of Intergovernmental Relations. It is important that bills bearing on the City's ability to access the capital markets are tracked through the legislative process to ensure that the City's position is expressed to members of the State Legislature or Congress. Various Federal tax reform legislation proposals are periodically considered and debated, such as the taxability of corporate dividends, flat tax and elimination of tax exemption on municipal bonds. These proposals, if enacted, could result in higher borrowing costs for the City.

It is also important for the City to monitor regulatory changes proposed by governmental agencies such as the IRS, the Securities and Exchange Commission ("SEC") and the Municipal Securities Rule Making Board ("MSRB"), as well as industry organizations such as the National Association of Bond Lawyers ("NABL"), the National Federation of Municipal Analysts ("NFMA"), the National Association of State Auditors, Comptrollers and Treasurers ("NASACT") and the Government Finance Officers Association ("GFOA").

CITY OF
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## II. DEBT ISSUANCE

### A. Debt Issued During Fiscal Year 2004-05

Fiscal Year 2004-05 was an active year for City and Redevelopment Agency debt issuance, with a total of eleven series of bonds and a HUD Section 108 loan for seven projects totaling over $507 million. These financings are described below and are presented in the summary table at the end of this section.

**General Obligation Bonds, Series 2004 (Libraries, Parks and Public Safety Projects)**

The City issued $118,700,000 of Series 2004 general obligation bonds on July 14, 2004. The proceeds will be used to fund $58,300,000 of library projects, $46,000,000 of neighborhood parks and recreation projects, and $14,400,000 million of public safety projects. Debt service on the Series 2004 bonds is payable from *ad valorem* taxes levied upon all property subject to taxation by the City. The Series 2004 bonds bear interest at fixed rates ranging from 4.00% to 5.00%, and have a final maturity date of September 1, 2034.

**U.S. Department of Housing and Urban Development (HUD) Section 108 Loan (Land Acquisition Project Phase II)**

On February 10, 2005, the City of San José received a loan commitment in the amount of $25,810,000 from HUD under the Section 108 Loan Guarantee Program. The City plans to draw on the loan commitment to finance acquisition of property adjacent to the Airport. On February 16, 2005, the City made an initial draw on the loan commitment in the amount of $342,000 to place a deposit on the property and pay other costs associated with the land acquisition. Debt service on the HUD loan will initially be reimbursed from HUD grant funds received by the City, and then paid from lease revenue and sales tax revenue generated by commercial activities on the property to be acquired. The HUD Section 108 Loan bears interest at a monthly variable rate, which on June 30, 2005, was 3.53%, and has a final maturity date of August 1, 2024.

**City of San José Financing Authority Lease Revenue Bonds, Series 2005A (Taxable) and 2005B (AMT) (Land Acquisition Project)**

On February 17, 2005, the City of San José Financing Authority issued $54,480,000 of Series 2005A (Taxable) and $25,545,000 of Series 2005B (AMT) lease revenue bonds. The bond proceeds were used to finance acquisition of and improvements to property adjacent to the Airport to be temporarily used by the Airport for aviation purposes. Debt service on the bonds during the period the property is used for aviation purposes will be paid from base rental payments received by the City from the Airport. The Series 2005A Bonds, which are insured by XL Capital, bear interest at weekly variable rate, which on June 30, 2005, was 3.30%, and have a final maturity date of March 1, 2029. The Series 2005B Bonds, also insured by XL Capital, bear interest at a weekly variable rate, which on June 30, 2005, was 2.30%, and have a final maturity date of March 1, 2034.

**General Obligation Bonds, Series 2005 (Libraries and Public Safety Projects)**

The City issued $46,300,000 of Series 2005 general obligation bonds on June 23, 2005. The proceeds will be used to fund $21,300,000 of library projects and $25,000,000 of public safety projects. Debt service on the Series 2005 bonds is payable from *ad valorem* taxes levied upon all property subject to taxation by the City. The Series 2005 bonds bear interest at fixed rates ranging from 3.00% to 7.50%, and have a final maturity date of September 1, 2035.

**City of San José General Obligation Bonds Summary**
*As of June 30, 2005*

| Date of Election | Projects | Amount Authorized | Amount Issued to Date | Amount Authorized but Unissued |
|---|---|---|---|---|
| 11/07/2000 | San José Neighborhood Libraries Bonds | $211,790,000 | $140,600,000 | $71,190,000 |
| 11/07/2000 | San José Neighborhood Parks and Recreation Bonds | 228,030,000 | 132,715,000 | 95,315,000 |
| 03/05/2002 | San José 911, Fire, Police and Paramedic Neighborhood Security Act | 159,000,000 | 78,775,000 | 80,225,000 |
| Total | | $598,820,000 | $352,090,000 | $246,730,000 |

**Redevelopment Agency of the City of San José Merged Area Redevelopment Project Housing Set-Aside Tax Allocation Bonds, Series 2005A, Series 2005B (Taxable), Series 2005C (AMT) and Series 2005D (AMT)**

On June 30, 2005, the Redevelopment Agency issued $10,445,000 of Series 2005A, $119,275,000 of Series 2005B (Taxable), $33,075,000 of subordinate Series 2005C (AMT) and $33,075,000 of subordinate Series 2005D (AMT) housing set-aside tax allocation bonds (collectively, the “Series 2005 Bonds”). The proceeds of the Series 2005A bonds were used to current refund the Agency’s Series 1993D housing set-aside tax allocation bonds. The proceeds of the Series 2005B bonds were used to advance refund all of the Agency’s Series 2000F housing set-aside tax allocation bonds and repay a portion of the Agency’s Series 2002G and Series 2002H housing set-aside tax allocation bonds. Proceeds of the Series 2005C and Series 2005D bonds were used to repay the remaining portion of the Agency’s Series 2002G and Series 2002H bonds and to finance and refinance affordable housing projects. Debt service will be payable from the 20% portion of Agency tax increment revenues set aside for affordable housing.

The Series 2005A bonds, which are insured by FGIC, bear interest at tax-exempt fixed rates ranging from 3.75% to 5.00%, and have a final maturity date of August 1, 2024. The Series 2005B bonds, which are also insured by FGIC, bear interest at taxable fixed rates ranging from 3.89% to 5.46%, and have a final maturity date of August 1, 2035.

The Series 2005C and Series 2005D bonds, which are supported by a Bank of New York direct-pay letter of credit, bear interest at tax-exempt (AMT) weekly variable rates, and have a final maturity date of August 1, 2035. The initial interest rates were 1.96% and 2.00% for the 2005C and 2005D bonds respectively.

The Series 2002G and Series 2002H Bonds were redeemed on June 30, 2005. The redemption of the Series 2002G Bonds and Series 2002H Bonds, both of which were taxable and paid interest at weekly variable rates, with proceeds of the taxable fixed rate Series 2005B bonds and tax-exempt (AMT) variable rate Series 2005C and Series 2005D bonds, allowed the Agency to achieve a more economic allocation of variable and fixed rate debt and to refund a portion of its taxable debt on a tax-exempt basis.

The Series 1993D Bonds were redeemed on August 1, 2005, and the Series 2000F Bonds are considered defeased and will be redeemed on August 1, 2006. These refundings achieved economic savings in the following amounts:

**Economic Savings Achieved by Housing Set-Aside Tax Allocation Bond Refunding**
*Series 2005A (tax-exempt) and Series 2005B (taxable)*

| | **Series 1993D** | **Series 2000F** |
|---|---|---|
| Aggregate Debt Service Savings (net available funds) | $2,054,468 | $16,609,793 |
| Net Present Value (NPV) Debt Service Savings | $1,409,867 | $8,994,208 |
| NPV Savings as a Percentage of Refunded Principal | 13.40% | 20.35% |

**City of San José Financing Authority Lease Revenue Commercial Paper Notes**

On January 13, 2004, the City Council and the City of San José Financing Authority each adopted a resolution authorizing the issuance of City of San José Financing Authority tax-exempt lease revenue commercial paper notes in an amount not to exceed $98,000,000. This commercial paper program was established as a mechanism for financing public improvements of the City including the offsite parking garage for the new Civic Center and non-construction costs for technology, furniture, equipment and relocation services for the new Civic Center. On November 9, 2004, the City Council and the Authority authorized use of the commercial paper program to finance procurement costs of the City's consolidated utility billing system. Subsequently, on June 21, 2005, the City Council and the City of San José Financing Authority each adopted a resolution authorizing the issuance of taxable lease revenue commercial paper notes, under the same $98,000,000 not to exceed limitation as the tax-exempt notes. This subsequent authorization permits the Authority to issue taxable commercial paper notes to pay for expenses otherwise authorized under the commercial paper program, but ineligible to be paid from tax-exempt commercial paper proceeds.

Under this program, the Authority is able to issue commercial paper notes at prevailing interest rates for periods of maturity not to exceed 270 days. The commercial paper notes are secured by a pledge of lease revenues from various City assets and additionally secured by a letter of credit provided by State Street Bank and Trust Company and the California State Teachers' Retirement System (CalSTRS).

At the beginning of fiscal year 2004-05, $22,673,000 of commercial paper notes were outstanding. During fiscal year 2004-05, the Authority issued $1,301,249 of commercial paper notes for the new City Hall offsite parking garage, $7,184,556 for technology, furniture and relocation services for the new City Hall, $40,195 for municipal facility improvements, and $1,904,000 for the consolidated utility billing system. On June 30, 2005, $33,003,000 of Authority tax-exempt commercial paper notes were outstanding at interest rates ranging from 1.85% to 2.90%, and $100,000 of Authority taxable commercial paper notes were outstanding at a 3.50% interest rate.

**City of San José, California, San José International Airport Subordinated Commercial Paper Notes, Series A (Non-AMT), Series B (AMT), and Series C (Taxable)**

On November 2, 1999, the City Council adopted a resolution authorizing the issuance of City of San José, San José International Airport subordinated commercial paper notes in three series (Series A -- Tax-Exempt, Series B -- Subject to the AMT, Series C -- Taxable) in an amount not to exceed $100,000,000. The commercial paper program was established to provide an interim source of financing for the initial capital projects in the Airport Master Plan until a permanent financing plan was finalized and implemented. Subsequently, on April 1, 2003, the City Council authorized use of the commercial paper program to fund costs associated with implementation of the requirements under the federal Aviation and Transportation Security Act (ATSA).

Under this program, the City is able to issue commercial paper notes at prevailing interest rates for periods of maturity not to exceed 270 days. The commercial paper is secured by a subordinate pledge of the Airport's revenues and additionally secured by a letter of credit provided by JPMorgan Chase Bank.

During fiscal year 2004-05, no Series A or Series B commercial paper notes were issued or outstanding. During fiscal year 2004-05, the City issued $164,439 of Series C commercial paper notes to pay the interest cost associated with renewing mature notes, $1,800,000 to fund a claim loss reserve related to the owner-controlled insurance program ("OCIP") for the Airport Master Plan construction program and $4,561 for other authorized purposes. On June 30, 2005, $7,755,000 of Series C commercial paper notes were outstanding at an interest rate of 3.35%.

**Multifamily Housing Revenue Bonds**

Federal tax law limits the amount of tax-exempt private activity debt that may be issued. Prior to financing multifamily housing projects on a tax-exempt basis, these projects must receive an allocation of the State's private activity volume cap. The City received allocations from the California Debt Limit Allocation Committee ("CDLAC") and completed financings for the following two projects.

**Multifamily Housing Revenue Bonds Issuance Summary**
*Fiscal Year 2004-05*

| Project Name | Date Issued | Amount Issued | Affordable Units |
|---|---|---|---|
| Delmas Park Apartments | 10/15/2004 | $ 19,379,000 | 122 |
| Raintree Apartments | 02/01/2005 | 21,100,000 | 174 |
| Totals | | $40,479,000 | 296 |

**Summary of Debt Issued During Fiscal Year 2004-05**

The table on the following pages presents a summary of debt issued in Fiscal Year 2004-05.

## Summary of Debt Issuance
*Fiscal Year 2004-05*

| Issue Date | Issue | Size (millions) | Type | Sale Type | Financial Advisor | Bond Counsel | Underwriter | Credit Enhancement |
|---|---|---|---|---|---|---|---|---|
| 07/14/2004 | CSJ 2004 Libraries, Parks & Public Safety | $118.700 | General Obligation | Competitive | RBC Dain Rauscher | Sidley, Austin, Brown & Wood | Goldman, Sachs & Co. | MBIA[1] |
| 10/15/2004 | CSJ 2004C-1 Delmas Park | $13.780 | Multifamily Housing | Private Placement | Ross Financial | Quint & Thimmig | N/A | None |
| 10/15/2004 | CSJ 2004C-2 Delmas Park | $5.599 | Multifamily Housing | Private Placement | Ross Financial | Quint & Thimmig | N/A | None |
| 02/01/2005 | CSJ 2005A Raintree Apartments | $21.100 | Multifamily Housing | Negotiated | Ross Financial | Jones Hall | E.J. De La Rosa | Freddie Mac[2] |
| 02/10/2005 | HUD Loan Land Acquisition | $25.810 | Section 108 | N/A | N/A | N/A | N/A | N/A |
| 02/17/2005 | CSJFA 2005A (Taxable) Land Acquisition | $54.480 | Lease Revenue | Negotiated | Public Resources Advisory Group/ Fullerton & Friar | Orrick, Herrington & Sutcliffe | Lehman Brothers | XL Capital[3] |
| 02/17/2005 | CSJFA 2005B (AMT) Land Acquisition | $25.545 | Lease Revenue | Negotiated | Public Resources Advisory Group/ Fullerton & Friar | Orrick, Herrington & Sutcliffe | JPMorgan | XL Capital[3] |
| 06/23/2005 | CSJ 2005 Libraries and Public Safety | $46.300 | General Obligation | Competitive | Public Resources Advisory Group | Jones Hall | Banc of America | MBIA[4] |

*(continued on next page)*

**Issuer Key**: CSJ-City of San José; CSJFA-City of San José Financing Authority; RDA-Redevelopment Agency of the City of San José.

[1] MBIA has insured the current interest bonds maturing 2007 through 2017 and the term bonds maturing in 2027, 2030 and 2034.

[2] Credit enhancement provided through a Washington Mutual Bank letter of credit during the construction period.

[3] Bank of America provides liquidity support through a standby letter of credit.

[4] MBIA has insured the term bonds maturing in 2031 and 2035.

## Summary of Debt Issuance

*Fiscal Year 2004-05 (continued)*

| Issue Date | Issue | Size (millions) | Type | Sale Type | Financial Advisor | Bond Counsel | Underwriter | Credit Enhancement |
|---|---|---|---|---|---|---|---|---|
| 06/30/2005 | RDA 2005A Housing Set-Aside | $10.445 | Tax Allocation Refunding | Negotiated | Ross Financial | NixonPeabody | 5 | FGIC |
| 06/30/2005 | RDA 2005B (Taxable) Housing Set-Aside | $119.275 | Tax Allocation Refunding | Negotiated | Ross Financial | NixonPeabody | 5 | FGIC |
| 06/30/2005 | RDA 2005C (AMT) Housing Set-Aside | $33.075 | Tax Allocation Refunding/New $ | Negotiated | Ross Financial | NixonPeabody | Citigroup | Bank of New York LC |
| 06/30/2005 | RDA 2005D (AMT) Housing Set-Aside | $33.075 | Tax Allocation Refunding/New $ | Negotiated | Ross Financial | NixonPeabody | Banc of America Securities, LLC | Bank of New York LC |
| **FY 2004-05** | **12 Series** | **$507,184** | | | | | | |

**Issuer Key**: CSJ-City of San José; CSJFA-City of San José Financing Authority; RDA-Redevelopment Agency of the City of San José.

[5] Underwriting team consisted of Citigroup as senior manager and Banc of America Securities LLC, E.J. De La Rosa & Co., Inc., Stone & Youngberg LLC, and UBS Financial Services, Inc. as co-managers.

## B. Debt Issued and Planned for Fiscal Year 2005-06

The Debt Management Program has identified six financing projects which are expected to result in issuance of seven series of bonds and expansion of the lease revenue commercial paper program by the end of Fiscal Year 2005-06. Through October 2005, four series of bonds have closed with an aggregate par amount of $301.2 million. These financings are briefly described below and are presented in the summary table at the end of this section. The information presented relating to the financings in progress should be considered preliminary and used for discussion and planning purposes only.

### 1. Completed Financings

**Redevelopment Agency of the City of San José Merged Area Redevelopment Project Tax Allocation Refunding Bonds, Series 2005A and Series 2005B**

On July 25, 2005, the Redevelopment Agency issued $152,950,000 of Series 2005A and $67,130,000 of Series 2005B tax allocation bonds. The proceeds of the Series 2005A bonds were used to current refund a portion of the Agency's Series 1993 tax allocation bonds and advance refund portions of the Agency's Series 1997 and Series 2002 tax allocation bonds. The proceeds of the Series 2005B bonds were used to current refund portions of the Agency's Series 1998 and Series 1999 tax allocation bonds. Debt service is payable from the Agency's tax increment revenues.

The refunding generated aggregate debt service savings (net of available funds) of $8,532,108, net present value savings of $6,886,437, representing a 3.06% net present value reduction in debt service payments. The Series 2005A bonds, which are insured by MBIA, bear interest at fixed rates ranging from 3.25% to 5.00%, and have a final maturity date of August 1, 2028. The Series 2005B bonds, which are insured by Ambac, bear interest at fixed rates ranging from 4.50% to 5.00%, and have a final maturity date of August 1, 2015.

**San Jose-Santa Clara Clean Water Financing Authority Sewer Revenue Refunding Bonds, Series 2005A and Series 2005B**

On October 5, 2005, the Clean Water Financing Authority issued $54,020,000 of Series 2005A and $27,130,000 of Series 2005B sewer revenue refunding bonds. The proceeds of the Series 2005A bonds were used to current refund the Authority's Series 1995A sewer revenue bonds. The proceeds of the Series 2005B bonds were used to current refund the Authority's Series 1995B sewer revenue bonds. Debt service is payable from the Authority's revenues which consist primarily of payments from the City of San José's sewer revenues.

The Series 2005A bonds, which are insured by FSA, bear interest at fixed rates ranging from 3.25% to 5.00%, and have a final maturity date of November 15, 2016. The Series 2005B bonds, which are also insured by FSA, bear interest at weekly variable rates and have a final maturity date of November 15, 2020.

The Series 1995A bonds will be redeemed on November 15, 2005. The refunding of the Series 1995A bonds generated aggregate debt service savings (net of available funds) of $24,325,971, net present value savings of $9,454,860, representing a 14.47% net present value reduction in debt service payments.

The Series 1995B bonds will be redeemed on December 7, 2005. The redemption of the Series 1995B bonds, which paid interest at weekly variable rates, with proceeds of the variable rate Series 2005B bonds, allowed the Authority to achieve a more economic amortization of its variable and fixed rate debt.

## 2. Planned Financings

Debt Management staff anticipates completing financings for the following four projects during the remainder of Fiscal Year 2005-06.

### Expansion of City of San José Financing Authority Lease Revenue Commercial Paper Program

In Fall 2005, City staff anticipates requesting City Council and City of San José Financing Authority Board approval to use the City's existing lease revenue commercial paper program as a means to finance the construction of the Central Service Yard Phase II Project. At the same time, staff will bring the necessary documents to the Council/Authority Board for approval to expand the capacity of the City of San José Financing Authority lease revenue commercial paper program from $98 million to $115 million to fully accommodate the estimated $22.5 million cost of the Central Service Yard Phase II Project. The tax-exempt commercial paper notes issued for the Central Service Yard Phase II Project are expected to be repaid from lease revenue bonds and proceeds from the sale of the Main Yard.

### General Obligation Bond Series 2006 (Libraries, Parks and Public Safety)

The City plans to issue another series of general obligation bonds in June 2006. The proceeds of those bonds would be used to fund a portion of the libraries, parks, and public safety projects approved by voters in November 2000 and March 2002. The timing, size, and purpose of the bond issue will depend upon the expenditure and encumbrance needs of the various projects to be financed.

### Multifamily Housing Revenue Bonds

The City submitted applications to CDLAC on behalf of the following projects, with allocations awarded on September 21, 2005:

- Paseo Senter I ($29.95 million, 117 affordable units)
- Paseo Senter II ($24.68 million, 101 affordable units)

The table on the following page presents a summary of debt which the City has either issued or plans to issue during Fiscal Year 2005-06.

## Summary of Completed and Planned Debt Issuance

*Fiscal Year 2005-06*

| Issue Date | Issue | Size (millions) | Type | Sale Type | Financial Advisor | Bond Counsel | Underwriter | Credit Enhancement |
|---|---|---|---|---|---|---|---|---|
| 07/25/2005 | RDA 2005A Merged Area | $152.950 | Tax Allocation Refunding | Negotiated | Ross Financial | Jones Hall | JPMorgan | MBIA |
| 07/25/2005 | RDA 2005B Merged Area | $67.130 | Tax Allocation Refunding | Negotiated | Ross Financial | Jones Hall | JPMorgan | Ambac |
| 10/05/2005 | CWFA 2005A | $54.020 | Sewer Revenue Refunding | Competitive | Stone & Youngberg | Nixon Peabody | JP Morgan | FSA |
| 10/05/2005 | CWFA 2005B | $27.130 | Sewer Revenue Refunding | Negotiated | Stone & Youngberg | Nixon Peabody | Citigroup | FSA[1] |
| Fall 2005 | CSJFA Commercial Paper Program | $17.000 | Lease Revenue Commercial Paper | Negotiated | Public Resources Advisory Group | Jones Hall | Lehman Brothers | State Street/ CalSTRS[2] |
| December 2005 | CSJ 2005B Paseo Senter I | $29.95 | Multifamily Housing | Private Placement | Ross Financial | Jones Hall | N/A | TBD |
| December 2005 | CSJ 2005C Paseo Senter II | $24.68 | Multifamily Housing | Private Placement | Ross Financial | Jones Hall | N/A | TBD |
| June 2006 | CSJ 2006 Libraries, Parks & Public Safety | $75.000 | General Obligation | TBD | TBD | TBD | TBD | TBD |
| **FY 2005-06** | **8 Series** | **$472.860** | | | | | | |

**Issuer Key**: CSJ-City of San José; CSJFA-City of San José Financing Authority; RDA-Redevelopment Agency of the City of San José.

[1] DEPFA Bank is providing liquidity support through a standby letter of credit.

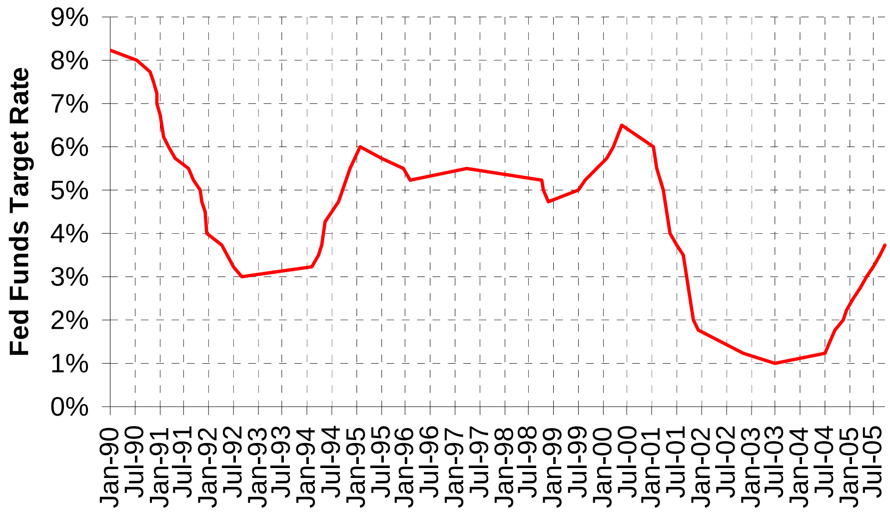
[2] State Street Bank and CalSTRS are providing liquidity support to the lease revenue commercial paper program.

## C. Current and Anticipated Market Conditions

The Federal Open Market Committee (the "FOMC") began systematically raising its Fed Funds target interest rate on June 30, 2004, and increased that target by 25 basis points at each of its ten subsequent meetings through September 2005. As a result of these actions, the Fed Funds target rate stood at 3.75% on September 20, 2005. To justify this policy of credit tightening, the FOMC has noted consistent growth in the economy and increasing inflationary pressure.

**Fed Funds Rate Targets**

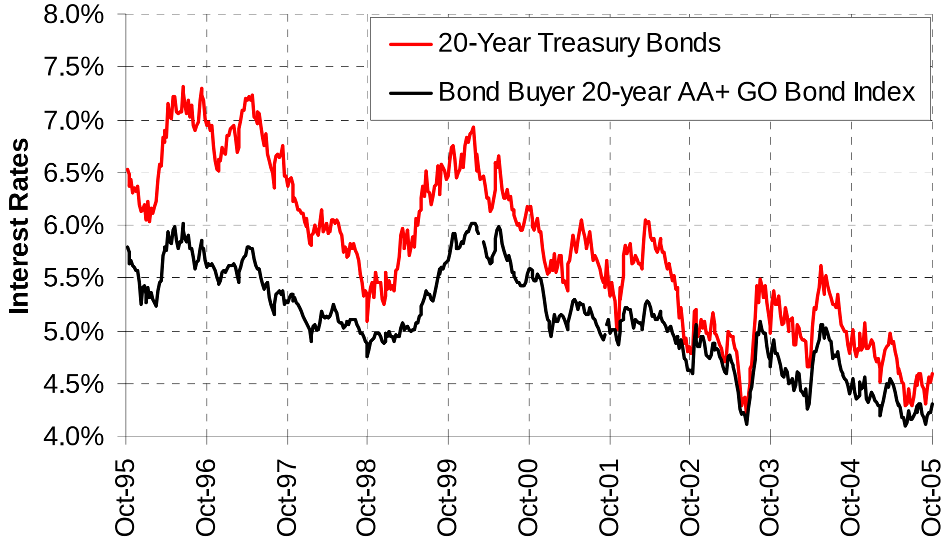
*January 1990 through September 2005*




The FOMC continues to believe that the stance of monetary policy remains accommodative and, coupled with robust underlying growth in productivity, is providing ongoing support to economic activity. The FOMC also notes, however, that higher energy and other costs have the potential to add to inflation pressures.

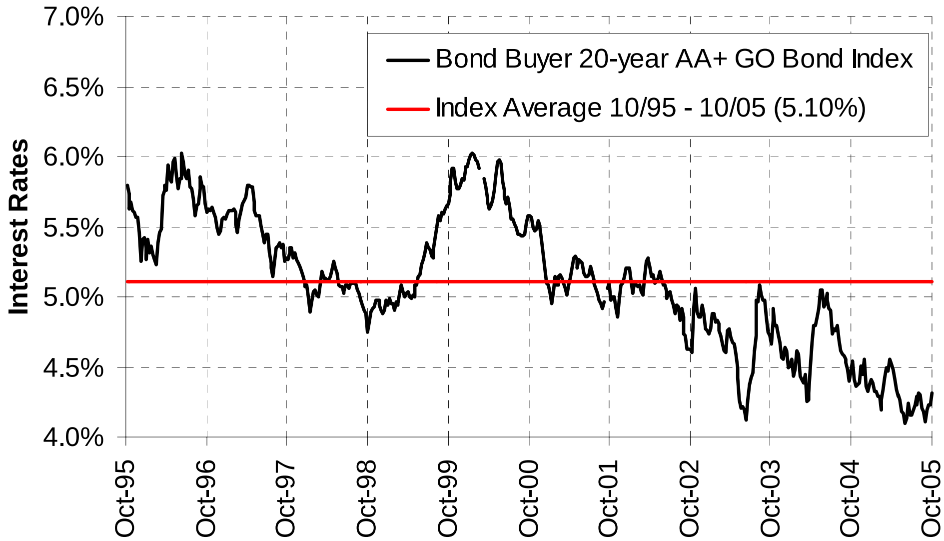
The spread between taxable and tax-exempt interest rates declined throughout the past year, averaging about 35 basis points, which is about half of the historical average spread.

**Comparison of Tax-Exempt and Taxable Interest Rates**
*October 1995 through September 2005*




As can be seen in the charts above and below, tax-exempt interest rates have exhibited volatility during the past year, but they have remained well below their ten-year average.

**Ten-Year History of Tax-Exempt Interest Rates**
*October 1995 through September 2005*



## D. Selection of Debt Financing Teams

The selection of the financial advisor and underwriter for a financing project is generally done in the form of a competitive request for proposal/qualifications (RFP or RFQ) process. Written proposals are reviewed by representatives from the Finance Department and other city departments involved with the financing and, when appropriate, by other cities' finance directors or finance personnel.

The Finance Department conducted a competitive selection process in Fiscal Year 2000-01 for the City's general financial advisor and for financial advisory services for a number of other pending City projects. As a result of this process, a pool of eligible financial advisors was created and approved by the City Council on April 24, 2001 (see table below). This pool expired on June 30, 2005, and a new pool is anticipated to be selected in early 2006. Considering the large number of financing projects Debt Management staff is working on, a pool of eligible financial advisors is crucial. It allows for a more efficient selection of financing teams for each separate bond issue, minimizes the time and the costs spent preparing and reviewing requests for proposals, and shortens the timeline required to finance City projects for the community.

**Financial Advisory Pool Eligible List**
Financial Advisory Firms Approved by the City Council on April 24, 2001
*May 2001 to June 2005*

| | |
|---|---|
| **City General Financial Advisor** | **Housing Program Financial Advisor** |
| Public Resources Advisory Group | Ross Financial |
| **General Obligation Bonds** | **Lease Revenue Bonds** |
| Public Resources Advisory Group | Kitahata & Company |
| RBC Dain Rauscher | Public Resources Advisory Group |
| | RBC Dain Rauscher |
| | Ross Financial |
| **Multifamily Housing Revenue Bonds** | **Land-Secured Financings** |
| CSG Advisors | E. Wagner & Associates |
| E. Wagner & Associates | Kelling, Northcross & Nobriga |
| Ross Financial Group | Public Financial Management |
| **Housing Set-Aside Tax Allocation Bonds** | |
| CSG Advisors | |
| Kitahata & Company | |
| Stone & Youngberg | |

The Finance Department, in coordination with the Airport Department, conducted a separate RFP process for financial advisory services for the Airport in the Fall of 1999. As a result of this process, Fullerton & Friar and Public Resources Advisory Group serve as co-financial advisors to the City for Airport related services and financing projects under a Master Agreement which terminated on June 30, 2005. The financial advisory services for the Airport will be included in the RFP for the pool of financial advisors to be completed in early 2006.

In addition to its project-specific financial advisors, the Debt Management Program continues to utilize the expertise of its general financial advisor, Public Resources Advisory Group ("PRAG"). PRAG has assisted the City in the examination of several financing options for various City projects, including the Lease Revenue Commercial Paper Program, as well as ongoing review of refunding opportunities.

In January 2005, Debt Management, in coordination with the Housing Department, began the RFP process to select a new underwriting pool for the City's multifamily housing revenue bond program. This underwriting pool was approved by the City Council on March 22, 2005, and will remain in place until December 31, 2007.

**Multifamily Housing Revenue Bond Underwriting Pool**
Underwriting Firms Approved by the City Council on March 22, 2005
*March 22, 2005 to December 31, 2007*

| | |
|---|---|
| Banc of America Securities, LLC | Red Capital Group |
| E.J. De La Rosa & Co., Inc. | UBS Financial Services, Inc. |
| Newman & Associates | |

In July 2000, an RFP process was undertaken for an underwriting pool for the Airport Master Plan. This underwriting pool was approved by the Council on October 31, 2000, and will remain in place until December 31, 2005.

As a result of changes in personnel and the level of airport-specific financing expertise at firms in the Airport pool, in September 2002 a questionnaire was sent to those firms designated as Senior Managers and Co-Managers for the purpose of reevaluating assignments in the pool. Based on the responses from that questionnaire, on November 19, 2002, staff recommended and Council approved a reallocation of underwriting roles within the Airport pool.

**Airport Master Plan Financing Underwriting Pool**
Underwriting Firms Approved by the City Council on October 31, 2000
*(Incorporating Changes Approved by City Council on November 19, 2002)*
*November 1, 2000 to December 31, 2005*

| Senior Managers | Co-Managers |
|---|---|
| Lehman Brothers | E.J. De La Rosa & Company |
| Morgan Stanley & Company | Merrill Lynch & Company |
| Citigroup (formerly Salomon Smith Barney) | RBC Dain Rauscher |
| UBS Financial Services | |
| **Selling Group** | |
| A.G. Edwards & Sons | |
| Bank of America | |
| eBondTrade | |
| Prudential Securities Incorporated | |
| Raymond James & Associates | |

The Summary of Debt Issuance tables shown earlier in this section provide a summary of information on all of the financing team participants for debt issues completed in Fiscal Year 2004-05 and for the debt issues completed and underway in Fiscal Year 2005-06.

CITY OF

SAN JOSE

CAPITAL OF SILICON VALLEY

## III. DEBT ADMINISTRATION

### A. Debt Administration System

The Debt Management Program continually works to improve its comprehensive debt administration system. Inputs to the system come from financing documents, trustee reports, reports from the City's remarketing agents and collateral agents, contracts with financial services providers, and reports and requests from City staff. These inputs provide the data needed to ensure that the City is complying with its bond covenants, that reporting to third parties is done timely and accurately, that its bond funds are appropriately allocated, invested and disbursed, that its debt service payments are timely and accurate, that it has correctly calculated its estimated arbitrage rebate liabilities, that its variable rates are set at market levels, that its investment agreements are properly collateralized, and that its liquidity and credit enhancement contracts are renewed in a timely manner.

### B. Compliance and Monitoring

Compliance and monitoring activities constitute a large and growing portion of the Debt Management Program's daily tasks. While the process of assembling a specific bond financing project may take only three to six months, compliance with the provisions of bond covenants last the entire life that the bonds are outstanding, up to 40 years or more. Debt Management staff work very closely with other City departments as well as with the City Attorney's Office and the Budget Office to coordinate the investment and disbursement of bond funds to assure expenditures are in compliance with IRS Regulations and the California State Constitution. Debt Management staff also work closely with the bond trustees and the Finance Department's Treasury cash management staff and Accounting Division staff to ensure that bond proceeds are invested properly, funds and accounts are properly established, cash flows are fully accounted for, and all bond covenants are complied with.

#### 1. Trustee Activities

As of June 30, 2005, the City has over $615 million in bond and commercial paper note funds that are held by three trustees and invested in 283 Funds and Accounts. These figures do not include the Redevelopment Agency's merged area redevelopment project (80%) bonds, Airport commercial paper program, or the City's multifamily housing revenue bonds. Each Fund is managed separately according to the provisions of a trust indenture or fiscal agent agreement, tax certificate, and other documents governing the issuance of the bonds. Depending on the terms of the bond issue, bond funds may include, but are not limited to, construction and improvement, capitalized interest, escrow, reserve, debt service and other funds held for the benefit of the bondholders. The table below summarizes the City's trustee activity.

| Trustee Summary[1] *as of June 30, 2005* | | | |
|---|---|---|---|
| **Trustee** | **Number of Bond Issues** | **Original Par Amount of Bonds** | **Trustee Fund Balance** |
| Bank of New York | 11 | $ 558,075,000 | $203,633,534 |
| US Bank | 15 | 444,098,420 | 31,358,914 |
| Wells Fargo Bank | 27 | 1,435,220,000 | 380,113,765 |
| Total | 53 | $2,437,393,420 | $615,106,213 |

[1] Does not include RDA bonds issued for merged area redevelopment projects, Airport commercial paper, or multifamily housing revenue bonds.

Debt Management staff maintains frequent contact with trustees with respect to each trustee's fund management responsibilities. Fund management includes review of, and compliance with, the provisions governing Funds and Accounts of each series of bonds. Fund management also includes compliance with the City's investment policy, financial reporting requirements, and generally accepted accounting principles. Debt Management staff closely monitor investment and cash flows to and from each fund under management, including payment of debt service obligations, to insure accuracy and timeliness.

**2. Bond Proceeds Expenditures and Reimbursement Procedures**

As an issuer of tax-exempt debt, the City's use of bond proceeds is limited by Federal and State law, and in some cases by the ballot language authorizing the debt. Generally, tax-exempt bond proceeds, including interest earnings on bond funds, may only be spent for governmental purposes and only on capital projects. In the case of voter-approved debt, the bond proceeds may only be used for the purposes described in the ballot language authorizing the debt.

To provide accountability in managing bond funds, most of the City's bond-financed project funds are held by trustees, who disburse the construction or improvement funds only after Debt Management has reviewed a disbursement request from the City department managing the project. As of June 30, 2005, of the $615 million held by the trustees, over $495 million is construction proceeds from the sale of both taxable and tax-exempt bonds and commercial paper notes. These are funds awaiting disbursement for expenditures related to the construction of specific improvements or acquisition of real property as defined in the governing documents of each bond series.

Disbursement requests are reviewed and approved by department heads or their deputies before they are submitted to Debt Management. Debt Management staff then reviews, reconciles and qualifies the bond-financed project expenditures before submitting disbursement requests to the trustees. When there is an ambiguity, the City Attorney's Office assists in determining the eligibility of expenditure items. During Fiscal Year 2004-05, Debt Management staff reviewed and processed 180 disbursement requests totaling over $195 million. The Finance Department is currently in the process of reviewing these procedures to identify streamlining and efficiency opportunities.

**3. Arbitrage Rebate**

Debt Management actively monitors the investment and disbursement of proceeds of tax-exempt bonds for arbitrage compliance purposes. Arbitrage is the profit that results from investing low-yield tax-exempt bond proceeds in higher-yield securities (also referred to as positive arbitrage). Federal law stipulates that investment earnings in excess of the bond yield are arbitrage earnings and must be rebated to the Federal Government. However, if a jurisdiction meets certain IRS expenditure exceptions for bond proceeds, the arbitrage earnings will not have to be rebated to the Federal Government. Arbitrage regulations apply to all of the City's tax-exempt financings.

Debt Management staff, working in conjunction with Treasury staff, endeavor to invest bond proceeds at the highest yield possible, subject to the City's primary Investment Policy objectives of safety, liquidity and yield. The investment of bond proceeds is in accordance with the City's Investment Policy and the Permitted Investment provisions of the governing documents of each series of bonds. For some types of bond funds, particularly a construction fund that must be held in short-term securities, it may be the case that the fund earns at a rate less than the bond yield. Therefore, the fund is said to be earning negative arbitrage. Through careful management of its investments, the City can use negative arbitrage earnings in one account of a bond series to offset positive arbitrage in another account of the same series.

In Fiscal Year 2004-05, 265 funds and accounts held by trustees or by the City, containing $605 million of tax-exempt bond proceeds, were actively monitored for arbitrage compliance. Debt Management staff continually monitors and documents investments and cash flows of the City's bond funds, and then annually reviews all arbitrage provisions of individual bond funds and computes arbitrage earnings. The resulting arbitrage reports are then submitted to the relevant City departments and bond trustees so that the estimated rebate liability can be budgeted and set aside for future payment. Although arbitrage earnings are rebated to the United States Treasury on a five-year installment basis, Debt Management staff conducts annual rebate calculations to assure that the City stays current on compliance issues and to facilitate accountability for any potential rebate liability.

Debt Management staff prepares the annual arbitrage calculations for most of the City's debt, except the Redevelopment Agency bonds issued for redevelopment projects and the conduit multifamily housing revenue bonds. Agency staff tracks arbitrage for redevelopment project bonds, and in the case of conduit multifamily housing revenue bonds, the developer is responsible for the annual arbitrage calculations during the construction period and thereafter on each fifth-year bond anniversary date. Debt Management staff tracks the developer's compliance with this requirement.

In addition to performing its own annual calculations, the City retains the services of Bond Logistix, a subsidiary of Orrick, Herrington & Sutcliffe LLP, to: (1) review the City's arbitrage compliance at five year anniversary dates when rebate is actually due to the Federal Government; (2) compute annual and five-year installment arbitrage rebate liability on the more complex financings; and (3) provide technical assistance to the City in the area of arbitrage rebate compliance. This third-party review provides an added level of confidence that the City is in compliance with the arbitrage regulations. Such review is particularly important given that the Internal Revenue Service has stepped-up its random audit and target audit programs for tax-exempt bond issues. Indeed the IRS has recently conducted random audits on two of the City's multifamily housing revenue bond issues and, in both cases, the audits were closed with no change to the status of the bonds.

The table below lists the City's tax-exempt bond issues that have balances in their respective rebate funds and the next rebate installment date:

**Summary of Rebate Fund Balances**
*as of June 30, 2005*

| Bond Issue | Rebate Fund Balance | Next Rebate Installment Date |
|---|---|---|
| City of San José Financing Authority, Series 1997A | $ 5,656.96 | 09/08/2007 |
| City of San José Financing Authority, Series 1997B | 6,895.44 | 09/27/2007 |
| City of San José Financing Authority, Series 2001D | 123,247.56 | 10/1/2005 |
| City of San José Financing Authority, Series 2001E | 32,262.02 | 01/01/2006 |
| Clean Water Financing Authority, Series 1995A and C | 125,187.90 | 01/14/2006 |
| City of San José Community Facilities District No. 1 | 31,943.09 | 12/31/2007 |
| Total | $ 325,192.97 | |

## 4. Continuing Disclosure

On November 10, 1994, the Securities and Exchange Commission ("SEC") adopted amendments to existing federal regulations ("Rule 15c-12" or the "Rule") under which municipalities issuing securities on or after July 3, 1995 are required to:

1. Prepare official statements meeting current requirements of the Rule;
2. Annually file certain financial information and operating data with national and state repositories; and
3. Prepare announcements of the significant events enumerated in the Rule.

As of June 30, 2005, the City had 33 series of bonds subject to continuing disclosure requirements, excluding the Redevelopment Agency and multifamily housing revenue bonds, some of which are also subject to continuing disclosure requirements under the Rule. In cooperation with the Redevelopment Agency and other City departments, and with the assistance of the City Attorney's Office, the Finance Department collects, validates, and disseminates financial and operating information to the national repositories. Debt Management staff also monitors compliance with respect to continuing disclosure obligations of the multifamily housing projects. Timely and accurate communication with the municipal marketplace is vital in retaining the City's creditworthiness and market access. Continuing disclosure and compliance reporting constitute a significant part of Debt Management's compliance activity for the life of each series of bonds.

Beginning with the disclosure reports for fiscal year 2003-04, filed before December 31, 2004, Debt Management, through the dissemination agents, utilized the newly-established "central post office" for continuing disclosure reporting: DisclosureUSA. DisclosureUSA is an Internet-based electronic distribution system established by the municipal finance industry which functions as a one-stop conduit that receives continuing disclosure filings from issuers, or issuers' dissemination agents, and then transmits them electronically to the nationally recognized municipal securities information repositories ("NRMSIRs") as required by continuing disclosure agreements. Upon receiving a filing, the document repositories automatically send a return receipt to the DisclosureUSA website, which is posted to the site so issuers and the general public can view both the time the filing was sent and the acknowledgement that it was received. Additionally, Disclosure USA electronically informs the issuer of the filing on real time basis. Debt Management anticipates that transitioning to "paperless" continuing disclosure will result in a reduction of resources needed to support this activity.

## C. Investment of Bond Proceeds

Debt Management works closely with bond trustees as well as with Treasury cash management and Accounting Division staff in managing the investment and disbursement of bond proceeds. Bond proceeds are invested in accordance with bond covenants and with the provisions of the City's Investment Policy, which was most recently amended on December 14, 2004. As requested in 2002 by the City Council, as part of the approval of the use of investment agreements for bond proceeds, the status of the investment agreements in place as of June 30, 2004, is briefly summarized below.

**City of San José Airport, Series 2001A Reserve Account**: The Series 2001A Airport Bond Reserve Account was invested with MBIA in August 2001 and has a maturity of March 1, 2031. The amount invested was $10.5 million and the balance as of June 30, 2004, was $10.7 million. The agreement is collateralized with US Treasuries at 104% and Agencies at 105%, and has a yield of 5.78%. The bond yield on these fixed rate bonds is 5.01%.

**City of San José Financing Authority Lease Revenue Bonds, Series 2002B,C,D (Civic Center Project) Reserve Fund:** The Reserve Fund for the Series 2002 Civic Center Bonds was invested with AIG Matched Funding Corporation in November 2002 and had a maturity of June 1, 2005. The amount invested was $32.8 million and the balance as of June 30, 2005, was $32.8 million (while the City Hall project is under construction, interest earnings on the Reserve Fund flow to the Construction Fund). The agreement was collateralized with US Treasuries at 104% and Agencies at 105%, and had a yield of 2.41%. The blended bond yield on these fixed and variable rate bonds is 5.06%.

The term of this investment agreement was limited to the expected construction period for the Civic Center Project to provide the City with maximum flexibility. Upon completion of the Project, the City can decide whether to reinvest the Reserve Fund, possibly at a higher yield than was available at the time of the financing, or to purchase a surety bond for all or a portion of the Reserve Requirement. Purchase of a surety bond would release a corresponding amount of Reserve funds, which could then be applied to City capital projects.

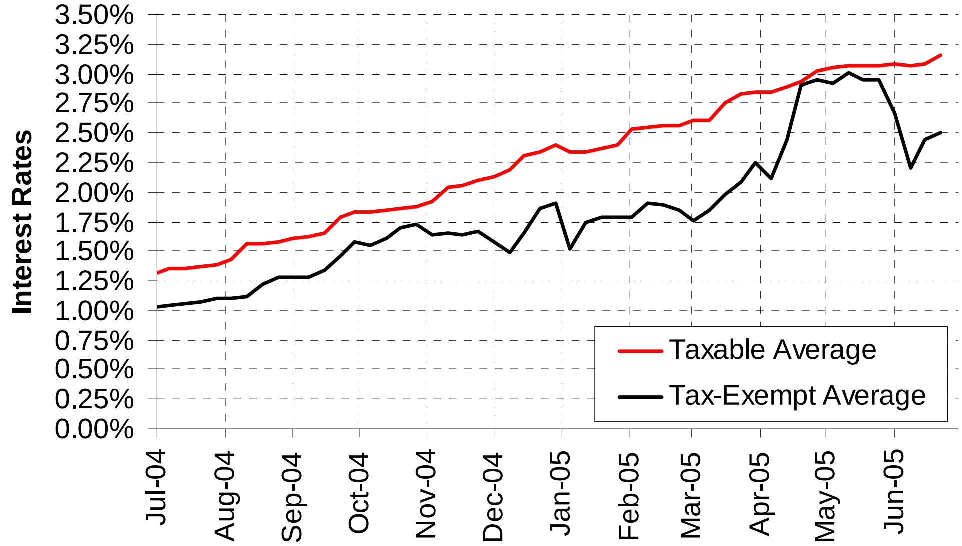
On June 1, 2005, the agreement reached its maturity and the Reserve Fund proceeds became available for reinvestment. As of the date of this report, the balance of the Reserve Fund is $33,141,821 and is invested in Federal Home Loan Bank (FHLB) discount notes, yielding 3.06%. Upon the completion of the Civic Center Project, a decision will be made to either reinvest the Reserve Fund or purchase a surety.

## D. Outstanding Variable Rate Debt

During Fiscal Year 2004-05, the City had thirty-one variable-rate bond series outstanding, including three series of auction rate securities, of which fifteen are multifamily housing issues. Of the thirty-one series, eight are taxable and twenty-three are tax-exempt. Debt Management staff track the rates weekly to ensure that the rates are consistent with market conditions, taking into consideration the differences among securities, ratings, and credit enhancement. As short-term interest rates have risen during the past year, the spread between variable interest rates and long-term fixed interest rates has decreased.

The graph below provides a history of the average variable rates the City paid during Fiscal Year 2004-05 for both taxable and tax-exempt bond issues. The graph shows that while taxable rates increased steadily with the Fed's consistent raising of the Fed Funds target rate throughout the year, the tax-exempt rates were subject to tax season cyclic volatility. The spread between the June 30, 2005, tax-exempt average of 2.50% and the taxable average of 3.16% was somewhat narrower than the historical average spread.

**Average Weekly Taxable and Tax-Exempt Rates**
*Fiscal Year 2004-05*




## E. Refunding Opportunities

As part of its role as manager of the City's debt portfolio, Debt Management undertakes a continual review and analysis of all outstanding debt. The objective of this ongoing process is to identify opportunities to refund or restructure the debt portfolio with the goal of reducing the City's annual debt service obligations. A discussion of bonds refunded in Fiscal Year 2004-05 and anticipated refundings for Fiscal Year 2005-06 is included in the Debt Issuance section of this report. Although fixed-rate bonds can only be redeemed on or after the first call date specified in the financing documents, variable-rate bonds can be redeemed on any tender date.

Generally, bonds can be refunded in two ways: as a current refunding or as an advance refunding. A current refunding is a refinancing in which the refunding bonds (new bonds) are issued less than 90 days before a date on which the refunded bonds (old bonds) can be called. The proceeds of the refunding bonds are applied immediately to pay principal, interest, and a call premium, if any, on the refunded bonds. Thereafter, the revenues originally pledged to the payment of the refunded bonds are pledged to the payment of the refunding bonds.

An advance refunding is the refinancing of outstanding bonds by the issuance of a new issue of bonds more than 90 days prior to the date on which the outstanding bonds are callable. The proceeds of advance refunding bonds are invested in an escrow until the first call date of the bonds to be refunded. Accordingly, for a period of time, both the issue being refunded and the refunding bond issue are outstanding until the refunded bonds are redeemed from the refunding escrow on their call date. The Internal Revenue Service restricts the yield which may be earned on investment of the proceeds of the refunding bonds and allows for only one advance refunding of any series of bonds issued after 1986.

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

## IV. CITY'S OUTSTANDING DEBT PORTFOLIO

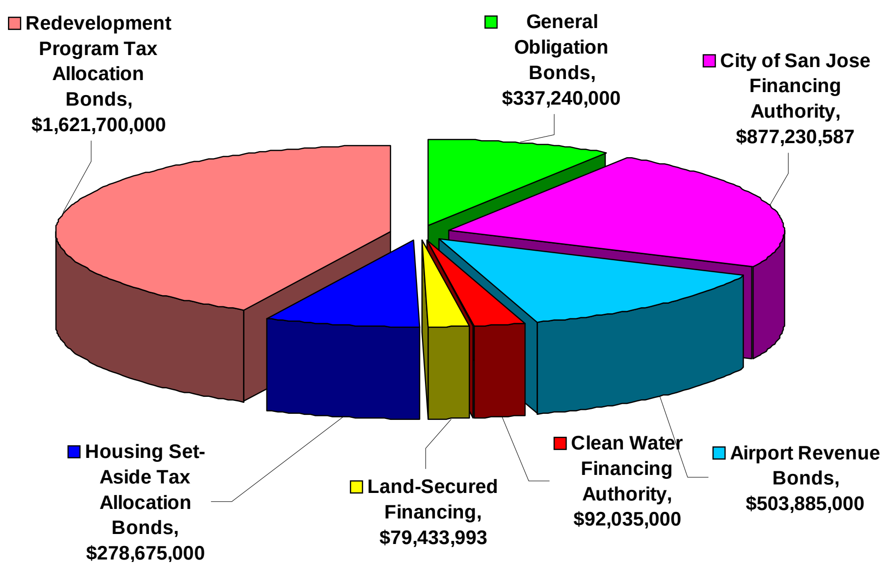
Debt Management continues the task of ongoing development and maintenance of a debt management database and tracking system. This database and tracking system provides the opportunity to prepare detailed analyses and track issues and requirements related to the City's debt portfolio. The following section includes both a descriptive and illustrative presentation of the City's debt portfolio, comprised of 119 series of bonds totaling over $4.3 billion, as of June 30, 2005. This analysis includes all debt issued by the City of San José, its Redevelopment Agency, and various financing authorities of which the City is a member. ***Note that the City has no obligation or connection in any way to Redevelopment Agency debt.***

As of June 30, 2005, the City, the Redevelopment Agency, and related entities had 62 series of bonds outstanding, totaling $3.79 billion. The pie chart below shows the distribution of outstanding bonds among the various categories of debt issued by the City and its related entities: general obligation, City of San José Financing Authority, airport, sewer (Clean Water Financing Authority), land-secured (assessment district and community facilities district), and Redevelopment Agency tax increment debt (Housing Set-Aside and Agency Merged Area TABs). The chart below does not include the portions of outstanding City of San José Financing Authority or Airport commercial paper that will be repaid from issuance of long-term debt, amounts drawn on the Housing Department Line of Credit, or multifamily housing revenue bonds, but those items are addressed in the more detailed breakouts that follow.

A table of the 57 series of outstanding multifamily housing revenue bonds, totaling over $571 million, is shown later in this section of the report, and a summary table of all other debt by series is presented in Appendix B.

**Outstanding Bonds Issued by All Agencies**

*Outstanding Debt as of June 30, 2005: $3,790,199,580*



In addition to examining the par amount of debt outstanding, it is helpful to also examine the debt service repayment schedule. Interest projections for weekly variable rate debt in the annual debt service charts that follow are based on assumptions used in developing the Fiscal Year 2005-06 Adopted Budget as shown in the table below.

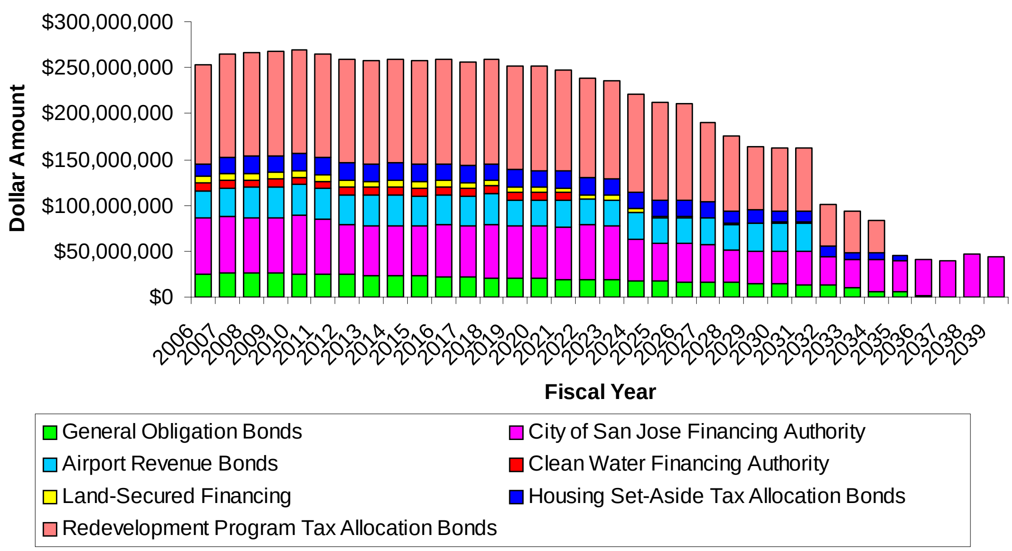
**Average Weekly Variable Interest Rate Assumptions**
*for Annual Debt Service Projections*

| | Tax-Exempt Rates | AMT Rates | Taxable Rates |
|---|---|---|---|
| Fiscal Year 2005-06 | 3.20% | 3.25% | 4.45% |
| Subsequent Fiscal Years | 3.20% | 3.25% | 4.55% |

*Source: City of San José Fiscal Year 2005-06 Adopted Budget.*

With the exception of the City's conduit multi-family housing revenue bonds, the stacked bar graph below illustrates the annual debt service payments for all of the debt category types shown in the above pie chart. The multifamily indebtedness was omitted from the bar graph due to the complicated nature of multifamily housing amortization schedules. In addition, omitting multifamily housing bonds from the chart more appropriately illustrates the annual debt service obligations for which the City/Redevelopment Agency/other agencies are responsible, either through direct payments or through the effort of collecting payments through the tax roll as in the case of general obligation and land-secured debt.

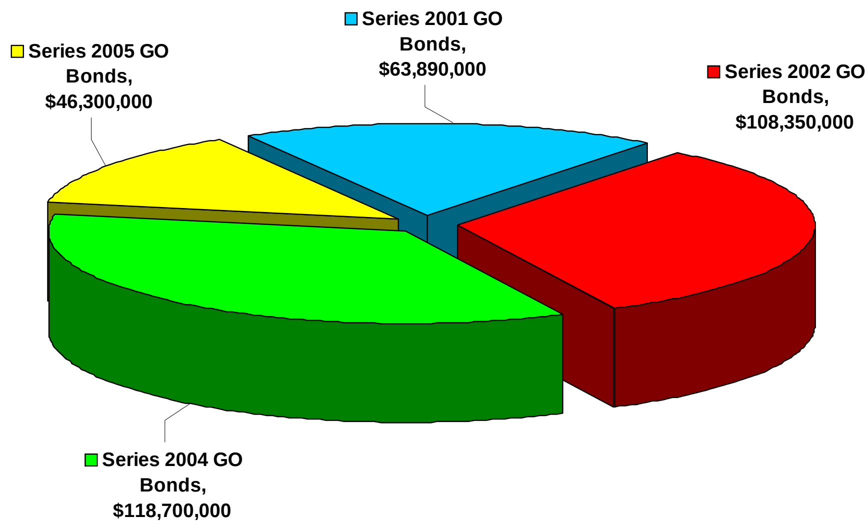
**Outstanding Bonds Issued by All Agencies**
*Annual Debt Service*



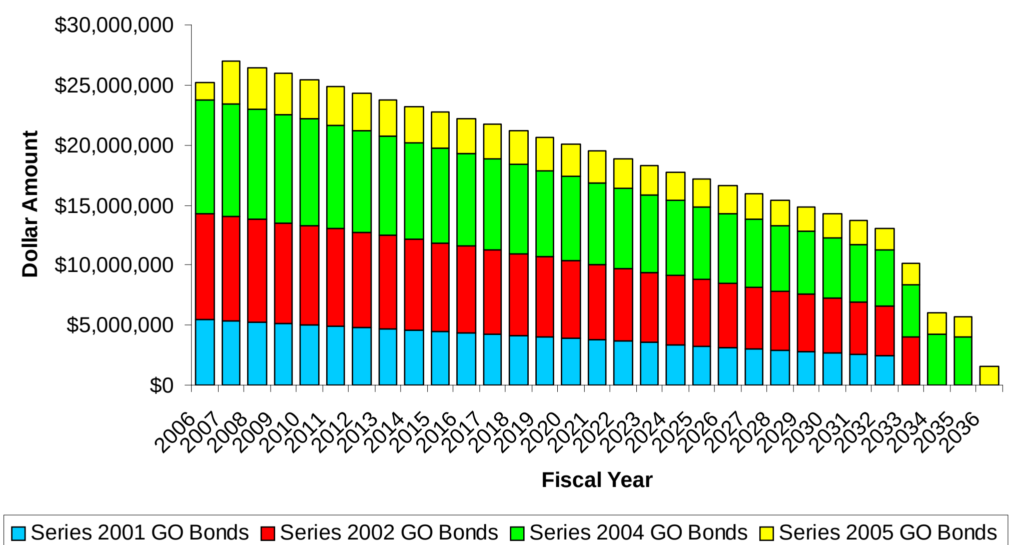
## A. General Obligation Bonds

In 2000 and 2002, the voters approved three ballot measures (Measures 2000 O and P and Measure 2002 O) that authorize total issuance of $598,820,000 of general obligation (GO) bonds for library, parks, and public safety projects which are secured by the taxing power of the City. As of June 30, 2005, the City of San José had issued $352.09 million of GO bonds with the proceeds split for three purposes: library projects ($140.6 million), parks and recreation projects ($132.715 million), and public safety projects ($78.775 million). Through June 30, 2005, $14.85 million in principal payments had been made, resulting in an outstanding balance of $337.24 million.

**General Obligation Bonds**
*Outstanding Debt as of June 30, 2005: $337,240,000*




**General Obligation Bonds**
*Annual Debt Service*



## B. City of San José Financing Authority Obligations

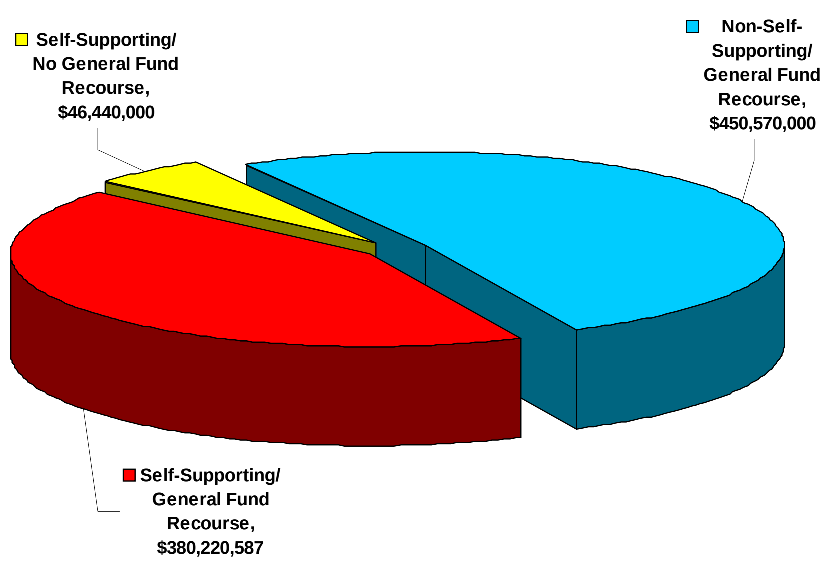
The City of San José Financing Authority (the "Authority") is a joint exercise of powers authority established under state law between the City and the Redevelopment Agency, and is authorized to finance public capital improvements for public entities. Bonds and notes issued by the Authority are repaid through revenues generated by the financed facilities or assets, or lease payments from the City for the use of specified facilities, which in some cases are different from those that were financed. Although payment for a few of the Authority's obligations is limited to specific revenue sources, most of the Authority's obligations are ultimately payable from the City's General Fund.

To better illustrate the variety of Authority debt outstanding, Authority obligations are presented here in several categories. These include:

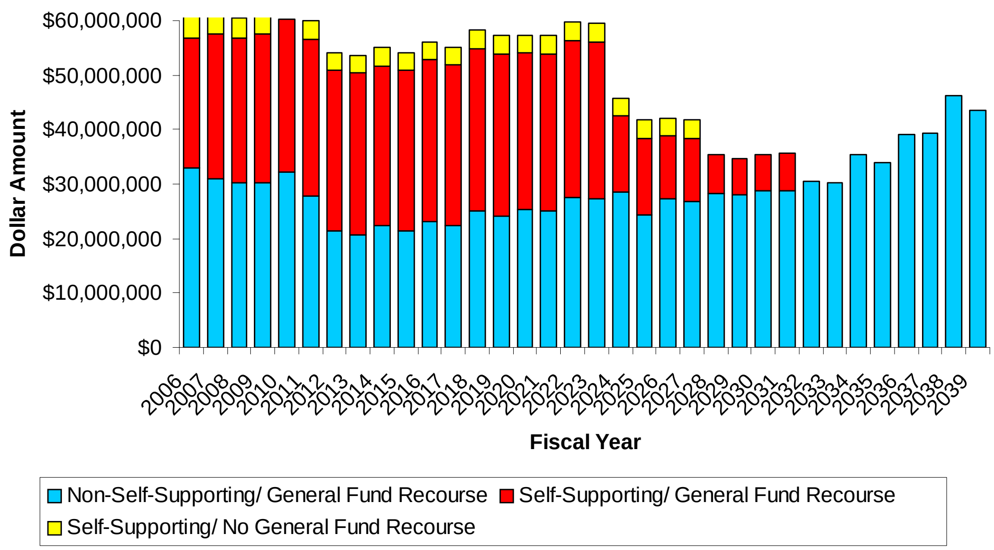
1. Non-Self-Supporting Debt with Recourse to the City's General Fund;
2. Self-Supporting Debt with Recourse to the City's General Fund; and
3. Self-Supporting Debt with No Recourse to the City's General Fund.

The next two charts illustrate the total amount of Authority bonds outstanding by category along with a bar chart illustrating annual debt service obligations by category.

**City of San José Financing Authority Obligations**
*Outstanding Debt as of June 30, 2005: $877,230,587*



**City of San José Financing Authority Obligations**
*Annual Debt Service*




## 1. Non-Self-Supporting Debt with Recourse to the City's General Fund

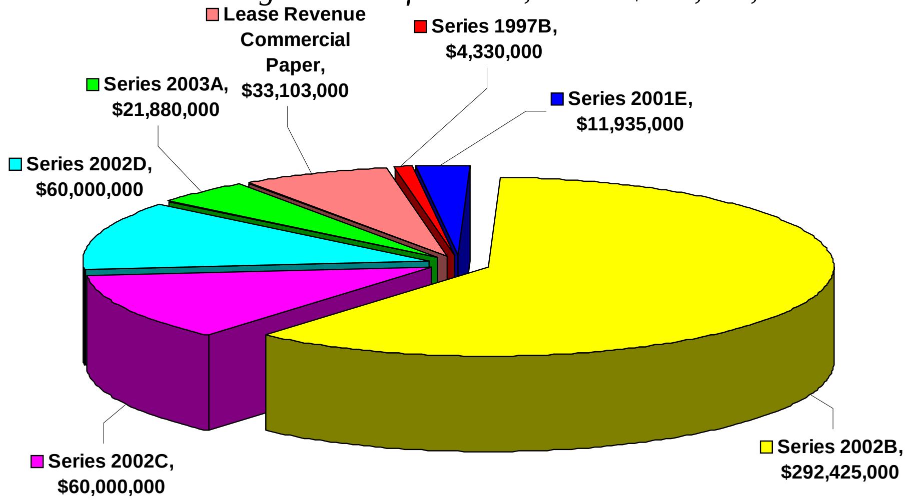
The financings included in this category and the next are structured as lease revenue bonds which are repaid from City lease payments for specified facilities. The leased facilities are typically those that are being financed, but in some cases may consist of other City assets.

The financing projects included in this category do not generate revenues that can be applied to offset the City's lease payments. Although City special funds or other revenue sources may be earmarked to make these payments, the City's General Fund bears the majority of the debt burden. The 1997B Bonds financed fire apparatus, childcare facilities, and library land acquisition, the Series 2001E Bonds refunded the City's outstanding debt on its Communications Center, the Series 2002B, 2002C, and 2002D Bonds financed a portion of the new Civic Center project, and the Series 2003A Bonds refunded the bonds issued to finance site acquisition and construction costs of the City's Central Service Yard. The Commercial Paper Notes provide interim financing for land acquisition and construction of the Civic Center Offsite Parking Garage, short-term financing for technology, furniture, equipment and relocation expenses associated with the new Civic Center, and the cost of the Consolidated Utility Billing System.

The pie chart below illustrates the total amount of outstanding debt in the category of non-self-supporting Authority debt with recourse to the General Fund. As of June 30, 2005, the total amount was $483,673,000, consisting of $450,570,000 of lease revenue bonds and $33,103,000 of taxable and tax-exempt commercial paper.

**Non-Self-Supporting Debt/ General Fund Recourse**

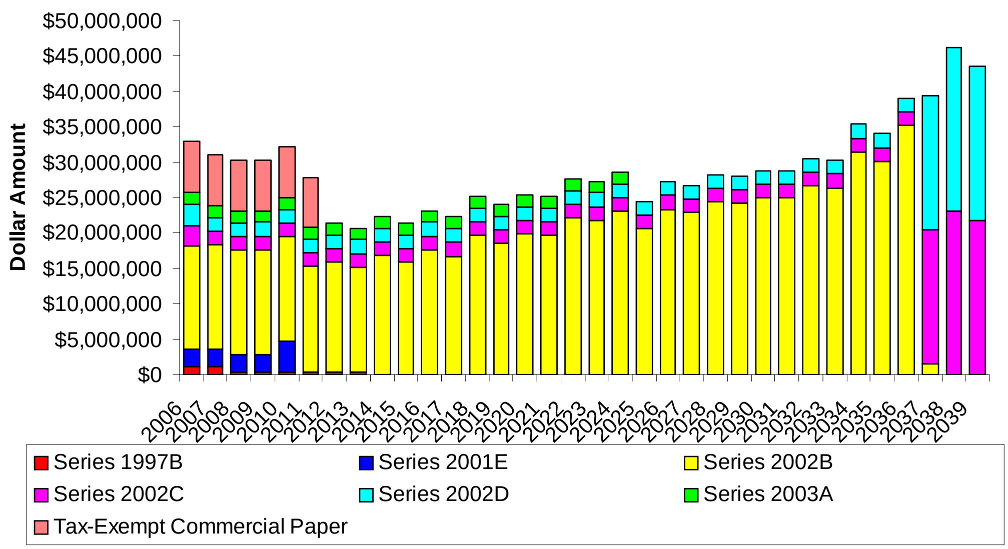
*Outstanding Debt as of June 30, 2005:  $483,673,000*




The bar chart illustrates the annual debt service obligations for this category.  The portion of the commercial paper that is anticipated to be repaid from bond proceeds from the future sale of long-term debt is not included in the bar graph since the interest due on the notes is "rolled" and funded from the issuance of additional commercial paper notes.

**Non-Self-Supporting Debt/ General Fund Recourse**

*Annual Debt Service*



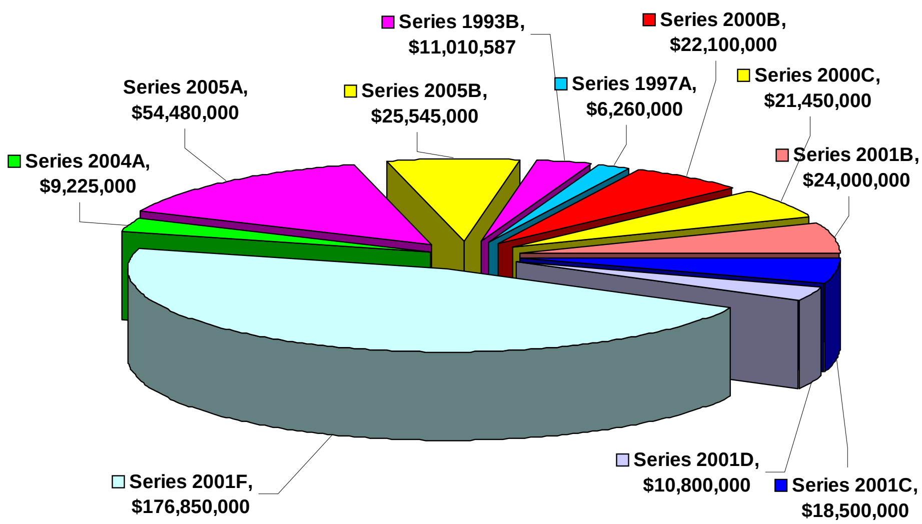
## 2. Self-Supporting Debt with Recourse to the City's General Fund

As with the previous category of Authority debt, the financings included in this category are structured as lease revenue bonds which are repaid from City lease payments for specified facilities.

This category, Self-Supporting Debt with Recourse to the City's General Fund, includes bond-financed capital projects which generate revenue that can be applied to offset the City's lease payments. This category also includes the Convention Center refunding, for which the City's lease payments are reimbursed by the Redevelopment Agency. To the extent that offsetting revenues are insufficient to completely cover the debt service payments for any of these bonds, the City's General Fund is committed to make up the difference. A short description of each of these self-supporting projects follows the charts.

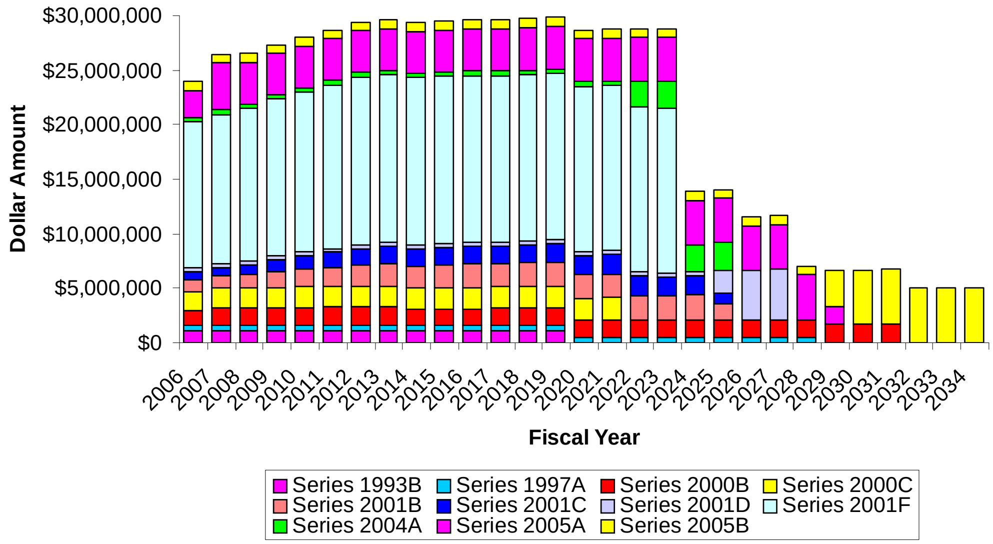
**Self-Supporting Debt/ General Fund Recourse**

*Outstanding Debt as of June 30, 2005: $380,220,587*



**Self-Supporting Debt/ General Fund Recourse**

*Annual Debt Service*




**Series 1993B (Community Facilities Project)**: These fixed-rate bonds funded the first phase of renovation for the Hayes Mansion, construction of the Berryessa Community Center, acquisition of Murdock Park, and construction of the City's Logitech Ice Centre. The Ice Centre portion of these bonds was refunded with proceeds of the Series 2000C Bonds. Debt service on the Series 1993B Bonds is paid primarily from revenues of the Hayes Mansion. To the extent these revenues are insufficient to fully pay the debt service, the General Fund or other available funds make up the difference.

**Series 1997A (Golf Course Project)**: These fixed-rate bonds financed the acquisition, renovation, and conversion of an 18-hole course to a 9-hole course with a driving range (the Rancho del Pueblo Golf Course). Debt service on the 1997A Bonds is paid from golf course revenues. To the extent golf course revenues are insufficient to fully pay the debt service, the General Fund or other available funds make up the difference. The Series 1997A Bonds are backed by motor vehicle license fee revenues under the State Controller's Intercept Program. Under that program, the State Controller only makes payments to the Trustee from the City's motor vehicle license fees if the City fails to meet its obligations under the Project Lease.

**Series 2000B (Tuers-Capitol Golf Course/Camden Park Refunding)**: These fixed-rate bonds financed construction of the City's 18-hole Los Lagos Golf Course and refunded outstanding certificates of participation issued by the Association of Bay Area Governments ("ABAG") for the Camden Neighborhood Park. Debt service on the 2000B Bonds is paid from golf course revenues and construction and conveyance tax revenues from Council District #9 funds. To the extent these revenues are insufficient to fully pay the debt service, the General Fund or other available funds make up the difference. The Series 2000B Bonds are backed by motor vehicle license fee revenues under the State Controller's Intercept Program.

**Series 2000C (Ice Centre of San José Refunding and Improvement Project)**: These variable-rate bonds refunded the Ice Centre portion of the Series 1993B Bonds and financed construction of an additional ice rink at the facility. Under the operator's Lease and Management Agreement with the City, the City receives fixed quarterly payments to cover debt service on the bonds and to fund capital repair and replacement reserves. To the extent these payments are insufficient to fully pay the debt service, the General Fund or other available funds make up the difference.

**Series 2001B, 2001C, and 2001D (Hayes Mansion Phase III Improvement and Refunding Project)**: These variable-rate bonds financed the Hayes Mansion Phase III improvements and refunded the Series 1995 Bonds issued to finance the Hayes Mansion Phase II improvements. Under the operator's Management Agreement, revenues of the Hayes Mansion are used to pay debt service and financing costs of the Series 2001 Hayes Mansion Bonds and the Hayes Mansion share of debt service of the Series 1993B Bonds. To the extent these payments are insufficient to fully pay the debt service, the General Fund or other available funds make up the difference.

**Series 2001F (Convention Center Refunding Project)**: These fixed-rate bonds refunded the Authority's outstanding debt on the City's Convention Center. Under a Reimbursement Agreement between the City and the Redevelopment Agency, the Redevelopment Agency has committed to pay the debt service on the Series 2001F Bonds, subordinate to all other debt issued by the Agency. To the extent the Agency payments are insufficient to fully pay the debt service, the General Fund or other available funds make up the difference.

**Series 2004A (Ice Centre of San José Expansion Project)**: These auction-rate bonds financed expansion and renovation of the facility, including construction of an additional ice rink. Under the operator's Lease and Management Agreement with the City, the City receives fixed quarterly payments to cover debt service on the bonds and to fund capital repair and replacement reserves. To the extent these payments are insufficient to fully pay the debt service, the General Fund or other available funds make up the difference.

**Series 2005A and 2005B (Land Acquisition)**: These variable-rate bonds financed acquisition of property adjacent to the Airport. Under an Operating Lease with the Airport, the City receives rental payments to cover debt service on the bonds. To the extent these payments are insufficient to fully pay the debt service, the General Fund or other available funds make up the difference.

### 3. Self-Supporting Debt with No Recourse to the City's General Fund

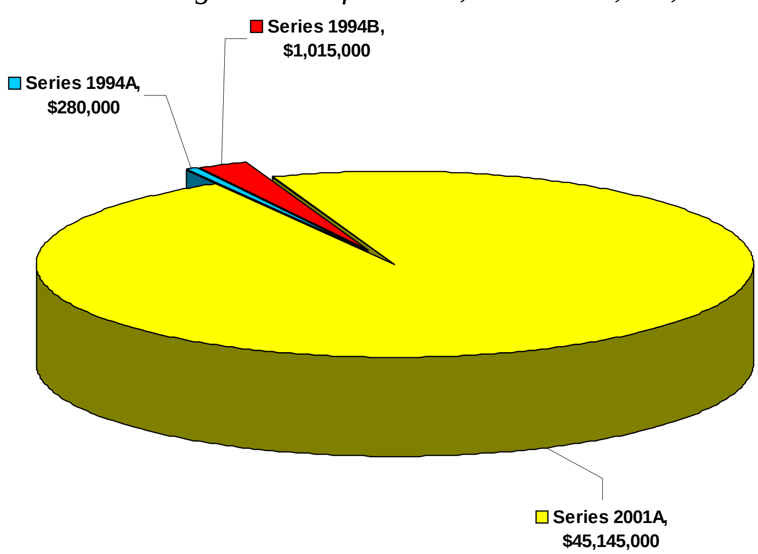
This category includes Authority bond issues for which repayment is limited to specific sources of revenue, and for which bondholders do not have recourse to the City's General Fund in the event those revenues are insufficient to pay debt service on the bonds.

The Series 1994A and Series 1994B are reassessment revenue bonds issued by the Authority to consolidate and refund six series of improvement district bonds. The refunding was accomplished by first creating a consolidated reassessment district and issuing the City of San José Limited Obligation Refunding Bonds, Series 24M. The proceeds of the Authority's Series 1994A and 1994B Bonds were then used to purchase the Series 24M Bonds. Repayment of the Authority reassessment revenue bonds is limited to special assessments levied on property-owners in Consolidated Reassessment District No. 94-214SJ. These bonds were called on September 2, 2005 and are no longer outstanding.

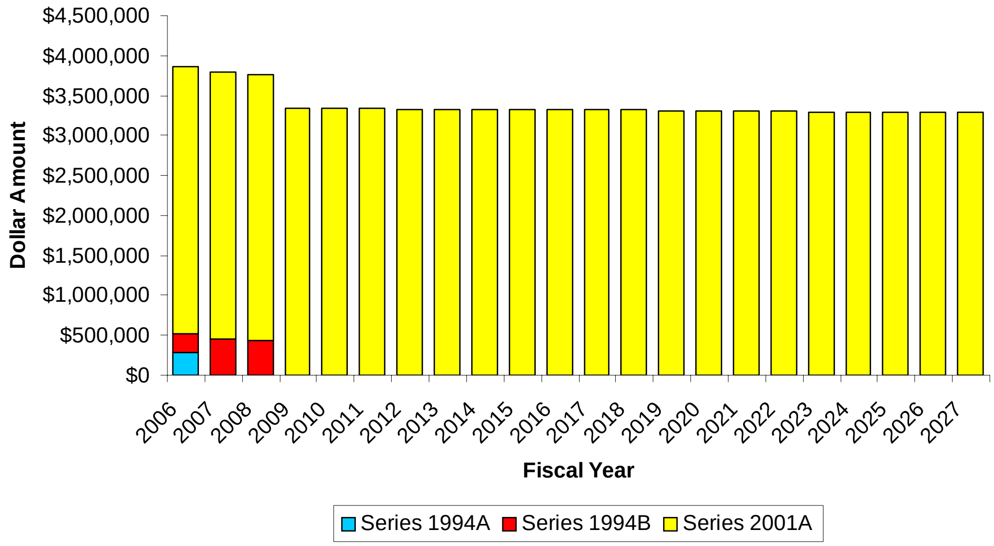
The Series 2001A are revenue bonds issued by the Authority to finance construction of the City parking garage located on the corner of North 4th Street and East San Fernando Street (the "4th & San Fernando Parking Garage"). Repayment of these revenue bonds is limited to gross revenues of the City's parking system and surplus revenues of the Redevelopment Agency.

**Self-Supporting Debt/ No General Fund Recourse**

*Outstanding Debt as of June 30, 2005: $46,440,000*



**Self-Supporting Debt/ No General Fund Recourse**
*Annual Debt Service*



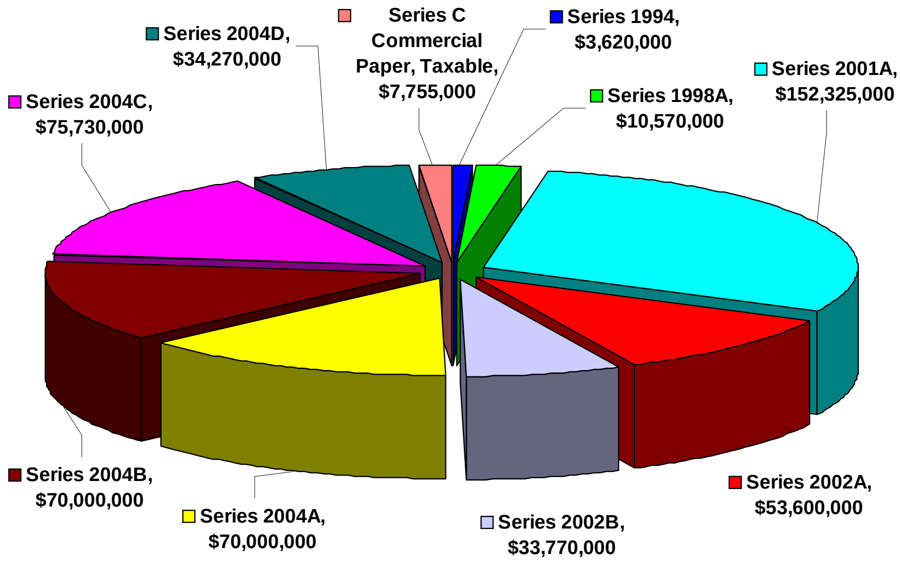

## C. Enterprise Fund Obligations

### 1. Airport

The following pie chart illustrates the total amount of outstanding Airport debt, secured by Airport revenues, broken out by issue series and type. The Airport Revenue Bonds, Series 2004A-D, were issued to finance a portion of the construction of the North Concourse and other related security improvements. As of June 30, 2005, the total amount of Airport obligations outstanding was $511,640,000, consisting of senior debt of $503,885,000 and $7,755,000 in outstanding Commercial Paper. The Airport's commercial paper is subordinate to the revenue bonds.

**Airport Obligations**

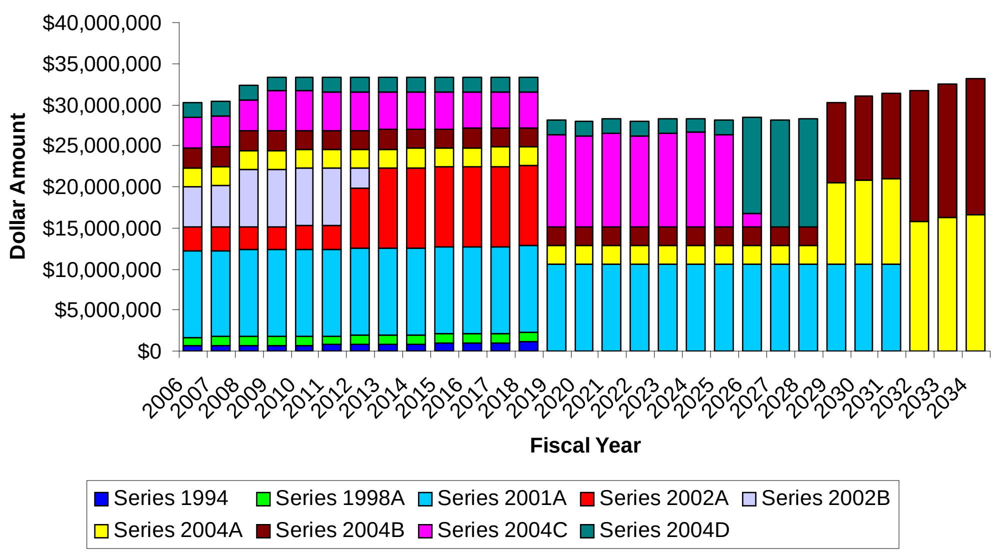
*Outstanding Debt as of June 30, 2005: $511,640,000*




The following bar graph illustrates the annual debt service requirements by airport revenue bond issue. The commercial paper is not included in the bar graph since the interest due on the notes is "rolled" and funded from the issuance of additional commercial paper notes. The outstanding commercial paper is anticipated to be repaid from bond proceeds from the future sale of long-term debt. Appendix C provides the annual commercial paper debt service certification, which gives an estimate of the annual debt service payment that would result from refunding the outstanding commercial paper with sale proceeds of long-term bonds.

**Airport Revenue Bonds**

*Annual Debt Service*

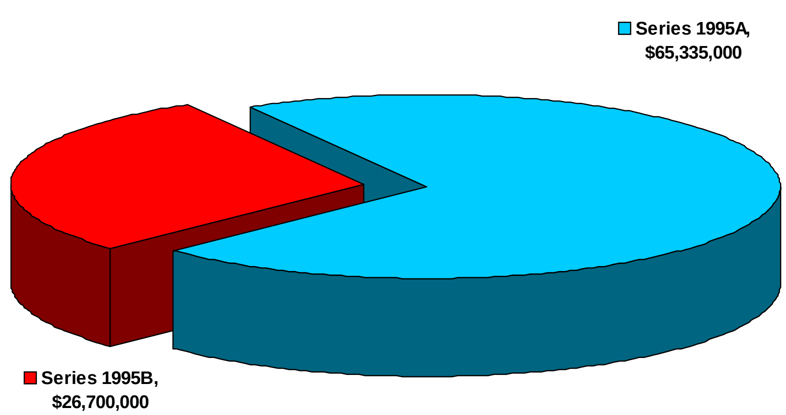


## 2. Clean Water Financing Authority

The pie chart below illustrates the total amount of outstanding sewer revenue bonds issued by the San José-Santa Clara Clean Water Financing Authority as of June 30, 2005. As noted previously, the San José-Santa Clara Clean Water Revenue Bonds Series 1995A and 1995B were refunded on October 5, 2005. The Clean Water Financing Authority is the obligor for repayment of this debt. The Improvement Agreement, by and among the San José-Santa Clara Clean Water Financing Authority, the City of San José and the City of Santa Clara, provides the terms and conditions under which the Cities of San José and Santa Clara agree to make payments to the Authority for debt service on the bonds. With respect to the Series 1995A and 1995B Bonds and the bonds which refunded them, Santa Clara has no repayment obligation under the Improvement Agreement. Santa Clara cash-funded its share of the South Bay Water Recycling Project for which the 1995B Bonds were issued.

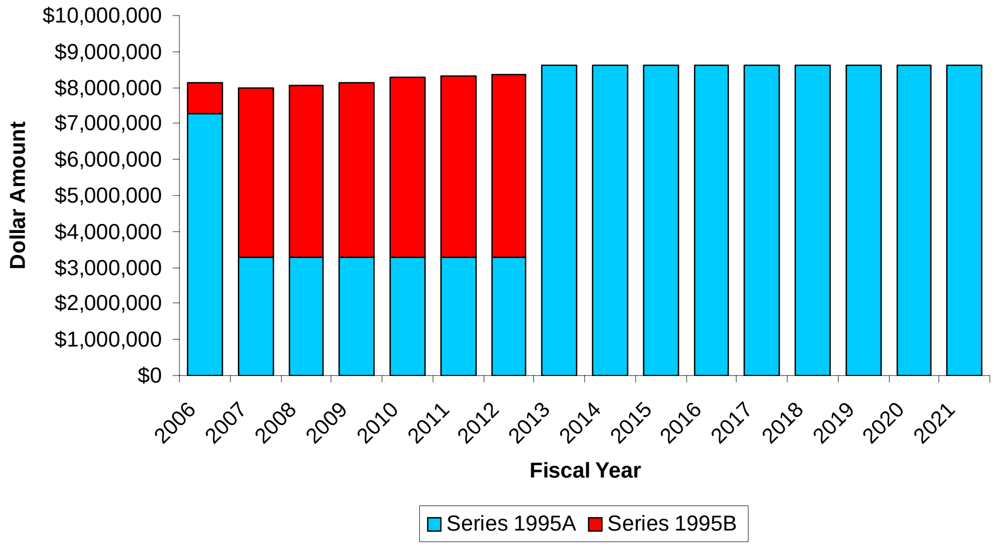
The City of San José and the City of Santa Clara have agreements with each of the tributary agencies for those agencies' share of capital costs and ongoing operation expenses of the waste water treatment system. These revenue streams along with other revenue sources generated from the waste water treatment system are applied toward the payment obligation the cities of San José and Santa Clara have to the Authority. The tributary agencies include the City of Milpitas, West Valley Sanitation District, Cupertino Sanitation District, Burbank Sanitary District, Sunol Sanitary District and County Sanitation District 2-3.

**Clean Water Financing Authority Sewer Revenue Bonds**
*Outstanding Debt as of June 30, 2005: $92,035,000*




The bar graph below illustrates the annual debt service requirements by each Clean Water Financing Authority issue.

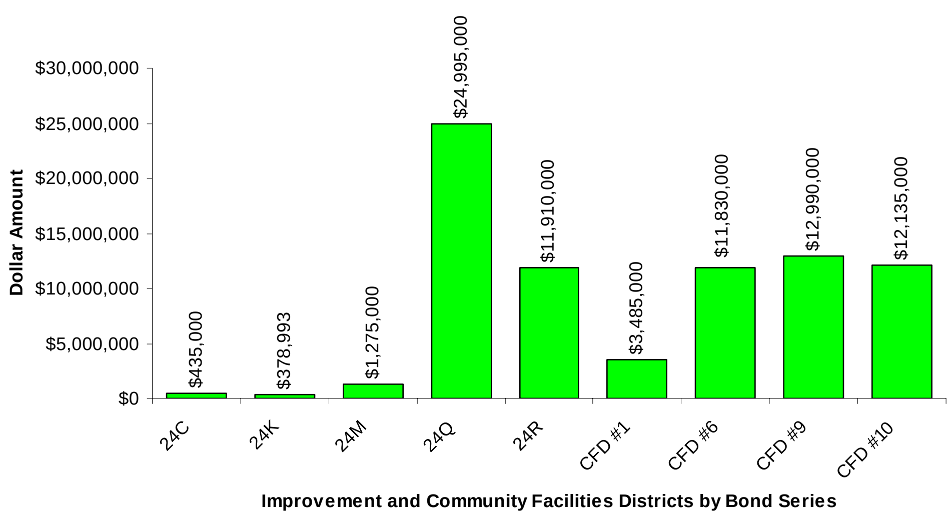
**Clean Water Financing Authority Sewer Revenue Bonds**
*Annual Debt Service*




## D. Land-Secured Financing

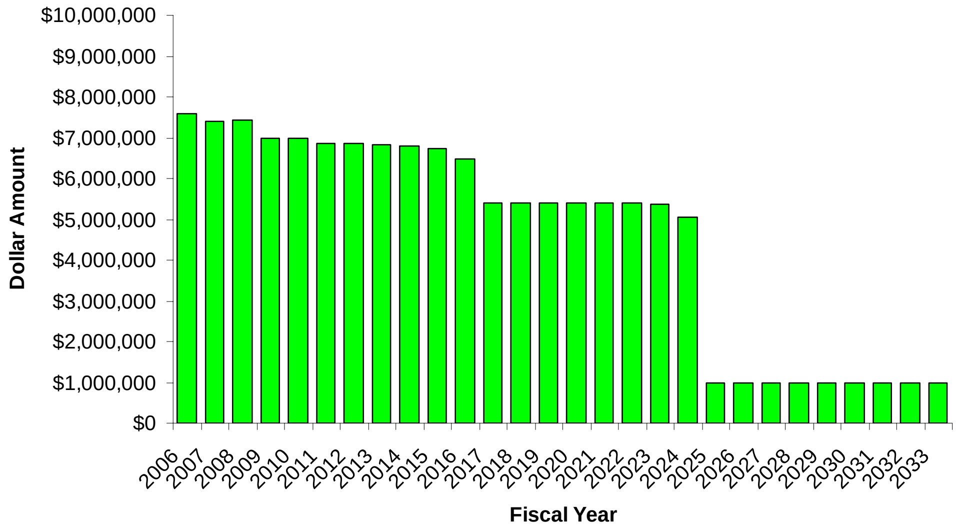
The following bar chart illustrates the total amount of land-secured debt outstanding backed by special assessments and special taxes. As of June 30, 2005, the City had four community facilities district and five improvement district bond issues outstanding. The largest issue was Series 24Q, the Hellyer-Piercy Improvement District. This bond issue represented 31% of all land-secured outstanding debt.

**Land-Secured Bonds**
*Outstanding Debt as of June 30, 2005: $79,433,993*



The bar graph below illustrates the total annual debt service requirements for all of the improvement district and community facilities district debt outstanding.

**Land-Secured Bonds**
*Annual Debt Service*




## E. Multifamily Housing Revenue Bonds

Multifamily housing revenue bonds are issued to finance the development (which includes new construction as well as acquisition and rehabilitation) by private developers of certain rental apartment projects. The City issues the bonds and then loans the proceeds to the developer/borrower. The bonds are typically issued as tax-exempt securities. The Bonds are limited obligations of the City, payable solely from loan repayments by the Borrower and any credit enhancement. For multifamily housing revenue bonds to qualify for tax-exemption, generally one of two restrictions must apply: either (1) at least 20 percent of the units in the housing development must be reserved for occupancy by individuals and families of very-low income (50% of area median income) or (2) at least 40 percent of the units must be reserved for occupancy by individuals and families of low income (60% of area median income).

The City remains an active issuer of conduit multifamily housing revenue bonds, although the frequency of issuance has slowed recently due to a variety of factors, including the softening of the real estate market and diminished resources available to subsidize affordable housing. The table presented on page 50 summarizes the City's portfolio of multifamily revenue bonds.

Since November 1985, the City has issued $631,277,000 of bonds for the City's multifamily housing program, which has financed 5,172 affordable housing units. As of June 30, 2005, the total principal amount of bonds outstanding for the housing program was $571,080,725. It is important to note that in addition to conduit financing through multifamily housing revenue bonds, there are other vehicles available to the City for assisting with financing of affordable housing units, including loans, grants and 9% tax-credits. The information presented in this report only represents affordable housing projects that were financed, in whole or in part, with bonds issued by the City.

## Multifamily Housing Revenue Bonds
*As of June 30, 2005*

| Project Name | Date Issued | Bonds Issued | Bonds Outstanding | Affordable Units |
|---|---|---|---|---|
| Fairway Glen | 11/18/1985 | $ 10,100,000 | $ 9,580,000 | 29 |
| Foxchase Drive | 11/18/1985 | 11,700,000 | 9,600,000 | 29 |
| Somerset Park Apartments | 11/20/1987 | 8,000,000 | 7,800,000 | 26 |
| Timberwood Apartments (2 series) | 02/01/1990 | 14,925,000 | 11,605,000 | 166 |
| Countrybrook Apartments | 04/15/1992 | 21,090,000 | 16,965,000 | 72 |
| Siena at Renaissance Square (Reissued in 2001) | 08/22/1996 | 60,000,000 | 60,000,000 | 271 |
| Almaden Lake Village Apts. (Reissued in 2000) | 03/27/1997 | 27,000,000 | 27,000,000 | 142 |
| *Subtotal for Fiscal Years 1985-1997* | | $152,815,000 | $142,550,000 | 735 |
| Carlton Plaza | 04/24/1998 | $ 14,600,000 | 12,000,000 | 26 |
| Coleman Senior Apartments | 04/24/1998 | 8,050,000 | 7,787,528 | 140 |
| Italian Gardens Senior Apartments | 04/24/1998 | 8,000,000 | 7,737,767 | 139 |
| *Subtotal for Fiscal Year 1997-1998* | | $ 30,650,000 | $ 27,525,295 | 305 |
| The Gardens Apartments Project (2 series) | 05/12/1999 | $ 21,900,000 | $ 21,000,000 | 286 |
| Helzer Court Apartments (3 series) | 06/02/1999 | 23,169,000 | 19,798,000 | 154 |
| Ohlone-Chynoweth Commons Apartments | 06/04/1999 | 16,200,000 | 13,665,000 | 192 |
| *Subtotal for Fiscal Year 1998-1999* | | $ 61,269,000 | $ 54,463,000 | 632 |
| Kimberly Woods Apartments | 12/20/1999 | $ 16,050,000 | 16,050,000 | 42 |
| *Subtotal for Fiscal Year 1999-2000* | | $ 16,050,000 | $ 16,050,000 | 42 |
| Sixth and Martha Family Apartments Phase I | 07/21/2000 | $ 9,900,000 | $ 9,655,000 | 102 |
| Craig Gardens Senior Housing | 12/05/2000 | 7,100,000 | 4,741,775 | 89 |
| El Parador Senior Housing (3 series) | 12/07/2000 | 11,530,000 | 6,850,000 | 124 |
| Monte Vista Gardens Senior Housing Phase I | 12/08/2000 | 3,740,000 | 3,308,933 | 68 |
| Willow Glen Senior Housing (2 series) | 12/08/2000 | 11,020,000 | 0 | 132 |
| *Subtotal for Fiscal Year 2000-2001* | | $ 43,290,000 | $ 24,555,708 | 515 |
| Immanuel Lutheran Senior Housing | 07/11/2001 | $ 5,000,000 | $ 3,850,000 | 62 |
| Sixth and Martha Family Apartments Phase II | 08/01/2001 | 9,000,000 | 8,160,000 | 87 |
| Villages Parkway Senior Apartments | 08/01/2001 | 6,800,000 | 5,660,000 | 78 |
| Lenzen Affordable Housing Project (2 series) | 08/22/2001 | 9,495,000 | 8,280,000 | 87 |
| North White Road Family Apartments | 11/15/2001 | 16,845,000 | 16,759,271 | 156 |
| Villa de Guadalupe Apartments (2 series) | 11/27/2001 | 7,600,000 | 7,409,451 | 100 |
| Almaden Senior Apartments | 12/05/2001 | 6,050,000 | 3,205,000 | 65 |
| Betty Anne Gardens | 04/05/2002 | 11,000,000 | 7,510,000 | 75 |
| El Paseo Studios | 04/05/2002 | 9,600,000 | 5,145,000 | 97 |
| Sunset Square Apartments | 06/26/2002 | 10,904,000 | 6,494,000 | 94 |
| Villa Monterey | 06/27/2002 | 11,000,000 | 11,000,000 | 119 |
| *Subtotal for Fiscal Year 2001-2002* | | $103,294,000 | $ 83,472,722 | 1,020 |
| Monte Vista Gardens Senior Housing Phase II | 07/24/2002 | $ 3,665,000 | $ 3,465,000 | 48 |
| Pollard Plaza Apartments | 08/06/2002 | 14,000,000 | 14,000,000 | 129 |
| Evans Lane Apartments | 10/08/2002 | 31,000,000 | 31,000,000 | 236 |
| Hacienda Villa Apartments | 10/10/2002 | 7,000,000 | 6,975,000 | 79 |
| Kennedy Apartments | 12/11/2002 | 14,000,000 | 14,000,000 | 99 |
| Fallen Leaves Apartments | 12/18/2002 | 18,800,000 | 18,800,000 | 159 |
| Turnleaf Apartments | 06/26/2003 | 15,290,000 | 15,290,000 | 151 |
| *Subtotal for Fiscal Year 2002-03* | | $103,755,000 | $103,530,000 | 901 |

*(continued on next page)*

| Multifamily Housing Revenue Bonds<br>*As of June 30, 2005 (continued)* | | | | |
|---|---|---|---|---|
| **Project Name** | **Date Issued** | **Bonds Issued** | **Bonds Outstanding** | **Affordable Units** |
| The Oaks of Almaden Apartments | 07/28/2003 | $ 8,350,000 | $ 8,350,000 | 126 |
| Cinnabar Commons Apartments | 08/07/2003 | 25,900,000 | 25,900,000 | 245 |
| Almaden Family Apartments | 11/14/2003 | 31,300,000 | 31,300,000 | 225 |
| Trestles Apartments (2 series) | 03/04/2004 | 7,405,000 | 7,405,000 | 71 |
| Aspen Vintage Tower Apartments | 06/28/2004 | 5,500,000 | 5,500,000 | 59 |
| *Subtotal for Fiscal Year 2003-04* | | $78,455,000 | $78,455,000 | 726 |
| Delmas Apartments (2 series) | 10/15/2004 | $19,379,000 | $19,379,000 | 122 |
| Raintree Apartments | 02/01/2005 | 21,100,000 | 21,100,000 | 174 |
| *Subtotal for Fiscal Year 2004-05* | | $40,479,000 | $40,479,000 | 296 |
| **Grand Total** | | **$631,277,000** | **$571,080,725** | **5,172** |

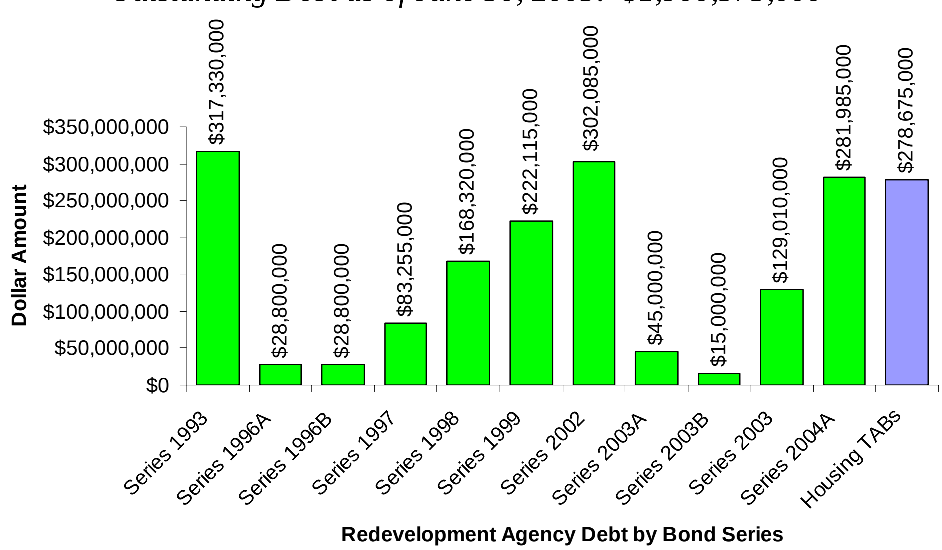
## F. Redevelopment Agency

***Please note that the City has no obligation or connection in any way to debt issued by the Redevelopment Agency*.**

The following bar chart illustrates the total amount of direct redevelopment agency tax increment debt outstanding. This includes both the debt issued for the 80% program, shown in green, and the 20% housing program, shown in blue.

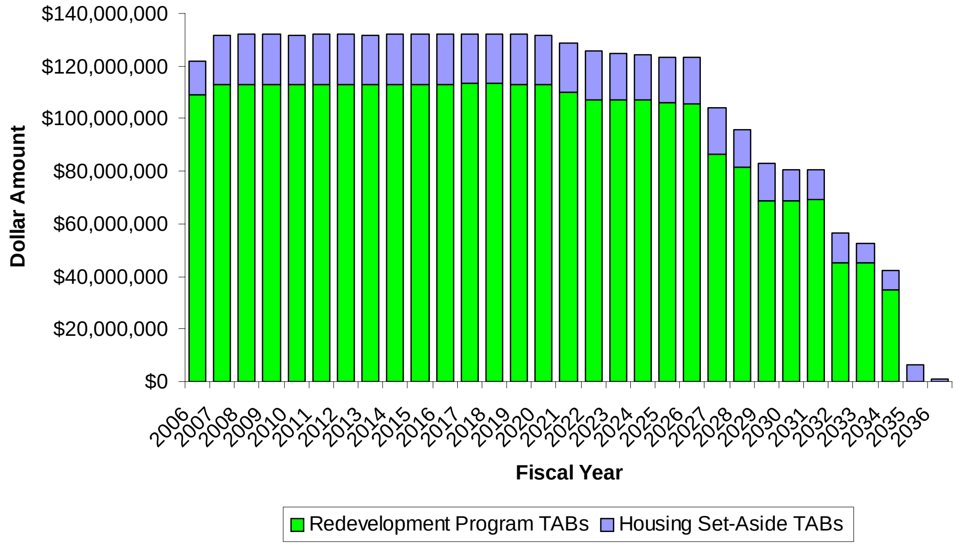
**Redevelopment Agency Tax Increment Debt**

*Outstanding Debt as of June 30, 2005: $1,900,375,000*



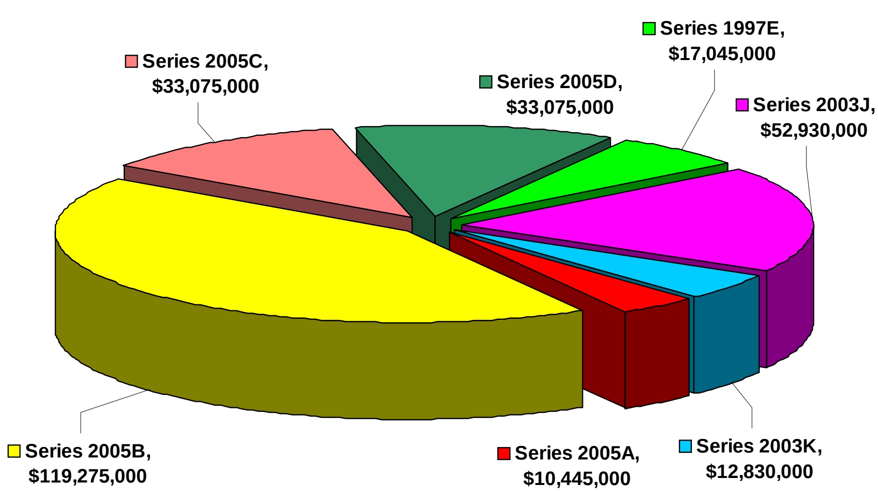
The following bar graph illustrates the total annual debt service requirements for all of the Agency debt outstanding, except for the Housing Department Line of Credit which will be redeemed with proceeds of future housing set-aside tax allocation bonds.

**Redevelopment Agency Tax Increment Debt**
*Annual Debt Service*




The pie chart below provides a more detailed view of the Agency's outstanding housing set-aside tax allocation bonds. The $50 million line of credit with Bank of New York was repaid on June 30, 2005, from proceeds of the Series 2005 Bonds.

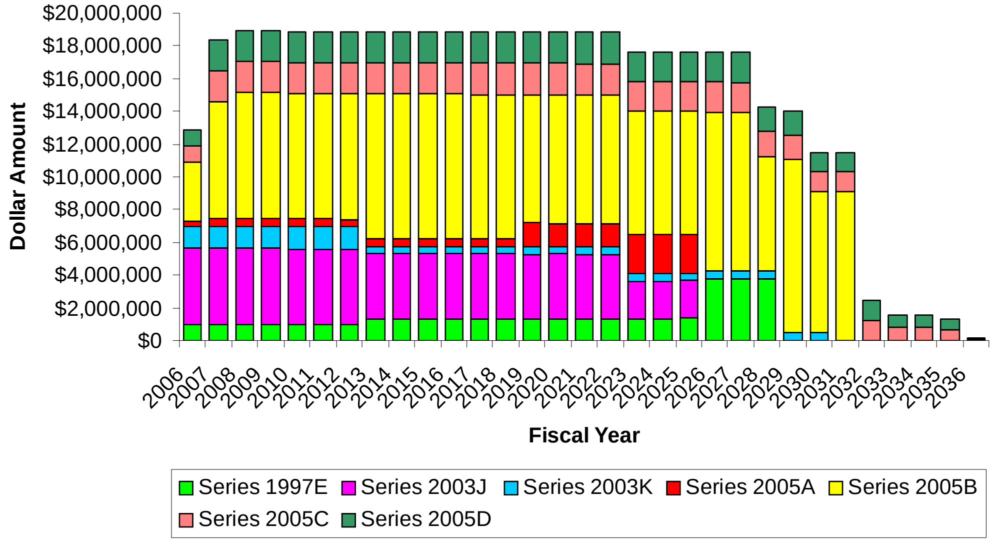
**Agency Housing Set-Aside Tax Allocation Bonds**
*Outstanding Debt as of June 30, 2005: $278,675,000*



The bar graph below illustrates the annual debt service requirements for the Agency's housing set-aside tax allocation bond issues, except for the Housing Department Line of Credit, which will be redeemed with proceeds of future housing set-aside tax allocation bonds.

**Agency Housing Set-Aside Tax Allocation Bonds**

*Annual Debt Service*



# APPENDIX A:  DEBT MANAGEMENT POLICY

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

# *CITY OF SAN JOSE, CALIFORNIA*

# CITY COUNCIL POLICY

| TITLE | PAGE | POLICY NUMBER |
|---|---|---|
| **DEBT MANAGEMENT POLICY** | **1 OF 5** | **1-15** |
| | **EFFECTIVE DATE** | **REVISED DATE** |
| | **5/21/02** | |

**APPROVED BY COUNCIL ACTION**

**May 21, 2002, Item 3.3, Resolution No. 70977**

## POLICY

This Debt Management Policy sets forth certain debt management objectives for the City, and establishes overall parameters for issuing and administering the City's debt. Recognizing that cost-effective access to the capital markets depends on prudent management of the City's debt program, the City Council has adopted this Debt Management Policy by resolution.

## DEBT MANAGEMENT OBJECTIVES

The purpose of this Debt Management Policy is to assist the City in pursuit of the following equally-important objectives:

- Minimize debt service and issuance costs;
- Maintain access to cost-effective borrowing;
- Achieve the highest practical credit rating;
- Full and timely repayment of debt;
- Maintain full and complete financial disclosure and reporting;
- Ensure compliance with applicable State and Federal laws.

## GENERAL PROVISIONS

### I. SCOPE OF APPLICATION

These policies establish the parameters within which debt may be issued by the City of San José, the City of San José Financing Authority, and the City of San José Parking Authority. Additionally, these policies apply to debt issued by the City on behalf of assessment, community facilities, or other special districts, and conduit-type financing by the City for multifamily housing or industrial development projects.

The City Council, as a member of Joint Powers Authorities such as the San José-Santa Clara Clean Water Financing Authority, shall take these policies into account when considering the issuance of Joint Powers Authority debt.

Supplemental policies, tailored to the specifics of certain types of financings, may be adopted by the City Council in the future. These supplemental policies may address, but are not limited to, the City's general obligation, lease revenue, enterprise, multifamily housing, and land-secured financings.

## II. RESPONSIBILITY FOR DEBT MANAGEMENT ACTIVITIES

The Finance Department shall be responsible for managing and coordinating all activities related to the issuance and administration of debt. The Director of Finance is appointed by the City Manager and is subject to his or her direction and supervision. In accordance with the City Charter, Article VIII, Section 806, the Director of Finance is charged with responsibility for the conduct of all Finance Department functions.

Departments implementing debt-financed capital programs will work in partnership with the Finance Department to provide information and otherwise facilitate the issuance and administration of debt.

### A. Debt Management Policy Review and Approval

This policy shall be adopted by City Council resolution, and reviewed annually by the Finance Department to insure its consistency with respect to the City's debt management objectives. Any modifications to this policy shall be reviewed and approved by the Finance and Infrastructure Committee and forwarded to the City Council for approval by resolution.

### B. Annual Debt Report

The Finance Department shall prepare an annual debt report for review and approval by the Finance and Infrastructure Committee and the City Council, containing a summary of the City's credit ratings, outstanding and newly-issued debt, a discussion of current and anticipated debt projects, refunding opportunities, a review of legislative, regulatory, and market issues, and an outline of any new or proposed changes to this Debt Management Policy.

### C. Debt Administration Activities

The Finance Department is responsible for the City's debt administration activities, particularly investment of bond proceeds, compliance with bond covenants, continuing disclosure, and arbitrage compliance, which shall be centralized within the Department.

## III. PURPOSES FOR WHICH DEBT MAY BE ISSUED

### A. Long-term Borrowing

Long-term borrowing may be used to finance the acquisition or improvement of land, facilities, or equipment for which it is appropriate to spread these costs over more than one budget year. Long-term borrowing may also be used to fund capitalized interest, costs of issuance, required reserves, and any other financing-related costs which may be legally capitalized. Long-term borrowing shall not be used to fund City operating costs.

**B. Short-term Borrowing**

Short-term borrowing, such as commercial paper and lines of credit, will be considered as an interim source of funding in anticipation of long-term borrowing. Short-term debt may be issued for any purpose for which long-term debt may be issued, including capitalized interest and other financing-related costs. Additionally, short-term borrowing may be considered if available cash is insufficient to meet short-term operating needs.

**C. Refunding**

Periodic reviews of outstanding debt will be undertaken to identify refunding opportunities. Refunding will be considered (within federal tax law constraints) if and when there is a net economic benefit of the refunding. Refundings which are non-economic may be undertaken to achieve City objectives relating to changes in covenants, call provisions, operational flexibility, tax status, issuer, or the debt service profile.

In general, refundings which produce a net present value savings of at least three percent (3%) of the refunded debt will be considered economically viable. Refundings which produce a net present value savings of less than three percent (3%) will be considered on a case-by-case basis. Refundings with negative savings will not be considered unless there is a compelling public policy objective that is accomplished by retiring the debt.

## DEBT ISSUANCE

### I. DEBT CAPACITY

The City will keep outstanding debt within the limits of the City's Charter and any other applicable law, and at levels consistent with its creditworthiness objectives.

The City shall assess the impact of new debt issuance on the long-term affordability of all outstanding and planned debt issuance. Such analysis recognizes that the City has limited capacity for debt service in its budget, and that each newly issued financing will obligate the City to a series of payments until the bonds are repaid.

### II. CREDIT QUALITY

The City seeks to obtain and maintain the highest possible credit ratings for all categories of short- and long-term debt. The City will not issue bonds directly or on behalf of others that do not carry investment grade ratings. However, the City will consider the issuance of non-rated special assessment, community facilities, multifamily housing, and special facility bonds.[1]

[1] In most cases, a bond which cannot achieve an investment-grade rating will not be rated at all, because there is little value from a bond-marketing perspective in a below investment-grade rating.

## III. STRUCTURAL FEATURES

### A. Debt Repayment

Debt will be structured for a period consistent with a fair allocation of costs to current and future beneficiaries of the financed capital project. The City shall structure its debt issues so that the maturity of the debt issue is consistent with the economic or useful life of the capital project to be financed.

### B. Variable-rate Debt

The City may choose to issue securities that pay a rate of interest that varies according to a pre-determined formula or results from a periodic remarketing of the securities. Such issuance must be consistent with applicable law and covenants of pre-existing bonds, and in an aggregate amount consistent with the City's creditworthiness objectives.

### C. Derivatives

Derivative products[2] may have application to certain City borrowing programs. In certain circumstances these products can reduce borrowing cost and assist in managing interest rate risk. However, these products carry with them certain risks not faced in standard debt instruments. The Director of Finance shall evaluate the use of derivative products on a case-by-case basis to determine whether the potential benefits are sufficient to offset any potential costs.

## IV. PROFESSIONAL ASSISTANCE

The City shall utilize the services of independent financial advisors and bond counsel on all debt financings. The Director of Finance shall have the authority to periodically select service providers as necessary to meet legal requirements and minimize net City debt costs. Such services, depending on the type of financing, may include financial advisory, underwriting, trustee, verification agent, escrow agent, arbitrage consulting, and special tax consulting. The City Attorney's Office shall be responsible for selection of bond counsel and, in those circumstances where the City Attorney's Office determines it to be necessary or desirable, disclosure counsel. The goal in selecting service providers, whether through a competitive process or sole-source selection, is to achieve an appropriate balance between service and cost.

## V. METHOD OF SALE

Except to the extent a competitive process is required by law, the Director of Finance shall be responsible for determining the appropriate manner in which to offer any securities to investors. The City's preferred method of sale is competitive bid. However, other methods such as negotiated sale and private placement may be considered on a case-by-case basis.

[2] A derivative product is a financial instrument which "derives" its own value from the value of another instrument, usually an underlying asset such as a stock, bond, or an underlying reference such as an interest rate index.

## DEBT ADMINISTRATION

### I. INVESTMENT OF BOND PROCEEDS

Investments of bond proceeds shall be consistent with federal tax requirements, the City's Investment Policy as modified from time to time, and with requirements contained in the governing bond documents.

### II. DISCLOSURE PRACTICES AND ARBITRAGE COMPLIANCE

#### A. Financial Disclosure

The City is committed to full and complete primary and secondary market financial disclosure in accordance with disclosure requirements established by the Securities and Exchange Commission and Municipal Securities Rulemaking Board, as may be amended from time to time. The City is also committed to cooperating fully with rating agencies, institutional and individual investors, other levels of government, and the general public to share clear, timely, and accurate financial information.

#### B. Arbitrage Compliance

The Department of Finance shall maintain a system of record keeping and reporting to meet the arbitrage compliance requirements of federal tax law.

## **APPENDIX B: POLICY FOR THE ISSUANCE OF MULTIFAMILY HOUSING REVENUE BONDS**

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

# *CITY OF SAN JOSE, CALIFORNIA*

# CITY COUNCIL POLICY

| Title | Page | Policy Number |
|---|---|---|
| **POLICY FOR THE ISSUANCE OF MULTIFAMILY HOUSING REVENUE BONDS** | **1 of 11** | **1-16** |
| | **Effective Date** 06/11/02 | **Revised Date** |

**APPROVED BY COUNCIL ACTION**

**June 11, 2002, Item 3.07, Resolution No. 71023**

**<u>GENERAL MATTERS</u>**

## I. ISSUER

The City of San Jose (the "City") shall be the issuer of all bonds financing multifamily housing rental projects (a "Project" or "Projects") within the City, except as provided below. The City's Housing Department and Finance Department will consider other issuing agencies as follows:

### A. The Redevelopment Agency

The Redevelopment Agency may issue bonds for any Project located within a redevelopment project area.

### B. ABAG, CSCDA, Other Conduits

The City may agree to the issuance of bonds by the Association of Bay Area Governments ("ABAG"), California Statewide Community Development Authority ("CSCDA") or a similar issuing conduit provided that the City is not making a loan or grant to the Project *and* the Project is one of multiple projects being financed by the Project Sponsor through such issuing conduit agency in the same California Debt Limit Allocation Committee ("CDLAC") round under a similar financing program so as to result in economies of issuance.

### C. Special circumstances

Another agency may issue bonds when merited by special circumstances of the Project and the financing.

Where the City is not the issuer of bonds for a Project, it shall be the City's policy to require the issuer to assume full responsibility for issuance and on-going compliance of the bond issue with federal tax and state laws. Where feasible, however, the City shall seek to hold The Equity and Fiscal Responsibility Act of 1986 Hearing, better known as the "TEFRA" Hearing for such Project.

## II. FINANCING TEAM

The City shall select the financing team for all multifamily housing revenue bonds issued by the City. The Finance Department is responsible for selecting the financial advisor, trustee and the investment banker/underwriter (assuming a negotiated public sale of bonds). The City Attorney's Office is responsible for selecting the bond counsel firm. The financial advisor, investment banker and bond counsel shall be selected from approved lists determined from time to time by a request for qualifications/proposal process.

## III. COORDINATION AMONG CITY DEPARTMENTS

The City recognizes that the issuance of housing bonds entails a coordinated effort among the Housing Department, Finance Department and City Attorney's Office. The Housing Department shall ensure that the Finance Department and the City Attorney's Office are provided with regular updates on projects that may involve the issuance of bonds.

## THE FINANCING PROCESS

## I. INITIAL MEETING WITH PROJECT SPONSOR

### A. Prior Due Diligence

Prior to arranging an initial meeting with the Project Sponsor, the Housing Department shall perform initial due diligence on the Project Sponsor, including whether the Project Sponsor has ever failed to use an allocation from CDLAC and whether the Project Sponsor has failed to comply with the terms of any other City financings or City loans.

### B. Determination of Readiness

Following the initial meeting, City representatives shall determine if the project is in a state of sufficient "readiness" to proceed with the CDLAC application process. This includes the status of the project in terms of the development process. In general, a project will be deemed "not ready" if the discretionary planning approvals will not have been completed by the time of the CDLAC application.

### C. Selection of Financing Team

Following a determination of readiness, the Finance Department and City Attorney shall recommend the financial advisor, underwriter (if applicable) and bond counsel, as the case may be, for each project.

## II. DEPARTMENTAL APPROVALS

Pursuant to the Delegation of Authority by the City Council, both the City's Directors of Finance and Housing must approve each Project, the financing, and the filing of a CDLAC application before the City can make an application to CDLAC for private activity bond allocation. The approval of the Finance and Housing Directors shall be evidenced by a jointly signed "Notice to Proceed" addressed to the Project Sponsor. The Notice to Proceed shall describe the project, identify the developer or Project Sponsor, the affordability mix, the proposed plan of finance and the amount of bond funding requested.

### A. Resolution

The City Attorney's Office will be responsible for preparing a resolution for joint approval by the Directors of Finance and Housing. The resolution will:

1. Memorialize the Council's intent to issue the debt in order to induce others to provide project financing;
2. Authorize the filing of a CDLAC application; and
3. Authorize the execution of a Deposit and Escrow Agreement.

### B. TEFRA Hearing

The TEFRA hearing will be held before the Director of Finance on the date specified in the TEFRA Notice. The Director of Finance has the discretion to have the TEFRA hearing held by the City Council.

## III. CDLAC APPLICATIONS

### A. Description

Before the City is legally able to issue private activity tax-exempt bonds for a project, an application must be filed with CDLAC in Sacramento and an allocation of the State ceiling on qualified private activity bonds must be approved by CDLAC.

### B. City to File

The City is the applicant to CDLAC for each project to be financed with tax-exempt bonds issued by the City. The Housing Department will file all applications to CDLAC on behalf of project sponsors.

### C. Project Sponsor to Prepare Application

Each project sponsor shall take responsibility for preparing the CDLAC application for its project with input from City representatives, the City's financial advisor and bond counsel.

### D. Deposit and Escrow Agreement

The City will not file a Project Sponsor's CDLAC application unless the Project Sponsor executes a Deposit and Escrow Agreement **and makes the necessary deposits specified in this Agreement**. The Deposit and Escrow Agreement shall contain the items identified below. It shall be the responsibility of the Housing Department to see that all requirements under the Deposit and Escrow Agreement are met.

#### *1. CDLAC Performance Deposit*

The Deposit and Escrow Agreement must require the payment of the CDLAC performance deposit, provided that current CDLAC rules require the payment of such deposit to the issuer.

### *2. City of San Jose Performance Deposit*

In addition to the CDLAC performance deposit, the Deposit and Escrow Agreement shall require the Project Sponsor to deposit $50,000 with the City as a City of San Jose performance deposit. This deposit shall be forfeited in the event that the City, on behalf of the Project Sponsor, receives an allocation but does not issue bonds. The deposit may be applied to pay costs of issuance or returned to the Project Sponsor as soon as practicable. By agreement between the City and the Project Sponsor, the Project Sponsor may designate its City loan as the source of payment in the event of forfeiture.

### *3. Financing Team Fees*

The Deposit and Escrow Agreement shall identify, if available, the fees of the bond counsel, financial advisor, and underwriter (if applicable). It shall be the responsibility of the Finance Department and the City Attorney's Office to identify these fees.

## IV. COUNCIL APPROVAL

### A. Staff Report

The Finance Department, in conjunction with the Housing Department and City Attorney's Office, shall prepare a staff report recommending final Council approval for a bond issue. The staff report shall be submitted to the City Manager's Office in accordance with the timing requirements of the then-current City procedures.

The staff report shall specify the approvals that are recommended, provide background on the project being financed, describe the financing structure, indicate any exceptions to the City's investment policy, describe the financing documents to be approved, identify the financing team participants, and seek approval of consultant agreements and financing participants that have not previously been approved by Council. The staff report should indicate if a separate City loan is being provided. However, the terms of that loan should be discussed in a separate staff report which, whenever possible, shall be submitted for the same agenda. The staff report shall be signed by the Directors of Finance and Housing.

The staff report should be submitted only after the major transaction terms (e.g., financing structure, security provisions, bond amount, maximum maturity, etc.) are identified and agreed to by the parties. The staff report may note that the bond issue is contingent upon certain other approvals and may identify certain issues to be resolved at a later time.

### B. Substantially Final Documents

The City Council shall approve documents that are "substantially final" documents. Documents are in "substantially final" form if they identify the final security provisions and financing structure for the transaction. The City Attorney's Office shall determine whether documentation is in substantially final form.

### C. Council Meeting

The Council meeting shall occur on a date after which all approvals from major financial participants (e.g., credit enhancement provider, bond purchaser, tax credit investor) have been obtained. At the discretion of the City Attorney and Finance Department, the Council may proceed with its approval process without such other final approvals if: (1) such final approval is likely; (2) the Council's approval is subject to such other party's final approval; and (3) the Council approval process cannot be delayed without jeopardizing the financing.

## V. BOND SALE AND CLOSING

### A. Timing

The bond sale and closing may commence only after the Council authorizes the bond issue, including the distribution of a Preliminary Official Statement, if applicable.

### B. Investment Agreements

If authorized by the Council, the Project Sponsor, through its representative, which may include the underwriter or financial advisor, may solicit investment agreement providers for the purpose of reinvesting bond proceeds and revenues. The investment agreement providers must meet the City's requirements and the requirements in the bond resolution and trust indenture for the bonds. Bond counsel and the financial advisor shall review the investment agreement solicitation forms, the eligible providers, and the investment agreements.

### C. Payment of Issuance Fee

The City's issuance fee shall be funded from the Costs of Issuance Fund held by the Trustee.

### D. Information Memorandum to Council

Promptly after the issuance of all bonds for a CDLAC round, the City Finance Department shall prepare an information memorandum summarizing the salient points of each bond issue.

# CITY FEES

## I. ISSUANCE FEE

The City shall charge a fee for the administrative costs associated with issuing the bonds for a Project Sponsor. The fee shall be payable at bond closing and may be contingent on the bond sale. The issuance fee shall be based on the total amount of the bonds (both tax-exempt and taxable) to be issued in accordance with the following sliding scale:

***$0 to $10 million***: 0.5% of the principal amount of bonds issued, with a minimum fee of $30,000.

***Over $10 million***: 0.5% of the first $10 million principal amount of bonds; 0.25% of any additional amount.

## II. ANNUAL MONITORING FEE

The City shall charge an annual fee for monitoring the restricted units. The fee shall be in an amount equal to 0.125% of the original principal amount of tax-exempt bonds issued. The fee shall not be reduced until all of the tax-exempt bonds are retired and the bond regulatory agreement ceases to have validity or is no longer in effect, at which time it will terminate.

The City annual monitoring fee shall be paid “above the line,” i.e., on a parity with bond debt service and trustee fees. This parity provides the greatest assurance that the City’s fee will be paid, although it may reduce the amount that the Project Sponsor’s lender may be willing to underwrite. The City may determine, at its sole discretion, to subordinate all or a portion of its annual fee to bond debt service only when the Housing Department has made a substantial loan to the Project, so long as the Project Sponsor provides adequate assurance of the payment of such fees. The City shall not subordinate its fee in circumstances where no City funds are subsidizing the Project.

## CREDIT CONSIDERATIONS

### I. CREDIT ENHANCEMENT

#### A. General Policy

It shall be the general policy of the City to encourage the use of credit enhancement for bonds issued by the City. Credit enhancement shall be a requirement for any multifamily bonds that are publicly distributed. The minimum rating on such credit enhancement shall be “A” or higher by Moody’s, Standard & Poor’s, and/or Fitch. This policy shall be subject to the exceptions described below.

#### B. Forms of Credit Enhancement

Credit enhancement may be in the form of a bank letter of credit, bond insurance, surety, financial guaranty, mortgage-backed security (e.g., Fannie Mae, Freddie Mac or Ginnie Mae) or other type of credit enhancement approved by the market. If the City has not previously issued bonds with a particular kind of credit enhancement, the Finance Department and financial advisor shall determine whether such credit enhancement is acceptable and whether marketing restrictions shall be imposed.

#### C. Project Sponsor Responsibility

It shall be the responsibility of the Project Sponsor to obtain and pay for the costs of credit enhancement. The City will assume no responsibility therefor.

### II. NON-CREDIT ENHANCED BONDS

#### A. General Policy

It shall be the general policy of the City to require bonds that are not secured with credit enhancement to be sold through private placement or through a limited public offering to institutional or accredited investors. As an exception to this policy, the City may authorize the public distribution of non-credit enhanced bonds that are rated at least in the “A” category by Moody’s, Standard & Poor’s, and/or Fitch, after consultation with the underwriter and financial advisor. In connection with such authorization, the City shall consider the sophistication of the Project Sponsor, its financial resources, commitment to the community and other factors.

### B. Additional Requirements for Non-Rated Bonds

Non-rated bonds must comply with the following additional requirements:

#### 1. Minimum Denominations and Number of Bondholders

In order to limit the transferability of non-rated bonds, the City shall seek minimum denominations of at least $100,000. In addition, the City may also limit the number of bondholders to further limit the transferability of non-rated bonds.

#### 2. Qualified Institutional Buyer ("QIB") Letter

The bond purchaser in a private placement or limited public offering must certify that it is a qualified or accredited investor (a "big boy letter"). Such letter must be signed by subsequent bond purchasers so long as the bonds remain unrated.

## REFUNDING/RESTRUCTURING/REMARKETING

### I. GENERAL

The City has issued both fixed rate and variable rate multifamily bonds. On occasion, the Project Sponsor may ask the City to refund those bonds to lower the interest rate, to remarket the bonds with a new credit enhancement, and/or to remarket the bonds as fixed rate bonds. The Project Sponsor will be responsible for all costs and fees related to the refunding.

### II. OPTIONAL REFUNDING

#### A. Reasons to Refund Outstanding Bonds

A Project Sponsor may ask the City to refund its outstanding bonds for one of several reasons:

1. Lower the interest rate on fixed rate bonds at the call date (through the issuance of fixed rate or variable rate refunding bonds);
2. Substitute a new credit structure that was not expressly provided for in the existing documents; or
3. Restructure the existing debt.

#### B. Financing Team

The City shall select the financing team to implement the refunding. Where possible and if desired by the City, the financing team shall consist of the bond counsel, financial advisor and, if applicable, underwriter that were retained for the original financing.

#### C. Legal/Documentation

New documents shall be prepared to meet the City's then-current legal, credit, financial, and procedural requirements. The City shall follow the documentation process applicable to new bonds. Because the City's primary purpose in issuing multifamily housing bonds is to preserve and increase the supply of affordable housing in the City, if federal or state affordability, income, and/or rent restrictions have changed between the time of the original financing and the refunding bonds, the more restrictive provisions shall apply. If new requirements are more restrictive than existing requirements, the new requirements shall be applied in phases to new tenants over a period of time, not to exceed five (5) years, as determined by the Housing Department staff and the City Attorney.

## D. Bond Maturity

Subject to the approval of bond counsel, the final maturity of the refunding bonds may be later than the final maturity of the prior bonds so as to allow the Project Sponsor the longest possible period for repayment under federal law.

## E. Compliance

The City shall not proceed with a refunding if the Project is not in compliance with the current regulatory agreement, continuing disclosure reporting, or arbitrage rebate reporting and payment.

## F. Fees

The Project Sponsor shall pay the following City fees in connection with the refunding:

### 1. Issuance Fee

The City shall charge an issuance fee in accordance with the City's current policy on issuance fees for new projects.

### 2. Annual Monitoring Fee

The City shall continue to charge the same annual fee for monitoring the Project as for the original bonds. Such fee shall not be reduced even if the refunding bond size is lower.

## G. Cash Flow Savings

Cash flow savings from refunding fixed rate bonds at a lower fixed interest rate or a variable rate shall be applied as follows:

### 1. Projects with a City Loan

A portion of the projected cash flow savings, to be determined by the Housing Department, shall be used to accelerate the repayment of the City loan, subject to restrictions in existing documents.

### 2. Projects with No City Loan

The City Housing Department shall require the Project Sponsor to provide affordability or other financial concessions to the City as a condition for refunding. Such concessions may include increasing the percentage of affordable units and extending the term of affordability restrictions.

### H. City Council Approval

All refunding bonds and related legal documentation must be approved by the City Council in accordance with the procedures set for the issuance of new bonds.

## III. DEFAULT REFUNDING

### A. General

In the event of a default on the bonds or the underlying mortgage, a fixed rate bond issue may be refundable in advance of the call date without premium. The issue does not arise with variable rate bonds, as such bonds are callable at any time. Default refunding bonds are an area of potential sensitivity for the City as it will not want a developer to manufacture a default to take advantage of more favorable interest rates.

### B. Financing Team

The City shall select the financing team to implement the refunding. Where possible and if desired by the City, the financing team shall consist of the bond counsel, financial advisor and, if applicable, underwriter that were retained for the original financing.

### C. Confirming the Default

To confirm a default, the City must receive a notice from an independent party, such as the bond trustee. If applicable, notice of cash flow insufficiency is then filed as part of the Continuing Disclosure Certificate. In addition, the City shall retain, at the expense of the Project Sponsor, an independent feasibility consultant to review the default. The City will proceed with the transaction only if a review by staff and the independent consultant indicates that:

1. Net cash flow from the Project is currently insufficient to pay debt service on the outstanding bonds and is unlikely to do so within a reasonable period;

2. The Project is being operated in accordance with reasonable real estate management practices and the net operating income has not been artificially reduced by failing to rent units actively, inflating operating expenses, or other reasons within the control of the Project Sponsor; and

3. The Project Sponsor has provided audited operating statements, Continuing Disclosure filings (if applicable), and arbitrage rebate reports for all years, has cooperated in providing requested information, and has used operating income and other resources to pay debt service.

### D. Additional Requirements

#### 1. Indemnification

The City shall be indemnified as to any costs incurred as a result of the refunding. Such indemnification shall come from a party or parties with adequate net worth or other financial capacity and whose assets are not limited to ownership of the Project.

**2. Future Debt Coverage**

The analysis of the feasibility consultant shall show that, upon the refunding, the Project's current net operating income will be at least sufficient to pay the revised debt service plus a reasonable coverage ratio (or adequate non-bond proceeds will be available to cover such deficiencies). In other words, ***the City shall not proceed with the refunding if it will not cure the cash flow problem*.**

**3. Bond Counsel Review**

Bond counsel shall have determined that the original bond and disclosure documents provided adequate disclosure of such a potential redemption and that the provisions of the prior documents have been satisfied.

**4. Compliance**

The City shall not proceed with a refunding if the Project is not in compliance with the current regulatory agreement, continuing disclosure reporting, or arbitrage rebate reporting and payment.

**E. Fees**

The fees and expenses of the feasibility consultant, financial advisor and bond counsel shall **not** be contingent on their findings or completion of a refunding. The City shall require that the Project Sponsor deposit the estimated fees and expenses with the City **prior** to the commencement of any analysis.

**F. Affordability Restrictions**

The affordability requirements for a default refunding shall be the same as those listed under "Legal/Documentation" for an optional refunding.

**G. City Council Approval**

**1. Initial City Council Approval**

The Finance Department, in conjunction with the Housing Department and City Attorney's Office, shall obtain initial City Council approval prior to proceeding with any documentation for a default refunding. Initial City Council approval shall occur after the independent feasibility consultant performs the initial analysis, a default is confirmed, and it is determined that a refunding will cure the cash flow problem.

**2. Final City Council Approval**

The Finance Department, in conjunction with the Housing Department and City Attorney's Office, shall obtain final City Council authorizing the bond issue and execution of the relevant documentation.

**H. City Fees**

The City shall charge the same issuance fee and annual monitoring fee that it otherwise would in conjunction with a new bond issue.

## IV. REMARKETING

### A. General

A Project Sponsor may ask the City to remarket outstanding bonds under one of three basic scenarios: (1) converting variable rate bonds to fixed rate bonds; (2) a mandatory tender of bonds; or (3) substituting a new credit enhancement for the bonds in accordance with existing documentation.

### B. Financing Team

The City shall select the financing team to implement the refunding. Where possible and if desired by the City, the financing team shall consist of the bond counsel, financial advisor and, if applicable, underwriter that were retained for the original financing.

### C. Legal/Documentation

A remarketing of fixed rate bonds will not require new legal documentation. However, the City Attorney's Office, in conjunction with bond counsel, may require a new disclosure document. A remarketing of bonds with a new credit enhancement may require amended documentation, as well as a new disclosure document, as determined by the City Attorney's Office and bond counsel.

### D. Fees

A remarketing will not result in the payment of additional or revised City issuance or annual fees. However, the City shall charge a fee of $10,000 to $25,000 to the Project Sponsor for administrative costs.

### E. Council Approval

All remarketed bonds and any related documentation shall be approved by the City Council prior to any remarketing.

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

## APPENDIX C:  CURRENT RATINGS SUMMARY

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

## Current Ratings Summary
*as of October 7, 2005*

| | Moody's | S&P | Fitch |
|---|---|---|---|
| **City of San José** | | | |
| General Obligation Bonds, Series 2001 | Aa1 | AA+ | AA+ |
| General Obligation Bonds, Series 2002 | | | |
| Maturities Insured by MBIA (2032) | Aaa | AAA | AAA |
| Uninsured Maturities | Aa1 | AA+ | AA+ |
| General Obligation Bonds, Series 2004 | | | |
| Maturities Insured by MBIA | Aaa | AAA | AAA |
| Uninsured Maturities (2006, 2018-2025) | Aa1 | AA+ | AA+ |
| General Obligation Bonds, Series 2005 | | | |
| Maturities Insured by MBIA (2031, 2035) | Aaa | AAA | AAA |
| Uninsured Maturities | Aa1 | AA+ | AA+ |
| **City of San José Financing Authority** | | | |
| Lease Revenue Bonds, Series 1993B | A1 | AA | -- |
| Lease Revenue Bonds, Series 1997A | | | |
| All Maturities Insured by Ambac | Aaa | AAA | AAA |
| Underlying Rating | (A1) | -- | (AA) |
| Lease Revenue Bonds, Series 1997B | | | |
| All Maturities Insured by Ambac | -- | AAA | AAA |
| Underlying Rating | (A1) | -- | (AA) |
| Lease Revenue Bonds, Series 2000B | | | |
| All Maturities Insured by Ambac | Aaa | AAA | AAA |
| Underlying Rating | (A1) | -- | -- |
| Lease Revenue Bonds, Series 2000C[1] | | | |
| MBIA Insured/JPMorgan Chase Liquidity | Aaa/VMIG-1 | AAA/A-1+ | AAA |
| Revenue Bonds, Series 2001A | | | |
| All Maturities Insured by Ambac | Aaa | AAA | AAA |
| Underlying Rating | (A2) | -- | (A-) |
| Lease Revenue Bonds, Series 2001B[1] | | | |
| Ambac Insured/ScotiaBank Liquidity | Aaa/VMIG-1 | AAA/A-1+ | AAA |
| Lease Revenue Bonds, Series 2001C[1] | | | |
| Ambac Insured/ScotiaBank Liquidity | Aaa/VMIG-1 | AAA/A-1+ | AAA |
| Lease Revenue Bonds, Series 2001D[1] | | | |
| Ambac Insured/ScotiaBank Liquidity | Aaa/VMIG-1 | AAA/A-1+ | AAA |
| Lease Revenue Bonds, Series 2001E | Aa3 | AA | AA |
| Lease Revenue Bonds, Series 2001F | | | |
| Maturities Insured by MBIA (2006-2020) | Aaa | AAA | AAA |
| Uninsured Maturities | Aa3 | AA | AA |
| Lease Revenue Bonds, Series 2002B | | | |
| Maturities Insured by Ambac (2008-2037) | Aaa | AAA | AAA |
| Uninsured Maturities | Con. Aa3 | AA | AA |
| Lease Revenue Bonds, Series 2002C | | | |
| All Maturities Insured by Ambac | Aaa | AAA | AAA |
| Underlying Rating | Con. (Aa3) | -- | (AA) |
| Lease Revenue Bonds, Series 2002D | | | |
| All Maturities Insured by Ambac | Aaa | AAA | AAA |
| Underlying Rating | Con. (Aa3) | -- | (AA) |
| Lease Revenue Bonds, Series 2003A | | | |
| All Maturities Insured by Ambac | Aaa | AAA | AAA |
| Underlying Rating | (Aa3) | (AA) | (AA) |

[1] Variable rate bonds.

## Current Ratings Summary (continued)

*as of October 7, 2005*

| | Moody's | S&P | Fitch |
|---|---|---|---|
| **City of San José Financing Authority (continued)** | | | |
| Lease Revenue Commercial Paper Notes | | | |
| State Street Bank/CalSTRS Letter of Credit | P-1 | A-1+ | F1+ |
| Lease Revenue Bonds, Series 2004A[1] | | | |
| All Maturities Insured by MBIA | Aaa | AAA | -- |
| Lease Revenue Bonds, Series 2005A[1] | | | |
| XL Capital Insured/Bank of America Liquidity | Aaa/VMIG-1 | AAA/A-1+ | AAA/F1+ |
| Underlying Rating | (Aa3) | (AA) | (AA) |
| Lease Revenue Bonds, Series 2005B[1] | | | |
| XL Capital Insured/Bank of America Liquidity | Aaa/VMIG-1 | AAA/A-1+ | AAA/F1+ |
| Underlying Rating | (Aa3) | (AA) | (AA) |
| **Redevelopment Agency of the City of San José** | | | |
| *Housing Set-Aside Tax Allocation Bonds* | | | |
| Series 1997E | | | |
| All Maturities Insured by MBIA | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | -- |
| Series 2003J | | | |
| All Maturities Insured by XL Capital | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A) |
| Series 2003K | | | |
| All Maturities Insured by XL Capital | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A) |
| Series 2005A | | | |
| All Maturities Insured by FGIC | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A) |
| Series 2005B | | | |
| All Maturities Insured by FGIC | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A) |
| Series 2005C[1] | | | |
| Bank of New York Direct-Pay Letter of Credit | Aa2/VMIG-1 | AA-/A-1+ | -- |
| Underlying Rating | (A2) | (A) | -- |
| Series 2005D[1] | | | |
| Bank of New York Direct-Pay Letter of Credit | Aa2/VMIG-1 | AA-/A-1+ | -- |
| Underlying Rating | (A2) | (A) | -- |
| *Redevelopment Project Tax Allocation Bonds* | | | |
| Series 1993 | | | |
| Maturities Insured by MBIA (2006-2020, 2024) | Aaa | AAA | AAA |
| Uninsured Maturities/Underlying Rating | (A3) | (A-) | (A) |
| Series 1997 | | | |
| All Maturities Insured by MBIA | Aaa | AAA | AAA |
| Underlying Rating | (A3) | (A-) | (A) |
| Series 1998 | | | |
| Maturities Insured by Ambac (2005-2026) | Aaa | AAA | AAA |
| Uninsured Maturities/Underlying Rating | (A3) | (A-) | (A) |
| Series 1999 | | | |
| All Maturities Insured by Ambac | Aaa | AAA | AAA |
| Underlying Rating | (A3) | (A-) | (A) |

[1] Variable rate bonds.

## Current Ratings Summary (continued)

*as of October 7, 2005*

| | Moody's | S&P | Fitch |
|---|---|---|---|
| **Redevelopment Agency of the City of San José (continued)** | | | |
| *Redevelopment Project Tax Allocation Bonds (continued)* | | | |
| Series 2002 | | | |
| All Maturities Insured by MBIA | Aaa | AAA | AAA |
| Underlying Rating | (A3) | (A-) | (A) |
| Series 2003 | | | |
| All Maturities Insured by FGIC | Aaa | AAA | AAA |
| Underlying Rating | (A3) | (A-) | (A) |
| Series 2004A | | | |
| Maturities Insured by MBIA (2006-2019) | Aaa | AAA | AAA |
| Underlying Rating | (A3) | (A-) | (A) |
| Series 2005A | | | |
| All Maturities Insured by MBIA | Aaa | AAA | AAA |
| Underlying Rating | (A3) | (A-) | (A) |
| Series 2005B | | | |
| All Maturities Insured by Ambac | Aaa | AAA | AAA |
| Underlying Rating | (A3) | (A-) | (A) |
| *Redevelopment Project Revenue Bonds (Subordinate)* | | | |
| Series 1996A[1] | | | |
| JP Morgan Chase Credit Facility | -- | AA-/A-1+ | -- |
| Series 1996B[1] | | | |
| JP Morgan Chase Credit Facility | -- | AA-/A-1+ | -- |
| Series 2003A[1] | | | |
| JP Morgan Chase Credit Facility | -- | AA-/A-1+ | -- |
| Series 2003B[1] | | | |
| JP Morgan Chase Credit Facility | -- | AA-/A-1+ | -- |
| **Norman Y. Mineta San José International Airport** | | | |
| Revenue Refunding Bonds, Series 1994 | | | |
| All Maturities Insured by FGIC | Aaa | AAA | AAA |
| Underlying Rating | -- | (A) | (A+) |
| Revenue Refunding Bonds, Series 1998A | | | |
| All Maturities Insured by FGIC | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A+) |
| Subordinated Commercial Paper Notes, Series A | | | |
| JPMorgan Chase Letter of Credit | P-1 | A-1+ | F1 |
| Subordinated Commercial Paper Notes, Series B | | | |
| JPMorgan Chase Letter of Credit | P-1 | A-1+ | F1 |
| Subordinated Commercial Paper Notes, Series C | | | |
| JPMorgan Chase Letter of Credit | P-1 | A-1+ | F1 |
| Revenue Bonds, Series 2001A | | | |
| All Maturities Insured by FGIC | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A+) |
| Revenue Bonds, Series 2002A | | | |
| All Maturities Insured by FSA | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A+) |
| Revenue Bonds, Series 2002B | | | |
| All Maturities Insured by FSA | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A+) |

[1] Variable rate bonds.

## Current Ratings Summary (continued)

*as of October 7, 2005*

| | Moody's | S&P | Fitch |
|---|---|---|---|
| **Norman Y. Mineta San José International Airport (continued)** | | | |
| Revenue Bonds, Series 2004A[1] | | | |
| All Maturities Insured by MBIA | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A+) |
| Revenue Bonds, Series 2004B[1] | | | |
| All Maturities Insured by MBIA | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A+) |
| Revenue Bonds, Series 2004C | | | |
| All Maturities Insured by MBIA | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A+) |
| Revenue Bonds, Series 2004D | | | |
| All Maturities Insured by MBIA | Aaa | AAA | AAA |
| Underlying Rating | (A2) | (A) | (A+) |
| **San José-Santa Clara Clean Water Financing Authority** | | | |
| Revenue Bonds, Series 2005A | | | |
| All Maturities Insured by FSA | Aaa | AAA | AAA |
| Underlying Rating | (Aa3) | (AA) | (AA) |
| Revenue Bonds, Series 2005B[1] | | | |
| FSA Insured/DEPFA Bank Liquidity | Aaa/VMIG-1 | AAA/A-1+ | AAA/F1+ |
| Underlying Rating | (Aa3) | (AA) | (AA) |
| **City of San José Reassessment District No. 02-219SJ** | | | |
| Limited Obligation Refunding Bonds, Series 24R | | | |
| All Maturities Insured by MBIA | Aaa | AAA | AAA |

[1] Variable rate bonds.

**<u>APPENDIX D: SUMMARY OF OUTSTANDING DEBT</u>**

## Summary of Outstanding Debt as of June 30, 2005

*(dollars in thousands)*

| | Issue Amount | Issue Date | Final Maturity | Balance 06/30/05 |
|---|---|---|---|---|
| **City of San José** | | | | |
| General Obligation Bonds | | | | |
| Series 2001 (Libraries and Parks Project) | 71,000 | 06/06/2001 | 09/01/2031 | 63,890 |
| Series 2002 (Libraries, Parks and Public Safety Projects) | 116,090 | 07/18/2002 | 09/01/2032 | 108,350 |
| Series 2004 (Libraries, Parks and Public Safety Projects) | 118,700 | 07/14/2004 | 09/01/2034 | 118,700 |
| Series 2005 (Libraries and Public Safety Projects) | 46,300 | 06/23/2005 | 09/01/2035 | 46,300 |
| General Obligation Bond Subtotal | | | | 337,240 |
| Special Assessment Bonds | | | | |
| Series 24C (Evergreen Creek) | 1,080 | 09/07/1988 | 09/02/2009 | 435 |
| Series 24K (Taxable) (Seismic Retrofit) | 823 | 07/29/1993 | 09/02/2013 | 379 |
| Series 24M (Consolidated Refunding) | 22,240 | 06/01/1994 | 09/02/2007 | 1,275 |
| Series 24Q (Hellyer-Piercy) | 27,595 | 06/26/2001 | 09/02/2023 | 24,995 |
| Series 24R (2002 Consolidated Refunding) | 13,940 | 07/03/2002 | 09/02/2015 | 11,910 |
| Special Tax Bonds | | | | |
| CFD No. 1 (Capitol Expressway Auto Mall) | 4,100 | 11/18/1997 | 11/01/2022 | 3,485 |
| CFD No. 6 (Great Oaks-Route 85) | 12,200 | 12/18/2001 | 09/01/2003 | 11,830 |
| CFD No. 9 (Bailey/Highway 101) | 13,560 | 02/13/2003 | 09/01/2032 | 12,990 |
| CFD No. 10 (Hassler-Silver Creek) | 12,500 | 07/23/2003 | 09/01/2023 | 12,135 |
| Special Assessment and Special Tax Bond Subtotal | | | | 79,434 |
| **City of San José Financing Authority** | | | | |
| Lease Revenue Bonds | | | | |
| Series 1993B (Community Facilities) | 18,045 | 03/01/1993 | 11/15/2018 | 11,011 |
| Series 1997A (Golf Course Project) | 6,875 | 07/01/1997 | 08/15/2027 | 6,260 |
| Series 1997B (Fire Apparatus, Childcare, Library) | 9,805 | 07/01/1997 | 08/01/2012 | 4,330 |
| Series 2000B (Tuers-Capitol/Camden) | 22,635 | 08/08/2000 | 08/15/2030 | 22,100 |
| Series 2000C (Taxable) (Ice Centre of San José) | 22,200 | 12/13/2000 | 12/01/2021 | 21,450 |
| Series 2001B (Taxable) (Hayes Mansion Phase III) | 24,000 | 02/14/2001 | 07/01/2024 | 24,000 |
| Series 2001C (Taxable) (Hayes Mansion Phase III) | 18,500 | 02/14/2001 | 07/01/2024 | 18,500 |
| Series 2001D (Hayes Mansion Phase III) | 10,800 | 02/14/2001 | 07/01/2026 | 10,800 |
| Series 2001E (Communication Center) | 18,610 | 03/01/2001 | 05/10/2010 | 11,935 |
| Series 2001F (Convention Center Refunding) | 186,150 | 07/01/2001 | 09/01/2022 | 176,850 |
| Series 2002B (Civic Center Project) | 292,425 | 11/14/2002 | 06/01/2037 | 292,425 |
| Series 2002C (Civic Center Project) | 60,000 | 11/14/2002 | 06/01/2039 | 60,000 |
| Series 2002D (Civic Center Project) | 60,000 | 11/14/2002 | 06/01/2039 | 60,000 |
| Series 2003A (Central Service Yard Refunding) | 22,625 | 09/18/2003 | 10/15/2023 | 21,880 |
| Series 2004A (Taxable) (Ice Centre Expansion Project) | 9,225 | 06/03/2004 | 12/01/2024 | 9,225 |
| Series 2005A (Taxable) (Land Acquisition) | 54,480 | 02/17/2005 | 03/01/2029 | 54,480 |
| Series 2005B (AMT) (Land Acquisition) | 25,545 | 02/17/2005 | 03/01/2034 | 25,545 |
| Parking Revenue Bonds | | | | |
| Series 2001A (4th & San Fernando Parking Facility) | 48,675 | 04/10/2001 | 09/01/2026 | 45,145 |
| Reassessment Revenue Bonds | | | | |
| Series 1994A | 16,680 | 06/23/1994 | 09/02/2005 | 280 |
| Series 1994B (Subordinate) | 8,035 | 06/23/1994 | 09/02/2007 | 1,015 |
| City of San José Financing Authority Subtotal | | | | 877,231 |

## Summary of Outstanding Debt as of June 30, 2004 (continued)

*(dollars in thousands)*

| | Issue Amount | Issue Date | Final Maturity | Balance 06/30/05 |
|---|---|---|---|---|
| **Redevelopment Agency:** | | | | |
| Merged Area Tax Allocation Bonds | | | | |
| Series 1993 (Merged Area Refunding) | 692,075 | 12/01/1993 | 02/01/2024 | 317,330 |
| Series 1997 (Merged Area) | 106,000 | 03/27/1997 | 08/01/2028 | 83,255 |
| Series 1998 (Merged Area) | 175,000 | 03/19/1998 | 08/01/2029 | 168,320 |
| Series 1999 (Merged Area) | 240,000 | 01/06/1999 | 08/01/2031 | 222,115 |
| Series 2002 (Merged Area) | 350,000 | 01/24/2002 | 08/01/2032 | 302,085 |
| Series 2003 (Merged Area) | 135,000 | 12/22/2003 | 08/01/2033 | 129,010 |
| Series 2004A (Merged Area Refunding) | 281,985 | 05/27/2004 | 08/01/2019 | 281,985 |
| Merged Area Tax Allocation Bonds Subtotal | | | | 1,504,100 |
| Merged Area Revenue Bonds (Subordinate) | | | | |
| Series 1996A (Merged Area) | 29,500 | 06/27/1996 | 07/01/2026 | 28,800 |
| Series 1996B (Merged Area) | 29,500 | 06/27/1996 | 07/01/2026 | 28,800 |
| Series 2003A (Taxable) (Merged Area) | 45,000 | 08/27/2003 | 08/01/2028 | 45,000 |
| Series 2003B (Merged Area) | 15,000 | 08/27/2003 | 08/01/2032 | 15,000 |
| Merged Area Revenue Bonds Subtotal | | | | 117,600 |
| Housing Set-Aside Tax Allocation Bonds | | | | |
| Series 1997E (AMT) (Merged Area) | 17,045 | 06/23/1997 | 08/01/2027 | 17,045 |
| Series 2003J (Taxable) (Merged Area) | 55,265 | 07/10/2003 | 08/01/2024 | 52,930 |
| Series 2003K (Merged Area) | 13,735 | 07/10/2003 | 08/01/2029 | 12,830 |
| Series 2005A (Merged Area) | 10,445 | 06/30/2005 | 08/012024 | 10,445 |
| Series 2005B (Taxable) (Merged Area) | 119,275 | 06/30/2005 | 08/01/2035 | 119,275 |
| Series 2005C (AMT) (Merged Area) | 33,075 | 06/30/2005 | 08/01/2035 | 33,075 |
| Series 2005D (AMT) (Merged Area) | 33,075 | 06/30/2005 | 08/01/2035 | 33,075 |
| Housing Set-Aside Tax Allocation Bonds Subtotal | | | | 278,675 |
| **Clean Water Financing Authority:** | | | | |
| Sewer Revenue Bonds | | | | |
| Series 1995A | 68,820 | 11/30/1995 | 11/15/2020 | 65,335 |
| Series 1995B | 26,700 | 11/30/1995 | 11/15/2011 | 26,700 |
| Sewer Revenue Bonds Subtotal | | | | 92,035 |
| **Norman Y. Mineta San José International Airport:** | | | | |
| Airport Revenue Bonds | | | | |
| Series 1994 | 19,345 | 01/25/1994 | 03/01/2007 | 3,620 |
| Series 1998A | 14,015 | 01/27/1998 | 03/01/2018 | 10,570 |
| Series 2001A | 158,455 | 08/14/2001 | 03/01/2031 | 152,325 |
| Series 2002A | 53,600 | 01/09/2003 | 03/01/2018 | 53,600 |
| Series 2002B (AMT) | 37,945 | 01/09/2003 | 03/01/2012 | 33,770 |
| Series 2004A (AMT) | 70,000 | 06/24/2004 | 06/01/2034 | 70,000 |
| Series 2004B (AMT) | 70,000 | 06/24/2004 | 06/01/2034 | 70,000 |
| Series 2004C (AMT) | 75,730 | 06/24/2004 | 03/01/2026 | 75,730 |
| Series 2004D | 34,270 | 06/24/2004 | 03/01/2028 | 34,270 |
| Airport Revenue Bonds Subtotal | | | | 503,885 |
| **Grand Total:** | | | | 3,790,200 |

# APPENDIX E:  OVERLAPPING DEBT REPORT

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

## City of San José Statement of Overlapping Debt
### *as of June 30, 2005*

| DIRECT AND OVERLAPPING TAX AND ASSESSMENT DEBT: | % Applicable | Debt on 6/30/05 |
|---|---|---|
| Santa Clara County Flood Control and Water Conservation District, Zone W-1 | 46.991 % | $ 1,766,862 |
| Foothill Community College District | 4.600 | 8,524,955 |
| Gavilan Joint Community College District | 7.933 | 2,379,900 |
| San José Community College District | 86.232 | 148,704,650 |
| Milpitas Unified School District | 0.0003 | 178 |
| Morgan Hill Unified School District | 21.007 | 14,925,002 |
| San José Unified School District | 97.745 | 295,106,388 |
| Santa Clara Unified School District | 4.225 | 5,069,578 |
| Campbell Union High School District | 59.488 | 55,880,053 |
| East Side Union High School District | 94.569 | 357,673,649 |
| Fremont Union High School District | 9.807 | 14,063,238 |
| Los Gatos Joint Union High School District | 0.717 | 524,557 |
| Alum Rock Union School District | 74.007 | 33,529,277 |
| Berryessa Union School District | 93.919 | 45,872,886 |
| Burbank School District | 17.658 | 294,006 |
| Cambrian School District | 67.235 | 13,934,416 |
| Campbell Union School District | 44.760 | 38, 562,220 |
| Cupertino Union School District | 16.364 | 20,655,468 |
| Evergreen School District | 99.472 | 84,496,193 |
| Evergreen School District Community Facilities District No. 92-1 | 100.000 | 5,805,000 |
| Franklin-McKinley School District | 98.074 | 56,890,108 |
| Los Gatos Union School District | 1.633 | 939,792 |
| Moreland School District | 75.466 | 55,217,915 |
| Mount Pleasant School District | 86.967 | 9,453,313 |
| Oak Grove School District | 99.786 | 71,993,163 |
| Orchard School District | 100.000 | 30,343,457 |
| Union School District | 72.263 | 53,526,119 |
| **City of San José** | **100.000** | **290,940,000** |
| City of San José Community Facilities Districts | 100.000 | 40,440,000 |
| San José Special Assessment Bonds | 100.000 | 38,993,993 |
| Santa Clara Valley Water District Benefit Assessment District | 39.20 | 74,910,314 |
| TOTAL GROSS DIRECT AND OVERLAPPING TAX AND ASSESSMENT DEBT | | $1,871,416,650 |

| DIRECT AND OVERLAPPING GENERAL FUND OBLIGATION: | % Applicable | Debt on 6/30/05 |
|---|---|---|
| Santa Clara County General Fund Obligations | 39.290 % | $316,374,867 |
| Santa Clara County Board of Education Certificates of Participation | 39.290 | 7,066,307 |
| Community College District Certificates of Participation | Various | 7,111,292 |
| San José Unified School District Certificates of Participation | 97.745 | 103,061,713 |
| Santa Clara Unified School District Certificates of Participation | 4.225 | 320,044 |
| Los Gatos-Saratoga Joint Union High School District Certificates of Participation | 0.717 | 31,154 |
| Alum Rock Union School District Certificates of Participation | 74.007 | 1,065,701 |
| Cupertino Union School District Certificates of Participation | 16.364 | 902,475 |
| Franklin-McKinley School District Certificates of Participation | 98.074 | 12,749,620 |
| Moreland School District Certificates of Participation | 75.306 | 4,251,024 |
| **City of San José General Fund Obligations** | **100.000** | **828,409,816** |
| Midpeninsula Regional Open Space Park District General Fund Obligations | 0.018 | 20,583 |
| TOTAL GROSS DIRECT AND OVERLAPPING GENERAL FUND OBLIGATION DEBT | | $1,277,113,572 |
| Less: **San José Convention Center (100% self-supporting from tax increment revenues)** [1] | | **176,850,000** |
| TOTAL NET DIRECT AND OVERLAPPING GENERAL FUND OBLIGATION DEBT | | 1,100,263,572 |
| GROSS COMBINED TOTAL DEBT [2] | | $3,148,530,222 |
| NET COMBINED TOTAL DEBT | | $2,971,680,222 |

[1] Supported from surplus tax increment revenues pursuant to a Reimbursement Agreement between the City and the Redevelopment
[2] Excludes tax and revenue anticipation notes, enterprise revenue, mortgage revenue and tax allocation bonds and non-bonded capital leases.

| | |
|---|---|
| Ratios to 2004-05 Assessed Valuation: | |
| **Direct Debt ($290,940,000)** | **0.32%** |
| Total Direct and Overlapping Tax and Assessment Debt | 2.04% |
| Ratios to Adjusted Assessed Valuation: | |
| **Gross Combined Direct Debt ($1,119,349,816)** | **1.44%** |
| **Net Combined Direct Debt ($942,499,816)** | **1.21%** |
| Gross Combined Total Debt | 4.04% |
| Net Combined Total Debt | 3.81% |
| STATE SCHOOL BUILDING AID REPAYABLE AS OF 6/30/05: | $6,018,360 |

*Source: California Municipal Statistics, Inc.*

CITY OF

SAN JOSE

CAPITAL OF SILICON VALLEY

# APPENDIX F: AIRPORT COMMERCIAL PAPER DEBT SERVICE CERTIFICATION

## AIRPORT COMMERCIAL PAPER DEBT SERVICE CERTIFICATION

In accordance with the Letter of Credit and Reimbursement Agreement between the City of San José and JPMorgan Chase Bank, dated November 1, 1999 (the "Reimbursement Agreement"), for the Airport's Commercial Paper Program, the certification presented in this appendix is included in the Annual Debt Report for transmission to the City Council.

Pursuant to Section 1.1(c) of the Reimbursement Agreement, the City's financial advisor, Public Resources Advisory Group, has prepared an estimate of the annual debt service needed to amortize over a 25-year period the outstanding principal, as of June 30, 2005, on the Airport's commercial paper notes. As specified in Section 1.1(c), the assumed interest rate is the average of the outstanding commercial paper notes during the 90-day period prior to June 30, 2005.

This estimate of annual debt service is used by the City to calculate the debt service coverage ratio in compliance with Section 7.9 of the Reimbursement Agreement.

**MEMORANDUM TO:** City of San José

**FROM:** Public Resources Advisory Group

**SUBJECT:** Certificate Related to Debt Service Coverage Calculations Required in Connection with the Commercial Paper Program for Norman Y. Mineta San José International Airport

**DATE:** August 18, 2005

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As requested, we have prepared this Certificate in order to enable the City of San José to comply with Section 7.9 of its Letter of Credit and Reimbursement Agreement (the "Agreement") with Morgan Guaranty Trust Company related to the commercial paper program for the Mineta San José International Airport. Using assumptions we believe are consistent with the requirements of part (c) of the definition of Debt Service contained in the Agreement, we have prepared an estimate of the annual debt service on the Series C (taxable) commercial paper outstanding as of June 30, 2005. This estimate assumes the commercial paper is amortized in equal annual amounts over 25 years at an interest rate equal to the average rate carried by the Series C (taxable) commercial paper over the 90 days prior to June 30, 2005.

The results of these calculations are provided below:

| Type of Commercial Paper | Principal Outstanding | Assumed Interest Rate | Assumed Debt Service |
|---|---|---|---|
| Taxable | $7,755,000 | 3.0276% | $446,722 |

Please do not hesitate to contact us if you have any questions or require additional information.

Signed: Wesley C. Hough, Co-President

**APPENDIX G:  SPECIAL TAX ANNUAL REPORT**

## SPECIAL TAX ANNUAL REPORT

This information is provided in the Annual Debt Report to the City Council pursuant to California Government Code Sections 50075 and 50075.3. California Government Code Section 50075 requires that on or after January 1, 2001, any local special tax measure that is subject to voter approval that would provide for the imposition of a special tax by a local agency shall provide accountability measures that include an annual report.

Pursuant to Government Code Section 50075.3, the Chief Financial Officer of the levying local agency shall file the annual report with its governing body no later than January 1, 2002, and at least once a year thereafter. The annual report shall contain both of the following: (a) the amount of funds collected and expended; and (b) the status of any project required or authorized to be funded as identified in the special tax measure indicating the specific purposes of the special tax.

**Special Tax Annual Report**
*Fiscal Year 2004-05*

| Date of Election | Special Tax Measure | Funds Collected | Funds Expended | Status of Funded Projects |
|---|---|---|---|---|
| 11/07/2000 | San José Neighborhood Libraries Bonds | See Note 1 | $6,489,778 | 2 Completed<br>11 Under Design or Construction |
| 11/07/2000 | San José Neighborhood Parks and Recreation Bonds | See Note 1 | $8,111,145 | 76 Completed<br>19 Under Design or Construction |
| 03/05/2002 | San José 911, Fire, Police and Paramedic Neighborhood Security Act | See Note 1 | $3,448,550 | 5 Completed<br>25 Under Design or Construction |
| 03/27/2001 | Community Facilities District No. 6 (Great Oaks-Route 85) | $1,057,266 | $1,014,100 | 99% Completed |
| 06/19/2001 | Community Facilities District No. 5A (North Coyote Valley Facilities) | $0 | $0 | No Activity |
| 06/19/2001 | Community Facilities District No. 5B (North Coyote Valley Services) | $0 | $0 | No Activity |
| 09/03/2002 | Community Facilities District No. 8 (Communications Hill) | $304,900 | $51,000 | On-going maintenance[2] |
| 12/17/2002 | Community Facilities District No. 9 (Bailey/Highway 101) | $1,241,348 | $1,006,230 | 95% Completed |
| 04/01/2003 | Community Facilities District No. 10 (Hassler-Silver Creek) | $1,048,001 | $922,987 | Project Completed |

[1] The City has issued four series of General Obligation Bonds through Fiscal Year 2004-05 for a total of $352,090,000 to fund a portion of the projects authorized by voters under these measures. A total of $23,510,898 was collected in Fiscal Year 2004-05 to pay debt service on the series 2001, 2002 and 2004 Bonds.

[2] Significant increases in maintenance expenditures expected next fiscal year due to accelerated development in District.

CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

## GLOSSARY

**Accrued Interest**: In general, interest that has been earned on a bond, but not yet paid – usually because it is not yet due. More specifically, this term is often used to refer to interest earned on a bond from its dated date to the closing date.

**Ad Valorem Tax**: A tax which is based on the value (assessed value) of property.

**Advance Refunding**: A procedure whereby outstanding bonds are refinanced from the proceeds of a new bond issue more than ninety (90) days prior to the date on which the outstanding bonds ("refunded bonds") become due or are callable.

**Alternative Minimum Tax (AMT)**: An income tax based on a separate and alternative method of calculating taxable income and separate and alternative schedule of rates. With respect to bonds, the interest on certain types of qualified tax-exempt private activity bonds is included in income for purposes of the individual and corporate alternative minimum tax.

**Arbitrage**: With respect to municipal bonds, "arbitrage" is the profit made from investing the proceeds of tax-exempt bonds in higher-yielding securities.

**Arbitrage Rebate**: Payment of arbitrage profits to the United States Treasury by a tax-exempt bond issuer.

**Basis Point**: One basis point is equal to 1/100 of one percent. If interest rates increase from 4.50% to 4.75%, the difference is referred to as a 25 basis point increase.

**BMA Index**: An index published by the Bond Market Association (BMA). The index is produced from Municipal Market Data and is a 7-day high-grade market index comprised of tax-exempt variable rate demand obligations.

**Bond**: Any interest-bearing or discounted government or corporate security that obligates the issuer (borrower) to pay the bondholder a specific sum of money (interest), usually at specific intervals, and to repay the principal amount of the loan at maturity.

**Bond Counsel**: An attorney or a firm of attorneys, retained by the issuer, that gives the legal opinion delivered with the bonds confirming that (i) the bonds are valid and binding obligations of the issuer; (ii) the issuer is authorized to issue the proposed securities; (iii) the issuer has met all legal requirements necessary for issuance, and; (iv) and in the case of tax-exempt bonds, that interest on the bonds is exempt from federal and state income taxes.

**Bond Insurance**: Noncancellable insurance purchased from a bond insurer by the issuer or purchaser of a bond or series of bonds pursuant to which the insurer promises to make scheduled payments of interest, principal and mandatory sinking fund payments on an issue if the issuer fails to make timely payments. When an issue is insured, the investor relies on the creditworthiness of the insurer rather than the issuer. Payment of an installment by the insurer does not relieve the issuer of its obligation to pay that installment; the issuer remains liable to pay that installment to the insurer.

**Bond Insurer**: A company that pledges to make all interest and principal payments when due if the issuer of the bonds defaults on its obligations. In return, the bond issuer or purchaser pays a premium ("bond insurance premium") to the insurance company. Insured bonds generally trade on the rating of the bond insurer rather than the rating on the underlying bonds, since the bond insurer is ultimately at risk for payment of the principal and interest due on the bonds. The municipal bond insurers used by the City include: Ambac, MBIA, FGIC, FSA and XL Capital, which are all rated Aaa/AAA/AAA.

**Bond Purchase Contract or Agreement**: In a negotiated sale, the bond purchase contract is an agreement between an issuer and an underwriter or group of underwriters in a syndicate or selling group who have agreed to purchase the issue pursuant to the price, terms and conditions outlined in the agreement.

**Bond Resolution**: See Indenture/Bond Resolution/Trust Agreement.

**Bond Series**: An issue of bonds may be structured as multiple bond series reflecting differences in tax status, priority of debt service payment, or interest rate mode, as well as to facilitate marketing of the bonds.

**Bondholder**: The owner of a bond. Bondholders may be individuals or institutions such as banks, insurance companies, mutual funds, and corporations. Bondholders are generally entitled to receive regular interest payments and return of principal when the bond matures.

**Call**: The terms of the bond giving the issuer the right or requiring the issuer to redeem or "call" all or portion of an outstanding issue of bonds prior to their stated date of maturity at a specified price, usually at or above par.

**Closing Date (Delivery Date)**: The date on which an issue is delivered by the issuer to, and paid for by, the original purchaser (underwriter), also called the delivery date. This date may be a different date than the sale date or the dated date.

**Commercial Paper**: Short term, unsecured promissory notes, usually backed by a line of credit with a bank, with maturities of fewer than 270 days.

**Competitive Sale**: The sale of bonds to the bidder presenting the best sealed bid at the time and place specified in a published notice of sale (also called a "public sale").

**Coupon**: Interest rate on a bond or note that the issuer promises to pay to the bondholder until maturity, expressed as an annual percentage of the face value of the bond.

**CUSIP:** The acronym for "Committee on Uniform Security Identification Procedures", which was established under the auspices of the American Bankers Association to develop a uniform method of identifying municipal, United States government and corporate securities. A separate CUSIP number is assigned for each maturity of each issue and is printed on each bond and generally on the cover of the Official Statement.

**Dated Date**: The dated date is the date on which interest on the bonds begins to accrue to the benefit of bondholders.

**Debt Retirement**: Repayment of debt.

**Debt Service**: The total interest, principal and mandatory sinking fund payments due at any one time.

**Debt Service Coverage**: The ratio of pledged revenues available annually to pay debt service on the annual debt service requirement. Pledged revenues are either calculated before operating and maintenance expenses ("Gross Revenue") or net of operating and maintenance expenses ("Net Revenue"). This ratio is one indication of the margin of safety for payment of debt service.

**Debt Service Reserve Fund/Account**: An account from which moneys may be drawn to pay debt service on an issue of bonds if pledged revenues and other amounts available to satisfy debt service are insufficient. The size of the debt service reserve fund and investment of moneys in the fund/account are subject to restrictions contained in federal tax law for tax-exempt bonds.

**Default or Event of Default**: Failure to make prompt debt service payment or to comply with other covenants and requirements specified in the financing agreements for the bonds.

**Defeasance**: Usually occurs in connection with the refunding of an outstanding issue by final payment or provision for future payment of principal and interest on a prior issue. In an advance refunding, the defeasance of the bonds being refunded is generally accomplished by establishing an escrow of high quality securities to provide for payment of debt service on the bonds to redemption or maturity.

**Federal Open-Market Committee (FOMC)**: Committee that sets interest and credit policies for the Federal Reserve Board (the "Fed"), the United States' central bank. The Committee's decisions are closely watched and interpreted by economists and stock and bond markets analysts, who try to predict whether the Fed is seeking to tighten credit to reduce inflation or to loosen credit to stimulate the economy.

**Financial Advisor**: A consultant who advises the issuer on matters pertinent to a bond issue, such as structure, cash flow, timing, marketing, fairness of pricing, terms, bond ratings, and at times investment of bond proceeds. A financial advisor may also be hired to provide analysis relating to an issuer's debt capacity or future debt issuance.

**Fiscal Agent**: A commercial bank or trust company designated by an issuer under the Indenture or Bond Resolution to act as a fiduciary and as the custodian of moneys related to a bond issue. The duties are typically limited to receiving moneys from the issuer which is to be held in funds and accounts created under the Indenture or Bond Resolution and paying out principal and interest to bondholders.

**General Obligation Bond**: A bond which is secured either by a pledge of the full faith and credit of an issuer or by a promise to levy taxes in an unlimited amount as necessary to pay debt service, or both. With very few exceptions, local agencies in California are not authorized to issue "full faith and credit" bonds. Typically, general obligation bonds of a city are payable only from ad valorem property taxes which are required to be levied in an amount sufficient to pay debt service. Under the State Constitution, a city's authority to issue general obligation bonds must be approved by a two-thirds vote of the electorate and the bond proceeds are limited to the acquisition and improvement of real property.

**Indenture/Bond Resolution/Trust Agreement**: An agreement executed by an issuer and a fiscal agent/trustee which pledges certain revenues and other property as security for the repayment of the bonds, sets forth the terms of the bonds and contains the responsibilities and duties of the trustee and the rights of the bondholders. The rights of the bondholders are set forth in the indenture provisions relating to the timing of the interest and principal payments, interest rate setting mechanisms (in the case of variable rate bonds), redemption provisions, events of default, remedies and the mailing of notices of various events.

**Issuance**: Sale and delivery of a series of bonds or other securities.

**Issue**: One or more bonds or series of bonds initially delivered by an issuer in a substantially simultaneous transaction and which are generally designated in a manner that distinguishes them from bonds of other issues. Bonds of a single issue may vary in maturity, interest rate, redemption and other provisions.

**Issuer**: An entity that borrows money through the sale of bonds or notes and is committed to making timely payments of interest and principal to bondholders.

**Lease Revenue Bonds**: Bonds issued by one public entity, such as the City of San Jose Financing Authority, on behalf of another public entity, such as the City of San Jose. A bond issue which is repaid from lease payments on an asset pledged as security to the bondholders. The pledged asset is not necessarily the asset financed with the bond proceeds. The City makes the lease payments to the Authority and covenants to annually budget and appropriate funds to make the lease payments so long as the leased asset is able to be used. These payments are included in the City Budget as part of the annual appropriation process.

**Letter of Credit**: An arrangement between an issuer and a bank which provides additional security that money will be available to pay debt service on a bond issue.

Customarily, a letter of credit is issued by a commercial bank directly to the trustee allowing the trustee, if certain conditions are met, to draw upon the letter of credit by submitting to the bank a written request for payment. Letters of Credit are also referred to as liquidity facilities in connection with obligations such as commercial paper and variable rate bonds.

**LIBOR**: An acronym for London Interbank Offered Rate, a rate that the most creditworthy international banks dealing in Eurodollars charge each other for large loans. The LIBOR rate is usually the basis for other large Eurodollar loans to less creditworthy corporate and government borrowers. This rate is often used as a benchmark for short-term taxable municipal securities.

**Line of Credit**: A Line of Credit, also referred to as a liquidity facility, is a contract between the issuer and a bank that provides a source of borrowed moneys to the issuer in the event that moneys available to pay debt service, for example on commercial paper.

**Liquidity**: The ease with which an investment may be converted to cash.

**Liquidity Facility**: See "Letter of Credit" and "Line of Credit".

**Maturity**: With respect to a single bond, the date upon which the principal of the bond is due; with respect to an issue, all of the bonds of an issue which are due on a single date.

**Municipal Securities Rulemaking Board (MSRB)**: An independent, self-regulatory organization established by Congress in 1975 having general rulemaking authority over municipal securities market participants, generally brokers and dealers. The MSRB is required by federal law to propose and adopt rules in the areas which include professional qualification standards, rules of fair practice, record keeping, the scope and frequency of compliance examinations, the form and content of municipal bond quotations, and sales to related portfolios during the underwriting period.

**National Association of Security Dealers (NASD)**: A self-regulatory organization established as a "registered securities association" pursuant to the Securities Exchange Act of 1934, for the purpose of preventing fraudulent and manipulative acts and practices; promoting just and equitable principles of trade among over-the-counter brokers and dealers; and promoting rules of fair practice and self-discipline in the securities industry.

**Negotiated Sale**: The sale of bonds, the terms and price of which are negotiated by the issuer through an exclusive agreement with a previously selected underwriter and/or underwriting syndicate.

**NRMSIR**: An acronym for Nationally Recognized Municipal Securities Information Repository. NRMSIRs are the repositories for all annual reports and event notices filed under SEC Rule 15c2-12. NRMSIRs are required to be approved by the MRSB.

**Official Statement**: A document containing information about the bonds being offered, the issuer, and the sources of repayment of the bonds. Federal securities law generally requires that if an Official Statement is used to market an issue of bonds, it must fully and accurately disclose all facts that would be of interest (material) to a potential buyer of bonds.

**Par/Par Value**: Refers to the principal amount of a bond or the total principal amount of a bond series or issue.

**Parity Bonds**: Two or more issues of bonds which have the same priority of claim or lien against the issuer's pledge of particular revenues, e.g., revenues from an enterprise such as an airport or parking garage. With respect to the initial issue of bonds, called the "prior issue", the indenture or bond resolution normally provides the requirements which must be satisfied before subsequent issues of bonds, called "additional parity bonds" may be issued.

**Present Value**: The current value of a future payment, or stream of payments, calculated by discounting the future payments by an appropriate interest rate. Alternatively, present value is the amount of money which should be invested today to return a certain sum at a future time.

**Private Placement**: The sale of bonds by the issuer directly to one or more investors rather than through an underwriter. Often, the terms of the issue are negotiated directly between the issuer and the investor. Sometimes, an investment banker will act as the placement agent; bring parties together and acting as an intermediary in the negotiations. Instead of and Official Statement, an Offering Circular, Offering Memorandum or Private Placement Memorandum may be prepared.

**Project Lease**: The document, in a Lease Revenue Bond issue, is the means by which the issuer leases to another public entity (the "obligor") the project to be acquired or constructed with the proceeds of the bond issue and by which the obligor agrees to make periodic lease payments to the issuer, generally for the period of time the bond issue is outstanding.

**Proceeds**: Funds received by the issuer upon sale of the bonds which may include accrued interest and a premium. For tax purposes bond proceeds include interest earnings on the sale proceeds.

**Rating Agencies**: The organizations which provide, for a fee customarily paid by the issuer, an independent appraisal of the credit quality and likelihood of timely repayment of a bond issue. The term is most often used to refer to the three nationally recognized agencies, Moody's Investor Services, Inc., Standard & Poor's Corporation, and Fitch Ratings.

**Redemption**: The payment of principal of a bond, whether at maturity, or, under certain circumstances described in the bond, prior to maturity. Redemption of a bond by the issuer prior to maturity is sometimes referred to as "calling the bond."

**Refunding**: An issue of new bonds (the "refunding bonds") to pay debt service on a prior issue (the "refunded bonds"). Generally, the purpose of a refunding is either to reduce the debt service on the financing or to remove or replace restrictive covenant imposed by the terms of the refunded bonds. The proceeds of the refunding bonds are either deposited in a defeasance escrow to pay the refunded bonds on a date more than 90 days after the issuance ("Advance Refunding") or applied to the payment of the refunded bonds within 90 days of the issuance ("Current Refunding").

**Reserve Fund/Account**: See Debt Service Reserve Fund/Account

**Revenue Bond**: A bond which is payable solely from a specific source of revenue. Revenue bonds do not permit the bondholders to compel taxation or legislative appropriation of funds not pledged for payment of debt service. Revenue bonds are issued to acquire or construct assets owned by the City whereby the City pledges income derived from the asset or enterprise to pay the debt service.

**Sale Date**: In the case of a negotiated sale, the date on which the bond purchase agreement is signed, and in the case of a competitive sale, the date on which the bonds are awarded to the winning bidder.

**Serial Bonds**: Bonds of an issue which are payable as to principal in amounts due at successive regular intervals, generally annual or semiannual and generally in the early years of the term of the issue. An issue may consist of both serial bonds and term bonds.

**Sinking Fund**: An account, sometimes called a debt service fund or sinking fund to provide for the redemption or payment at maturity of term bonds. Generally, sinking fund payments are mandatory in a specified amount for each payment period to provide for the periodic redemption of term bonds prior to their final maturity. The individual term bonds to be redeemed each year are customarily selected at random by the trustee.

**Surety**: In the public finance context, a surety policy is a form of insurance provided by a bond insurer to satisfy a reserve fund requirement for a bond issue. Under this arrangement, instead of depositing cash in a reserve fund, the issuer buys a surety policy by paying a one-time premium equal to a percentage of the face amount of the policy. If the reserve fund is needed to make a debt service payment, the trustee notifies the surety provider and the provider makes the payment, up to the face amount of the policy. The issuer then has an obligation to reimburse the provider for the payment, plus interest.

**Tax Allocation Bonds**: Bonds secured by the incremental property tax revenues generated from a redevelopment project area. As usually structured, a project area is designated, its property tax base frozen, and revenue from the incremental growth of the property tax base is used to provide additional funds for further redevelopment or for debt service on bonds issued for redevelopment purposes.

**Tax-Exempt Bonds**: Bonds whose interest is exempt from federal income taxation. In California, the interest on bonds issued by a California governmental entity is also exempt from state income tax.

**Term Bonds**: Bonds coming due in a single maturity. The issuer generally agrees to make periodic payments into a sinking fund for mandatory redemption of term bonds before maturity or for payment at maturity.

**Trustee**: Financial institution, with trust powers which acts in a fiduciary capacity for the benefit of the bondholders in enforcing the terms of the Trust Agreement or Indenture.

**Underwriter**: An investment banking firm which, singly or as a member of an underwriting group or syndicate, agrees to purchase a new issue of bonds from an issuer for resale and distribution to investors. The underwriter may acquire the bonds either by negotiation with the issuer or by award on the basis of competitive sale.

**Variable Rate**: An interest rate which periodically changes based upon an index or pricing procedure. Variable rate bonds generally have a "demand" feature allowing the bondholder to demand that the issuer or another party repurchases the bond upon a specified number of days' notice or at certain times which reflect the intervals at which the rate varies.

**Yield**: In general, rate of return on bonds or on any capital investment. Technically, yield is the discount rate which makes the present value of all future streams of payments equal to the present value.