

*In the opinion of Orrick, Herrington & Sutcliffe LLP, Bond Counsel to the City, based upon an analysis of existing laws, regulations, rulings and court decisions and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Series 2014 Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 and is exempt from State of California personal income taxes, except that no opinion is expressed as to the status of interest on any Series 2014A Bond for any period that such Series 2014A Bond is held by a "substantial user" of the facilities refinanced by the Series 2014A Bonds or by a "related person" within the meaning of Section 147(a) of the Internal Revenue Code of 1986. Bond Counsel observes that interest on the Series 2014A Bonds is a specific preference item for purposes of the federal individual and corporate alternative minimum taxes. In the further opinion of Bond Counsel, interest on the Series 2014B Bonds and Series 2014C Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when calculating federal corporate alternative minimum taxable income. Bond Counsel expresses no opinion regarding any other tax consequences related to the ownership or disposition of, or the amount, accrual or receipt of interest on, the Series 2014 Bonds. See "TAX MATTERS" herein.*



<b>\$125,645,000</b>		
<b>CITY OF SAN JOSE, CALIFORNIA</b>		
<b>AIRPORT REVENUE REFUNDING BONDS</b>		
<b>\$57,350,000</b>	<b>\$28,010,000</b>	<b>\$40,285,000</b>
Series 2014A (AMT)	Series 2014B (Non-AMT)	Series 2014C (Non-AMT)

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

The City of San José Airport Revenue Refunding Bonds, Series 2014A (AMT) (the "Series 2014A Bonds"), the City of San José Airport Revenue Refunding Bonds, Series 2014B (Non-AMT) (the "Series 2014B Bonds") and the City of San José Airport Revenue Refunding Bonds, Series 2014C (Non-AMT) (the "Series 2014C Bonds" and together with the Series 2014A Bonds and the Series 2014B Bonds, the "Series 2014 Bonds") are being issued by the City of San José, California (the "City"). The Series 2014A Bonds are being issued (i) to refund all of the outstanding City of San José Airport Revenue Bonds, Series 2004C and (ii) to pay costs of issuing the Series 2014A Bonds. The Series 2014B Bonds are being issued (i) to refund all of the outstanding City of San José Airport Revenue Bonds, Series 2004D and (ii) to pay costs of issuing the Series 2014B Bonds. The Series 2014C Bonds are being issued (i) to refund all of the outstanding City of San José Airport Revenue Bonds, Series 2001A and (ii) to pay costs of issuing the Series 2014C Bonds.

The Series 2014 Bonds are being issued pursuant to the City Charter and pursuant to a Master Trust Agreement between the City and The Bank of New York Mellon Trust Company, N.A., as trustee (the "Trustee"). The Series 2014 Bonds are limited obligations of the City payable solely from, and secured by a pledge of, General Airport Revenues and certain other funds held or made available under the Master Trust Agreement, after Maintenance and Operation Costs are paid. The pledge is on a parity with the pledge of General Airport Revenues made to secure Outstanding Bonds and any additional Bonds issued under the Master Trust Agreement. The City has covenanted in the Master Trust Agreement not to issue any obligations secured by a pledge of General Airport Revenues senior to the claim of the Series 2014 Bonds.

Interest on the Series 2014 Bonds will be payable on March 1 and September 1, commencing March 1, 2015. The Series 2014 Bonds are issuable as fully registered bonds and, when issued, will be registered in the name of Cede & Co., as registered owner and nominee of The Depository Trust Company ("DTC"), New York, New York. Individual purchases and sales of the Series 2014 Bonds may be made in book-entry form only, in denominations of \$5,000 and integral multiples thereof. Purchasers will not receive certificates from the City or the Trustee representing their interest in the Series 2014 Bonds purchased. So long as the Series 2014 Bonds are held by DTC, the principal of and interest on the Series 2014 Bonds will be payable by wire transfer to DTC, which in turn is required to remit such principal and interest to the DTC Participants for subsequent disbursement to the Beneficial Owners of the Series 2014 Bonds, as more fully described herein.

The Series 2014 Bonds are subject to optional redemption prior to maturity as more fully described herein.

**The principal of and interest on the Series 2014 Bonds are secured solely by the General Airport Revenues and certain other funds held or made available under the Master Trust Agreement, after Maintenance and Operation Costs are paid, and the City is not obligated to pay the Series 2014 Bonds except from the General Airport Revenues and such other funds held or made available under the Master Trust Agreement. The General Fund of the City is not liable, and the credit or taxing power of the City is not pledged, for the payment of the principal of or interest on the Series 2014 Bonds. The Series 2014 Bonds are not secured by a legal or equitable pledge of, or charge, lien or encumbrance upon, any of the property of the City or any of its income or receipts, except the General Airport Revenues. The owners of the Series 2014 Bonds have no right to compel the exercise of any taxing power of the City.**

The cover page is not intended to be a summary of the terms of, or the security for, the Series 2014 Bonds. Investors are advised to read this Official Statement in its entirety to obtain information essential to the making of an informed investment decision.

*The Series 2014 Bonds are offered when, as and if issued by the City and received by the Underwriters, subject to the approval of validity by Orrick, Herrington & Sutcliffe LLP, Bond Counsel to the City. Certain legal matters will be passed upon on behalf of the City by the City Attorney, and certain legal matters will be passed upon for the City by Orrick, Herrington & Sutcliffe LLP as disclosure counsel. Certain legal matters will be passed upon for the Underwriters by their counsel, Kutak Rock LLP. It is expected that the Series 2014 Bonds in book-entry form will be available for delivery through the facilities of DTC on or about October 7, 2014.*



FIDELITY  
CAPITAL  
MARKETS



## MATURITY SCHEDULE

**\$57,350,000  
CITY OF SAN JOSE, CALIFORNIA  
AIRPORT REVENUE REFUNDING BONDS  
SERIES 2014A (AMT)**

<b>Maturity (March 1)</b>	<b>Amount</b>	<b>Interest Rate</b>	<b>Yield/Price</b>	<b>CUSIP 798136<sup>†</sup></b>
2015	\$ 1,025,000	1.000%	0.340%	TW7
2016	140,000	2.000	0.640	TX5
2017	95,000	2.000	0.910	TY3
2018	50,000	2.000	1.230	TZ0
2019	6,885,000	5.000	1.540	UA3
2020	7,020,000	5.000	1.940	UB1
2021	7,655,000	5.000	2.310	UC9
2022	7,745,000	5.000	2.620	UJ4
2022	20,000	3.000	2.620	UD7
2023	8,475,000	5.000	2.880	UE5
2024	85,000	3.000	100	UF2
2024	8,840,000	5.000	3.000	UK1
2025	9,175,000	5.000	3.120 <sup>C</sup>	UG0
2026	140,000	3.375	3.420	UH8

**\$28,010,000  
CITY OF SAN JOSE, CALIFORNIA  
AIRPORT REVENUE REFUNDING BONDS  
SERIES 2014B (NON-AMT)**

<b>Maturity (March 1)</b>	<b>Amount</b>	<b>Interest Rate</b>	<b>Yield</b>	<b>CUSIP 798136<sup>†</sup></b>
2026	\$ 360,000	3.100%	3.120%	UL9
2026	7,615,000	5.000	2.920 <sup>C</sup>	UP0
2027	9,665,000	5.000	2.990 <sup>C</sup>	UM7
2028	10,370,000	5.000	3.090 <sup>C</sup>	UN5

**\$40,285,000  
CITY OF SAN JOSE, CALIFORNIA  
AIRPORT REVENUE REFUNDING BONDS  
SERIES 2014C (NON-AMT)**

<b>Maturity (March 1)</b>	<b>Amount</b>	<b>Interest Rate</b>	<b>Yield</b>	<b>CUSIP 798136<sup>†</sup></b>
2027	\$ 7,295,000	5.000%	2.990% <sup>C</sup>	UQ8
2028	7,655,000	5.000	3.090 <sup>C</sup>	UR6
2029	8,035,000	5.000	3.160 <sup>C</sup>	US4
2030	8,440,000	5.000	3.210 <sup>C</sup>	UT2
2031	8,520,000	5.000	3.260 <sup>C</sup>	UV7
2031	340,000	3.625	3.630	UU9

<sup>†</sup> Copyright 2014, American Bankers Association. CUSIP data provided herein by Standard & Poor's, CUSIP Service Bureau, a division of The McGraw-Hill Companies, Inc. This data is not intended to create or maintain a database of CUSIP descriptions or numbers and is not intended to create and does not serve in any way as a substitute for the CUSIP Service. CUSIP numbers are provided only for the convenience of the reader. Neither the City nor the Underwriters take any responsibility for the accuracy of such CUSIP numbers.

<sup>C</sup> Priced to the par call date of March 1, 2024.

## CITY OF SAN JOSE

City Council

Chuck Reed, Mayor

District 1: Pete Constant, Member  
District 2: Ash Kalra, Member  
District 3: Sam Liccardo, Member  
District 4: Kansen Chu, Member  
District 5: Xavier E. Campos, Member

District 6: Pierluigi Oliverio, Member  
District 7: Madison Nguyen, Member (Vice Mayor)  
District 8: Rose Herrera, Member  
District 9: Donald Rocha, Member  
District 10: Johnny Khamis, Member

## Airport Commission

Andrés Quintero, Chair  
Arsia Azadgan  
Spencer Horowitz  
E. Ronald Blake  
Julie Riera Matsushima  
Robert Varich

Matt Domenici, Vice Chair  
Keith Ian Graham  
AJ Borade  
Alain Dussau  
Stephen McMinn

## City Officials

Edward Shikada, City Manager  
Toni Taber, City Clerk  
Sharon Winslow Erickson, City Auditor  
Richard Doyle, City Attorney  
Kim Becker Aguirre, Director of Aviation  
Julia Harper Cooper, Director of Finance

## City Staff

Pamela Antil, Assistant City Manager  
John Aitken, Acting Assistant Director of Aviation  
Terri A. Gomes, Deputy Director, Finance and Administration  
Kim Hawk, Deputy Director, Finance and Administration (incoming)  
Steve Peters, Acting Debt Administrator  
Janet Shum, Financial Analyst

## Professional Services

### *Bond Counsel*

Orrick, Herrington & Sutcliffe LLP  
San Francisco, California

### *Financial Advisors*

Public Financial Management  
San Francisco, California

### *Disclosure Counsel*

Orrick, Herrington & Sutcliffe LLP  
San Francisco, California

Public Resources Advisory Group  
Oakland, California

### *Trustee*

The Bank of New York  
Mellon Trust Company,  
N.A.  
San Francisco, California

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

**Use of this Official Statement.** This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the Series 2014 Bonds by a person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale. This Official Statement does not constitute a contract between any owner of the Series 2014 Bonds and the City or the Underwriters.

**Preparation of this Official Statement.** The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall under any circumstances create any implication that there has been no change in the affairs of the Norman Y. Mineta San José International Airport since the date hereof. This Official Statement is submitted in connection with the sale of the Series 2014 Bonds referred to herein and may not be reproduced or used, in whole or in part, for any other purpose.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as a part of, their respective responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

**Estimates and Forecasts.** Certain statements contained in this Official Statement do not reflect historical facts but are forecasts and “forward-looking statements.” No assurance can be given that the future results discussed herein will be achieved, and actual results may differ materially from the forecasts described herein. In this respect, the words “estimate,” “forecast,” “project,” “anticipate,” “expect,” “intend,” “plan,” “believe” and similar expressions are intended to identify forward-looking statements. All projections, forecasts, assumptions and other forward-looking statements are expressly qualified in their entirety by the cautionary statements set forth in this Official Statement.

**Document Summaries.** All summaries of documents contained in this Official Statement are made subject to the provisions of such documents and do not purport to be complete statements of any or all such provisions. Each reference in this Official Statement to a document is qualified in its entirety by reference to such document, which is on file with the City. Copies of documents referred to herein are available from the Finance Department—Debt Management, City of San José City Hall, 200 East Santa Clara Street, San José, CA 95113; Phone (408) 535-7010; Fax (408) 292-6482. The City may impose a charge for copying, mailing and handling.

**No Registration or Qualification.** The issuance and sale of the Series 2014 Bonds have not been registered under the Securities Act of 1933 or the Securities Exchange Act of 1934, both as amended, and the Master Trust Agreement has not been qualified under the Trust Indenture Act of 1939, as amended, in reliance upon exemptions provided thereunder.

**Airport and City Websites.** The City maintains a number of websites, including a website for the Airport. However, the information presented on the City’s websites is not part of this Official Statement and should not be relied upon in making an investment decision with respect to the Series 2014 Bonds.

**IN CONNECTION WITH THE OFFERING OF THE SERIES 2014 BONDS, THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS THAT STABILIZE OR MAINTAIN THE MARKET PRICE OF THE SERIES 2014 BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME. THE UNDERWRITERS MAY OFFER AND SELL THE SERIES 2014 BONDS TO CERTAIN DEALERS, INSTITUTIONAL INVESTORS AND OTHERS AT PRICES LOWER OR YIELDS HIGHER THAN THE PUBLIC OFFERING PRICES AND YIELDS STATED ON THE INSIDE COVER PAGE HEREOF, AND THE PUBLIC OFFERING PRICES AND YIELDS MAY BE CHANGED FROM TIME TO TIME BY THE UNDERWRITERS WITHOUT PRIOR NOTICE.**

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## **OFFICIAL STATEMENT**

### **RELATING TO**

**\$125,645,000  
CITY OF SAN JOSE, CALIFORNIA  
AIRPORT REVENUE  
REFUNDING BONDS**

<b>\$57,350,000 Series 2014A (AMT)</b>	<b>\$28,010,000 Series 2014B (Non-AMT)</b>	<b>\$40,285,000 Series 2014C (Non-AMT)</b>
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### **INTRODUCTION**

#### **General**

The purpose of this Official Statement, which includes the cover page, inside cover page, table of contents and appendices, is to provide information concerning the sale and delivery by the City of San José, California (the “City”) of \$57,350,000 aggregate principal amount of City of San José Airport Revenue Refunding Bonds, Series 2014A (AMT) (the “Series 2014A Bonds”), \$28,010,000 aggregate principal amount of City of San José Airport Revenue Refunding Bonds, Series 2014B (Non-AMT) (the “Series 2014B Bonds”) and \$40,285,000 aggregate principal amount of City of San José Airport Revenue Refunding Bonds, Series 2014C (Non-AMT) (the “Series 2014C Bonds” and, collectively with the Series 2014A Bonds and Series 2014B Bonds, the “Series 2014 Bonds”)

Pursuant to Sections 200 and 1220 of the Charter of the City of San José (the “City Charter”), the City has the power to issue revenue bonds for airport facilities. The Series 2014 Bonds are to be issued and secured pursuant to the City Charter and Chapter 4.38 of the City Municipal Code (collectively, the “Law”) and pursuant to the Master Trust Agreement, dated as of July 1, 2001, between the City and The Bank of New York Mellon Trust Company, N.A., as successor to BNY Western Trust Company, as trustee (the “Trustee”), as supplemented by the First Supplemental Trust Agreement, dated as of July 1, 2001 (the “First Supplemental Trust Agreement”), by the Second Supplemental Trust Agreement, dated as of December 1, 2002 (the “Second Supplemental Trust Agreement”), by the Third Supplemental Trust Agreement and the Fourth Supplemental Trust Agreement, each dated as of June 1, 2004 (respectively, the “Third Supplemental Trust Agreement” and the “Fourth Supplemental Trust Agreement”), by the Fifth Supplemental Trust Agreement, dated as of September 1, 2007 (the “Fifth Supplemental Trust Agreement”), by the Sixth Supplemental Trust Agreement, dated as of May 1, 2009 (the “Sixth Supplemental Trust Agreement”), by the Seventh Supplemental Trust Agreement, dated as of July 1, 2011 (the “Seventh Supplemental Trust Agreement”), by the Eighth Supplemental Trust Agreement, dated as of December 1, 2011 (the “Eighth Supplemental Trust Agreement”), by the Ninth Supplemental Trust Agreement, dated as of November 1, 2012, and by a Tenth Supplemental Trust Agreement, to be dated as of October 1, 2014, each between the City and the Trustee (collectively, the “Master Trust Agreement”). All capitalized terms used in this Official Statement, unless otherwise defined herein, have the meanings assigned to such terms in the Master Trust Agreement. See “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER TRUST AGREEMENT—Certain Definitions” in Appendix C.

## **Purpose of the Series 2014 Bonds**

The Series 2014 Bonds are being issued to refund all of certain outstanding City of San José Airport Revenue Bonds and to pay costs of issuing the Series 2014 Bonds. See “PLAN OF REFUNDING” and “ESTIMATED SOURCES AND USES OF PROCEEDS.”

## **The City and the Airport**

The City is the third largest city in California and the tenth largest city in the United States based on its population of approximately 1,000,536 as of January 1, 2014 (as reported by the California Department of Finance). The territory of the City encompasses approximately 178 square miles. Located at the southern end of the San Francisco Bay, the City is the county seat of the County of Santa Clara (the “County”).

The Norman Y. Mineta San José International Airport (the “Airport”) is a commercial service and general aviation airport owned and operated by the City. The Airport is classified by the Federal Aviation Administration (the “FAA”) as a “medium hub” airport (an airport that enplanes at least 0.25% but less than 1.0% of the total number of passenger boardings at all commercial service airports in the United States). The Airport is located approximately two miles north of downtown San José and serves the California counties of Alameda, Monterey, San Benito, San Mateo, Santa Clara and Santa Cruz (the “Air Service Area”). In the City’s fiscal year ended June 30, 2014 (“fiscal year 2013-14”), the Airport served approximately 4.5 million enplaned passengers (passengers embarking on airplanes, representing approximately 50% of the total number of passengers enplaning and deplaning at the Airport), compared to approximately 4.2 million in fiscal year 2012-13, reflecting a 6.7% increase year over year. The City estimates that approximately 98.0% of enplaned passengers at the Airport in fiscal year 2013-14 were passengers beginning their trips at the Airport (often referred to as “origin and destination” or “O&D” passengers), as opposed to passengers connecting through the Airport to other cities. See “CERTAIN FACTORS AFFECTING THE AIRPORT” below and “PASSENGER SERVICES AND OPERATIONS” in Appendix A.

Fourteen passenger airlines and two air cargo carriers provided scheduled service at the Airport as of June 30, 2014. Passenger airlines serving the Airport and leasing space directly from the City are operating at the Airport pursuant to the terms of an operating agreement and terminal building lease with the City (the “Airline Lease Agreement”). All passenger airlines are operating at the Airport as Signatory Airlines (as defined in Appendix A). See “LEASE AND OPERATING AGREEMENTS—Airline Agreements” in Appendix A.

Passenger airline traffic at the Airport declined significantly between fiscal years 2006-07 and 2009-10. In addition to this significant reduction in airline traffic, the debt service obligations of the Airport have increased significantly in recent years. In response, the Airport commenced numerous initiatives, including measures to reduce costs and enhance revenues, in order to meet its increasing financial obligations. See “AIRPORT FINANCIAL MATTERS—Management Discussion of Recent Financial Results” in Appendix A.

## **Security for the Series 2014 Bonds**

The Series 2014 Bonds are limited obligations of the City secured by a pledge of General Airport Revenues and certain other funds held or made available under the Master Trust Agreement, after the payment of Maintenance and Operation Costs. As of June 30, 2014, the City had outstanding its City of San José Airport Revenue Bonds, Series 2001A (the “Series 2001A Bonds”), City of San José Airport Revenue Bonds, Series 2004C (the “Series 2004C Bonds”) and Series 2004D (the “Series 2004D Bonds”)

and, together with the Series 2004C Bonds, the “Series 2004C/D Bonds”), City of San José Airport Revenue Bonds, Series 2007A (the “Series 2007A Bonds”) and Series 2007B (the “Series 2007B Bonds” and, together with the Series 2007A Bonds, the “Series 2007 Bonds”), City of San José Airport Revenue Bonds, Series 2011A-1 (the “Series 2011A-1 Bonds”) and Series 2011A-2 (the “Series 2011A-2 Bonds” and, together with the Series 2011A-1 Bonds, the “Series 2011A Bonds”), City of San José Airport Revenue Bonds, Series 2011B (the “Series 2011B Bonds”), and City of San José Airport Revenue Refunding Bonds, Series 2012A (the “Series 2012A Bonds”) in a total aggregate principal amount of \$1,384,680,000 (including \$149,710,000 aggregate principal amount of the Series 2001A Bonds and the Series 2004C/D Bonds, all of which will be refunded with proceeds of the Series 2014 Bonds). See “OUTSTANDING OBLIGATIONS AND DEBT SERVICE SCHEDULE.”

On October 2, 1984, the City Council adopted Resolution No. 57794 providing for the issuance of City of San José airport revenue bonds (the “1984 Resolution”). On June 26, 2001, in connection with the issuance of the Series 2001A Bonds, the City Council adopted a resolution amending and restating the 1984 Resolution as the Master Trust Agreement. The Series 2001A Bonds, the Series 2004C/D Bonds, the Series 2007 Bonds, the Series 2011A Bonds, the Series 2011B Bonds and the Series 2012A Bonds (collectively, the “Outstanding Bonds”) are secured under the Master Trust Agreement on a parity with the Series 2014 Bonds. The Series 2014 Bonds, together with the Outstanding Bonds and any other future parity bond obligations issued under the Master Trust Agreement (the “Additional Bonds”), are referred to in this Official Statement as the “Bonds.” See “SECURITY FOR THE BONDS.”

**The principal of and interest on the Bonds, including the Series 2014 Bonds, are secured solely by the General Airport Revenues and certain other funds held or made available under the Master Trust Agreement, after Maintenance and Operation Costs are paid, and the City is not obligated to pay the Bonds except from the General Airport Revenues and such other funds held or made available under the Master Trust Agreement. The General Fund of the City is not liable, and the credit or taxing power of the City is not pledged, for the payment of the principal of, premium, if any, or interest on the Bonds. The Bonds are not secured by a legal or equitable pledge of, or charge, lien or encumbrance upon, any of the property of the City or any of its income or receipts, except the General Airport Revenues. The Owners of the Bonds have no right to compel the exercise of any taxing power of the City. See “SECURITY FOR THE BONDS.”**

### **Continuing Disclosure**

The City is covenanting for the benefit of the Holders and Beneficial Owners of the Series 2014 Bonds to provide certain financial information and operating data and to give notices of certain events if material, to assist the Underwriters in complying with the Securities and Exchange Commission Rule 15c2-12(b)(5). See “CONTINUING DISCLOSURE.”

### **Miscellaneous**

The summaries of or references to the Master Trust Agreement, the Series 2014 Bonds, the Airline Lease Agreement and all other documents and instruments referred to in this Official Statement do not purport to be comprehensive or definitive. Each reference to any of the foregoing is qualified in its entirety by reference to each such document or instrument, copies of which are available for inspection at the Finance Department—Debt Management, City of San José City Hall, 200 East Santa Clara Street, San José, CA 95113.

The information herein is subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall under any circumstances create any implication that there has been no change in the affairs of the Airport or the City since the date hereof.

**Certain statements contained in this Official Statement do not reflect historical facts but are forecasts and “forward-looking statements.” No assurance can be given that the future results discussed herein will be achieved, and actual results may differ materially from the forecasts described herein. In this respect, the words “estimate,” “forecast,” “project,” “anticipate,” “expect,” “intend,” “plan,” “believe” and similar expressions are intended to identify forward-looking statements. All projections, forecasts, assumptions and other forward-looking statements are expressly qualified in their entirety by the cautionary statements set forth in this Official Statement.**

This Official Statement is not to be construed as a contract or agreement between the City and purchasers or owners of any of the Series 2014 Bonds.

### **PLAN OF REFUNDING**

The Series 2014A Bonds are being issued (i) to refund all of the outstanding City of San José Airport Revenue Bonds, Series 2004C and (ii) to pay costs of issuing the Series 2014A Bonds. The Series 2014B Bonds are being issued (i) to refund all of the outstanding City of San José Airport Revenue Bonds, Series 2004D and (ii) to pay costs of issuing the Series 2014B Bonds. The Series 2014C Bonds are being issued (i) to refund all of the outstanding City of San José Airport Revenue Bonds, Series 2001A and (ii) to pay costs of issuing the Series 2014C Bonds. The Series 2004C Bonds, Series 2004D Bonds and Series 2001A Bonds will be redeemed on the date of issuance of the Series 2014 Bonds. See “ESTIMATED SOURCES AND USES OF PROCEEDS.”

The following table identifies the Series 2001A Bonds, Series 2004C Bonds and Series 2004D Bonds that are expected to be refunded with the proceeds of the Series 2014 Bonds.

#### **Summary of Bonds to be Refunded**

<u><b>Series</b></u>	<u><b>Maturity (March 1)</b></u>	<u><b>Principal Refunded (000)</b></u>	<u><b>Redemption Date</b></u>	<u><b>CUSIP</b></u>
2001A	2031	\$45,710	October 7, 2014	798136LW5
2004C	2015	1,000	October 7, 2014	798136NE3
	2016	1,000	October 7, 2014	798136NF0
	2017	1,000	October 7, 2014	798136NG8
	2018	1,000	October 7, 2014	798136NH6
	2019	7,885	October 7, 2014	798136NJ2
	2020	8,070	October 7, 2014	798136NK9
	2021	8,765	October 7, 2014	798136NL7
	2022	8,945	October 7, 2014	798136NM5
	2023	9,735	October 7, 2014	798136NN3
	2024	10,275	October 7, 2014	798136NP8
	2025	10,590	October 7, 2014	798136NQ6
	2026	1,465	October 7, 2014	798136NR4
2004D	2028	34,270	October 7, 2014	798136NS2

The specific principal amount and maturity date, if any, of the Series 2001A Bonds and Series 2004C/D Bonds that will be refunded (the “Refunded Bonds”) will be determined by the City at the time the City and the Underwriters (as defined herein) sign the Bond Purchase Agreement (as defined herein). The issuance of the Series 2014 Bonds and the refunding of the Refunded Bonds are subject to market conditions, and the City will only issue the Series 2014 Bonds to refund any of the Refunded Bonds if such issuance and refunding result in acceptable debt service savings to the City.

#### **ESTIMATED SOURCES AND USES OF PROCEEDS**

The following table sets forth the estimated sources and uses of proceeds of the Series 2014 Bonds.

	<u><b>Series 2014A</b></u>	<u><b>Series 2014B</b></u>	<u><b>Series 2014C</b></u>	<u><b>Total</b></u>
<b>Sources of Funds:</b>				
Principal Amount	\$57,350,000.00	\$28,010,000.00	\$40,285,000.00	\$125,645,000.00
Net Original Issue Premium	8,731,372.75	4,479,010.05	5,980,911.75	19,191,294.55
Release from 2004 Reserve Account	8,874,327.07	4,334,261.58	-	13,208,588.65
<b>Total Sources</b>	<b>\$74,955,699.82</b>	<b>\$36,823,271.63</b>	<b>\$46,265,911.75</b>	<b>\$158,044,883.20</b>
<b>Uses of Funds:</b>				
Deposit to Redemption Fund	70,086,556.25	34,441,350.00	45,938,550.00	150,466,456.25
Deposit to General Account of the Bond Reserve Fund	4,405,957.01	2,151,889.38	-	6,557,846.39
Costs of Issuance <sup>(1)</sup>	463,186.56	230,032.25	327,361.75	1,020,580.56
<b>Total Uses</b>	<b>\$74,955,699.82</b>	<b>\$36,823,271.63</b>	<b>\$46,265,911.75</b>	<b>\$158,044,883.20</b>

<sup>(1)</sup> Includes underwriters’ discount, rating agency fees, legal and other professional fees and other costs of issuing the Series 2014 Bonds.

## DESCRIPTION OF THE SERIES 2014 BONDS

### **Form and Denomination**

The Series 2014 Bonds are to be dated the date of their initial delivery and are to mature and bear interest as set forth on the inside cover page of this Official Statement. Interest on the Series 2014 Bonds is to be payable on each March 1 and September 1 (each a “Payment Date”), commencing March 1, 2015. The interest on the Series 2014 Bonds is to be payable to the person whose name appears on the bond registration books of the Trustee as the Owner thereof (the “Owner”) as of the close of business on the fifteenth day of the month immediately preceding an interest Payment Date (the “Record Date”) (DTC so long as the book entry system with DTC is in effect), whether or not such day is a business day, such interest to be paid by check mailed by first class mail on such Payment Date to such Owner at such address as appears on such registration books. Any Owner of at least \$1,000,000 aggregate principal amount of Series 2014 Bonds may elect to have interest payable by wire transfer to the bank account number on file with the Trustee (provided the Owner makes a written request to the Trustee before the Record Date).

Each of the Series 2014 Bonds will bear interest from the Payment Date next preceding the date of authentication thereof unless it is authenticated as of a day during the period from the sixteenth day of the month next preceding any Payment Date to the Payment Date, inclusive, in which event it is to bear interest from such Payment Date, or unless it is authenticated on or before February 15, 2015, in which event it is to bear interest from the date of its initial delivery; provided, however, that if, at the time of authentication of any Series 2014 Bond, interest is in default on the Outstanding Series 2014 Bonds, such Series 2014 Bond is to bear interest from the Payment Date to which interest has previously been paid or made available for payment on the Outstanding Series 2014 Bonds.

The Series 2014 Bonds will be issued in denominations of \$5,000 and any integral multiple thereof. The Series 2014 Bonds will be issued in fully registered form and, when issued, will be registered in the name of Cede & Co., or such other name as may be requested by an authorized representative of DTC, as registered owner and nominee of DTC. DTC will act as securities depository for the Series 2014 Bonds. Individual purchases may be made in book entry form only. Purchasers will not receive certificates representing their interest in the Series 2014 Bonds purchased. So long as Cede & Co., or such other name as may be requested by an authorized representative of DTC, is the registered owner of the Series 2014 Bonds, as nominee of DTC, references to the Owners or registered owners mean Cede & Co. and not the Beneficial Owners of the Series 2014 Bonds.

So long as Cede & Co., or such other nominee as may be requested by an authorized representative of DTC, is the registered owner of the Series 2014 Bonds, principal of and premium, if any, and interest on the Series 2014 Bonds are payable by wire transfer by the Trustee to Cede & Co., or such other name as may be requested by an authorized representative of DTC, as nominee for DTC, which is required, in turn, to remit such amounts to the DTC Participants for subsequent disbursement to the Beneficial Owners. See “DTC AND THE BOOK ENTRY SYSTEM” in Appendix H.

### **Redemption of the Series 2014 Bonds**

***Optional Redemption of the Series 2014A Bonds.*** The Series 2014A Bonds maturing on and after March 1, 2025 are subject to redemption prior to their stated maturity dates, at the option of the City, from any source of available funds, as a whole or in part on any date on or after March 1, 2024, at a redemption price equal to 100% of the principal amount of the Series 2014A Bonds called for redemption, together with interest accrued thereon to the date fixed for redemption, but without premium.

***Optional Redemption of the Series 2014B Bonds.*** The Series 2014B Bonds are subject to redemption prior to their stated maturity dates, at the option of the City, from any source of available funds, as a whole or in part on any date on or after March 1, 2024, at a redemption price equal to 100% of the principal amount of the Series 2014B Bonds called for redemption, together with interest accrued thereon to the date fixed for redemption, but without premium.

***Optional Redemption of the Series 2014C Bonds.*** The Series 2014C are subject to redemption prior to their stated maturity dates, at the option of the City, from any source of available funds, as a whole or in part on any date on or after March 1, 2024, at a redemption price equal to 100% of the principal amount of the Series 2014C Bonds called for redemption, together with interest accrued thereon to the date fixed for redemption, but without premium.

***Selection of Series 2014 Bonds for Redemption.*** Whenever less than all of the Series 2014A Bonds, Series 2014B Bonds, or Series 2014C Bonds, respectively, are called for redemption, the Bonds of such Series and the maturities thereof shall be called as directed by the City, and if less than all of any maturity shall be called for redemption, the portion of such maturity shall be selected by lot. The Trustee is required to notify the City promptly in writing of the numbers of the Series 2014 Bonds so selected for redemption.

### **Notice of Redemption**

A notice of redemption is required to be mailed to the respective registered Owners of any Series 2014 Bonds (DTC so long as the book entry system with DTC is in effect) designated for redemption at their addresses appearing on the bond registration books, at least 20 days but not more than 60 days prior to the redemption date, provided, however, that such notice may be mailed as late as 15 days prior to the redemption date if the Bonds are no longer Book-Entry Bonds, which notice, in the case of each Series 2014 Bond called only in part, the portion of the principal thereof that is to be redeemed; provided that neither failure to mail such notice nor any defect in any notice so mailed will affect the sufficiency of the proceedings for the redemption of such Series 2014 Bonds.

### **Conditional Notice of Redemption and Rescission of Notice of Redemption**

The City may condition any notice of optional redemption upon receipt of funds or any other event. The City may, at its option, prior to the date fixed for redemption in any notice of optional redemption rescind and cancel such notice of optional redemption.

### **Effect of Redemption**

When notice of redemption has been duly given, and moneys for payment of the redemption price are held by the Trustee, the Series 2014 Bonds so called for redemption will, on the redemption date designated in such notice, become due and payable at the redemption price specified in such notice; and from and after the date so designated interest on the Series 2014 Bonds so called for redemption will cease to accrue, said Series 2014 Bonds will cease to be entitled to any benefit or security under the Master Trust Agreement, and the Owners of said Series 2014 Bonds will have no rights in respect thereof except to receive payment of the redemption price thereof. The Trustee is required, upon surrender for payment of any of said Series 2014 Bonds, to pay such Series 2014 Bonds at the redemption price as aforesaid, together with interest accrued thereon to the date fixed for redemption.

The Master Trust Agreement requires that all Series 2014 Bonds redeemed pursuant to the provisions described above be cancelled upon surrender and that no Series 2014 Bonds be issued in place thereof.

## **Purchase of Series 2014 Bonds**

The City may, at its option, direct the Trustee to purchase any Series 2014 Bond at public or private sale as and when and at such prices not in excess of the par value thereof (including brokerage and other charges, but excluding accrued interest, which is payable from the applicable interest account established for such Series 2014 Bonds) as the Trustee may in its discretion determine, and all Series 2014 Bonds so purchased are to be cancelled by the Trustee.

## **SECURITY FOR THE BONDS**

### **Pledge of General Airport Revenues**

Pursuant to the Master Trust Agreement, the City has irrevocably pledged the General Airport Revenues and certain other funds held or made available under the Master Trust Agreement, first, to the payment of Maintenance and Operation Costs of the Enterprise, and second, to the payment of principal of and premium, if any, and interest on the Bonds. See “—Flow of Funds.” The facilities comprising the Enterprise, however, have not been mortgaged to secure payment of the Bonds. Under certain circumstances described below under “Other Available Funds, CFC Revenues and Available PFC Revenues,” Other Available Funds and Available PFC Revenues may be pledged to and/or used to pay debt service on the Bonds. Although PFC Revenues generally do not fall within the definition of pledged General Airport Revenues, PFC Revenues may be used at the discretion of the Airport, and PFC Revenues are expected to be used but not pledged, to pay a portion of the Debt Service on the Series 2007A Bonds, the Series 2011A Bonds and the Series 2014 Bonds. PFC Revenues are not pledged, and may not be used, to pay debt service on the Series 2011B Bonds, the Series 2007B Bonds, the Series 2012A Bonds, or the Series 2014B Bonds. See “—Other Available Funds, CFC Revenues and Available PFC Revenues” below and “AIRPORT FINANCIAL MATTERS” in Appendix A.

The Master Trust Agreement generally defines “Enterprise” as meaning the Airport, as now located partially within and partially outside the City, including runways, taxiways, landing pads, navigational and landing aids, control towers, facilities for storage of aircraft and for parking of automobiles, roadways, passenger and freight terminals, land, easements and rights in land for clear zone and approach purposes, maintenance hangars and related facilities and all equipment, buildings, grounds, facilities, utilities and structures owned, leased or operated by the City in connection with or for the promotion or the accommodation of air commerce and air navigation and services in connection therewith, together with all additions, betterments, extensions and improvements thereto, to the fullest extent permitted by the City Charter and the Law. The term “Enterprise,” unless otherwise specifically limited in any Supplemental Trust Agreement, also includes all other airports, airfields, landing places, heliports or places for the take-off and landing of aircraft, and all airport facilities appurtenant thereto, wheresoever situated, subsequently owned or operated by the City.

The Master Trust Agreement generally defines “General Airport Revenues” as meaning all revenues, income, receipts and moneys derived by the City from the operation of the Enterprise, including income derived from landing fees, the sale or use of airplane fuel, all other rents and charges made to or for the account of airplanes making use of the Enterprise, receipts from agriculture, automobile service stations and automobile parking on Airport land, proceeds of loss of use or business interruption insurance, and all receipts from leases and concessions, including rents, percentages of income or receipts for business conducted on any property in the Enterprise or from services performed by the City in connection with or incidental to the operation of the Enterprise. General Airport Revenues also includes all interest, profits or other income derived from the deposit or investment of any moneys in the General Revenue Fund or any account therein established under the Master Trust Agreement. General Airport Revenues expressly excludes:

- (a) any money received by or for the account of the City from the levy or collection of taxes,
  - (b) moneys received from the State of California and the United States of America to the extent required to be deposited in restricted funds and/or used for purposes inconsistent with the terms of the Master Trust Agreement,
  - (c) lease deposits and security deposits,
  - (d) moneys required to be paid to the State of California and the United States of America pursuant to agreements with the City,
  - (e) moneys received from insurance proceeds or settlements (except as otherwise provided in the Master Trust Agreement) or the sale of or upon the taking by or under the threat of eminent domain of all or any part of the Enterprise,
  - (f) proceeds from Bonds or Subordinate Obligations issued by the City or proceeds from loans, indebtedness or other obligations entered into by the City,
  - (g) moneys or securities received by the City as gifts or grants, to the extent the use thereof is restricted by the donor or grantor to purposes inconsistent with their use as General Airport Revenues under the terms of the Master Trust Agreement,
  - (h) CFC Revenues (generally, customer facilities charges; see Appendix C for a more complete definition and see “Other Available Funds, CFC Revenues and Available PFC Revenues” below),
  - (i) PFC Revenues (see “Other Available Funds, CFC Revenues and Available PFC Revenues” below),
  - (j) Special Facility Revenues (see “Special Facility Revenues” below),
  - (k) Unrealized Items (for a definition of this term, see Appendix C),
  - (l) Qualified Hedge Termination Payments (for a definition of this term, see Appendix C),
- and
- (m) Cargo facility charges or similar fees imposed on any of cargo operators, cargo facilities or cargo parcels.

None of the City’s agreements with its Airport tenants, including the Airline Lease Agreement, is or will be assigned or pledged to the Trustee as security for the Bonds, including the Series 2014 Bonds. See “LEASE AND OPERATING AGREEMENTS” in Appendix A and “SUMMARY OF CERTAIN PROVISIONS OF THE AIRLINE LEASE AGREEMENT” in Appendix G.

#### **Other Available Funds, CFC Revenues and Available PFC Revenues**

***Other Available Funds and CFC Revenues.*** Under the Master Trust Agreement, the City may for any period elect to designate as Other Available Funds any amounts (excluding PFC Revenues) available to the City but not otherwise a part of General Airport Revenues, including without limitation CFC Revenues, the Rolling Coverage Amount (see definition below under “Rate Maintenance Covenant”) and other fund balances as described below, by filing with the Trustee a written statement designating the amount and

source of such Other Available Funds and containing a statement that such Other Available Funds are legally available to be applied to pay Debt Service during such period. After the filing of such written statement, the Other Available Funds designated therein are required to be deposited in the General Revenue Fund and applied as provided in the Master Trust Agreement. Notwithstanding any other provision, if such Other Available Funds are subject to any prior pledge or lien, the application thereof to the payment of Debt Service will be subordinate to the terms of such pledge or lien and the written statement designating the Other Available Funds is required to indicate the amount of the obligation payable in such fiscal year (currently the period beginning July 1 and ending June 30) from the Other Available Funds pursuant to such pledge or lien. Additionally, on the first day of each fiscal year, any additional beginning uncommitted balance of the General Revenue Fund (see “—Rate Maintenance Covenant” below) will automatically be considered Other Available Funds unless the City provides otherwise in a written statement of the City delivered to the Trustee.

Since fiscal year 2010-11, the City has designated CFC Revenues as Other Available Funds, and it has and expects to continue to apply the CFC Revenues (and Facility Rent, if necessary) to the payment of debt service on the Series 2011B Bonds. See “AIRPORT FINANCIAL MATTERS—Customer Facility Charges” in Appendix A for a discussion of CFC Revenues.

***Available PFC Revenues.*** Under the Master Trust Agreement, the City may for any period elect to designate any PFC Revenues as “Available PFC Revenues” by filing with the Trustee a written statement designating the amount of such Available PFC Revenues and containing a statement that the Available PFC Revenues are legally available to be applied to pay Debt Service during such period. After the filing of a written statement, the Available PFC Revenues designated therein are required to be deposited in the Interest Fund and the Principal Fund, as directed by the City, and used to pay Debt Service. Notwithstanding any other provision, if such Available PFC Revenues are subject to any prior pledge or lien, the application thereof to the payment of Debt Service will be subordinate to the terms of such pledge or lien and the written statement of the City designating the Available PFC Revenues is required to indicate the amount of the obligation payable in such fiscal year from the Available PFC Revenues pursuant to such pledge or lien.

Use of Available PFC Revenues to pay Debt Service reduces the amount of Debt Service for purposes of compliance with the Rate Maintenance Covenant under the Master Trust Agreement. In addition, if Available PFC Revenues are pledged to pay Debt Service, then the amount of such Debt Service is reduced by the amount of such pledged Available PFC Revenues for purposes of compliance with the additional debt tests under the Master Trust Agreement. See “—Rate Maintenance Covenant” and “—Additional Series of Bonds” below. Available PFC Revenues are expected to be used, but are not pledged, to pay a portion of the Debt Service on the Series 2007A Bonds, the Series 2011A Bonds and the Series 2014 Bonds. “PFC Revenues” are defined under the Master Trust Agreement as passenger facility charges collected by the City pursuant to applicable law, as amended from time to time, and interest earnings thereon, net of amounts that collecting air carriers are entitled to retain for collecting, handling and remitting such passenger facility charge revenues. See “AIRPORT FINANCIAL MATTERS” and “CAPITAL DEVELOPMENT AT THE AIRPORT” in Appendix A. See also “CERTAIN FACTORS AFFECTING THE AIRPORT—Bankruptcy Risks—Airline or Other Tenant Bankruptcies” and “—Availability of Funding from PFC Revenues and CFC Revenues” herein.

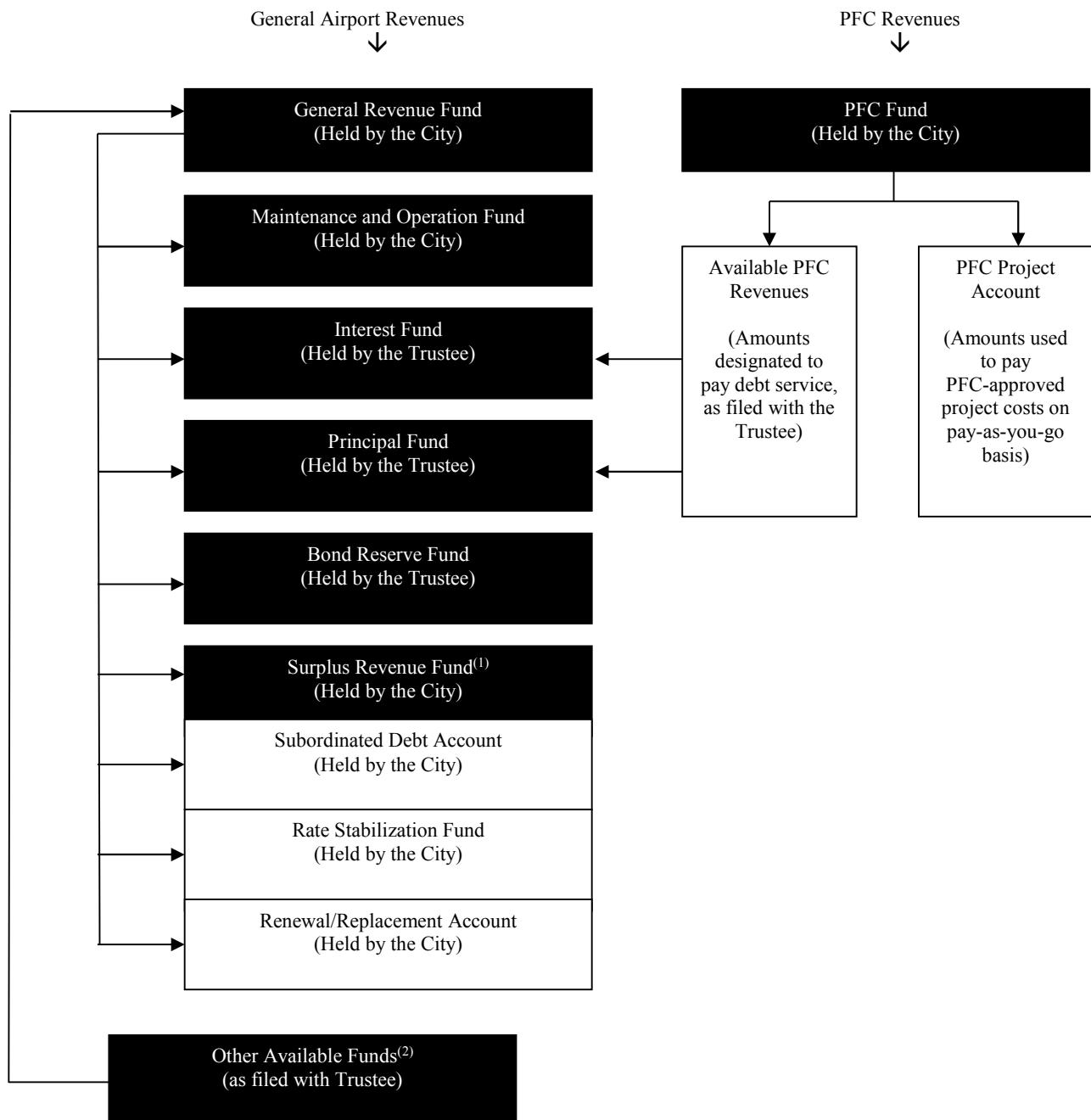
## **Flow of Funds**

Pursuant to the Master Trust Agreement, all General Airport Revenues are required to be deposited, upon receipt, by the City in a special fund in the City Treasury designated as the “City of San José Airport Revenue Fund” (the “General Revenue Fund”). Such fund was established by an ordinance of the City pursuant to Resolution No. 45333, adopted on March 12, 1974, as amended and

supplemented (the “1974 Resolution”), and continues to be maintained under the Master Trust Agreement. For a summary of the flow of funds under the Master Trust Agreement, see Table 1.

The Master Trust Agreement requires that moneys or deposits in the General Revenue Fund shall be applied solely in accordance with the order of priorities established by the Master Trust Agreement. The first priority against the General Revenue Fund is the payment of Maintenance and Operation Costs of the Enterprise. The second priority is interest on the Bonds, followed by principal of the Bonds, including any Guaranteed Obligations and Regularly Scheduled Hedge Payments under a Qualified Hedge (unless otherwise provided in a Supplemental Trust Agreement). All moneys in the General Revenue Fund are required either to be set aside by the City or to be paid over to the Trustee and deposited in one or more of the funds described below. The Interest Fund, the Principal Fund and the Bond Reserve Fund are required to be maintained by the Trustee, and the Maintenance and Operation Fund and the Surplus Revenue Fund are required to be maintained by the City.

**Table 1**  
**Norman Y. Mineta San José International Airport**  
**Summary of Flow of Funds Under the Master Trust Agreement**



- (1) Amounts remaining in the Surplus Revenue Fund at the end of each fiscal year (after required deposits have been made to the accounts therein) may be released to the City and used for any lawful Airport purpose.
- (2) Other Available Funds includes the Rolling Coverage Amount, uncommitted balances in the General Revenue Fund at the end of each Fiscal Year, CFC Revenues that are used to pay debt service, and grant funds that are used to pay debt service.

If at any time the City is in payment default under the Master Trust Agreement, the City is required, within five days after receipt of the written request of the Trustee or of a Municipal Bond Insurer or of the Owners of 10% of the aggregate principal amount of Bonds Outstanding, to transfer to the Trustee all moneys held in all funds maintained by the City under the Master Trust Agreement, and thereafter is required, at least monthly, to transfer all General Airport Revenues received by the City to the Trustee until such default is cured.

General Airport Revenues are required to be so transferred to and deposited in the following respective funds in the following order of priority, the requirements of each such fund to be satisfied before any transfer is made to any fund subsequent in priority. In general, if General Airport Revenues are insufficient for the full deposit requested in any fund, the Trustee is required to apply the amount available pro rata in proportion to the amount required in each account within such fund.

(a) Maintenance and Operation Fund. On or before the first day of each month, the City is required to set aside out of the General Revenue Fund and to deposit in the Maintenance and Operation Fund an amount equal to (i) one-twelfth of the amount budgeted by the City in the original or a revised budget for Maintenance and Operation Costs of the Enterprise for the then-current fiscal year or (ii) such other amount as the City determines is necessary to pay the Maintenance and Operations Cost of the Enterprise in such month. Moneys in the Maintenance and Operation Fund are required to be used to pay the Maintenance and Operation Costs of the Enterprise as they become due and payable.

(b) Interest Fund. After making the deposit required by subsection (a) above, the City is required to transfer to the Trustee for deposit in the Interest Fund: (i) on or before the second Business Day before each Payment Date, the amount necessary to make the required interest payment on the Outstanding Series 2014 Bonds, Series 2012A Bonds, Series 2011A Bonds, Series 2011B Bonds, and Series 2007 Bonds on such Payment Date; and (ii) the amounts required to be deposited in the Interest Fund with respect to any Additional Bonds pursuant to the Supplemental Trust Agreement providing for the issuance of such Additional Bonds. Moneys in each account of the Interest Fund are required to be used and withdrawn by the Trustee solely for the purpose of paying the interest on the applicable series of Bonds as it becomes due and payable.

(c) Principal Fund. After making the deposits required by subsections (a) and (b) above, the City is required to transfer to the Trustee for deposit in the Principal Fund: (i) on or before the second Business Day before each Payment Date, the amount necessary to make the required principal payment on the Outstanding Series 2014 Bonds, Series 2012A Bonds, Series 2011A Bonds, Series 2011B Bonds, and Series 2007 Bonds on such Payment Date; and (ii) the amounts required to be deposited in the Principal Fund with respect to the Principal Installments for any Additional Bonds and any associated Guaranteed Obligation Requirements pursuant to the Supplemental Trust Agreement providing for the issuance of such Additional Bonds. Moneys in each account of the Principal Fund are required to be used and withdrawn by the Trustee solely for the purpose of paying the Principal Installments on the applicable series of Bonds as they become due and payable, the Guaranteed Obligation Requirements with respect to such Bonds when due and payable, and the purchase price of Bonds purchased pursuant to the Master Trust Agreement.

(d) Bond Reserve Fund. After making the deposits required by subsections (a), (b) and (c) above, on or before the first day of each month, the City is required to transfer to the Trustee for deposit in the Bond Reserve Fund such amount as will be required to maintain in each account in the Bond Reserve Fund a balance equal to the applicable Required Reserve for such account; provided that at the written direction of the City, the amount to be replenished to any account within the Bond Reserve Fund after a draw on such account to pay debt service on any Bonds may be divided into no more than 12 equal monthly installments. Moneys in each account within the Bond Reserve Fund are required to be

used and withdrawn by the Trustee solely for the purpose of paying the principal of and interest on the Bonds for which such account within the Bond Reserve Fund is available as provided in the Master Trust Agreement or in any Supplemental Trust Agreement in the event that no other moneys are available therefor, or for payment or redemption of all of such Bonds then outstanding. See “—Bond Reserve Fund.”

(e) Surplus Revenue Fund. On the fifteenth day of each month, the City is required to determine the moneys remaining in the General Revenue Fund attributable to a prior calendar month which are available for transfer to the Surplus Revenue Fund after having set aside and transferred all amounts required to be set aside or transferred by the Trustee or the City as provided in the Master Trust Agreement, and the City will, at a minimum, transfer and deposit in the Surplus Revenue Fund an amount equal to the lesser of (i) the amount, if any, required to be deposited in the Subordinated Debt Account pursuant to the provisions of any Subordinate Obligations payable therefrom, or (ii) the amount remaining in the General Revenue Fund. The City may retain any moneys in excess of such minimum amount in the General Revenue Fund. All moneys in the Surplus Revenue Fund are required to be deposited in the following respective special accounts within the Surplus Revenue Fund in the following order of priority:

- (1) Subordinated Debt Account;
- (2) Rate Stabilization Fund; and
- (3) Renewal and Replacement Account.

The inability of the City to make any deposit described by this paragraph (e) by reason of a lack of General Airport Revenues will not constitute an event of default under the Master Trust Agreement. If at any time any moneys in the Surplus Revenue Fund are needed to pay the interest on or principal of the Bonds, or to pay Maintenance and Operation Costs of the Enterprise for the then-current fiscal year for which no adequate budgeted amount from General Airport Revenues was provided by the City, the City may transfer such moneys from any such account (except the Subordinated Debt Account) for such purposes. The procedures under the Master Trust Agreement with respect to funding and application of amounts within the Surplus Revenue Fund may be amended at any time without the consent of the Bondholders.

(1) Subordinated Debt Account. On or before the fifteenth day of each month, the City is required to set aside out of the Surplus Revenue Fund and deposit in the Subordinated Debt Account until there have been deposited in each month in the Subordinated Debt Account an amount equal to the amount, if any, required to be paid prior to the next scheduled deposit for all expenses, indebtedness, and other charges on all Subordinate Obligations payable therefrom. If in any month insufficient moneys are available in the Surplus Revenue Fund to provide for the required deposit into the Subordinated Debt Account, such deficit must be made up from moneys in any account in the Surplus Revenue Fund subsequent in priority to the Subordinated Debt Account.

(2) Rate Stabilization Fund. The Rate Stabilization Fund is established to facilitate the deposit and collection of moneys from the rates and charges of users of the facilities of the Enterprise in the amounts and at the times needed to satisfy the financial requirements of the Enterprise and to insure the City's ability to meet its obligations under the Master Trust Agreement. The moneys deposited in the Rate Stabilization Fund may be accumulated from any rates, fees, charges or surcharges which the City allocates or designates for the purposes of this Account (herein called the “Allocated General Airport Revenues”). Collection of moneys into the

Rate Stabilization Fund may be implemented by the City, in its discretion, upon a determination that due to unusual or exceptional circumstances it is necessary to accumulate and reserve sufficient amounts of moneys to assure the proper operation of the Enterprise and the City's compliance with the Master Trust Agreement. By way of example only, and not as a limitation, such a determination may be made upon a projected significant imbalance of rates and charges for various facilities of the Enterprise, projected extraordinary vacancy rates for certain facilities of the Enterprise, unusual discrepancies in activity levels which lead to anomalies in the calculation of rates and charges, or seismic disturbances or other natural disasters affecting the operation of the Enterprise. Moneys in the Rate Stabilization Fund also may be applied by the City to facilitate administration of revenue sharing or rate stabilization provisions of contractual agreements with airlines or other tenants of the Airport.

Moneys in the Rate Stabilization Fund are required to be used and withdrawn by the City from time to time for deposit into the Maintenance and Operation Fund, the Interest Fund and the Principal Fund, and the City may budget the payment of Maintenance and Operation Costs of the Enterprise and payment of principal of and interest on Bonds from moneys in the Rate Stabilization Fund.

The Airline Lease Agreements currently include specific conditions for depositing and withdrawing funds in the Rate Stabilization Fund. See "APPENDIX G – SUMMARY OF CERTAIN PROVISIONS OF THE AIRLINE LEASE AGREEMENT". No assurance can be given that such conditions will continue through the term of the Series 2014 Bonds.

(3) Renewal and Replacement Account. On or before the fifteenth day of each month, the City is required to set aside out of the Surplus Revenue Fund and deposit in the Renewal and Replacement Account all remaining moneys in the Surplus Revenue Fund (after the deposits described by paragraphs (e)(1) and (e)(2) above have been made) until such time as there have been deposited in the Renewal and Replacement Account in each fiscal year such amount as has been budgeted by the City for deposit into such account in such fiscal year. Moneys in the Renewal and Replacement Account are to be withdrawn by the City from time to time and deposited in a special fund of the City known as the Airport Renewal and Replacement Fund, as directed by a resolution of the Council.

All moneys remaining in the Surplus Revenue Fund on the fifteenth day of the last month of each fiscal year (after the deposits described by paragraphs (e)(1), (e)(2), and (e)(3) above have been made), may be transferred by the City to any other fund or account of the City to be used for any other lawful aviation-related purpose of the City; provided, however, the City may not withdraw any moneys held by the City in the Surplus Revenue Fund if and when the City is in default under the Master Trust Agreement.

### **Rate Maintenance Covenant**

The City has covenanted in the Master Trust Agreement that it will, at all times while any of the Bonds remain outstanding, manage its operations and establish, fix, prescribe and collect rentals, rates, fees and charges in connection with the services and facilities furnished by the Enterprise in each fiscal year so that the sum of (i) Net General Airport Revenues (generally, General Airport Revenues less Maintenance and Operations Costs of the Enterprise, but not including such Maintenance and Operations Costs as may be paid from available moneys other than General Airport Revenues; see Appendix C for a summary of the definition of the term "Maintenance and Operation Costs of the Enterprise") for such fiscal year, plus (ii) any Other Available Funds for such fiscal year after making reasonable allowances for contingencies and errors in the estimates, will be at least sufficient to pay the sum of:

- (a) the Annual Debt Service for such fiscal year on all of the Bonds as it becomes due and payable;
- (b) all other payments required in such fiscal year for compliance with the terms of the Master Trust Agreement (except any requirement to apply funds with respect to the Surplus Revenue Fund), and of any Supplemental Trust Agreement providing for the issuance of Additional Bonds pursuant to the Master Trust Agreement; and
- (c) all other payments relating to Subordinate Obligations of the City in such fiscal year which are charges, liens or encumbrances upon, or payable from, the General Airport Revenues.

Additionally, the City will, at all times while any of the Bonds remain outstanding, manage its operations and establish, fix, prescribe and collect rentals, rates, fees and charges in connection with the services and facilities furnished by the Enterprise so that (i) the sum of (1) Net General Airport Revenues for each fiscal year, plus (2) any Other Available Funds for such fiscal year is equal to at least 125% of Annual Debt Service for such fiscal year, and (ii) the sum of (1) Net General Airport Revenues for each fiscal year, plus (2) any Other Available Funds for such fiscal year (excluding, however, the Rolling Coverage Amount and any amounts not generated from actual cash receipts during the fiscal year unless such amounts are included in the initial or amended budget for the Enterprise in that fiscal year and in the initial or amended calculation of airline and other rates and charges for such fiscal year), is equal to at least 100% of Annual Debt Service for such fiscal year. “Annual Debt Service” is defined under the Master Trust Agreement as the Debt Service for the fiscal year less the Available PFC Revenues for such fiscal year. See Appendix C for a definition of “Debt Service.” “Rolling Coverage Amount” is defined under the Master Trust Agreement as the uncommitted amounts in the Maintenance and Operation Fund or the General Revenue Fund, in an amount not to exceed 25% of Annual Debt Service in any fiscal year, that are available to pay Maintenance and Operation Costs of the Enterprise or Debt Service on Bonds and that are designated as the Rolling Coverage Amount by the City.

The Master Trust Agreement provides that the City may make adjustments from time to time in such rentals, rates, fees and charges and may make such classification thereof as it deems necessary during such fiscal year, but shall not reduce such rentals, rates, fees and charges below those then in effect unless the Net General Airport Revenues and Other Available Funds from such reduced rates will at all times be sufficient to meet the requirements described above. Such covenants are collectively referred to in this Official Statement as the “Rate Maintenance Covenant.”

In general, if the City does not achieve financial results that comply with the Rate Maintenance Covenant in any fiscal year, the City is required under the Master Trust Agreement to hire during the next fiscal year a Qualified Independent Airport Consultant to make recommendations as to a revision of the rates, fees and charges, or Maintenance and Operations Costs of the Enterprise, or methods of operations of the Enterprise, if any, that will result in producing the amounts so required in the then-current fiscal year. Non-compliance with the Rate Maintenance Covenant is not an Event of Default under the Master Trust Agreement unless it occurs in two consecutive fiscal years.

### **Bond Reserve Fund**

The Master Trust Agreement requires the establishment and maintenance of a Bond Reserve Fund and requires the City to deposit to the General Account or to another Reserve Account within the Bond Reserve Fund the amount required to maintain in such account a balance equal to the applicable Required Reserve for such account. The General Account of the Bond Reserve Fund secures the Series 2001A Bonds (to the extent any remain outstanding after the issuance of the Series 2014 Bonds), the Series 2011A Bonds, and the Series 2012A Bonds, will secure the Series 2014 Bonds (the “General Account Bonds”),

and, at the election of the City, may secure Additional Bonds issued in the future. The Series 2004C/D Bonds (to the extent any remain outstanding after the issuance of the Series 2014 Bonds), the Series 2007 Bonds and the Series 2011B Bonds are, respectively, secured by a separate 2004 Reserve Account, a separate 2007 Reserve Account and a separate 2011B Reserve Account, each described below.

***The General Account.*** The Master Trust Agreement provides for the establishment and maintenance of an account designated as the “General Account” in the Bond Reserve Fund. Amounts in the General Account are available only to pay principal of and interest on (i) the General Account Bonds, and (ii) any Additional Bonds for which the General Account is made available pursuant to the Supplemental Trust Agreement providing for the issuance of such Additional Bonds. The General Account is not available to pay the Series 2004C/D Bonds, the Series 2007 Bonds or the Series 2011B Bonds.

The Required Reserve for the General Account Bonds and any Additional Bonds issued on a parity therewith and secured by the General Account within the Bond Reserve Fund shall be the lesser of (i) the Maximum Annual Debt Service on all General Account Bonds and such Additional Bonds, or (ii) the amount permitted to be held in the General Account within the Bond Reserve Fund by the arbitrage bond regulations issued by the United States Department of the Treasury under Section 148 of the Code, as such regulations are, at the time, applicable and in effect (the “General Account Required Reserve”); provided, however, that any Required Reserve may be provided in whole or in part by one or more Qualified Reserve Facilities.

The General Account Required Reserve, as of the date of issuance of the Series 2014 Bonds, will be approximately \$35,454,862.50. Upon the issuance of the Series 2014 Bonds, approximately \$31.2 million of cash and investments will be held in the General Account of the Bond Reserve Fund. In addition to the cash and investments, there is on deposit in the General Account of the Bond Reserve Fund an approximately \$6.56 million surety bond from National Public Finance Guaranty Corporation (“NPFG”), as successor to MBIA Insurance Corporation, that expires on March 1, 2016 and an approximately \$4.25 million surety bond from Ambac Indemnity Corporation (currently known as Ambac Assurance Corporation, the principal operating subsidiary of Ambac Financial Group Inc., “Ambac”) that expires on March 1, 2018.

Each of Moody’s Investors Service (“Moody’s”), Fitch Ratings (“Fitch”) and Standard and Poor’s Ratings Service (“S&P”) downgraded the claims-paying ability and financial strength of Ambac and NPFG subsequent to the deposit of the respective surety bonds into the General Account and, in certain cases, withdrew their ratings on Ambac or NPFG. Starting in March 2010, certain of the policy liabilities of Ambac were allocated to a segregated account, which has been subject to a plan of rehabilitation. Policy obligations not allocated to such segregated account, including obligations in respect of the surety bond provided by Ambac on deposit in the General Account of the Bond Reserve Fund, are not subject to, and therefore will not be directly impacted by, such rehabilitation proceeding. Information concerning NPFG and Ambac Financial Group, Inc. is available in reports and statements filed with the Securities and Exchange Commission (the “SEC”). This information is available on the SEC’s website at <http://www.sec.gov>. Such information is not incorporated by reference herein.

The Master Trust Agreement does not require that the rating of any surety bond held in the General Account be maintained after the date of its deposit to the General Account. As of the date of issuance of the Series 2014 Bonds, cash and investments in the General Account, together with the amount of the surety bond from Ambac that expires on March 1, 2018 (but without taking into account the amount of the surety bond from NPFG that expires on March 1, 2016), will be in an amount at least equal to the General Account Required Reserve. Until March 1, 2018, when the Ambac surety bond expires, no additional deposits to the General Account of the Bond Reserve Fund are expected to be required to satisfy the General Account Required Reserve (unless the General Account is drawn upon to pay principal of or

interest on Bonds or is made available to any Additional Bonds in the future). If no Additional Bonds are issued and no additional amounts were to be deposited in or paid from the General Account of the Bond Reserve Fund prior to March 1, 2018, the City expects that, upon expiration of the Ambac surety bond, amounts on deposit in the General Account would not be sufficient to satisfy the General Account Required Reserve at that time. Therefore, the City expects that it will be required to deposit approximately \$4.25 million to the General Account from either the proceeds of Additional Bonds, accumulated Airport surplus funds or a Qualified Reserve Facility in the same amount.

In addition, the City may be required to make a deposit of cash or another Qualified Reserve Facility in order to maintain the Required Reserve in the General Account in the case of non-payment under, or cancellation of, the Ambac surety bond, including as a result of the liquidation of Ambac. See “—Flow of Funds—Bond Reserve Fund.”

**Other Reserve Accounts.** Pursuant to any Supplemental Trust Agreement providing for the issuance of Additional Bonds, the Trustee may establish a separate account within the Bond Reserve Fund available only for the payment of such series of Additional Bonds and which account will have its own Required Reserve. The Master Trust Agreement provides that if such a separate account is created, said Additional Bonds do not have any claim on the other accounts maintained in the Bond Reserve Fund.

As permitted by the Master Trust Agreement, an account designated the “2004 Reserve Account”, an account designated the “2007 Reserve Account” and an account designated the “2011B Reserve Account” have each been established within the Bond Reserve Fund. Amounts in the 2004 Reserve Account are available only to pay the Series 2004C/D Bonds and any Additional Bonds for which the 2004 Reserve Account is made available pursuant to the Supplemental Trust Agreement providing for the issuance of such Additional Bonds. A portion of the amounts in the 2004 Reserve Account will be transferred to the General Account upon the issuance of the Series 2014 Bonds and redemption of the Series 2004 Bonds. Amounts in the 2007 Reserve Account are available only to pay the Series 2007 Bonds and any Additional Bonds for which the 2007 Reserve Account is made available pursuant to the Supplemental Trust Agreement providing for the issuance of such Additional Bonds. Amounts in the 2011B Reserve Account are available only to pay the Series 2011B Bonds and any Additional Bonds for which the 2011B Reserve Account is made available pursuant to the Supplemental Trust Agreement providing for the issuance of such Additional Bonds. Neither the 2004 Reserve Account, the 2007 Reserve Account nor the 2011B Reserve Account is available to pay or secure the Series 2014 Bonds.

**Amounts Held in the Bond Reserve Fund.** The approximate amounts held in the accounts within the Bond Reserve Fund as of June 30, 2014 are shown in the following table.

**Table 2**  
**Bond Reserve Requirement Funding Sources**  
**As of June 30, 2014**

<b>Account</b>	<b>Account Valuation</b>	<b>Surety Policy Limit</b>	<b>Surety Policy Provider</b>
General Account <sup>(1)</sup>	\$24,668,670	\$6,557,882 <sup>(2)</sup> 4,251,000 <sup>(4)</sup>	NPFG <sup>(3)</sup> Ambac
General Account Totals:	\$24,668,670	\$10,808,882	
2004 Reserve Account <sup>(5)</sup>	\$13,209,510		
2007 Reserve Account <sup>(6)</sup>	\$45,573,397		
2011B Reserve Account <sup>(7)</sup>	\$27,198,637		

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- (1) Secures the Series 2011A Bonds, the Series 2012A Bonds and will secure the Series 2014 Bonds. See "PLAN OF REFUNDING."
  - (2) Expires on March 1, 2016.
  - (3) Successor to MBIA Insurance Corporation.
  - (4) Expires on March 1, 2018.
  - (5) On the date of issuance of the Series 2014 Bonds, approximately \$6.6 million currently on deposit in the 2004 Reserve Account is expected to be transferred to the General Account and the remaining balance in the 2004 Reserve Account will be used to redeem a portion of the Series 2004 C/D Bonds.
  - (6) Amounts in the 2007 Reserve Account are available only to pay the Series 2007 Bonds and any Additional Bonds for which the 2007 Reserve Account is made available pursuant to the Supplemental Trust Agreement providing for the issuance of such Additional Bonds.
  - (7) Amounts in the 2011B Reserve Account are available only to pay the Series 2011B Bonds and any Additional Bonds for which the 2011B Reserve Account is made available pursuant to the Supplemental Trust Agreement providing for the issuance of such Additional Bonds.

*Source:* City of San José.

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## **Additional Series of Bonds**

**General.** The Master Trust Agreement provides that in addition to any Outstanding Bonds, the City may by Supplemental Trust Agreement issue other series of Additional Bonds payable from the General Airport Revenues on a parity with Outstanding Bonds and secured by a lien upon and pledge of such General Airport Revenues equal to the lien and pledge securing the Outstanding Bonds, but only upon compliance by the City with certain general conditions under the Master Trust Agreement, (additional conditions are described further below):

- (a) The City will not be in default under the Master Trust Agreement or any Supplemental Trust Agreements or such default shall be cured by the delivery of such Additional Bonds.
- (b) The aggregate principal amount of Additional Bonds proposed to be issued shall not exceed any limitation imposed by law, the Master Trust Agreement or any Supplemental Trust Agreement.
- (c) If the Supplemental Trust Agreement providing for the issuance of such series of Additional Bonds provides that such series of Additional Bonds is required to be secured by the General Account or another account of the Bond Reserve Fund, such Supplemental Trust Agreement shall require that the Bond Reserve Fund established pursuant to the Master Trust Agreement be increased, if and to the extent necessary to an amount at least equal to the Required Reserve for such account. Said deposit may be satisfied from such proceeds or any other source, as provided in said Supplemental Trust Agreement.
- (d) Principal Installments are required to be established in amounts sufficient to provide for the retirement of all of the Additional Bonds of such series on or before their respective maturity dates.
- (e) The conditions for the issuance of such Additional Bonds contained in the Master Trust Agreement and in any applicable Supplemental Trust Agreement are complied with as certified by a Written Statement of the City.

**Conditions for the Issuance of Additional Bonds.** Subject to compliance with the Master Trust Agreement, the City may issue and the Trustee may authenticate and deliver Additional Bonds provided that the City satisfies the conditions described below. In the case of the Series 2014 Bonds, the City intends to comply with the alternative described in paragraph (b) below.

- (a) If the proceeds derived from the sale of an earlier series of Bonds which are available for the payment of the cost of acquisition and construction of any portion of a Project to be financed from such proceeds, together with any other available funds, are not sufficient to pay the entire cost of acquisition and construction of such portion of such Project, and it is necessary to provide additional funds for completing

the acquisition and construction of such portion of such Project and paying the cost thereof in an amount determined by the City, a series of Additional Bonds may be issued by the City in a principal amount not to exceed 15% of the principal amount of the prior series of Bonds to which such Additional Bonds relate.

(b) For the purpose of refunding any Bonds issued under the Master Trust Agreement, a series of Additional Bonds may be issued by the City only if (i) the proceeds of the Additional Bonds of such series (except for proceeds used to pay costs of issuance, accrued interest and to fund any required reserve for such series of Additional Bonds) are required to be used, together with any other available moneys, to pay or defease all or a portion of the Bonds then outstanding, and (ii) the Annual Debt Service for the Additional Bonds of such series shall be less than or equal to the Annual Debt Service on the Bonds to be paid or defeased in each year that such Additional Bonds are to be outstanding.

(c) For any other airport purpose authorized under the Master Trust Agreement, provided, that either:

(i) the Trustee receives a Certificate of the City setting forth a calculation showing that, for either (A) the most recently completed fiscal year for which audited financial statements are available preceding the issuance of such series of Additional Bonds, or (B) such other consecutive twelve month period during the eighteen months immediately preceding the issuance of such series of Additional Bonds selected by the City, the sum of (i) Net General Airport Revenues for such period, plus (ii) any Other Available Funds (subject to the provisions described in paragraph (d) below) for such period is at least 125% of Maximum Annual Debt Service after the proposed Additional Bonds are issued; provided that if a period other than a fiscal year is used to make the above calculation, the Certificate of the City is required to include a statement to the effect that the City does not expect Net General Airport Revenues for the fiscal year in which such Certificate is delivered to be lower than the Net General Airport Revenues as calculated in such Certificate; or

(ii) the Trustee receives a written report of a Qualified Independent Airport Consultant setting forth estimates of General Airport Revenues, Maintenance and Operation Costs of the Enterprise, Net General Airport Revenues, Other Available Funds and Available PFC Revenues, for the longer of (X) the next five fiscal years, or (Y) if any portion of the proceeds of such series of Additional Bonds is to be used to finance construction and capitalized interest on such Additional Bonds for the expected period of construction, the three fiscal years following the fiscal year in which the City estimates such portion of the Project will be completed. The Trustee must also receive a Certificate of the City setting forth the Annual Debt Service on all Bonds (including such Additional Bonds) for each of the fiscal years covered by said report, including Annual Debt Service as estimated in such Certificate of the City with respect to future series of Bonds, if any, which the City estimates will be required to complete payment of the estimated cost of construction of such portion of the Project and any other uncompleted portion of the Project from which the report projects additional revenues. Such Certificate of the City must demonstrate that the sum of (A) the estimated Net General Airport Revenues in each of the fiscal years set forth in the report of the Qualified Independent Airport Consultant, plus (B) the Other Available Funds, if any, pledged by the City to the payment of the Bonds as provided in subsection (d), is at least equal to 125% of Annual Debt Service for the corresponding fiscal years as set forth in the Certificate of the City.

(d) With respect to both paragraphs (c)(i) and (c)(ii) above, the sum of (i) Net General Airport Revenues plus (ii) Other Available Funds (excluding, however, the Rolling Coverage Amount) will not be less than 100% of Maximum Annual Debt Service, Annual Debt Service or Debt Service for a 12-month period, as the case may be. In addition, Other Available Funds and Available PFC Revenues may not be included in the calculations pursuant to subsections (c)(i) or (c)(ii) above unless the City has pledged such

Other Available Funds or Available PFC Revenues, as the case may be, to the payment of Debt Service until the final maturity date of the Bonds and such Additional Bonds pursuant to a Supplemental Trust Agreement; provided, however, that the City may at any time release such Other Available Funds or Available PFC Revenues, in whole or in part, from such pledge, pursuant to a Supplemental Trust Agreement, to the extent that the Net General Airport Revenues and any Other Available Funds or Available PFC Revenues not so released are sufficient to meet the coverage calculations described by paragraphs (c)(i) or (c)(ii) above; and provided further, that prior to any such release, the City will have obtained a confirmation from each Rating Agency then rating on the Bonds, that such release will not adversely affect the rating on the Bonds. Any such pledge need not be a first lien on the source of revenue from which such Other Available Funds or Available PFC Revenues are derived, but the City must certify that it expects that any prior pledge of such Other Available Funds or Available PFC Revenues will not cause the amount of Other Available Funds or Available PFC Revenues in any fiscal year to be less than the amount so pledged.

### **Subordinate Obligations**

In November 1999, the City authorized the issuance from time to time of Subordinated Commercial Paper Notes (the “Subordinated Commercial Paper Notes”) that are secured by a lien on Surplus Revenues (which are General Airport Revenues remaining after the payment of Maintenance and Operating Costs of the Enterprise and the payment of debt service on the Bonds and the funding of any reserve funds established for the Bonds). In 2008, the City authorized the Subordinated Commercial Paper Notes to be issued in an aggregate principal amount of up to \$600 million outstanding at any one time. In February 2014, the City entered into a letter of credit and reimbursement agreement (the “Reimbursement Agreement”) with Barclays Bank PLC (“Barclays”), pursuant to which Barclays issued a letter of credit supporting the Subordinated Commercial Paper Notes. The maximum principal component of the Subordinated Commercial Paper Note is currently \$60 million. The letter of credit is stated to expire on February 10, 2017, unless such letter of credit is extended or terminated earlier pursuant to its terms.

An event of default under the Reimbursement Agreement would entitle Barclays to demand that no additional Subordinated Commercial Paper Notes be issued, that the City reimburse Barclays immediately for draws under the letter of credit and that all other amounts owed by the City to Barclays be accelerated and become due immediately. Events of default under the Reimbursement Agreement include, among others: a default under the Master Trust Agreement or the issuing and paying agent agreement for the Subordinated Commercial Paper Notes; non-payment; a breach of a covenant; bankruptcy; and ratings events including a suspension or withdrawal of the long-term, unenhanced debt rating assigned to the Bonds (other than where the Bonds shall continue to be rated by any two of Moody’s, Fitch, or S&P), or downgrades by any of Moody’s, Fitch or S&P of its ratings on the Bonds below “Baa2,” “BBB” and “BBB,” respectively for a period of 120 consecutive calendar days. All amounts payable by the City to Barclays under the Reimbursement Agreement are secured by a lien on the Surplus Revenues held in the Subordinated Debt Account of the Surplus Revenue Fund, including the earnings on such Surplus Revenues, which lien is subordinate to the lien of the Bonds.

Although the Master Trust Agreement does not limit the City’s right to issue additional Subordinate Obligations, in the Reimbursement Agreement, the City agreed that it would not issue any additional indebtedness secured by General Airport Revenues if a term loan under the Reimbursement Agreement is outstanding (except to repay all such term loans) and that it would not issue any additional indebtedness secured by General Airport Revenues unless the City certifies that certain financial metrics are projected to be met.

## **Special Facility Revenues**

The Master Trust Agreement provides that, the City may enter into contracts, leases, subleases or other agreements (“Special Facility Agreements”) pursuant to which the City or the other parties to such agreements will agree to construct a building or facility incident or related to the Enterprise and designated in such agreement as a Special Facility (a “Special Facility”) on land constituting part of the Enterprise or will agree to acquire or construct a Special Facility on land not then constituting part of the Enterprise (which land if not then owned or leased by the City may be acquired for such purpose), or to acquire and remodel, renovate or rehabilitate a building, structure, or other facility (including the site thereof) for a Special Facility under the following conditions:

- (1) No Special Facility may be constructed or acquired and subject to a Special Facility Agreement under the Master Trust Agreement if the result of the use or occupation of such Special Facility under the Special Facility Agreement would result in a reduction of Net General Airport Revenues and Other Available Funds below the minimum amount of Net General Airport Revenues and Other Available Funds covenanted to be produced and maintained in accordance with the Master Trust Agreement as determined by a certificate of the City (see “Rate Maintenance Covenant” above); and
- (2) Any financing for the Special Facility is required to be secured as provided in the Special Facility Agreement and may not be secured by or payable from the General Airport Revenues or any of the funds or accounts held under the Master Trust Agreement. The Special Facility Agreement may provide the terms and conditions under which any revenues of the Special Facility will become General Airport Revenues.

There are currently no Special Facilities at the Airport.

## **Other Security Features of the Master Trust Agreement**

The Master Trust Agreement contains other covenants that relate to the security for the Bonds, including covenants concerning the sale of property, insurance, eminent domain proceeds, events of default and remedies, defeasance and other matters. The Master Trust Agreement does not provide for acceleration of the payment of principal and interest on the Bonds in the event of a default. See Appendix C for a summary of certain of these provisions.

## **OUTSTANDING OBLIGATIONS AND DEBT SERVICE SCHEDULE**

Table 3 provides information as of June 30, 2014 relating to each issue of the Outstanding Bonds and the City’s currently outstanding Subordinated Commercial Paper Notes.

**Table 3**  
**Norman Y. Mineta San José International Airport**  
**Certain Information Related to the Outstanding Bonds and Subordinated Commercial Paper Notes**  
**As of June 30, 2014**

Name of Issue	Date of Issuance	Original Principal Amount	Outstanding Principal Amount	Final Maturity Date
<b>Senior Lien</b>				
City of San José Airport Revenue Bonds				
Series 2001A <sup>(1)</sup>	August 14, 2001	\$158,455,000	\$45,710,000	March 1, 2031
Series 2004C <sup>(1)</sup>	June 24, 2004	75,730,000	69,730,000	March 1, 2026
Series 2004D <sup>(1)</sup>	June 24, 2004	34,270,000	34,270,000	March 1, 2028
Series 2007A	September 13, 2007	545,755,000	539,975,000	March 1, 2047
Series 2007B	September 13, 2007	179,260,000	177,015,000	March 1, 2037
Series 2011A-1	July 28, 2011	150,405,000	139,900,000	March 1, 2034
Series 2011A-2	July 28, 2011	86,380,000	80,390,000	March 1, 2034
Series 2011B	December 14, 2011	271,820,000	264,085,000	March 1, 2041
Series 2012A	November 8, 2012	49,140,000	33,605,000	March 1, 2018
<b>Total Senior Lien</b>		<b>\$1,551,215,000</b>	<b>\$1,384,680,000</b>	
<b>Subordinate Lien</b>				
City of San José Norman Y. Mineta San José International Airport Subordinated Commercial Paper Notes, Series A-1, Series A-2, Series B, Series C <sup>(2)</sup>	Varies	-	\$41,159,000	Rolling maturities of 270 days or less
<b>Total Subordinate Lien</b>			<b>\$41,159,000</b>	

<sup>(1)</sup> See "PLAN OF REFUNDING."

<sup>(2)</sup> See "SECURITY FOR THE BONDS – Subordinate Obligations."

Source: City of San José.

**Senior Lien.** Table 4 shows the debt service requirements on the Series 2014 Bonds and the Outstanding Bonds.

**Table 4**  
**Norman Y. Mineta San José International Airport**  
**Airport Revenue Bonds Debt Service Requirements**

<b>Fiscal Year Ended June 30</b>	<b>Series 2014 Bonds Debt Service Requirements</b>			<b>Airport Revenue Bonds Debt Service Requirements</b>	
	<b>Principal Requirements on Series 2014 Bonds</b>	<b>Interest Requirements on Series 2014 Bonds</b>	<b>Total Debt Service on Series 2014 Bonds</b>	<b>Total Debt Service Requirements on Outstanding Bonds<sup>*†</sup></b>	<b>Total Debt Service Requirements on All Bonds<sup>†</sup></b>
2015	\$1,025,000	\$2,486,724	\$3,511,724	\$88,808,026	\$92,319,750
2016	140,000	6,206,560	6,346,560	89,105,226	95,451,786
2017	95,000	6,203,760	6,298,760	89,423,164	95,721,924
2018	50,000	6,201,860	6,251,860	89,764,711	96,016,571
2019	6,885,000	6,200,860	13,085,860	80,298,123	93,383,983
2020	7,020,000	5,856,610	12,876,610	80,656,033	93,532,643
2021	7,655,000	5,505,610	13,160,610	81,021,595	94,182,205
2022	7,765,000	5,122,860	12,887,860	81,395,835	94,283,695
2023	8,475,000	4,735,010	13,210,010	81,772,943	94,982,953
2024	8,925,000	4,311,260	13,236,260	82,168,860	95,405,120
2025	9,175,000	3,866,710	13,041,710	82,562,948	95,604,658
2026	8,115,000	3,407,960	11,522,960	82,977,848	94,500,808
2027	16,960,000	3,011,325	19,971,325	75,588,198	95,559,523
2028	18,025,000	2,163,325	20,188,325	76,016,975	96,205,300
2029	8,035,000	1,262,075	9,297,075	92,821,080	102,118,155
2030	8,440,000	860,325	9,300,325	93,573,378	102,873,703
2031	8,860,000	438,325	9,298,325	93,969,975	103,268,300
2032	-	-	-	104,925,440	104,925,440
2033	-	-	-	138,623,263	138,623,263
2034	-	-	-	138,686,875	138,686,875
2035	-	-	-	137,505,185	137,505,185
2036	-	-	-	138,031,715	138,031,715
2037	-	-	-	138,572,335	138,572,335
2038	-	-	-	37,427,763	37,427,763
2039	-	-	-	37,935,095	37,935,095
2040	-	-	-	38,722,033	38,722,033
2041	-	-	-	39,325,615	39,325,615
2042	-	-	-	10,191,600	10,191,600
2043	-	-	-	10,190,500	10,190,500
2044	-	-	-	10,188,600	10,188,600
2045	-	-	-	10,189,400	10,189,400
2046	-	-	-	10,191,100	10,191,100
2047	-	-	-	10,191,900	10,191,900
<b>Totals</b>	<b>\$125,645,000</b>	<b>\$67,841,159</b>	<b>\$193,486,159</b>	<b>\$2,452,823,331</b>	<b>\$2,646,309,490</b>

*Source:* City of San José.

\* Debt Service on Outstanding Bonds after giving effect to the refunding and defeasance of the Refunded Bonds.

† The numbers may not total due to rounding.

## CERTAIN FACTORS AFFECTING THE AIRPORT

The following is a general discussion of certain factors that may affect activities at the Airport and does not purport to be an exhaustive listing of factors and other considerations affecting the Airport. There are other factors not discussed below, in the Appendices hereto or elsewhere in this Official Statement that may affect activities at the Airport.

### General Factors Affecting Airline and Passenger Activity

Future airline traffic at the Airport and demand for air travel will be affected by, among other things, the growth of or decline in the population and economy of the Air Service Area and by national, regional and international economic conditions, federal regulatory actions, airline service, air fare prices and operation of the national air traffic control system. In general, the price of air travel is, in turn, affected by the number of airlines serving a particular airport and a particular destination, the financial condition, cost structure, aircraft choices, hubbing strategies and route decisions of the airlines serving an airport, the willingness and ability of competing airlines to enter an airport market, the cost of operating at an airport, the price of fuel and any operating constraints (due to capacity, environmental concerns, noise restrictions and other related factors) limiting the frequency or timing of airport traffic within the national system or at a particular airport.

Reductions in airline traffic and/or shifts in airline traffic and market share at the Airport and financial difficulties at individual airlines could, over time, materially alter the relative financial obligations of the individual airlines operating at the Airport and lead to increases in per-passenger-mile costs of service and to reductions of service at the Airport. Factors which could have an adverse effect on air travel in the future include, but are not limited to, terrorist attacks, additional or continued military activities involving U.S. troops, outbreaks of illness, airline accidents, the availability of business travel substitutes including video conferencing and streaming technology, regulatory changes, rising fuel prices, continuing elevated levels of unemployment, turmoil in the capital markets or general weakness in the national, state, regional or local economy. See “—Uncertainties in the Air Service Area and — Uncertainties of the Airline Industry.”

**Possible Downtown High-Rise Development Impacts on Air Service.** Downtown San José is directly under the primary aircraft approach and departure paths for the Airport. Historically, in the review of proposed high-rise building projects, the City has relied upon the FAA’s issuance of a project-specific “No Hazard Determination” as the finding that the development would not adversely impact airspace or Airport operations. However, airlines must satisfy other, often more-restrictive, safety criteria mandated by the FAA (commonly referred to as “one engine inoperative” or “OEI” procedures) that may constrain their ability to economically operate due to high-rise buildings which, in turn, can impact City goals to retain or attract airline service. Because of the proximity of downtown San José to the Airport, further downtown high rise development could impact the Airport’s ability to attract more long-haul domestic and international service. In the event that obstructions in the takeoff path are too high, the airlines have to fly lighter aircraft or carry lighter loads (i.e. less fuel or fewer passengers) to be able to clear the obstructions with one engine inoperative. This, in turn, could adversely impact or preclude the air carriers’ ability to schedule long-haul flights (which typically require larger aircraft and more fuel) at the Airport. The City has been reviewing the potential impacts of OEI procedures for several years, and staff has considered but not yet proposed amendments to the City’s general plan to limit building heights downtown and in other parts of the City that are in the takeoff path. On April 28, 2014, the FAA issued a Notice of Proposed Policy regarding consideration of OEI flight procedures in evaluations of the potential aeronautical impact of obstructions. As indicated in the Notice of Proposed Policy, the FAA proposes to establish a new policy that would enable airport sponsors, working with their airlines and other aircraft operator partners, to voluntarily define OEI departure surfaces. If defined, the FAA would treat OEI

surfaces in the same manner as the FAA No Hazard Determination, making objects under the OEI surface subject to the full scope of FAA No Hazard Determination notification and airspace determination requirements. The City currently cannot predict the impact of either further downtown high-rise development or implementation of proposed FAA OEI regulations on future air service at the Airport.

## **Uncertainties in the Air Service Area**

Approximately 98.0% of the enplaned passengers at the Airport are O&D passengers as opposed to passengers connecting through the Airport to other cities. As described in Appendix A, air traffic at the Airport is thus dependent upon the economy of the Airport's Air Service Area as well as on the route decisions and financial condition of individual airlines. Although the Airport's six-county Air Service Area is large and has a relatively diversified socio-economic base, the economy in the Air Service Area depends in significant part upon the financial strength and stability of the software, technology and communications industries, and upon the success of major employers in the Air Service Area. A combination of the national credit crisis, aviation fuel cost spike, and global recession caused traffic to fall between fiscal years 2008-09 and 2009-10. Starting in fiscal year 2010-11, passenger traffic at the Airport began to recover and between fiscal year 2010-11 and fiscal year 2013-14, enplanements increased at a compound annual growth rate of 1.9%. Passenger enplanements at the Airport increased by approximately 6.7% between fiscal years 2012-13 and 2013-14. No assurance can be given that the passenger traffic at the Airport will continue to grow or that the current enplanement levels will be maintained. Reduced demand for air travel in and out of the Air Service Area could also result in fewer airlines serving the Airport. See "AIRPORT FINANCIAL MATTERS—Historical Operating Results" in Appendix A.

## **Competition**

The Airport competes for passengers and cargo with San Francisco International Airport ("SFO"), approximately 34 miles northwest of the Airport, and with Oakland International Airport ("OAK"), approximately 36 miles north of the Airport. These three airports serve the entire 12-County Area, ranging from Sonoma County to the north and Monterey County to the south. Both the Airport and OAK serve predominately domestic O&D traffic, while SFO is considered the Bay Area's international gateway, serving as the primary point of departure and arrival for international passengers. Given the relatively close proximity of all of the Bay Area airports, passengers are willing to utilize any of the three airports in the region, which spurs competition between the Airport, SFO and OAK to capture passenger activity market share. A smaller commercial service airport that services portions of the Air Service Area, Monterey Peninsula Airport, is approximately 75 driving miles from the Airport.

***California High Speed Rail.*** The California High Speed Rail Authority (the "CHSR Authority") is pursuing a statewide, high speed rail system in California linking Los Angeles to the San Francisco Bay Area, with a proposed station to be located in the City. The CHSR Authority has indicated it will pursue a phased implementation of service. Groundbreaking on the first phase of the project (Merced to Fresno) is expected to take place in early fall of 2014. The CHSR Authority has a schedule that would complete all necessary work to operate trains between San Francisco and Los Angeles by 2029. The CHSR Authority has stated that it plans to price its rail fares below air fares.

The City is unable to predict if or when a statewide, high speed rail system will become operational between the San Francisco Bay Area, the City and Los Angeles, or what effect such rail system would have, if any, on passenger traffic at the Airport or its revenues.

## **Uncertainties of the Airline Industry**

The airline industry is highly cyclical and is characterized by intense competition, high operating and capital costs and varying demand. Passenger and cargo volumes are highly sensitive to general and localized economic trends, and passenger traffic varies substantially with seasonal travel patterns. The profitability of the airline industry can fluctuate dramatically from quarter to quarter and from year to year, even in the absence of catastrophic events such as the terrorist attacks of September 11, 2001 and the economic recession of 2008 and 2009.

Since 2001, the global airline industry has undergone substantial structural changes and has sustained significant financial losses. Airlines continue to face significant challenges. Due to the discretionary nature of business and personal travel spending, airline passenger traffic and revenues are heavily influenced by the state of the U.S. economy, other regional and world economies, corporate profitability, fuel prices, security concerns and other factors. Structural changes to the industry also result from the impact of low cost carriers, internet travel web sites and carriers reorganizing under the U.S. Bankruptcy Code. A number of airlines serving the Airport have filed for bankruptcy in the past ten years, and most of these airlines have emerged from bankruptcy and continue to operate at the Airport. See “—Bankruptcy Risks—Airline or Other Tenant Bankruptcies.”

Over the last six years, the airline industry has seen a significant amount of consolidation. Four examples of this consolidation are the mergers between Delta Airlines and Northwest Airlines (“Delta Airlines”) in 2008, United Airlines and Continental Airlines (“United Airlines”) in 2010, Southwest Airlines and AirTran Airways (“Southwest Airlines”) in 2011, and American Airlines and US Airways (“American Airlines Group”) in 2013. The City does not expect a reduction in service at the Airport as a result of any of these mergers. See “—Bankruptcy Risks—Airline or Other Tenant Bankruptcies.”

Market conditions may limit further most of the airlines’ access to additional financing if their existing sources of funds are exhausted. Business conditions within the airline industry, such as increases in fuel and other costs and aging aircraft fleets, together with increased competition from airlines that shed debt and other obligations in bankruptcy, among other factors, could adversely affect the ability of some of the airlines that serve the Airport to meet their financial obligations to the City. Such conditions are generally beyond the control of the City and, in some cases, the airlines. For example, after rising through most of the last decade, jet fuel spot prices declined in late 2008 and early 2009. Jet fuel spot prices began rising again in 2010 and continued to rise through the first half of 2011 before leveling off in August. From the middle of 2011 to March of 2014, the spot prices of jet fuel have been somewhat level, with monthly price fluctuations of less than 10%. Political instability in Ukraine pushed up jet fuel prices in early 2014 and may continue to impact the future fuel prices. These and other market conditions could in the future result in additional airline bankruptcies, the inability of other weakened airlines to take over routes abandoned by a faltering airline, increased airline concentration at the Airport and a restructuring of the airline industry.

Other business decisions by airlines, such as abandoning domestic routes in favor of fewer but more lucrative international routes, increasing the use of smaller, regional jets and changing hubbing strategies, have also affected air traffic at the Airport and could have a more pronounced effect in the future. Although the Airline Lease Agreement permits the City to adjust rental rates and landing fees to take into account amounts that go unpaid by a defaulting airline, no assurance can be given that the non-defaulting airlines will continue to serve the Airport and to pay the higher rates and fees.

## **Bankruptcy Risks**

The rights of the owners of the Bonds and the enforceability of the City's obligation to make payments on the Bonds may be subject to bankruptcy, insolvency, reorganization, moratorium and similar laws affecting creditors' rights under existing law or under laws enacted in the future and may also be subject to the exercise of judicial discretion under certain circumstances. The opinions of Bond Counsel and of the City Attorney as to the enforceability of the obligations of the City will be qualified as to bankruptcy and similar events and as to the application of equitable principles and the exercise of judicial discretion in appropriate cases and to common law and statutes affecting the enforceability of contractual obligations generally and to principles of public policy concerning, affecting or limiting the enforcement of rights or remedies against governmental entities such as the City.

***Airline or Other Tenant Bankruptcies.*** A bankruptcy of an airline or of another tenant or tenants operating at the Airport could result in delays or reductions in payments on the Bonds.

The automatic stay provisions of the United States Bankruptcy Code (the "Bankruptcy Code") could prevent (unless approval of the bankruptcy court were obtained) any action to collect any amount owing by the airline or other tenant to the City or any action to enforce any obligation of the airline or other tenant to the City. With the authorization of the bankruptcy court, the airline or other tenant may be able to repudiate some or all of its agreements with the City and stop performing its obligations (including payment obligations) under such agreements. Such a repudiation could also excuse the other parties to such agreements from performing any of their obligations. The airline or other tenant may be able, without the consent and over the objection of the City, the Trustee and the Owners of the Bonds, to alter the terms, including the payment terms, of its agreements with the City, so long as the bankruptcy court determines that the alterations are fair and equitable. In addition, with the authorization of the bankruptcy court, the airline or other tenant may be able to assign its rights and obligations under any of its agreements with the City to another entity, despite any contractual provisions prohibiting such an assignment. The Trustee and the Owners of the Bonds also may be required to return to the airline or other tenant, as preferential transfers, any money that was used to make payments on the Bonds and that was received by the City or the Trustee from the airline or other tenant during the 90 days immediately preceding the filing of the bankruptcy petition. Claims by the City under any lease with the airline or other tenant may be subject to limitations.

As described in Appendix A, airlines that serve the Airport are required not only to make payments under various agreements with the City but also to pay to the City the PFCs collected from passengers on behalf of the City. An airline is likely to be in possession of PFCs at the time it goes into bankruptcy. Although there are provisions in the law requiring airlines to treat PFCs as trust funds, the application of these provisions in a bankruptcy case is not clear. The airline may not be required to turn over to the City or to the Trustee any PFCs in its possession at the time it goes into bankruptcy. Even while the airline is in bankruptcy, it may not be required to turn over PFCs that are collected prior to the time that the City or the Trustee demands the turnover of the PFCs. Even after a demand is made, it is possible that the airline would not be required to turn over subsequently-collected PFCs. See "AIRPORT FINANCIAL MATTERS—Passenger Facility Charges" in Appendix A for a discussion of other factors concerning PFC Revenues.

A number of rental car companies that operate at the Airport have also been the subject of bankruptcy proceedings. As described in Appendix A (see "LEASE AND OPERATING AGREEMENTS—Parking, Rental Car, Concession and Other Agreements—Rental Car Agreements"), in addition to lease and other payments, the rental car companies operating at the Airport remit CFCs to the Airport. Under the Master Trust Agreement, CFC Revenues are excluded from the definition of "General Airport Revenues" and are not pledged, but may be used, to pay debt service on certain series of the

Bonds. The Airport has applied, and expects to continue to apply, CFC Revenues to the repayment of the Series 2011B Bonds. A rental car company may owe current or future lease payments to the Airport and is likely to be in possession of CFCs at the time it goes into bankruptcy. Although there are provisions in the agreements between the City and the rental car companies requiring the rental car companies to treat CFCs as trust funds, the enforceability and application of these provisions in a bankruptcy case is not clear. A rental car company in bankruptcy may not be required to turn over to the City or to the Trustee any CFCs in its possession at the time it goes into bankruptcy. Even while the rental car company is in bankruptcy, it may not be required to turn over CFCs that it collects to the City or the Trustee.

There could be delays in payments on the Bonds, including the Series 2014 Bonds, while the court considers any of these and other issues. There may be other effects of a bankruptcy of an airline or other tenant that could result in substantial delays or in reductions in payments to the holders of the Bonds, including the Series 2014 Bonds. Regardless of any specific adverse determinations in a bankruptcy proceeding, a bankruptcy proceeding could have an adverse effect on the liquidity and value of the Bonds, including the Series 2014 Bonds.

***City Bankruptcy.*** The City is authorized under California law to file for bankruptcy protection under Chapter 9 of the United States Bankruptcy Code (the “Bankruptcy Code”). However, third parties cannot bring involuntary bankruptcy proceedings against the City. The Airport, being a department of the City, cannot itself file for bankruptcy protection. Should the City file for bankruptcy, there could be adverse effects on the holders of the Series 2014 Bonds.

If the General Airport Revenues are “special revenues” under the Bankruptcy Code, then General Airport Revenues collected after the date of the bankruptcy filing should be subject to the lien of the Master Trust Agreement. “Special revenues” are defined in the Bankruptcy Code to include receipts derived from the ownership or operation of projects or systems that are primarily used to provide transportation services. While the General Airport Revenues appear to satisfy this definition and thus should be “special revenues,” no assurance can be given that a court would not hold that the General Airport Revenues are not “special revenues.” If the General Airport Revenues are determined to not be “special revenues,” then General Airport Revenues collected after the commencement of the bankruptcy case will likely not be subject to the lien of the Master Trust Agreement. The holders of the Series 2014 Bonds may not be able to assert a claim against any property of the City or the Airport other than the General Airport Revenues, and if these amounts are no longer subject to the lien of the Master Trust Agreement, then there may be no amounts from which the holders of the Series 2014 Bonds are entitled to be paid.

The Bankruptcy Code provides that “special revenues” can be applied to necessary operating expenses of the project or system, before they are applied to other obligations. This rule applies regardless of the provisions of the transaction documents. Thus, the City may be able to use General Airport Revenues to pay necessary operating expenses of the Airport, before the remaining General Airport Revenues are turned over to the Trustee to pay amounts owed to the holders of the Series 2014 Bonds. It is not clear precisely which expenses would constitute necessary operating expenses.

If the City is in bankruptcy, parties (including the holders of the Series 2014 Bonds) may be prohibited from taking any action to collect any amount from the City or to enforce any obligation of the City, unless the permission of the bankruptcy court is obtained. These restrictions may also prevent the Trustee from making payments to the holders of the Series 2014 Bonds from funds in the Trustee’s possession. The rate covenant may not be enforceable in bankruptcy by the Trustee or the holders of the Series 2014 Bonds.

The City is permitted to hold General Airport Revenues for up to one year before transferring General Airport Revenues to the Trustee. If the City goes into bankruptcy, the City may not be required to turn over to the Trustee any General Airport Revenues that are in its possession at the time of the bankruptcy filing and have been commingled with other moneys. If the City has possession of General Airport Revenues (whether collected before or after commencement of the bankruptcy) and if the City does not voluntarily turn over such General Airport Revenues to the Trustee, it is not entirely clear what procedures the Trustee and the holders of the Series 2014 Bonds would have to follow to attempt to obtain possession of such General Airport Revenues, how much time it would take for such procedures to be completed, or whether such procedures would ultimately be successful. Under such circumstances, there may be delays or reductions in payments on the Series 2014 Bonds.

Under the Bankruptcy Code, the City may be able to borrow additional money that is secured by a lien on any of its property (including the General Airport Revenues), which lien could have priority over the lien of the Master Trust Agreement, as long as the bankruptcy court determines that the rights of the Trustee and the holders of the Series 2014 Bonds will be adequately protected. The City may be able to cause some of the General Airport Revenues to be released to it, free and clear of lien of the Master Trust Agreement, as long as the bankruptcy court determines that the rights of the Trustee and the holders of the Series 2014 Bonds will be adequately protected.

Under the Bankruptcy Code, the City may be able, without the consent and over the objection of the Trustee and the holders of the Series 2014 Bonds, to alter the principal, priority, interest rate, payment terms, collateral, maturity dates, payment sources, covenants (including tax-related covenants), and other terms or provisions of the Master Trust Agreement and the Series 2014 Bonds, as long as the bankruptcy court determines that the alterations are fair and equitable.

### **Information Concerning the Airlines**

The City makes no representation as to the business operations, financial condition or future viability of any airline and makes no representation about the filings referred to below.

The principal domestic airlines, or their respective parent corporations, and foreign airlines with American Depository Receipts (“ADRs”) registered on a national exchange are subject to the information requirements of the Securities Exchange Act of 1934, as amended, and in accordance therewith file reports and other information with the Securities and Exchange Commission (the “SEC”). Certain information, including financial information, concerning such domestic airlines or their respective parent corporations and such foreign airlines, is disclosed in certain reports and statements filed with the SEC. Such reports and statements can be inspected at the Public Reference Room of the SEC, 100 F Street, N.E., Washington, D.C. 20549, and at the offices of The New York Stock Exchange, Inc., 20 Broad Street, New York, New York 10005 (for certain airlines whose stock or whose parent’s stock is traded on the New York Stock Exchange). Copies of such reports and statements can be obtained from the Public Reference Section of the SEC at 100 F Street, N.E., Washington, D.C. 20549, at prescribed rates or from the SEC website at <http://www.sec.gov>. In addition, each airline is required to file periodic reports of financial and operating statistics with the Department of Transportation. Such reports can be inspected at the Bureau of Transportation Statistics, Research and Innovative Technology Administration, Department of Transportation, 1200 New Jersey Avenue, SE, Washington, D.C. 20590.

Airlines owned by foreign governments, or foreign corporations operating airlines (unless such airlines have ADRs registered on a national exchange), are not required to file information with the SEC. Airlines owned by foreign governments, or foreign corporations operating airlines, file limited information only with the United States Department of Transportation.

## **Regulatory Uncertainties**

**General.** As described in Appendix A, development at the Airport is regulated extensively by the City and by the State of California and requires a number of reviews and permits. Operations and development at the Airport are also subject to extensive federal oversight. The City operates the Airport pursuant to an airport operating certificate issued annually by the FAA after on-site review. In addition to this operating certificate, the Airport is required to obtain other permits and/or authorizations from the FAA and from other regulatory agencies and is bound by contractual agreements included as a condition to receiving grants under the federal Airport Improvement Program. All long-term planning and development is subject to the FAA's approval; outside audits of the Airport's financial statements are subject to periodic audits by the FAA; the City's use of Airport revenues, which is generally limited to airport-related purposes, is subject to audit and review by the FAA; and the City's use of PFC Revenues and grant proceeds is also subject to approval, audit and review. See "AIRPORT FINANCIAL MATTERS—Federal Grants" and "—Passenger Facility Charges" and "LITIGATION" in Appendix A.

The Airport is also subject to regulation and mandates by the Transportation Security Administration (the "TSA") as required by the Federal Aviation and Transportation Security Act. As described in Appendix A, the TSA has required the Airport to implement additional security-related projects and may in the future require the Airport to implement additional security-related projects, but the timing, scope and source of funding of such projects cannot be predicted. See "AIRPORT FINANCIAL MATTERS—Federal Security Grants—Aviation Security Act" in Appendix A.

**Rates and Charges Regulation.** The Federal Aviation Administration Authorization Act of 1994, as amended (the "1994 Act") and FAA regulations require that an airport maintain a rate structure that is as "self-sustaining" as possible and limit the use of all revenue generated by an airport receiving federal financing assistance (including local taxes on aviation fuel and other airport-related receipts) to purposes related to the airport. The statutes and regulations provide that for all airports, with certain exceptions, the use of airport revenue for purposes other than the capital or operating costs of the airport, the local airport system or other local facilities owned or operated by the airport owner or operator and directly and substantially related to the air transportation of passengers or property is unlawful revenue diversion and provide for monetary penalties and other remedies in the event of violations.

The 1994 Act also provides that without air carrier approval, an airport may not include in its rate base debt service allocable to projects not yet completed and in service. Section 113 of the 1994 Act ("Section 113") requires that airport fees be "reasonable" and provides a mechanism by which the Secretary of Transportation can review rates and charges complaints brought by air carriers. Section 113 specifically states that its provisions do not apply to (a) a fee imposed pursuant to a written agreement with air carriers using airport facilities, (b) a fee imposed pursuant to a financing agreement or covenant entered into prior to August 23, 1994, the date of enactment of Section 113, or (c) any other existing fee not in dispute as of August 23, 1994.

The 1994 Act also mandates an expedited administrative process by which the Secretary of Transportation is required to review rates and charges complaints brought by airlines. In January 1995, the U.S. Department of Transportation, acting through the FAA, issued its final rule outlining the procedures to be followed in determining the reasonableness of new fees or fee increases imposed on airlines and in June 1996, issued a policy statement (the "Policy Statement") setting forth the standards that the U.S. Department of Transportation will use in determining the reasonableness of the fees charged to airlines and other aeronautical users.

On August 1, 1997, the U.S. Court of Appeals to the District of Columbia Circuit in a case brought by the Air Transport Association vacated and remanded the Policy Statement to the Secretary of

the U.S. Department of Transportation for reconsideration of the standards set forth in the Policy Statement. On October 15, 1997, the U.S. Court of Appeals amended its previous order to vacate only certain sections of the Policy Statement, including sections relating to valuation of the airfield, permissible components of the airfield rate base, use of any “reasonable methodology” for valuation of non-airfield assets and recovery of imputed interest in the airfield rate base. In February 2003, the FAA withdrew its advance notice of proposed policy regarding rates and charges and has not issued further guidance. In September 2013, the FAA, in conjunction with the U.S. Department of Transportation, held three meetings with aviation industry participants (airports, airlines and consultants) seeking both historical and forward-looking feedback regarding industry developments and practices to assist the FAA in its comprehensive review of its current rates and charges policy and whether revisions or other future actions may be necessary. The City cannot determine at this time when or whether new guidelines will be published, the costs that will be permitted to be included in determining an airport’s rate base and/or the extent to which such future guidelines may limit the City’s flexibility in negotiating airline agreements or in setting rates and charges by resolution or ordinance for use of the Airport’s facilities. Any new federal legislation or other federal guidelines or any standards promulgated by a court in connection with a dispute could limit substantially the amounts and/or allocation of costs payable by airlines serving the Airport. In establishing any new rates and charge methodology for the Airport, the City intends to comply with federal law and with the Rate Maintenance Covenant contained in the Master Trust Agreement.

There is currently no dispute between the City and any of the air carriers over any existing rates and charges or the Airline Lease Agreement. No assurances can be given that disputes will not arise in the future. See “LEASE AND OPERATING AGREEMENTS” and “AIRPORT FINANCIAL MATTERS—Management Discussion of Recent Financial Results” in Appendix A.

### **Availability of Funding From PFC Revenues and CFC Revenues**

The amount of PFC Revenues received by the City in future years will vary based upon the actual number of PFC-eligible passenger enplanements at the Airport and the level of the PFC. No assurance can be given that any level of enplanements will be realized or that the level of PFC the City may impose will not change. A shortfall in PFCs may require the City to increase rates and charges at the Airport to meet the debt service requirements on the Bonds, and/or require the City to identify other sources of funding for the payment of debt service.

Additionally, under current law the FAA may terminate the City’s authority to impose PFCs, subject to informal and formal procedural safeguards, if (a) PFC Revenues are not being used for approved projects in accordance with the FAA’s approval, the statutes authorizing the PFC or the regulations promulgated thereunder, or (b) the City otherwise violates such statutes or regulations. The City’s authority to impose PFCs may also be terminated if the City violates certain provisions of the Airport Noise and Capacity Act of 1990 (“ANCA”) and its implementing regulations relating to the implementation of noise and access restrictions for certain types of aircraft. The regulations under ANCA also contain procedural safeguards to ensure that the City’s authority to impose PFCs will not be summarily terminated. No assurance can be given that the City’s authority to impose PFCs will not be terminated by Congress or the FAA, that the PFC program will not be modified or restricted by Congress or the FAA so as to reduce PFC Revenues available to the City or that the City will not seek to decrease the amount of PFCs to be collected. In the event the FAA or Congress reduced or terminated the City’s ability to impose PFCs or reduced or eliminated the FAA’s grant program or the size of the grants the City could receive, the City may need to increase rates and charges at the Airport to meet the debt service requirements on the Bonds. See “—Regulatory Uncertainties—Rates and Charges Regulation” above.

CFC Revenues are currently applied to pay debt service on the Series 2011B Bonds. See “AIRPORT FINANCIAL MATTERS—Customer Facility Charges” in Appendix A for a discussion of CFC Revenues. No assurance can be given that the City’s authority to impose CFCs will not be affected by future legislation or by future legal challenges so as to reduce CFC Revenues available to the City or that the City will not seek to decrease the amount of CFCs to be collected. To the extent that the City’s authority to impose CFCs were reduced or eliminated, or the City decided to decrease the amount of CFCs it collects from customers of the rental car companies, the lease payments that rental car companies are required to make in connection with their operations at the Consolidated Rental Car Facility (the “ConRAC”) would increase pursuant to the lease agreements entered into with the rental car companies. No assurance can be given, however, that such increases would be sufficient to avoid the City needing to increase other rates and charges, including Facility Rent for the rental car companies, at the Airport to meet the debt service requirements on the Bonds.

## **Seismic Hazards**

According to the safety element of the City’s “2040 General Plan” (the “General Plan”), the City, including the Airport, is located in a region of very high seismic activity. There are several geological faults in the greater San Francisco Bay Area that have the potential to cause serious earthquakes which could result in damage to buildings, roads, bridges, and property within the City. The Airport is located within 6 to 12 miles of the San Andreas Fault, the Hayward Fault and the Calaveras Fault, which are known to be active earthquake faults and pose the greatest potential for surface rupture in the Bay Area. The City has experienced at least nine recorded earthquakes with a Richter scale magnitude of 6.0 or greater, and with the epicenter located within the Bay Area. The South Napa earthquake with a Richter scale magnitude of 6.0 according to the U.S. Geological Survey (“USGS”), occurred on August 24, 2014; however little or no damage was reported in the City and no damage occurred at the Airport. Prior to the South Napa earthquake, the City experienced the Loma Prieta earthquake on October 17, 1989 which had a Richter scale magnitude of 6.9 according to the USGS.

The seismic risks to a structure are dependent upon several factors, including the distance of the structure from the active fault, the character of the earthquake, the nature of construction of the structure, and the geologic conditions underlying the structure. Ground surface rupture tends to occur along lines of previous faulting, where fault displacement intersects the ground surface. Displacement may either occur suddenly during an earthquake or it may occur slowly as the fault “creeps” over a long period of time. Pursuant to applicable state law, the California Geological Survey has prepared maps to identify certain areas as liquefaction hazard zones. “Liquefaction” is the transformation of soil from a solid state to a liquid state during a major earthquake, and liquefaction hazard zones are areas where historic occurrence of liquefaction or local geological, geotechnical and ground water conditions indicate a potential for permanent ground displacements during a major earthquake. According to the most recent published maps prepared by the California Geological Survey, the Airport is located within an area subject to a high potential for liquefaction during a major earthquake.

The Airport and its then existing facilities remained open after the Loma Prieta earthquake. Terminal A has been designed and inspected in accordance with the “essential facility” standards of the 1985 Uniform Building Code (the “UBC”). This standard means that Terminal A has been designed with a higher force factor, to a seismic factor of 1.5, as compared to non-essential facilities constructed to a seismic factor of 1.0. An “essential facility,” as defined by the UBC, is a structure which must remain operational for emergency post-earthquake operations. Terminal A sustained no damage during the Loma Prieta earthquake. At the time of the Loma Prieta earthquake, Terminal A was nearing completion and was not yet occupied. Terminal B and its concourse, substantially completed in June 2010, were designed and constructed in accordance with the California Building Code, 2001 Edition.

Because the Airport is located within an area of active earthquake faults, the possibility does exist for operations at the Airport to be disrupted or for facilities at the Airport to be damaged by a strong earthquake. The Master Trust Agreement does not require earthquake insurance on the Airport facilities, and the City does not currently carry a policy of earthquake insurance. All Airport facilities, however, are designed and constructed in accordance with applicable state and local building codes, with stringent requirements for earthquake resistant design.

### **Natural Gas Transmission Pipelines**

On September 9, 2010, a Pacific Gas and Electric Company (“PG&E”) high pressure natural gas transmission pipeline exploded in San Bruno, California, with catastrophic results. In a final Pipeline Accident Report, adopted by the National Transportation Safety Board (the “NTSB”) on August 30, 2011, the NTSB found recurring deficiencies in PG&E’s pipeline integrity management program, which the NTSB concluded were evidence of a systemic problem. There are numerous similar pipelines owned, operated and maintained by PG&E located throughout the City. In the immediate vicinity of the Airport, publicly available information on PG&E’s website ([www.pge.com](http://www.pge.com)) indicates that the three closest transmission level gas pipelines are approximately 1,200 to 4,000 feet from the Airport’s property lines, but that there are 4 inch and 6 inch gas mains on Airport Boulevard. PG&E’s website also provides information regarding its high pressure natural gas transmission pipelines and its long range natural gas transmission pipeline planning. PG&E has also indicated that it considers the proximity of its natural gas transmission pipelines to high density populations, potential reliability impacts and environmentally sensitive areas, and uses the data it collects to help plan and prioritize future work on its pipelines.

The effects of any failure of the high pressure natural gas transmission pipelines closest to the Airport or the gas mains on Airport Boulevard are difficult to predict, but could include explosion and concussive force, fire, smoke, transportation delays and detours on routes to and from the Airport, and potential forced evacuation of nearby structures. However, given the distance and the significant infrastructure separating PG&E’s transmission pipelines from Airport facilities, it is anticipated that no immediate damage to the Airport would result from such a failure. In addition, any ancillary effects on transportation routes would in part be mitigated by the fact that the Airport has three entrances, and traffic could be rerouted should one entrance be impacted by such a failure. Finally, smoke from fires could impact air traffic depending on intensity and wind direction.

The City is not able to independently confirm the information set forth above or the information contained in the NTSB’s Pipeline Accident Report or on the PG&E website, including the exact distances of any high pressure transmission lines from Airport facilities, and can provide no assurances as to the accuracy or completeness of such information. Information available in the NTSB’s Pipeline Accident Report and from PG&E’s website is not part of this Official Statement nor has such information been incorporated by reference herein, and should not be relied upon in making an investment decision with respect to the Series 2014 Bonds. Further, the City can provide no assurances as to the condition of PG&E pipelines and other facilities in the City, or predict the extent of the damage to the surrounding property that would occur if a PG&E pipeline located within the City were to experience any type of failure, including a possible fire or explosion.

### **Flooding**

The City and the Santa Clara Valley have a history of flooding due to heavy rain and inadequate storm drains and flood protection conveyance systems, which has resulted in property damage. The Santa Clara Valley Water District (the “District”) is responsible for flood protection infrastructure in Santa Clara County on streams and waterways. The District coordinates flood hazard mitigation efforts for the

major creeks and waterways in the City and assists the City in the review of development proposals that could impact flood protection efforts.

The Federal Emergency Management Agency (“FEMA”) oversees the delineation of flood zones. FEMA publishes Flood Insurance Rate Maps (“FIRMs”) that show the expected frequency and severity of flooding by area, typically for the existing land use and drainage/flood control facilities. The maps prepared by FEMA for the San José area indicate that during a 100-year flood event (area subject to a flood that has a one percent chance of being equaled or exceeded in any given year), sections of the City would be subject to flooding from creek overbanking, inadequate storm drains and levees or inundation from the San Francisco Bay. Approximately 20,000 parcels in the City are within the 100-year flood hazard area established by FEMA. This represents approximately 10 percent of the total number of properties within the City. This can be extrapolated to estimate that roughly 10 percent of the area of the City may be inundated by flood waters of at least one foot in depth.

The Guadalupe River channel on the east side of the Airport is designated on the FEMA maps as Zone A (areas of 100-year flood). In June 2005, the District informed the City of the completion of the Guadalupe River flood control improvements which removed a majority of the Airport from the 100-year flood zone. Additionally, the Airport has completed construction of airfield improvements and Airport Master Plan EIR mitigation measures designed to accommodate runoff from a 100-year flood event. The majority of the central, northern and eastern portions of the Airport are located in an area designated by FEMA as Zone X while some portions are in Zone AH. According to FEMA, Zone X is the flood insurance rate zone that corresponds to the areas of moderate or minimal flood hazard. Zone AH is used in areas subject to inundation by 1-percent-annual-chance shallow flooding (usually areas of ponding) where average depths are between one and three feet. The western portion of the Airport is in an area designated by FEMA as Zone D. The Zone D designation is used for areas where there are possible but undetermined flood hazards. In areas designated as Zone D, no analysis of flood hazards have been conducted.

The District is also responsible for several dams located upstream of the City. In a catastrophic event, damage to one or more of these dams could result in flooding within the City as shown on inundation maps originally prepared by the District in the early 1970's (the map for Lenihan Dam was further updated in the mid 1990's and the map for Anderson Dam updated in 2009). These inundation maps are on file with the California Emergency Management Agency and with the City.

The District has commenced seismic stability studies on eight of the District's dams. On July 6, 2011, the District issued a press release announcing the results of a seismic study of the Anderson Dam, an earth and rockfill structure constructed in 1950, which concluded that the dam could be affected by a major earthquake with a magnitude of 7.25 on the Calaveras Fault within two kilometers of the dam. The study further stated that the analysis found loosely compacted layers of liquefiable materials in the foundation of the dam. These materials are susceptible to a reduction in strength when subjected to severe earthquake shaking. If the foundation were damaged, part of the dam could experience 15 to 25 feet of vertical deformation, with an additional 15 feet of potential cracking. The study stated that if the reservoir were full at the time, there could be an uncontrolled release of water. As a result, the District's dam operators have established a policy to keep the water at no higher than 45 feet below the dam crest. Although the chances are very remote, a complete failure of the Anderson Dam could send a wall of water 35 feet high into downtown Morgan Hill in 14 minutes, and 8 feet deep into San José within three hours.

In response to the study, the District initiated a project to retrofit the Anderson Dam. The planning phase of the Anderson Dam Seismic Retrofit project has been completed and currently the project is in the early part of the engineering design phase. The project is scheduled for completion in

fiscal year 2019-20 at an estimated cost of \$200 million. The Anderson Dam is regulated by the State of California Division of Safety of Dams, which performs yearly reviews and requires maintenance and safety standards to be enforced by the dam owners and operators. Additionally, the Federal Energy Regulatory Commission has dam safety jurisdiction at the Anderson Dam.

On October 26, 2011, the District announced preliminary findings from a seismic study indicating that its Calero and Guadalupe dams could be subject to significant damage if a major earthquake occurred near either dam. In response to these preliminary findings, the District has further restricted reservoir levels at the Calero and Guadalupe dams. Failure of either of these two dams would impact the City, but it is not anticipated that the water released would reach the Airport. In 2012, the District initiated a project to retrofit Calero and Guadalupe Dams. The planning phase of the project is currently underway. The design phase of the project is expected to commence in 2015. Construction of these two dam retrofit projects is scheduled for completion in fiscal year 2019-20 at an estimated cost of \$92 million.

Reports or studies were completed for the Almaden Dam in October 2012, the Lenihan Dam in December 2012, and the Stevens Creek Dam in December 2013, that concluded that the dams are in suitable condition and that no retrofit work is required. The District continues to work with the State of California Division of Safety of Dams to study seismic stability of its other dams and is adapting operations accordingly. Depending on the severity of flooding, flooding at the Airport could result in reduced operations at the Airport that could have a negative effect on the Airport's finances.

## RATINGS

The Series 2014 Bonds have been rated "A-", "A2" and "BBB+" by S&P, Moody's and Fitch, respectively. The ratings assigned by Moody's, S&P and Fitch reflect only the views of such organizations. The explanation of the significance of such ratings should be obtained from the rating agency furnishing the same. Generally, a rating agency bases its rating on the information and materials furnished to it and on investigations, studies and assumptions of its own. There is no assurance that such ratings will continue for any given period of time or that such ratings will not be revised downward or withdrawn entirely by the rating agencies, if in the judgment of such rating agencies, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Series 2014 Bonds. Neither the City nor the Underwriters have the obligation to contest any revision or withdrawal by the rating agencies of any such ratings.

## TAX MATTERS

In the opinion of Orrick, Herrington & Sutcliffe LLP, Bond Counsel to the City, based upon an analysis of existing laws, regulations, rulings and court decisions and assuming, among other matters, the accuracy of certain representations and compliance with certain covenants, interest on the Series 2014 Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 (the "Code") and is exempt from State of California personal income taxes, except that no opinion is expressed as to the status of interest on any Series 2014A Bond for any period that such Series 2014A Bond is held by a "substantial user" of the facilities refinanced by the Series 2014A Bonds or by a "related person" within the meaning of Section 147(a) of the Code. Bond Counsel observes that interest on the Series 2014A Bonds is a specific preference item for purposes of the federal individual and corporate alternative minimum taxes. In the further opinion of Bond Counsel, interest on the Series 2014B Bonds and Series 2014C Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when calculating federal corporate alternative minimum taxable income. Bond Counsel expresses no opinion regarding any other tax consequences related to the

ownership or disposition of, or the amount, accrual or receipt of interest on, the Series 2014 Bonds. A complete copy of the proposed form of opinion of Bond Counsel is set forth in Appendix E hereto.

To the extent that the issue price of any maturity of the Series 2014 Bonds is less than the amount to be paid at maturity of such Series 2014 Bonds (excluding amounts stated to be interest and payable at least annually over the term of such Series 2014 Bonds), the difference constitutes “original issue discount,” the accrual of which, to the extent properly allocable to each Beneficial Owner thereof, is treated as interest on the Series 2014 Bonds which is excluded from gross income for federal income tax purposes and State of California personal income taxes. For this purpose, the issue price of a particular maturity of the Series 2014 Bonds is the first price at which a substantial amount of such maturity of the Series 2014 Bonds is sold to the public (excluding bond houses, brokers or similar persons or organizations acting in the capacity of underwriters, placement agents or wholesalers). The original issue discount with respect to any maturity of the Series 2014 Bonds accrues daily over the term to maturity of such Series 2014 Bonds on the basis of a constant interest rate compounded semiannually (with straight line interpolations between compounding dates). The accruing original issue discount is added to the adjusted basis of such Series 2014 Bonds to determine taxable gain or loss upon disposition (including sale, redemption or payment on maturity) of such Series 2014 Bonds. Beneficial Owners of the Series 2014 Bonds should consult their own tax advisors with respect to the tax consequences of ownership of the Series 2014 Bonds with original issue discount, including the treatment of Beneficial Owners who do not purchase such Series 2014 Bonds in the original offering to the public at the first price at which a substantial amount of such Series 2014 Bonds is sold to the public.

The Series 2014 Bonds purchased, whether at original issuance or otherwise, for an amount higher than their principal amount payable at maturity (or, in some cases, at their earlier call date) (“Premium Bonds”) will be treated as having amortizable bond premium. No deduction is allowable for the amortizable bond premium in the case of bonds, like the Premium Bonds, the interest on which is excluded from gross income for federal income tax purposes. However, the amount of tax exempt interest received, and a Beneficial Owner’s basis in a Premium Bond, will be reduced by the amount of amortizable bond premium properly allocable to such Beneficial Owner. Beneficial Owners of Premium Bonds should consult their own tax advisors with respect to the proper treatment of amortizable bond premium in their particular circumstances.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the Series 2014 Bonds. The City has made certain representations and has covenanted to comply with certain restrictions, conditions and requirements designed to ensure that interest on the Series 2014 Bonds will not be included in federal gross income. Inaccuracy of these representations or failure to comply with these covenants may result in interest on the Series 2014 Bonds being included in gross income for federal income tax purposes, possibly from the date of original issuance of the Series 2014 Bonds. The opinion of Bond Counsel assumes the accuracy of these representations and compliance with these covenants. Bond Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken) or events occurring (or not occurring) or any other matters coming to Bond Counsel’s attention after the date of issuance of the Series 2014 Bonds may adversely affect the value of, or the tax status of interest on, the Series 2014 Bonds. Accordingly, the opinion of Bond Counsel is not intended to, and may not, be relied upon in connection with any such actions, events or matters.

Although Bond Counsel is of the opinion that interest on the Series 2014 Bonds is excluded from gross income for federal income tax purposes and is exempt from State of California personal income taxes, the ownership or disposition of, or the accrual or receipt of amounts treated as interest on, the Series 2014 Bonds may otherwise affect a Beneficial Owner’s federal, state or local tax liability. The nature and extent of these other tax consequences depends upon the particular tax status of the Beneficial

Owner or the Beneficial Owner's other items of income or deduction. Bond Counsel expresses no opinion regarding any such other tax consequences.

Future legislative proposals, if enacted into law, clarification of the Code or court decisions may cause interest on the Series 2014 Bonds to be subject, directly or indirectly, in whole or in part, to federal income taxation or to be subject to or exempted from state income taxation, or otherwise prevent Beneficial Owners from realizing the full current benefit of the tax status of such interest. For example, Representative Dave Camp, Chair of the House Ways and Means Committee released draft legislation that would subject interest on the Bonds to a federal income tax at an effective rate of 10% or more for individuals, trusts, and estates in the highest tax bracket, and the Obama Administration proposed legislation that would limit the exclusion from gross income of interest on the Bonds to some extent for high-income individuals. The introduction or enactment of any such future legislative proposals, clarification of the Code or court decisions may also affect – perhaps significantly, the market price for, or marketability of, the Series 2014 Bonds. Prospective purchasers of the Series 2014 Bonds should consult their own tax advisors regarding the potential impact of any pending or proposed federal or state tax legislation, regulations or litigation, as to which Bond Counsel is expected to express no opinion.

The opinion of Bond Counsel is based on current legal authority, covers certain matters not directly addressed by such authorities, and represents Bond Counsel's judgment as to the proper treatment of the Series 2014 Bonds for federal income tax purposes. It is not binding on the Internal Revenue Service ("IRS") or the courts. Furthermore, Bond Counsel cannot give and has not given any opinion or assurance about the future activities of the City, or about the effect of future changes in the Code, the applicable regulations, the interpretation thereof or the enforcement thereof by the IRS. The City has covenanted, however, to comply with the requirements of the Code.

Bond Counsel is not obligated to defend the City or the Beneficial Owners regarding the tax exempt status of the Series 2014 Bonds in the event of an audit examination by the IRS. Under current procedures, parties other than the City and their appointed counsel, including the Beneficial Owners, would have little, if any, right to participate in the audit examination process. Moreover, because achieving judicial review in connection with an audit examination of tax exempt bonds is difficult, obtaining an independent review of IRS positions with which the City legitimately disagrees, may not be practicable. Any action of the IRS, including but not limited to selection of the Series 2014 Bonds for audit, or the course or result of such audit, or an audit of bonds presenting similar tax issues may affect the market price for, or the marketability of, the Series 2014 Bonds, and may cause the City or the Beneficial Owners to incur significant expense.

## LITIGATION

There is no litigation now pending against the City with service of process accomplished or, to the knowledge, after due inquiry, of its Director of Finance, Director of Aviation or City Manager, threatened in writing, seeking to restrain or enjoin the issuance, sale, execution or delivery of the Series 2014 Bonds or contesting the validity of the Series 2014 Bonds or any proceedings of the City taken with respect to the issuance or sale thereof, or the pledge or application of any moneys or security provided for the payment of the Series 2014 Bonds or the use of the Series 2014 Bond proceeds. As described in "APPENDIX A—LITIGATION," a number of litigation matters relating to the Airport are pending against the City.

The City is not able to predict the outcome of this litigation, but does not believe that it will adversely impact the ability of the City to pay debt service on the Series 2014 Bonds.

## **LEGAL MATTERS**

The validity of the Series 2014 Bonds and certain other legal matters are subject to the approving opinion of Orrick, Herrington & Sutcliffe LLP, Bond Counsel to the City. Orrick Herrington & Sutcliffe LLP, as Bond Counsel, undertakes no responsibility for the accuracy, completeness or fairness of this Official Statement. Certain legal matters will be passed upon for the Underwriters by Kutak Rock LLP, Underwriters' Counsel, and for the City by the City Attorney. Certain legal matters will be passed upon for the City by Orrick, Herrington & Sutcliffe LLP, as Disclosure Counsel. All of the fees of Bond Counsel, Disclosure Counsel and Underwriters' Counsel with regard to the issuance of the Series 2014 Bonds are contingent upon the issuance and delivery of the Series 2014 Bonds.

## **CONTINUING DISCLOSURE**

The City has covenanted for the benefit of owners of the Series 2014 Bonds to provide certain financial information and operating data relating to the City and the Airport by not later than nine months after the end of the City's fiscal year (resulting in a deadline of March 31 of each year) beginning with the fiscal year ending June 30, 2014 (the "Annual Report") and to provide notices of the occurrence of certain enumerated events, in some cases only if such events material. The filing of the Annual Bond Disclosure Report or notices of material events will be made solely by transmitting such filing to the Municipal Securities Rulemaking Board pursuant to its Electronic Municipal Market Access ("EMMA") system as provided at <http://www.emma.msrb.org>. These covenants have been made to assist the Underwriters in complying with Securities Exchange Commission Rule 15c2-12(b)(5) (the "Rule"). For the specific nature of the information to be contained in the Annual Report or the notices of material events delivered by the City to provide certain information, see Appendix F. The Trustee has no obligation to enforce the undertakings of the City in the Continuing Disclosure Certificate, and a failure by the City to provide any information required thereunder shall not constitute an Event of Default under the Master Trust Agreement.

The City engaged third-party consultants to conduct an analysis of the City's historical compliance with its continuing disclosure obligations from fiscal year 2006-07 through July 31, 2014, during which the City was responsible for 45 bond issuances of the City, the City of San José Financing Authority, and the San José-Santa Clara Clean Water Financing Authority. During the five year period preceding the date of this Official Statement, the City failed to file, or file on a timely basis, notices of rating changes, or insurer-related rating changes or rating withdrawals with respect to numerous series of bonds, and the City failed to file on a timely basis notices of certain optional redemptions.

In a number of these instances, the City believes that these omissions were the result of human error; however, it is in the process of developing written procedures to address material compliance with its continuing disclosure undertakings in the future.

## **FINANCIAL ADVISORS**

The City has retained the services of Public Financial Management, San Francisco, California, and Public Resources Advisory Group, Oakland, California, as Financial Advisors in connection with the sale of the Series 2014 Bonds. The Financial Advisors are not obligated to undertake, and have not undertaken to make, an independent verification or to assume responsibility for the accuracy, completeness or fairness of the information contained in this Official Statement. All of the fees of the Financial Advisors with regard to the issuance of the Series 2014 Bonds are contingent upon the issuance and delivery of the Series 2014 Bonds.

## **UNDERWRITING**

### **Series 2014 Bonds**

The Series 2014 Bonds are being purchased from the City by Barclays Capital Inc., Fidelity Capital Markets, and RBC Capital Markets LLC (the “Underwriters”). The Underwriters have agreed to purchase the Series 2014 Bonds at a purchase price of \$144,520,060.35 (representing the aggregate principal amount of the Series 2014 Bonds of \$125,645,000.00, less an underwriting discount of \$316,234.20, plus a net original issue premium of \$19,191,294.55).

The Bond Purchase Agreement pursuant to which the Series 2014 Bonds are being sold (the “2014 Purchase Agreement”) provides that the Underwriters’ obligation to make such purchase is subject to certain terms and conditions set forth in the 2014 Purchase Agreement, the approval of certain legal matters by counsel and certain other conditions.

The Underwriters may offer and sell the Series 2014 Bonds to certain dealers and others at a price lower than the offering price stated on the inside cover hereof. The offering prices may be changed from time to time by the Underwriters.

### **Additional Information**

The following two paragraphs have been provided by the Underwriters for inclusion in this Official Statement and the City does not take any responsibility for or make any representations as to the accuracy or completeness of such statements or information.

Certain of the Underwriters and their respective affiliates are full service financial institutions engaged in various activities, which for certain of the Underwriters may include securities trading, commercial and investment banking, financial advisory, investment management, principal investment, hedging, financing and brokerage activities. Certain of the Underwriters and their respective affiliates have, from time to time, performed, and may in the future perform, various investment banking services for the City, for which they received or will receive customary fees and expenses.

In the ordinary course of their various business activities, the Underwriters and their respective affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (which may include bank loans and/or credit default swaps) for their own account and for the accounts of their customers and may at any time hold long and short positions in such securities and instruments. Such investment and securities activities may involve securities and instruments of the City. The market activities of the Underwriters and other market participants may impact the value of the Series 2014 Bonds.

## **FINANCIAL STATEMENTS**

The audited financial statements of the Airport set forth in Appendix D have been examined by Macias Gini & O’Connell LLP, independent certified public accountants, for the periods indicated and to the extent set forth in their report thereon. The Master Trust Agreement requires the City to have its financial statements audited annually by an independent certified public accountant. The audited financial statements prepared by the City each fiscal year are required to be provided to the Trustee within 180 days after the end of each such year in accordance with the Master Trust Agreement. Macias Gini & O’Connell LLP has not been requested to consent to the use of its name or to the inclusion of its report in this Official Statement, has not performed any post-audit review of the financial condition or operations of the Airport and has not reviewed this Official Statement.

## MISCELLANEOUS

Certain statements contained in this official statement, including the appendices, do not reflect historical facts but are forecasts and “forward-looking statements.” No assurance can be given that the future results discussed herein will be achieved, and actual results may differ materially from the forecasts described herein. In this respect, the words “estimate,” “project,” “anticipate,” “expect,” “intend,” “believe” and similar expressions are intended to identify forward-looking statements. All projections, forecasts, assumptions and other forward-looking statements are expressly qualified in their entirety by the cautionary statements set forth in this Official Statement.

Any statement made in this Official Statement indicated to involve matters of opinion or estimates are represented as opinions or estimates in good faith. No assurance can be given that the facts will materialize as so opined or estimated. The City and the Airport maintain websites at [www.sanjoseca.gov](http://www.sanjoseca.gov), [www.sjc.org](http://www.sjc.org) and [www.csjfinance.org](http://www.csjfinance.org). Information on such websites is not part of this Official Statement nor has such information been incorporated by reference herein and should not be relied upon in deciding whether to invest in the Series 2014 Bonds.

This Official Statement has been duly authorized and approved by the City Council and duly executed and delivered on its behalf by the officials signing below.

### CITY OF SAN JOSE, CALIFORNIA

By: /s/ Julia Harper Cooper  
Director of Finance

By: /s/ Kim Becker Aguirre  
Director of Aviation

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**APPENDIX A**

**THE NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**

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## AIR SERVICE AREA

### **General**

The Airport is located within the City of San José (two miles north of downtown), which is, by population, the third largest city in California (after Los Angeles and San Diego), the tenth largest city in the nation, and the largest city in Silicon Valley. Silicon Valley is home to many of the world's largest technology companies, including Hewlett-Packard, Apple, Cisco, Intel, Google and Oracle. As the largest city in Silicon Valley, the City of San José is often referred to as the "capital" of Silicon Valley.

The primary area served by the Airport consists of Santa Clara County, which is also the San José Primary Metropolitan Statistical Area (MSA). Furthermore, the primary service area includes the adjacent counties of Monterey, San Benito, and Santa Cruz and portions of two adjacent counties, Alameda and San Mateo (collectively, the "Air Service Area"). The Air Service Area is part of the larger San Francisco/San José/Oakland Area. The nearby counties of Merced, Stanislaus, and San Joaquin comprise a secondary service area. Three of the six Air Service Area counties belong to the Association of Bay Area Governments (ABAG) regional planning agency and rank within the top five most populated counties of the ABAG Region, with Santa Clara and Alameda Counties ranking first and second, and the County of San Mateo ranking fifth. In addition to the Airport, two other commercial airports serve the San Francisco/San José/Oakland area: San Francisco International Airport and Oakland International Airport. A separate unit of local government operates each of the three facilities independently.

The region enjoys a wide range of cultural, sporting, and recreational attractions that contribute to the quality of life in the region and will continue to attract visitors from all over the world. It is home to numerous major sporting and entertainment venues, museums, a world-renowned aquarium, theme parks, retail centers and other attractions.

The Air Service Area's expanding population base, relatively high per capita income, advanced levels of educational attainment, and high level of economic production provide a primary base for supporting air transportation at the Airport.

### **Demographic and Economic Profile**

The Airport is often referred to as an "origin and destination airport" because it primarily serves passengers beginning or ending their trips at the Airport, as opposed to passengers connecting through the Airport to other cities. The City estimates that during fiscal year 2013-14, approximately 98.0% of the passengers enplaning at the Airport were origin and destination ("O&D") passengers. In general, at airports primarily serving O&D passengers, air traffic is more dependent upon the population and economy of the air service area than upon the financial condition and route decisions of individual airlines.

**Population.** Population growth is a key factor influencing the demand for air travel. California is the most populous state in the nation, and the Air Service Area had a substantial population base with an estimated 5.3 million residents in 2013. The table below shows the growth in population in the Air Service Area experienced between 2010 and 2013.

**Air Service Area Population  
Historical 2010 and 2013 (Estimate)  
(as of July 1)**

County	Census 2010	Census 2013 (Estimate)	Total Increase 2010-2013
1. Santa Clara	1,781,642	1,862,041	80,399
2. Alameda	1,510,271	1,578,891	68,620
3. San Mateo	718,451	747,373	28,922
4. Monterey	415,057	428,826	13,769
5. Santa Cruz	262,382	269,419	7,037
6. San Benito	55,269	57,600	2,331
<b>Air Service Area</b>	<b>4,743,072</b>	<b>4,944,150</b>	<b>201,078</b>

*Source:* United States Census Bureau (Census 2010 & 2013 Population Estimates)

**Income.** According to U.S. Bureau of Economic Analysis' estimates updated as of May 30, 2014, for 2012 Santa Clara County had a Per Capita Personal Income ("PCPI") of \$66,535 and was 143% of the state average of \$46,477 and 152% of the national average of \$43,735. Within the Air Service Area, the remaining counties personal income and PCPI were as follows for 2010 through 2012:

Personal Income and Per Capita Personal Income within the Air Service Area As of May 30, 2014								
<u>County</u>	Personal Income (Thousands of Dollars)			2010-2012 Change	Per Capita Personal Income			2010-2012 Change
	<u>2010</u>	<u>2011</u>	<u>2012</u>		<u>2010</u>	<u>2011</u>	<u>2012</u>	
Alameda	\$72,870,057	\$78,550,471	\$85,017,099	\$12,147,042	\$48,144	\$51,286	\$54,683	\$6,539
Monterey	\$16,958,117	\$17,668,188	\$18,365,298	\$1,407,181	\$40,732	\$41,906	\$43,034	\$2,302
San Benito	\$1,920,847	\$2,037,248	\$2,163,294	\$242,447	\$34,588	\$36,273	\$38,030	\$3,442
San Mateo	\$47,787,433	\$51,931,876	\$55,139,354	\$7,351,921	\$66,362	\$71,232	\$74,582	\$8,220
Santa Cruz	\$12,361,716	\$13,284,573	\$13,990,306	\$1,628,590	\$46,925	\$50,138	\$52,442	\$5,517
Santa Clara	\$102,432,990	\$113,461,610	\$122,259,021	\$19,826,031	\$57,336	\$62,623	\$66,535	\$9,199
<b>Air Service Area<sup>(1)</sup></b>	<b>\$254,331,160</b>	<b>\$276,933,966</b>	<b>\$296,934,372</b>	<b>\$42,603,212</b>	<b>\$53,493</b>	<b>\$57,520</b>	<b>\$60,828</b>	<b>\$7,336</b>
<b>California</b>	<b>\$1,579,148,473</b>	<b>\$1,683,203,700</b>	<b>\$1,768,039,281</b>	<b>\$188,890,808</b>	<b>\$42,297</b>	<b>\$44,666</b>	<b>\$46,477</b>	<b>\$4,180</b>
<b>National</b>	<b>\$12,423,332,000</b>	<b>\$13,179,561,000</b>	<b>\$13,729,063,000</b>	<b>\$1,305,731,000</b>	<b>\$40,163</b>	<b>\$42,298</b>	<b>\$43,735</b>	<b>\$3,572</b>

<sup>(1)</sup> Per Capita Personal Income amounts for Air Service Area for years 2010 to 2012 are weighted average using US Census 2013 Population Estimates.

*Source:* US Bureau of Economic Analysis

**Educational Attainment.** The percentage of the Air Service Area's population with a bachelor's degree or higher (the category most likely to travel by air) was approximately 41.5%, according to the U.S. Census Bureau, 2008-2012 American Community Survey, substantially higher than that for California and for the nation. The high level of educational attainment is associated with its high labor force productivity and high per capita income.

The Air Service Area is also home to numerous public and private institutions of higher education, including Stanford University, California State University San Jose, Santa Clara University,

the University of California at Berkeley, the University of California at Santa Cruz, California State University Monterey Bay, and over 20 additional universities, colleges, and technical schools. Many of these universities and colleges were instrumental in the development of Silicon Valley and the technology industry and continue to play an important role in the economy of the region, through corporate, medical, and government research; large student populations; contributions to the high levels of educational attainment in the region; and significant contributions in terms of workforce for the technology industry and other industry sectors.

**Regional Economy.** The economic base of the Air Service Area is relatively stable and diversified. The Air Service Area has significant competitive advantages in its highly educated labor force, extensive research and development facilities, and high quality of life. These advantages have contributed to the region becoming a leading center of information technology, software, biotechnology, “clean technology,” and digital media.

**Employment.** California and U.S. unemployment rates remain high in comparison to pre-recession levels but are exhibiting a downward trend. According to the U.S. Bureau of Labor Statistics, the Air Service Area’s 2013 unemployment rate was 7.3% with approximately 182,257 unemployed, compared with 8.9% for California and 7.4% for the nation. All six counties comprising the Air Service Area experienced a decrease in unemployment from 2010, during which period the Air Service Area recorded an 11.1% unemployment rate.

## THE CITY AND THE AIRPORT DEPARTMENT

### **The City**

The City of San José (the “City”) was incorporated on March 27, 1850 and operates as a charter city, having had its first charter granted by the State of California (the “State”) in 1897. In 1916, another charter was adopted enabling the City to institute a council-manager form of government, making it one of the first cities in the nation to take this step. Under the California Constitution, charter cities are generally independent of the state legislature in matters relating to municipal affairs. The present charter became effective on May 4, 1965 and created the Airport Department as a separate department of the City.

The City is governed by a City Council consisting of a Mayor and ten other council members. The Mayor is elected at large for a four-year term. Council members are elected by district for staggered, four-year terms. The Mayor and the council members are limited to two consecutive four-year terms.

The City Council appoints the City Manager who is responsible for the operation of all municipal functions except the offices of City Attorney, City Clerk, City Auditor and Independent Police Auditor. The officials heading these offices are appointed by and carry out the policies set forth by the City Council.

### **The Airport Department**

The Airport Department is responsible to the City Manager and is headed by the Director of Aviation. The finances of the Airport Department are managed by Airport staff who coordinate with the staff of the City Department of Finance. An Airport Commission, made up of eleven members appointed by the City Council for three-year terms, serves in primarily an advisory capacity to the City Council.

In addition to the Office of the Director of Aviation, the Airport Department has five divisions: Airport Planning and Development, Airport Facilities and Engineering, Airport Operations, Airport Finance and Administration, and Airport Business Development. At its peak, the Airport Department had

400 authorized positions in fiscal year 2008-09. For fiscal year 2013-14, the Airport Department had 187 authorized positions and has 187 authorized positions in its budget for fiscal year 2014-15. For further information regarding the City's labor relations, see "OTHER MATTERS—Labor Relations" herein.

## THE AIRPORT

### **General**

The Airport is located on approximately 1,050 acres of land approximately two miles north of downtown San José, between the Bayshore Freeway (Highway 101) and Interstate 880. The Airport had its beginning in 1945, with the lease of approximately 16 acres of farmland from the City to Mr. James M. Nissen. Mr. Nissen and his associates formed an operating company (California Aviation Inc.), which undertook the construction of a 1,900-foot runway, a hangar and an office building. Flight operations began in 1946. In the Fall of 1948, the City assumed the operation of the San José Municipal Airport from California Aviation Inc. The Airport was renamed San José International Airport (SJC) in 1984 with the addition of airline service to Canada and was again renamed Norman Y. Mineta San José International Airport (SJC) in 2001.

The original terminal building (Terminal C) was built at the Airport in 1965. To accommodate increased commercial service at the Airport, Terminal C was expanded in 1969, 1970, 1971 and 1983. Terminal A, including the Terminal A+ extension, opened in 1990 and the International Arrivals Facility opened in 2002. Beginning in 2007, portions of Terminal C were closed as construction of Terminal B began. In June 2010, Terminal B opened and the remainder of Terminal C was permanently closed. Following its closure, Terminal C was demolished.

Passenger enplanements at the Airport grew slightly between fiscal years 2003-04 and 2005-06. Then passenger enplanements declined markedly during fiscal years 2006-07 and 2009-10, followed by growth between fiscal years 2010-11 and 2013-14. Although the airlines continually modify their flight schedules to accommodate market demand, the increase in passenger enplanements was primarily driven by All Nippon Airways' daily nonstop service to Tokyo, added capacity to the Los Angeles basin airports, and increased flights to both the Pacific Northwest and Mexico markets. See "AIRPORT FINANCIAL MATTERS" below. According to preliminary statistics published by the Airports Council International—North America ("ACI-NA"), in calendar year 2013 the Airport was the 40th busiest airport nationwide in terms of total passengers.

### **Existing Facilities**

**General.** Existing facilities at the Airport include three parallel runways; two commercial passenger terminals; an International Arrivals Facility; maintenance buildings; parking facilities; a control tower; and various other facilities.

For a description of the Airport's capital development program, see "CAPITAL DEVELOPMENT AT THE AIRPORT" below.

**Airfield Facilities.** The Airport's airfield facilities consist of three parallel runways, including two air carrier runways (Runway 30L and Runway 30R), one general aviation runway (Runway 11-29) and connecting taxiways. Runway 30R is the primary runway for departures, and Runway 30L is the primary runway for arrivals.

Staggered simultaneous operations on both runways are possible during Visual Flight Rules ("VFR") operations, which are implemented to reduce peak period delays. Runway 30L and Runway

30R can each accommodate the Boeing 747, the Boeing 787 and the Airbus 340 (but not the Airbus 380) aircraft on a limited basis with special operating procedures.

Runway 30R is approximately 11,000 feet long, and Runway 30L is 11,000 feet long, the maximum length allowed under the Airport Master Plan.

Runway 11-29, approximately 4,600 feet long, is a lighted, non-instrument runway located on the west side of the airfield which previously had been used exclusively by general aviation aircraft. Runway 11-29 is currently not in operation, and general aviation aircraft instead use Runway 30L and Runway 30R.

Lighting for the entire flight area, including lighting for the three runways and all connecting taxiways, approach lights, obstruction lights, lighted wind indicators and loading ramp floodlights, is provided on a 24-hour basis.

**Terminal Facilities.** Passenger services are located in Terminal A, Terminal B and the International Arrivals Facility, for a total of 28 gates, all of which have passenger loading bridges. Ground loading does occur on some flights. Delta Air Lines, American Airlines, JetBlue Airways, Hawaiian Airlines, US Airways, United Airlines, All Nippon Airways, and Volaris are currently located in Terminal A. Southwest Airlines, Alaska Airlines, and Horizon Air (which operates as Alaska Airlines) are currently located in Terminal B. The terminal facilities include food, beverage and other concessions.

Terminal A, including the Terminal A+ extension that opened in 1990 and the International Arrivals Facility, is a 16-gate, multi-story building. Terminal A, which was renovated and expanded in 2010, is designed to handle up to approximately 7.2 million passengers annually and the International Arrivals Facility is designed to handle up to approximately 1.1 million passengers annually.

The International Arrivals Facility, which opened in 2002, is located between Terminal A and Terminal B, and is accessible from both the south end of Terminal A and the north end of Terminal B. In addition to offices for U.S. Customs and Border Protection and U.S. Public Health Service, the International Arrivals Facility houses two of the 16 aircraft gates in Terminal A and a waiting area for departing international passengers. The Airport is modifying Gates 17 and 18 in Terminal B to accommodate international arrivals. These gates, as well as those at the International Arrivals Facility, can be used for either international or domestic flights, providing the Airport with flexibility to adjust to the changing schedules of the airlines. This work is expected to be completed during fiscal year 2014-15. In 2013, the Airport opened *The Club at SJC*, a lounge located in the International Arrivals Facility that is open to all airline passengers. By purchasing a day pass for \$35, travelers have access to the lounge where they can work quietly, rest between flights, or freshen up during their journey.

Terminal B, which opened in June 2010, includes 12 gates, ticket counters, baggage claim areas, concession areas, security screening areas, passenger holdroom areas and airline and other tenant offices. Terminal B also includes permanent facilities for the United Service Organizations (“USO”). Terminal B is designed to handle approximately 6.1 million passengers annually.

**Rental Car Facilities.** Currently, seven rental car companies, representing a total of eleven rental car brands, operate at the Airport in the seven-story ConRAC located immediately across the street from Terminal B. The ConRAC, which opened in June 2010, includes 3,000 ready/return spaces and approximately 320 hourly public parking spaces located on the first floor. See “LEASE AND OPERATING AGREEMENTS—Parking, Rental Car, Concession and Other Agreements—Rental Car Agreements”.

**Parking.** As of June 30, 2014, the Airport had a total of approximately 5,530 available public parking spaces. Terminal A is connected to a parking garage with approximately 1,300 spaces for hourly public parking. The first floor of the ConRAC is dedicated to hourly public parking for Terminal B and includes approximately 320 spaces. Two additional hourly surface parking lots, one adjacent to Terminal B and one adjacent to the ConRAC, provide approximately 880 hourly parking spaces for Terminal B. Two daily surface parking lots provide a total of approximately 1,360 daily rate spaces for Terminal B. The Airport's economy surface parking lot is located on 16 acres of Airport property northeast of Terminal A and includes approximately 1,670 economy parking spaces. See "LEASE AND OPERATING AGREEMENTS—Parking, Rental Car, Concession and Other Agreements—Parking Agreement" below.

**General Aviation Facilities.** As of June 30, 2014, there were approximately 60 general aviation aircraft based at the Airport. General aviation facilities include a combination of T-hangars and tie-down spaces. Other general aviation facilities are provided by fixed-base operators ("FBOs"), which provide services such as aircraft sales, rentals and maintenance, charter service, flight instruction and aircraft radio sales.

The Airport currently has three operating FBOs. ACM Property Services, LLC leases an FBO facility to TWC Aviation, offering aircraft management and charter services. Atlantic Aviation (formerly San José Jet Center) started operations in 1986 and currently has five hangars that offer full service to based and itinerant aircraft. ACM and Atlantic Aviation share a common parent entity, but operate as separate entities at the Airport. The third FBO, AvBase San José, LLC ("AvBase"), started operations in 2005, offering general aviation services to based aircraft. AvBase also offers fueling services to aircraft owned by AvBase and its sub-lessees.

The adopted Airport Master Plan currently designates the west side of the Airport for development of facilities to accommodate projected growth in general aviation demand. The City issued a Request for Proposals (the "RFP") in August 2012 for the long-term lease of land for the development and operation of a new fixed base operation facility by the successful proposer. In December 2013, after completing its review of proposals received in response to the RFP, the City approved a 50-year ground lease and operating agreement with Signature Flight Support ("Signature"), pursuant to which Signature will develop a new general aviation fixed base operation at the Airport serving the public and corporate general aviation operators. Under the agreement, Signature, with Blue City Holdings San José, LLC ("Blue City Holdings") as a major subtenant, will invest approximately \$82 million in the project with an estimated completion date of late 2015. Blue City Holdings is a corporation that owns and operates the personal aircraft of the officers at Google. In February 2014, Signature broke ground on the 29-acre west side complex that will eventually be home to the service provider's West Coast headquarters. Once operational, the development is projected to generate approximately \$3.0 million annually in new revenues for the Airport. An additional 15 acres north of the FAA air traffic control tower remains available for future development opportunities, but there are no immediate plans for development. See "LITIGATION--SJJC Aviation Services, LLC v. City of San Jose" in Appendix A.

Hewlett Packard has a ground lease for corporate aviation operations at the Airport and handles only Hewlett Packard aircraft. Hewlett Packard completed its first hangar in 1987 and a second hangar in 2001. Hewlett Packard's lease is scheduled to expire in November 2028.

**Fuel, Cargo and Other Support Facilities.** An Airport fuel farm completed in December 2009 is located on Airport property on the north side of Highway 101, with a pipeline under Highway 101 that connects the fuel farm to fuel dispensing racks located on the airfield apron north of Terminal A. The airlines serving the Airport formed a consortium which funded and oversaw construction of the fuel farm. The consortium is responsible for the operation and maintenance of the fuel farm. The storage capacity of

the fuel farm is 45,000 barrels of jet fuel (approximately equal to a seven day working supply at the Airport). Fuel is distributed to the fuel farm via a two-mile underground pipeline connected to the San José Kinder Morgan Products Terminal. Staging and maintenance of the fuel trucks is currently conducted at the southeast end of the Airport. Consistent with the Airport's Master Plan, in 2013 the City agreed to relocate the jet fueling staging and maintenance activities to the northeast side of the Airport. The project is expected to be completed in 2014. See "CAPITAL DEVELOPMENT AT THE AIRPORT—Environmental Matters."

Other facilities include the City's Aircraft Rescue and Firefighting Facility ("ARFF"), which is currently located near the southeast corner of the Airport, and ground support, equipment maintenance and belly freight facilities near the southeast corners of the airfield. On the northeast side of the Airport a taxi staging building was completed in March 2013, to help manage multiple taxi companies and drivers, dispatching both taxis and commercial door-to-door shuttles. By the end of 2014, the shuttle bus operations are anticipated to be relocated from the west side of the Airport to the northeast area.

## PASSENGER SERVICES AND OPERATIONS

### **Passenger Services**

As of June 30, 2014, fourteen passenger airlines provided nonstop service from the Airport to a total of 25 U.S. cities and three foreign cities, and two airlines provided scheduled all-cargo service at the Airport.

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**Table 5**  
**Norman Y. Mineta San José International Airport**  
**Airlines Serving the Airport**  
**as of June 30, 2014**

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<b>Domestic Airlines</b>	<b>Regional Commuter Airlines<sup>(1)</sup></b>	<b>Foreign-Flag Airline</b>
Alaska Airlines <sup>(2)</sup>	American Eagle <sup>(3)</sup>	Volaris
American Airlines <sup>(4)</sup>	Horizon Air <sup>(2)</sup>	All Nippon Airways
Delta Air Lines	SkyWest <sup>(5)</sup>	
Hawaiian Airlines	Mesa Airlines	
JetBlue Airways		
Southwest Airlines		
United Airlines		
US Airways <sup>(4)</sup>		
<b>All-Cargo Service</b>		
FedEx Corporation		
United Parcel Service		

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(1) Commuter service is service on aircraft weighing less than 75,000 pounds. Other airlines listed may provide commuter service to certain destinations.  
(2) Alaska Airlines and Horizon Air are separately certificated air carriers and wholly-owned subsidiaries of Alaska Air Group, Inc. Horizon Air is currently doing business at the Airport as Alaska Airlink.  
(3) American Eagle is currently doing business at the Airport as American Airlines.  
(4) American Airlines and US Airways merged in December 2013. The combined airlines (named American Airlines Group) will continue to operate as separate airlines until their operations have been fully integrated.  
(5) SkyWest is currently doing business at the Airport as United Express, American, Delta Connection and US Airways.

*Source:* Norman Y. Mineta San José International Airport.

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Passenger enplanement activity in fiscal year 2003-04 was approximately 5.3 million and was followed by two years of modest growth. From fiscal year 2006-07 through fiscal year 2009-10, passenger enplanements decreased at a compound annual rate of 6.3% in conjunction with an aviation fuel cost spike, the national credit crisis, and a global recession. From fiscal year 2010-11 to fiscal year 2013-14, passenger enplanement activity grew at a compound annual growth rate of 1.9%. Passenger enplanement increased in twenty-two of the twenty-four months ended June 30, 2014. Total enplanements were approximately 4.5 million during fiscal year 2013-14, which was higher than the level achieved in fiscal year 2008-09.

**Table 6**  
**Norman Y. Mineta San José International Airport**  
**Historical Passenger Enplanements**  
**Fiscal Years Ended June 30<sup>(1)</sup>**

<b>Fiscal Year</b>	<b>Air Carrier Domestic Enplanements</b>	<b>Air Carrier International Enplanements</b>	<b>Total Air Carrier Enplanements</b>	<b>Regional Commuter Enplanements<sup>(2)</sup></b>	<b>Total Enplanements</b>	<b>Percent Change in Total Enplanements</b>
2003-04	4,651,137	134,176	4,785,313	506,536	5,291,849	-
2004-05	4,660,730	138,142	4,798,872	546,761	5,345,633	1.0%
2005-06	4,706,038	137,054	4,843,092	571,739	5,414,831	1.3
2006-07	4,686,496	102,368	4,788,864	529,995	5,318,859	(1.8)
2007-08	4,584,448	67,459	4,651,907	526,696	5,178,603	(2.6)
2008-09	3,907,376	60,381	3,967,757	431,805	4,399,562	(15.0)
2009-10	3,636,146	62,437	3,698,583	407,270	4,105,853	(6.7)
2010-11	3,728,493	77,963	3,806,456	382,767	4,189,223	2.0
2011-12	3,672,704	83,261	3,755,965	368,920	4,124,885	(1.5)
2012-13	3,720,640	110,289	3,830,929	403,824	4,234,753	2.7
2013-14	3,891,911	163,638	4,055,549	461,472	4,517,021	6.7
<b>Compound Annual Growth Rates</b>						
FY04-FY06	0.4%	0.7%	0.4%	4.1%	0.8%	
FY07-FY10	(6.2%)	(11.6%)	(6.3%)	(6.4%)	(6.3%)	
FY11-FY14	(1.1%)	20.4%	1.6%	4.8%	1.9%	

(1) Some data reported previously have been revised to reflect more recent information.

(2) Includes scheduled and unscheduled commuter aircraft.

*Source:* Norman Y. Mineta San José International Airport

Table 7 lists the cities served by nonstop flights from the Airport as of June 30, 2014.

**Table 7**  
**Norman Y. Mineta San José International Airport**  
**Cities Served by Nonstop Service as of June 30, 2014**

**Domestic Cities**

Atlanta, Georgia  
Austin, Texas  
Boise, Idaho  
Boston, Massachusetts  
Burbank, California  
Chicago, Illinois  
Dallas, Texas  
Denver, Colorado  
Honolulu, Hawaii  
Houston, Texas  
Kahului, Hawaii  
Kona, Hawaii  
Las Vegas, Nevada  
Lihue, Hawaii  
Los Angeles, California  
Minneapolis, Minnesota  
New York, New York  
Ontario, California  
Orange County, California  
Phoenix, Arizona  
Portland, Oregon  
Reno, Nevada  
Salt Lake City, Utah  
San Diego, California  
Seattle, Washington

**Foreign Cities**

San José Cabo, Mexico  
Guadalajara, Mexico  
Tokyo, Japan

*Source:* Official Airline Guide, Inc., June 30, 2014.

The City offers an air service incentive program to support the development of new passenger air service at the Airport. In addition, the City has a program that reduces the Airport's share of indirect overhead expenses allocated to it by the City for support services the City provides to the Airport (the "Municipally-Funded Air Service Incentive Program").

As part of the new airline incentive program, the Director of Aviation has defined specific incentives for airport destinations that are considered short-haul domestic airport destinations, long-haul domestic airport destinations, North America airport destinations outside of the U.S., and international airport destinations. For the domestic airport destinations, a short-haul airport destination is defined as being within a 1,250 mile radius of the Airport. A long-haul airport destination is one that is greater than

1,250 miles from the Airport. The program provides for the waiver of landing fees for a period between one and two and a half years (the “Incentive Period”) for airlines providing service to a new airport destination for a specified period of time with a minimum frequency of three times weekly non-stop service. The program also provides for matching marketing funds ranging from \$25,000 to \$250,000, depending on the type of new service provided. For a new airline coming to the Airport, landing fees and eligible terminal fees will be waived during the Incentive Period. The terms and conditions of the airline incentive program are at the sole discretion of the Director of Aviation and can be modified at any time.

The Municipally-Funded Air Service Incentive Program reduces the Airport’s share of indirect overhead expenses allocated to it by the City for support services the City provides to the Airport. Terms and conditions of the Municipally-Funded Air Service Incentive Program are set forth in the Airline Lease Agreement.

***Enplanements by Airline.*** Currently ten different carriers serve approximately 28 nonstop destinations, offering the business and leisure traveler a range of domestic and international travel options. In addition, the Airport has service to nearly 20 airline hubs that provide access from around the nation and across the globe. The three largest carriers that anchor the Airport’s service continue to be Southwest, Alaska, and American, who combined for approximately 75% of passenger enplanements and collectively have nonstop service to 24 destinations. Southwest Airlines is the leading airline at the Airport, with a market share of approximately 51% in fiscal year 2013-14, while Alaska Airlines and American Airlines held market shares of approximately 16% and 9%, respectively, in the same time period. In December 2013, American Airlines and US Airways (“American Airlines Group”) merger was completed. The market share for the American Airlines Group was approximately 13% in fiscal year 2013-14. Delta continues to expand its service to the Los Angeles destinations. In fiscal year 2013-14 international enplanements increased by approximately 48%. In June of 2013, All Nippon Airways started service to Tokyo and has served 95,000 passengers since that time. Virgin America operated at the Airport from May 2013 until May 2014.

Table 8 sets forth enplanements for airlines (together with their affiliates) serving the Airport for the fiscal years 2009-10 through 2013-14.

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**Table 8**  
**Norman Y. Mineta San José International Airport**  
**Enplaned Commercial Passengers by Airline**  
**Fiscal Years Ended June 30**  
**(Ranked by Fiscal Year 2014 Results)**

Airline <sup>(1)</sup>	FY 2009-10		FY 2010-11		FY 2011-12		FY 2012-13		FY 2013-14	
	Enplanements	% of Total								
Southwest Airlines	2,121,917	51.7%	2,187,033	52.2%	2,192,234	53.1%	2,169,956	51.2%	2,280,346	50.5%
Alaska Carriers	393,982	9.6	561,400	13.4	609,315	14.8	727,616	17.2	704,944	15.6
American Carriers <sup>(2)</sup>	480,402	11.7	435,815	10.4	386,997	9.4	400,246	9.5	407,331	9.0
Delta Carriers <sup>(4)</sup>	175,775	4.3	216,757	5.2	218,447	5.3	228,824	5.4	332,544	7.4
United Airlines <sup>(3)</sup>	376,879	9.1	357,283	8.5	298,808	7.3	253,837	6.0	231,287	5.1
US Airways Carriers <sup>(2)</sup>	208,809	5.1	184,380	4.4	184,084	4.5	187,583	4.4	192,733	4.3
Hawaiian Airlines	72,266	1.8	85,571	2.0	103,483	2.5	116,928	2.8	113,381	2.5
Virgin America <sup>(5)</sup>							18,265	0.4	85,859	1.9
JetBlue Airways	95,118	2.3	80,797	1.9	76,063	1.8	71,506	1.7	70,860	1.6
Volaris	8,072	0.2	48,325	1.2	49,709	1.2	49,700	1.2	51,056	1.1
All Nippon Airways <sup>(5)</sup>							3,273	0.1	42,999	1.0
Other <sup>(6)</sup>	172,633	4.2	31,862	0.8	5,745	0.1	7,019	0.2	3,681	0.1
Total <sup>(7)</sup>	4,105,853	100.0%	4,189,223	100.0%	4,124,885	100.0%	4,234,753	100.0%	4,517,021	100.0%

(1) Unlike previous official statements with respect to the Outstanding Bonds, the information presented herein does not separately report flights operated by Skywest. The enplanement information of flights operated by Skywest is included in the data of certain other airlines as noted below.

(2) In December 2013 American Airlines and US Airways (“American Airlines Group”) merger was completed. They will continue to operate as separate airlines until their operations have been fully integrated. The enplanements include flights operated by Skywest.

(3) Continental and United merged in October 2010. The combined airlines (named United Airlines) received FAA approval to operate under a single operating certificate in December 2011 but continued to operate as separate airlines until their operations were fully integrated in 2012. The enplanements include flights operated by Skywest as United Express.

(4) Includes enplaned passengers on flights operated by Skywest as Delta Connection.

(5) Virgin America and All Nippon Airways started operations at the Airport in May 2013 and June 2013, respectively. Virgin America stopped operations at the Airport in May 2014.

(6) Consists of airlines no longer serving the Airport and charter airlines.

(7) Totals may not add due to rounding.

Source: Norman Y. Mineta San José International Airport.

## **Historical Air Cargo**

In addition to cargo carried by passenger airlines, FedEx Corporation and United Parcel Service provided domestic and international air cargo service at the Airport as of June 30, 2014. In fiscal year 2013-14, the total amount of enplaned and deplaned cargo carried by all-cargo carriers at the Airport increased by approximately 9.5% from fiscal year 2012-13 to approximately 86,239,000 pounds.

## **Landed Weight and Airport Operations**

Table 9 sets forth total landed weight of aircraft (other than general aviation and military aircraft) that used the Airport in fiscal years 2003-04 through 2013-14. Landed weights declined in nearly every year from fiscal year 2003-04 to fiscal year 2013-14. This trend is fairly consistent with the drops in passenger enplanement activity and a general trend of airlines cutting capacity in order to lower their costs and continuing to serve decreased levels of passengers without eliminating destinations.

**Table 9**  
**Norman Y. Mineta San José International Airport**  
**Historical Gross Landed Weight<sup>(1)</sup>**  
**(in thousand pounds)**  
**Fiscal Years Ended June 30**

<b>Fiscal Year</b>	<b>Mainline Air Carrier<sup>(2)</sup></b>	<b>Regional Commuter</b>	<b>All-Cargo<sup>(3)</sup></b>	<b>Total</b>	<b>Annual Percentage Change</b>
2003-04	6,795,591	677,143	547,057	8,019,791	--
2004-05	6,468,513	660,694	531,843	7,661,050	(4.5)%
2005-06	6,342,853	677,843	478,376	7,499,072	(2.1)
2006-07	6,351,084	638,449	511,763	7,501,296	<0.1
2007-08	6,255,828	656,298	492,624	7,404,750	(1.3)
2008-09	5,576,343	553,726	421,088	6,551,157	(11.5)
2009-10	4,903,780	506,737	322,267	5,732,784	(12.5)
2010-11	4,779,979	441,023	319,185	5,540,187	(3.4)
2011-12	4,719,483	405,907	268,748	5,394,139	(2.6)
2012-13	4,759,393	453,801	248,067	5,461,261	1.2
2013-14	4,999,691	536,903	235,002	5,771,595	5.7

<b>Compound Annual Growth Rates</b>				
FY04-FY06	(2.3%)	<0.1%	(4.4%)	(2.2%)
FY07-FY10	(6.3%)	(5.6%)	(10.9%)	(6.5%)
FY11-FY14	1.1%	5.0%	(7.4%)	(1.0%)

(1) Some data reported previously have been revised to reflect more recent information.

(2) Includes domestic and international airlines.

(3) Includes all-cargo service only. Includes cargo service provided by Air Transport International, which ceased cargo service operations from the Airport on September 2, 2011.

*Source:* Norman Y. Mineta San José International Airport.

Table 10 lists the number of aircraft operations (take-offs and landings) at the Airport for fiscal years 2003-04 through 2013-14. Total aircraft operations decreased at the Airport during this period, from 197,584 in fiscal year 2003-04 to 122,351 in fiscal year 2013-14. The decline in aircraft operations during this period is steeper than the decline in passenger activity, which is partially due to an increase in the load factor on flights during this time period.

**Table 10**  
**Norman Y. Mineta San José International Airport**  
**Historical Aircraft Operations<sup>(1)(2)</sup>**  
**Fiscal Years Ended June 30**

Fiscal Year	Mainline Air Carrier Operations <sup>(3)</sup>	Regional Commuter Operations	All-Cargo Operations	Total Commercial Operations <sup>(4)</sup>	Commercial Operations as a % of Total	General Aviation Operations	Military Operations	Total Operations	% Change in Total Operations
2003-04	103,526	30,838	3,586	137,950	69.8%	59,521	113	197,584	--
2004-05	98,892	29,672	3,594	132,158	67.4%	63,708	99	195,965	(0.8)%
2005-06	97,198	30,756	3,464	131,418	67.9%	61,907	83	193,408	(1.3)%
2006-07	97,596	28,806	3,388	129,790	70.2%	55,021	103	184,914	(4.4)%
2007-08	96,860	29,504	3,140	129,504	70.1%	55,146	64	184,714	(0.1)%
2008-09	86,668	23,830	2,558	113,056	70.7%	46,674	242	159,972	(13.4)%
2009-10	76,024	19,776	2,076	97,876	74.4%	33,439	275	131,590	(17.7)%
2010-11	73,094	16,172	2,046	91,312	74.8%	30,503	276	122,091	(7.2)%
2011-12	71,672	14,806	1,678	88,156	73.4%	31,664	285	120,105	(1.6)%
2012-13	71,598	15,910	1,536	89,044	73.8%	31,321	210	120,575	0.4%
2013-14	73,596	17,460	1,468	92,524	75.6%	29,619	208	122,351	1.5%
<b>Annual Compound Growth Rate</b>									
FY04-FY06	(2.1%)	(0.1%)	(1.2%)	(1.6%)		1.3%	(9.8%)	(0.7%)	
FY07-FY10	(6.1%)	(9.0%)	(11.5%)	(6.8%)		(11.7%)	27.8%	(8.2%)	
FY11-FY14	(0.2%)	(1.9%)	(8.0%)	(0.3%)		0.7%	(6.8%)	(0.1%)	

(1) An aircraft operation is defined as the takeoff or landing of an aircraft.

(2) Some data reported previously have been revised to reflect more recent information.

(3) Includes domestic and international airlines.

(4) Represents the sum of Mainline Air Carrier Operations, Regional Commuter Operations and All-Cargo Operations.

*Source:* Norman Y. Mineta San José International Airport.

## LEASE AND OPERATING AGREEMENTS

The Airport Department's operating revenues are derived primarily from airline agreements, parking, rental car and other concession agreements and from other business arrangements.

### **Airline Agreements**

***Airline Lease Agreement.*** The current Airline Lease Agreement for passenger and cargo airlines is a five-year agreement that expires on June 30, 2017. The original five-year agreement became effective in 2007 and was extended in 2012 for an additional five years. The agreement was entered into by mutual consent of the City and the Signatory Airline (defined below) and is subject to early termination under certain circumstances. In fiscal year 2012-13, approximately 42% of the Airport's operating revenues were derived from payments made pursuant to the Airline Lease Agreement. For a summary of certain provisions of the Airline Lease Agreement, see "SUMMARY OF CERTAIN PROVISIONS OF THE AIRLINE LEASE AGREEMENT" in Appendix G.

The provisions of the Airline Lease Agreement are subordinate to provisions of the Master Trust Agreement. The Airline Lease Agreement will not be assigned or pledged to the Trustee as security for the Series 2014 Bonds.

The Airline Lease Agreement provides that any passenger airline that (a) signs an agreement substantially similar to the Airline Lease Agreement, (b) provides passenger service at the Airport, (c) leases from the City an amount of Exclusive Use Premises (not including gates) in the terminal deemed sufficient by the Director of Aviation to support the airline's operation and (d) at the time the airline executes its agreement with the City, operates at least one scheduled flight, scheduled year round, at least three days per week shall be a "Signatory Airline." The Airline Lease Agreement provides that any air cargo carrier will also be a "Signatory Airline" if the air cargo carrier (a) signs an agreement with the City substantially similar to the Airline Lease Agreement (other than in connection with terminal facilities), (b) leases from the City cargo support space at the Airport for a term at least equal to the term of the Airline Lease Agreement, (c) guarantees a minimum of 142,000 pounds of maximum gross certificated landed weight per scheduled flight and (d) at the time it executes its agreement with the City, operates at least five scheduled flights per week. Signatory Airlines also participate in the "Majority-in-Interest" ("MII") review and approval process for capital projects proposed for the Airport.

***Rates and Charges Ordinance.*** All passenger airlines are operating at the Airport as Signatory Airlines. Any passenger or air cargo carrier that does not meet the minimum requirements to be a Signatory Airline is given the opportunity to become a "Non-Signatory Airline" by executing a non-signatory agreement in a form similar to that of the Airline Lease Agreement. Non-Signatory Airlines are charged a premium of 25% over the rates and charges applicable to Signatory Airlines and will not participate in the MII review process.

Any passenger or air cargo carrier operating at the Airport that is neither a Signatory Airline nor a Non-Signatory Airline is subject to the Airline Rates and Charges Ordinance, which requires such air carriers to comply with all applicable rules and regulations as established by the Director of Aviation regarding the proper use and occupancy of the Airport or any portion thereof. In addition, the Airline Rates and Charges Ordinance establishes all rates and charges applicable to such airline's operations at and use of the Airport or any portion thereof, including airfield and terminal rates and charges, at a 30% premium over the rates and charges as determined pursuant to the terms of the City's then current airline lease and operating agreement.

## **Parking, Rental Car, Concession and Other Agreements**

In addition to the Airline Lease Agreements, the City has entered into leases, concession agreements and other agreements with a parking operator, seven automobile rental companies (representing a total of eleven rental car brands), an in-flight kitchen operator, several Airport-based retailers, four FBOs and one corporate general aviation operator. Approximately 58% of the Airport's operating revenues in fiscal year 2012-13 were derived from these and other sources of non-airline revenues, compared to 60% in fiscal year 2011-12. See "AIRPORT FINANCIAL MATTERS—Historical Operating Results" and "—Management Discussion of Recent Financial Results."

***Parking Agreement.*** The City's public parking and employee parking lots at the Airport are managed by ABM Parking Services ("ABM") pursuant to a three year agreement that includes five one year options to extend. The agreement which became effective on April 1, 2014 provides that ABM will be paid an annual fixed management fee plus reimbursable expenses.

The City sets rates for parking in the Airport's public parking lots. The parking fee structure for the hourly lot is \$2.00 per 30 minutes, with a maximum first 24 hour charge of \$30.00 followed by \$30.00 per day flat rates per 24 hour period or portions thereof. In the daily parking lot a \$22.00 flat rate per day is charged, and a \$15.00 flat rate per day is charged in the economy lot. These rates have been in place since 2011. For fiscal year 2013-14, parking fees represented approximately 17% of Airport gross operating revenue. See "AIRPORT FINANCIAL MATTERS – Management Discussion of Recent Financial Results – Parking and Roadway Revenues."

***Rental Car Agreements.*** The City opened the ConRAC in June 2010. Each of the seven rental car companies (representing a total of eleven rental car brands) that currently operate on-Airport has an agreement with the City for its operations at the ConRAC that is to terminate on May 31, 2020, subject to two optional ten year extensions, which must be approved by the City and the rental car companies. Pursuant to these agreements, the rental car companies must pay facility rent to the City for use of the ConRAC and related transportation expenses (the "Facility Rent") and remit to the City customer facility charges that are collected from the rental car companies' customers ("CFCs"). Facility Rent is included in General Airport Revenues. For additional information regarding CFCs, see "AIRPORT FINANCIAL MATTERS—Customer Facility Charges."

Facility Rent is calculated by a two-step process under the terms of the rental car agreement. First, an amount equal to the sum of annual debt service on the Series 2011B Bonds and coverage amounts and reserve fund requirements applicable to the Series 2011B Bonds, less estimated CFC Revenues, is allocated to each rental car company based upon that company's percentage occupancy of the ConRAC. Second, each rental car company's share of: (a) operating costs for the transportation system operated by the City to transport passengers between the terminals and the ConRAC (the "ConRAC Transportation System"); and (b) the City's cost to demolish the previous temporary common use rental car facilities at the Airport, amortized over the initial ten-year term of the agreement are then added to the first amount to determine the Facility Rent due from each rental car company. In the event that CFC Revenues exceed the sum of annual debt service on the Series 2011B Bonds plus coverage amounts and reserve fund requirements, each rental car company's share of any such CFC Revenues will be deducted from its share of operating costs for the ConRAC Transportation System. In the event that CFC Revenues remain after CFC Revenues are deducted from each company's share of operating costs for the ConRAC Transportation System, the City may, in its sole discretion, deduct each rental car company's share of any such CFC Revenues from its share of Demolition Costs, as calculated under the terms of the rental car agreement. In order to apply the CFC Revenues to cover transportation costs, the specific rental car customer that used the transportation system must be identified. To date, no CFC

Revenues have been applied toward transportation costs or Demolition Costs. See “AIRPORT FINANCIAL MATTERS – Customer Facility Charges.”

Total Facility Rent for the ConRAC in fiscal year 2012-13 was approximately \$3.3 million. Facility Rent will vary each year in relation to any change in the total amount of CFC Revenues collected during such year. In the event that CFC Revenues are higher than estimated, the total Facility Rent would be lower. If the CFC Revenues are lower than estimated, total Facility Rent will be higher.

In addition to Facility Rent and CFC Revenues, the rental car companies pay the City a concession fee equal to the greater of a Minimum Annual Guarantee (“MAG”) or 10% of gross revenues, ground rent equal to the fair market rental value of the underlying Airport land, and utility charges allocated based upon relative square footages occupied by the rental car companies at the ConRAC. Ground rent is subject to annual adjustment based upon year-to-year increases in the consumer price index, with the adjustment in the sixth year made by appraisal. In fiscal year 2012-13, rental car concession and facility and ground rental revenue represented approximately 15.0% of Airport gross operating revenue.

***Terminal Concession, Advertising and Other Agreements.*** Food and beverage and retail concession services at the Airport are provided by four concessionaires under four separate agreements, each of which expires in June 2020. Host International, Inc. (“Host”) and Pacific Gateway Concessions, LLC (“PGC”) each provide food and beverage services at the Airport under a food and beverage concession agreement. AMS-SJC-JV and World Duty Free Group North America, LLC (“WDFG”) each provide retail services under a retail concession agreement. In October 2013, Areas USA assigned its food and beverage concession agreement to PGC, and Host assigned its retail concession agreement to WDFG. Each food and beverage and retail concession agreement provides for payment to the City of the greater of a MAG or a percentage of gross revenues. The agreements include a number of food and beverage and retail providers as sub-concessionaires and food and beverage and retail outlets in both terminals. Airport operating revenue from the food and beverage and retail concession agreements in both fiscal years 2011-12 and 2012-13 equaled approximately \$8.2 million of Airport gross operating revenue, representing the combined MAG for food and beverage, and retail concessions.

The City has an Airport Advertising Concession Agreement with Clear Channel Outdoor, Inc., d/b/a Clear Channel Airports (“Clear Channel”) for fixed display in terminal advertising, outdoor advertising, transit and bus shelter advertising, and promotional marketing opportunities at the Airport for a term running through July 31, 2020. The agreement guarantees the City the greater of a MAG of \$4,222,324 or a percentage of revenues through June 30, 2017. The MAG adjusts to \$1,800,000 on July 1, 2017, to \$1,900,000 on July 1, 2018, and to \$2,000,000 on July 1, 2019.

The City also has a ground lease with LSG/Skychefs, Inc. (“LSG/Skychefs”), the operator of an in-flight kitchen that provides catering services to some of the airlines at the Airport. The ground lease provides for a minimum payment of 10% of gross revenue or a MAG, whichever is greater, and expires in 2016.

The City issues licenses for the operation of newsracks and has agreements with operators of foreign currency exchanges, ATMs, luggage cart racks, pay phones, visitor information publications, prohibited item mailers and wireless antenna. A new luggage cart contract was signed on August 1, 2014. The new contract requires the luggage cart operator to pay a percentage of gross revenues. In order to do business at the Airport, all other operators pay fixed fees, subject to annual adjustment.

In July 2011, the City temporarily deactivated six gates in the Terminal A+ extension and shifted airline operations to gates in Terminal A and the International Arrivals Facility. In conjunction with the

temporary deactivation of gates in the Terminal A+ extension, the City amended its concession contract with Host to allow for the closure of certain concessions facilities in the Terminal A+ extension. Closure of these facilities decreased the MAG paid by Host to the City by approximately \$355,000. Since July 2011, the Airport gradually reopened the six gates in Terminal A+ as flight or passenger activity levels warranted. As a result of the re-activation of the six gates, some of the concessions opened in July 2014, and the remaining concessions are anticipated to be re-opened in calendar year 2014. The reinstated MAG for these re-opened concessions will be approximately \$355,000.

## AIRPORT FINANCIAL MATTERS

### **Airport and City Budget Process**

***Airport Rate-Setting.*** The Airline Lease Agreement sets forth the following procedures related to landing fee and terminal rent determinations, which represent key components of the Airport's budget: No later than May 1 of each year during the term of the Airline Lease Agreement, the City is to disclose to all Signatory Airlines the revised landing fees and terminal rents that the City expects to charge for the next fiscal year, effective July 1. No later than June 1 of each year, the City is to consult with the Signatory Airlines to discuss the proposed revised landing fees and terminal rents. In connection with this consultation, the City is to provide to each Signatory Airline the calculations the City has made in determining the revised charges with reasonable supporting documentation. No later than June 10 of each year, the City is to notify the Signatory Airlines of the actual landing fees and terminal rents it will charge for the next fiscal year, effective July 1. The Airline Lease Agreement provides that the City's obligation to consult with the Signatory Airlines does not limit in any way the City's rate setting powers or otherwise cause any delay in the effectiveness of the revised charges. See "SUMMARY OF CERTAIN PROVISIONS OF THE AIRLINE LEASE AGREEMENT" in Appendix G.

The Airline Rates and Charges Ordinance establishes all rates and charges applicable to the operations of airlines that are neither Signatory Airlines nor Non-Signatory Airlines at the Airport and use of the Airport or any portion thereof, including airfield and terminal rates and charges, at a 30% premium over the rates and charges as determined pursuant to the terms of the City's then current airline lease and operating agreement. See "LEASE AND OPERATING AGREEMENTS – Airline Agreements" above.

***City and Airport Budget.*** The Airport's and the City's fiscal year is from July 1 through June 30. Historically, the City's annual budget process begins each October with the determination by the City Council's Rules Committee (now the "Rules and Open Government Committee") of the budget schedule for the next fiscal year. The schedule sets dates for the release of the various documents (except those specified in the City Charter), the dates of the study sessions of the Council and of the public hearings to discuss the budget.

In the third quarter of each fiscal year, the City Manager releases the "City Manager's Budget Request and Five-Year Economic Forecast and Revenue Projections for the General Fund and Capital Improvement Program." Since 1986, the City has used this five-year forecast to assist in projecting revenue levels and expenditures based upon certain assumptions and expectations.

Pursuant to the City Charter, the Mayor releases an annual "budget message." This document describes the budget process, the current fiscal situation of the City and the strategy for developing the proposed budget, recommendations on specific budget items and other related issues. The City Council reviews the Mayor's budget message, and a public hearing is held to discuss the budget message prior to its approval by the City Council.

The City Charter requires that the City Manager release the Proposed Capital Budget and Capital Improvement Program and the Proposed Operating Budget at least thirty days prior to the beginning of each fiscal year, or at such earlier time as the City Council may specify. As currently directed by the City Council, in early May, the City Manager releases the Proposed Operating and Capital Budgets and a report recommending fees and charges to be imposed during the next fiscal year for City services, excluding the Airport (the “Proposed Fees and Charges Report”). Under current City practice, fees and charges related to the Airport are considered separately by the City Council.

The Proposed Operating Budget contains the complete financial plan for the City, including the Airport Department, for the next fiscal year. It describes activities by City Service Area, department and core service and makes recommended additions or reductions to those activities. The Proposed Operating Budget accounts for all revenue received by the City and accounts for the usage of the revenue. The City Council holds a number of study sessions beginning in May to discuss the proposed operating and capital budgets and also holds a series of public hearings on these proposed budgets in May and June.

In early June, the Mayor releases the final budget modification message. It contains changes to the proposed budget recommended by the Mayor after City Council review and discussion of the document during the budget study sessions and public hearings. In June, the City Council adopts the operating and capital budgets for the next fiscal year, along with the implementing appropriation ordinances and funding sources resolutions that appropriate the budgeted amounts to the respective departments. The City Council adopted the fiscal year 2014-15 Operating and Capital Budgets on June 10, 2014 and the implementing annual appropriation ordinance and related documents on June 17, 2014.

Though the Airport is a department within the City, and appears alongside other departments in the City’s budget documents, its revenues are accounted for separately from other City funds (including the General Fund) and cannot be redirected to other non-Airport uses.

There are a number of policies, agreements and legal restrictions that regulate the application of Airport revenue. The federal Airport and Airway Improvement Act of 1982 and related statutes mandate that airport owners/operators use all internally generated revenues for the capital/operating costs of their local aviation-related facilities. Federal grant agreements entered into by the Airport also contain this restriction. Additionally, the Airport is organized as a proprietary enterprise fund which requires that its costs be recovered with fees and charges, which must also be set on a cost-recovery basis. The amount the Airport paid for direct City services, excluding Police and Fire services, was approximately \$1.1 million in fiscal year 2012-13. The City also provides certain general support services to the Airport and charges a pro-rata fee. The amount charged to the Airport for these general support services for fiscal year 2012-13 was approximately \$3.1 million. See “LITIGATION—FAA Audit of Use of Airport Revenue—Cost Allocations.”

Current City practice calls for the preparation of Bi-Monthly Financial Reports that are distributed to the City Council as a method of monitoring the budget and financial status. In January of each year, the Mid-Year Budget Review is released providing a detailed and expanded analysis of the operating and capital budget status. In February of each year, the City Council considers this report and takes actions as necessary to maintain a balanced budget. The City Council’s Mid-Year Budget Review is not the only time that the City Council takes budget actions to maintain a balanced budget; at any public meeting, the City Council may amend or supplement the budget by affirmative vote of at least a majority of the total members of the City Council. Historically, the City Council has taken budget actions throughout the fiscal year to balance the budget or to make budget adjustments to respond to changing circumstances.

**Unrestricted Cash Balance.** As of May 31, 2014, the Airport's unrestricted cash balance was approximately \$98.7 million. Unrestricted cash balances fluctuate throughout the fiscal year due to timing of cash receipts and disbursements. During fiscal year 2012-13, month-end unrestricted cash balances ranged from a low of approximately \$66.9 million to a high of approximately \$94.7 million. No assurance can be given that the Airport's future unrestricted cash balances will be similar to its unrestricted cash balances in fiscal year 2012-13, and the Master Trust Agreement does not require that the Airport maintain any particular unrestricted cash balance.

**City Audit.** The City Council engages an independent certified public accountant (the "Accountant") who examines books, records, inventories and reports of all officers and employees who receive, control, handle, or disburse public funds and of any other officers, employees or departments as the City Council directs. These duties are performed both annually and upon request. For each fiscal year beginning with the fiscal year 2005-06 financial statements, the City retained Macias Gini & O'Connell LLP as the Accountant. Within 180 days following the end of each fiscal year, the Accountant submits the final audit to the City Council. The City then publishes the City's financial statements as of the close of the fiscal year in the Comprehensive Annual Financial Report.

In addition to the annual audit of the City's financial statements, the Accountant issues an annual audit report of the City's internal controls over financial reporting ("Management Report"). The deficiencies noted by the Accountant in the Management Report are incorporated in the Single Audit Reports for federal grant awards.

The 2012-13 Management Report noted two "significant deficiencies." A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. The first of these, which had also been made in the 2011-12 Management Report, related to the City's staffing reductions and the preparation of the City's financial statements. Specifically, the Accountant commented in the 2012-13 Management Report that "... the widespread reduction and displacement of staff through the Civil Service Rules resulted in a significant disruption in the City's ability to maintain appropriate financial internal controls." The Accountant recommended that the City should ensure that as additional staff are hired, adequate supervision and review processes should be put in place to mitigate against errors that the Accountant had identified during the 2012-13 audit.

The City's management, in its response to this finding in the 2012-13 Management Report, identified the actions it had taken to identify the existing internal controls throughout the City's organization during the fiscal year and its plan to retain a consultant "... to conduct a comprehensive study of the City's organizational structure for finance functions and ultimately recommend and aid in the facilitation of actions that will improve the effectiveness and efficiency of the City's internal controls." The consultant has been retained and is expected to provide a report of findings and recommendations by December 2014.

The second significant deficiency concerned the City's cost allocation plan methodology for the indirect costs of services provided to the Airport Department by other City departments. The specific issue raised by the Accountant was related to the City's procedure of using the budgeted number of full time Airport Department employees to allocate prior year's actual allowable costs, and that by not adjusting to actual numbers a disproportionate burden is placed on the Airport. A similar concern with respect to the Airport's indirect cost allocation plan was identified by the FAA as discussed below in "LITIGATION—FAA Audit of Use of Airport Revenue."

The City's management in its response to this second deficiency represented that the City's practice to apply the budgeted number of FTEs for all City departments included in the cost allocation

plan does not result in disproportionate allocation of indirect costs to any City department. The City also noted that it was in the process of updating its cost allocation procedures in order to ensure that the cost allocation methodology equitably distributes indirect costs. During fiscal year 2012-13, the City's internal auditor also had made recommendations on improvements to the development of the City's cost allocation plans. At this time, the City expects to update the procedures following the completion of the fiscal year 2015-16 plan.

The audited financial statements of the Airport for fiscal year 2012-13 are included as Appendix D to this Official Statement. The Accountant has not reviewed this Official Statement, has not been requested to consent to the inclusion herein of the audited financial statements and has not performed any post-audit review of the financial condition or operations of the Airport.

Except for City Charter requirements, the above-described budget and audit process is determined by internal policies and can be changed at any time.

### **Passenger Facility Charges**

Passenger Facility Charges ("PFCs") are fees authorized by the Aviation Safety and Capacity Expansion Act of 1990, as amended (the "PFC Act"), as implemented by the FAA pursuant to published regulations ("PFC Regulations"), to be collected from enplaned paying passengers to finance eligible, approved airport-related projects ("PFC Projects"). The PFC Act authorized the FAA to approve a PFC of \$1.00, \$2.00 or \$3.00. In 2000, the Wendell M. Ford Aviation Investment and Reform Act for the 21st Century ("AIR-21") was signed into law, allowing the FAA to authorize a PFC of \$4.00 or \$4.50. Airport operators are required to apply to the FAA for approval before imposing or using PFCs.

The City currently imposes a PFC of \$4.50 per paying enplaned passenger (net of a handling fee currently set at \$0.11 per PFC), except for passengers on carriers in the air taxis/commercial operators class of carriers which the FAA agreed could be excluded. PFCs are collected and remitted to the City by the airlines from paying passengers that enplane at the Airport. Pursuant to the PFC Regulations, the current \$4.50 PFC level collected by the City results in a 75% reduction in passenger based entitlement grants. See "—Federal Grants" below.

Airport industry groups have requested that federal PFC Regulations be changed to increase the PFC program's maximum PFC level from its current \$4.50 maximum. If the current \$4.50 maximum PFC level is increased by Congress, the City plans to seek FAA approval for a higher PFC level at the Airport.

As of June 30, 2013, the City is authorized by the FAA to impose and use PFCs, including investment income thereon (collectively, "PFC Revenues"), of up to \$1,067,934,000. The City estimates that it had collected approximately \$391.5 million in PFC Revenues from the Airport's passenger airlines through June 30, 2013 and had spent approximately \$355.06 million of that amount on approved projects (including debt service on certain Series of Bonds) as of the same date.

Debt Service paid with PFC Revenues is not included in the calculation of rates and charges payable by the airlines, and PFC Revenues are not included in the definition of pledged "General Airport Revenues" under the Master Trust Agreement. PFC Revenues, however, in some cases have been and, in the future, are expected again to be used (but not pledged) to pay the portion of Debt Service on the Outstanding Bonds that is allocable to PFC Projects, including Series 2007A Bonds, Series 2011A Bonds and Series 2014 Bonds. PFC Revenues may not be used to pay Maintenance and Operation Expenses or to pay debt service on Bonds other than Bonds that finance PFC Projects. Finally, when calculating Annual Debt Service, Debt Service in a given fiscal year will be reduced by the amount of any PFC

Revenues designated by the City as “Available PFC Revenues” and deposited with the Trustee to pay Debt Service in such fiscal year as provided in the Master Trust Agreement. See “SECURITY FOR THE BONDS—Other Available Funds, CFC Revenues and Available PFC Revenues” in the forepart of this Official Statement.

The annual amount of PFCs payable to the City depends upon the number of passenger enplanements at the Airport and the payment of PFCs to the City by the airlines. No assurance can be given that PFCs will actually be received in the amounts or at the times contemplated by the City. In addition, the FAA may terminate or reduce the City’s authority to impose PFCs, subject to informal and formal procedural safeguards, if the FAA determines that the City has violated certain provisions of the Airport Noise and Capacity Act of 1990, as amended (“ANCA”), the PFC Act (including as amended by the Vision 100-Century of Aviation Reauthorization Act, which was enacted on December 13, 2003 (the “Vision 100 Act”)), AIR-21 or the PFC Regulations, or if the FAA determines that PFC Revenues are not being used for PFC Projects or that implementation of such projects did not begin within the time frames specified in the PFC Act or the PFC Regulations. Future PFC applications may be denied if the FAA determines that the City violated any of its federal grant assurances or violated the PFC Act, AIR-21, the Vision 100 Act or certain other federal statutes and regulations applicable to airports. Amounts received or receivable under the PFC program are also subject to audit and adjustment by the FAA. See “CERTAIN FACTORS AFFECTING THE AIRPORT—Bankruptcy Risks” and “—Regulatory Uncertainties” in the forepart of this Official Statement and “LITIGATION—FAA Audit of Use of Airport Revenue” in this Appendix A.

### **Customer Facility Charges**

CFCs are collected by the rental car companies from their customers and then remitted to the City. From January 1, 2008 through November 30, 2011, the Airport imposed a CFC of \$10.00 per rental contract. Pursuant to Section 1936 of the California Civil Code (“Section 1936”) the City increased, effective December 1, 2011, the CFC to \$6.00 per contract day, to a maximum of five days, on each rental, and further increased the per contract day CFC to \$7.50 per contract day, to a maximum of five days, on each rental, commencing January 1, 2014. Section 1936 permits the City to further increase the per contract day CFC to \$9.00 commencing January 1, 2017, subject to an audit to be commissioned by the City, posted on the Airport website, and submitted to designated State Assembly and Senate Committees. Revenues from CFCs (referred to as “CFC Revenues” in the Master Trust Agreement) may be used to pay the reasonable costs to finance, design, and construct the ConRAC and to finance, design, construct and provide the ConRAC Transportation System (collectively, the “CFC Eligible Costs”). The City currently applies the CFC Revenues toward payment of debt service on debt obligations issued to fund CFC Eligible Costs (the “CFC Eligible Obligations”) and the City’s actual costs related to CFC Eligible Obligations. CFC Eligible Obligations currently include the Series 2011B Bonds. See “LEASE AND OPERATING AGREEMENTS—Parking, Rental Car, Concession and Other Agreements—Rental Car Agreements”.

Under the Master Trust Agreement, CFC Revenues (approximately \$13.4 million in fiscal year 2012-13) are excluded from the definition of “General Airport Revenues” and are not pledged to the payment of the Series 2011B Bonds; however, CFC Revenues may, at the option of the City, be designated as Other Available Funds to pay debt service on CFC Eligible Obligations. See “AIRPORT FINANCIAL MATTERS—Historical Operating Results” below and “SUMMARY OF CERTAIN PROVISIONS OF THE MASTER TRUST AGREEMENT—Other Available Funds” in APPENDIX C. While any Series 2011B Bonds remain outstanding, the City expects to designate CFC Revenues as Other Available Funds. Additionally, to the extent that any CFC Revenues have been designated as “Other Available Funds” and pledged to the payment of Debt Service as provided in the Master Trust Agreement, such CFC Revenues may be added to Net General Airport Revenues for the purpose of

satisfying certain requirements relating to the issuance of Additional Bonds. See “SECURITY FOR THE BONDS—Additional Series of Bonds—Conditions for the Issuance of Additional Bonds” in the forepart of this Official Statement.

The initial term of the City’s current agreements with the on-Airport rental companies for use of the ConRAC is 10 years, beginning June 1, 2010 and ending May 31, 2020, subject to two optional ten year extensions, which must be approved by the City and the rental car companies. Should all of the rental car companies determine at the expiration of the 10-year term not to extend the agreements, the City would not be able to continue to collect CFC Revenues after the on-Airport rental car companies vacate the ConRAC (other than for CFCs collected by off-Airport rental car companies for on-Airport common use transportation costs). In such event, the City would seek other tenants or uses for the ConRAC, but would remain responsible for payment of the remaining CFC Eligible Obligations from General Airport Revenues until such time as new rental car companies were to begin operations at the ConRAC and the City could again collect CFCs.

Because the ConRAC is located near Terminal B, only those rental car customers arriving or departing from Terminal A use the ConRAC Transportation System to and from the ConRAC. Therefore, in the event that any portion of CFC Revenues is available to pay ConRAC Transportation System costs, such transportation costs may only be paid from CFC Revenues collected by on-Airport rental car companies from customers arriving or departing from Terminal A. In order to apply the CFC Revenues to cover transportation costs, the specific rental car customer that used the transportation system must be identified. To date, no CFC Revenues have been applied toward transportation costs.

## **Federal Grants**

The Airport and Airway Improvement Act of 1982, as amended, created the Airport Improvement Program (the “AIP”), which is administered by the FAA. Grants are available to airport operators in the form of entitlement funds and discretionary funds and are payable on a reimbursement basis. Entitlement funds are apportioned annually based upon the number of enplaned passengers and the aggregate landed weight of all-cargo aircraft; discretionary funds are available at the discretion of the FAA based upon a national priority system. Funds obligated for the AIP are drawn from the Airport and Airway Trust Fund that is supported by user fees, fuel taxes, and other similar revenue sources that must be authorized and approved by Congress. Authority for the existing federal user fees, fuel taxes and other revenue sources for the Airport and Airway Trust Fund, FAA expenditure authority for the Trust Fund, AIP appropriations and FAA authority to issue AIP grants expire on September 30, 2015. See “CERTAIN FACTORS AFFECTING THE AIRPORT — Regulatory Uncertainties—General” in the forepart of this Official Statement.

The City currently receives approximately \$2.0 million of AIP entitlement grants per federal fiscal year ending September 30. In July 2013, the City received a grant agreement for \$5.2 million for the construction of the last phase of Taxiway W. In August 2014, the FAA notified the City that it would not disburse any further AIP entitlement grants to the City until the City submits an updated disadvantaged business enterprise (“DBE”) program for Airport capital projects to the FAA. The City submitted a draft updated capital project DBE program to the FAA on September 3, 2014, and the FAA acknowledged receipt of the City’s draft on September 4, 2014. Upon completion, the draft capital project DBE program will be subject to City Council approval, which is anticipated before the end of calendar year 2014. See “CAPITAL DEVELOPMENT AT THE AIRPORT—Five Year Capital Improvement Program.”

## **Federal Security Grants**

**Aviation Security Act.** In the immediate aftermath of the terrorist attacks of September 11, 2001, the FAA mandated new safety and security requirements, which have been implemented by the Airport and the airlines serving it. In addition, Congress passed the Aviation and Transportation Security Act (the “ASA”), which imposed additional safety and security measures. The ASA imposes additional security requirements on airlines and airport operators and imposes penalties against airport operators and airlines that violate ASA provisions (ranging from \$1,000 to \$10,000 for a single violation of a regulation by an airport operator).

Certain safety and security functions at the Airport were assumed by the TSA, which was established by the ASA and is now a part of the United States Department of Homeland Security (the “DHS”). Among other requirements, the ASA required that (i) explosive detection screening be conducted for all checked baggage; (ii) as soon as practicable after the date of enactment of the ASA, all individuals, goods, property, vehicles and other equipment entering secured areas of airports be screened; and (iii) security screeners be federal employees, United States citizens and satisfy other specified requirements. All ASA requirements currently mandated under TSA regulations have been implemented at the Airport. For passengers originating at the Airport, the TSA operates two separate security checkpoints, each containing eight security lanes. For passengers arriving on an international flight and connecting to a domestic flight, the TSA operates an additional checkpoint containing one security lane.

The Airport is one of a number of domestic airports in the nation where the backscatter x-ray whole-body imaging machines are being used by the TSA, although, under certain circumstances, passengers may still opt to be screened through the current metal detector system. The costs of acquisition and installation of the whole-body imaging machines at the Airport was paid for by the TSA.

**Security Grants.** The City currently participates in the TSA law enforcement officer reimbursement program over a three-year period, from October 1, 2012 through September 30, 2015. This program provides partial funding for the mandated security measure of providing a law enforcement officer presence at each passenger-screening location. Any federal funding provided through the reimbursement program would partially offset the Airport’s total security costs. In the first and second years of the program, the City was awarded approximately \$423,000 and \$161,000, respectively.

The TSA approved the renewal of a five-year cooperative agreement effective April 1, 2008, with an annual funding of \$200,500 for four explosive detection canine teams (\$50,000 per team plus \$500 for training). In April 2012, TSA awarded an increase in funding from \$50,000 to \$60,500 per team, or \$242,000 per year. The TSA has extended the funding agreement to March 31, 2015.

## **Historical Operating Results**

The following tables summarize operating revenues and maintenance and operation expenses at the Airport for fiscal years 2008-09 through 2012-13 and for the first ten months of fiscal years 2012-13 and 2013-14. The summary presented in Table 11 is derived from the audited financial statements of the Airport Department for fiscal years 2008-09 through fiscal year 2012-13.

**Table 11**  
**Norman Y. Mineta San José International Airport**  
**Summary of Operating Revenues and Maintenance and Operation Expenses**  
**Fiscal Years Ended June 30**

	2008-09 <sup>(1)</sup>	2009-10 <sup>(1)</sup>	2010-11 <sup>(1)</sup>	2011-12 <sup>(1)</sup>	2012-13 <sup>(1)</sup>
<b>Operating Revenues:</b>					
Airline Rates & Charges:					
Landing Fees	\$14,503,816	\$13,190,345	\$13,370,404	\$11,413,628	\$12,888,370
Terminal Rental	29,715,996	33,458,906	34,446,216	39,864,277	38,255,624
Total Airline Rates and Charges	<u>\$44,219,812</u>	<u>\$46,649,251</u>	<u>\$47,816,620</u>	<u>\$51,277,905</u>	<u>\$51,143,994</u>
Other Operating Revenues:					
Terminal Concessions	\$11,947,163	\$11,156,946	\$16,876,892	\$15,770,190	\$15,101,644
Airfield Area	3,170,562	2,791,491	2,924,976	2,783,446	3,038,241
Parking and Roadway <sup>(2)</sup>	44,228,032	38,934,371	47,320,098	51,023,465	46,700,448
Fuel Handling Fees	1,473,647	1,309,532	1,503,834	1,690,326	2,360,463
CFC Revenues <sup>(3)</sup>	6,713,160	6,021,365	0	0	0
General Aviation/Other	5,826,733	5,908,633	4,520,960	4,430,460	4,770,213
Total Other Revenues	<u>73,359,297</u>	<u>66,122,338</u>	<u>73,146,760</u>	<u>75,697,887</u>	<u>71,971,009</u>
Total Operating Revenues <sup>(4)</sup>	<u>\$117,579,109</u>	<u>\$112,771,589</u>	<u>\$120,963,380</u>	<u>\$126,975,792</u>	<u>\$123,115,003</u>
<b>Maintenance and Operation Expenses<sup>(5)</sup>:</b>					
Terminal Buildings	\$28,813,366	\$31,701,098	\$33,019,384	\$23,659,488	\$23,303,388
Airfield Area	16,170,121	10,911,014	9,748,512	9,068,812	8,706,904
Parking and Roadway	26,852,623	24,031,701	25,344,190	25,513,719	16,631,149
Fuel Handling Costs	557,036	885,303	287,530	556,312	1,064,804
General Aviation	4,072,008	3,052,466	2,409,245	1,676,382	1,605,119
General and Administrative	28,268,277	23,623,554	19,095,433	18,327,715	18,763,230
Depreciation and Amortization	20,646,758	55,288,220	51,532,165	51,519,769	54,352,406
Total Maintenance and Operation Expenses	<u>\$125,380,189</u>	<u>\$149,493,356</u>	<u>\$141,436,459</u>	<u>\$130,322,197</u>	<u>\$124,427,000</u>
<b>Net Operating Loss</b>	<b><u>(\$7,801,080)</u></b>	<b><u>(\$36,721,767)</u></b>	<b><u>(\$20,473,079)</u></b>	<b><u>(\$3,346,405)</u></b>	<b><u>(\$1,311,997)</u></b>

(1) Derived from the Airport Department's audited financial statements.

(2) Includes public parking, employee parking, taxi concession and other ground transportation fees, and rental car concession fees and space rentals.

(3) CFC Revenues are used to pay for capital and related debt service on Series 2011B Bonds associated with the ConRAC facility. CFC Revenues were reclassified from operating to nonoperating revenues beginning in fiscal year 2010-11 when the City started using them for the debt service associated with the ConRAC facility. CFC Revenues in 2010-11, 2011-12 and 2012-13 were approximately \$6.8 million, \$10.1 million and \$13.4 million, respectively.

(4) Does not include investment income, AIP grant proceeds or PFC Revenues. AIP grant proceeds and PFC Revenues are included in the City's audited financial statements as non-operating revenues.

(5) Includes certain expenditures for projects that are treated in the Airport Department's audited financial statements as maintenance and operation expenses, but that are paid from certain Airport capital funds, rather than from Operating Revenues deposited in the Maintenance and Operation Fund. This is the primary cause for the Net Operating Loss. See "—Management Discussion of Recent Financial Results—Airport Revenues and Expenses" and Table 12b.

Source: Norman Y. Mineta San José International Airport.

A "Net Operating Loss" is shown for each year in Table 11. This is primarily because the Maintenance and Operation Expenses in the audited financial statements include (1) depreciation and

amortization and (2) the non-capitalized construction costs, that are actually paid from certain Airport capital funds and not from the Maintenance and Operation Fund. These items are discussed in more detail under “Management Discussion of Recent Financial Results.” Table 12b, which presents the Airport’s historical debt service coverage, reflects adjustments to these items and certain other adjustments and demonstrates that the Airport’s actual debt service coverage has exceeded its Rate Covenant in each of the years shown.

The summary presented in Table 12a for the first ten months of fiscal years 2012-13 and 2013-14 is derived from the Airport Department’s unaudited, interim financial statements. The Airport Department’s unaudited, interim financial statements are prepared on a modified cash-basis, not on an accrual basis, and do not include items such as depreciation and amortization. In addition, the Airport Department’s unaudited interim financial statements do not include costs that are paid from capital funds but that are treated as maintenance and operation expenses in the Airport Department’s audited financial statements. The unaudited interim financial statements are also subject to year-end and other accounting adjustments and are not comparable to the financial statements summarized in Table 11.

While passenger enplanement activity declined between fiscal year 2008-09 and fiscal year 2012-13, the Airport increased revenues and decreased expenses during this period. Revenues were up primarily due to increases in rental rates for the airlines, rental car companies and concessionaires. Maintenance and operation expenses declined significantly during these fiscal years due to improved efficiencies and staffing reductions made in various service areas. See “Management Discussion of Recent Financial Results” herein for additional explanations regarding the changes in operating revenue and maintenance and operation expenses.

**Table 12a**  
**Norman Y. Mineta San José International Airport**  
**Unaudited Summary of Operating Revenues and Maintenance and Operation Expenses**  
**Ten Months Ended April 30, 2013 and 2014<sup>(1)</sup>**

	<b>Ten Months ended April 30, 2013</b>	<b>Ten Months ended April 30, 2014</b>
<b>Operating Revenues:</b>		
Airline Rates & Charges:		
Landing Fees	\$ 9,596,792	\$ 8,934,112
Terminal Rental	<u>31,002,931</u>	<u>30,869,273</u>
Total Airline Rates and Charges	\$40,599,723	\$39,803,385
Other Operating Revenues:		
Terminal Concessions	\$12,562,282	\$12,823,201
Airfield Area	2,370,850	2,777,102
Parking and Roadway <sup>(2)</sup>	36,253,045	38,097,760
Fuel Handling Fees	1,637,454	2,233,237
General Aviation and Other	4,968,563	6,412,868
Total Other Revenues	\$57,792,184	\$62,344,169
Total Operating Revenues <sup>(3)</sup>	\$98,391,907	\$102,147,553
<b>Maintenance and Operation Expenses</b>		
<sup>(4)</sup> :		
Terminal Buildings	\$16,369,954	\$16,969,438
Airfield Area	5,527,297	5,643,986
Parking and Roadway	11,864,659	11,519,983
Fuel Handling Costs	5,420	3,864
General Aviation	1,180,676	1,216,745
General and Administrative	13,179,489	13,347,459
Cost of Workers' Compensation Claims	291,702	22,436
Total Maintenance and Operation Expenses Before Depreciation and Amortization	\$48,419,196	\$48,723,910
Net Operating Income	\$49,972,711	\$53,423,643

<sup>(1)</sup> Unaudited. The information in this table is presented on a modified cash-basis and is derived from unaudited interim financial statements.

<sup>(2)</sup> Includes public parking, employee parking, taxi and other ground transportation fees, and rental car concession fees and space rentals.

<sup>(3)</sup> Includes investment income, but excludes PFC Revenues and CFC Revenues.

<sup>(4)</sup> Excludes depreciation and amortization and certain expenditures for projects that are treated in the Airport's audited financial statements as maintenance and operation expenses, but that are paid from certain Airport capital funds, rather than from Operating Revenues deposited in the Maintenance and Operation Fund. See "—Management Discussion of Recent Financial Results—Airport Revenues and Expenses."

Source: Norman Y. Mineta San José International Airport.

**Ten Months Ended April 30, 2014 (Unaudited).** The Airport Department's unaudited interim financial statements are prepared on a modified cash basis, not on an accrual basis, and do not include items such as depreciation and amortization. In addition, the Airport Department's unaudited interim financial statements do not include costs that are paid from capital funds but are treated as maintenance and operating expenses in the Airport Department's audited financial statements. The unaudited interim financial statements are also subject to year-end and other accounting adjustments and are not comparable to the financial statements discussed above in the section "Airport Revenues and Expenses."

The Airport achieved a net surplus of \$53,423,643 during the ten months ended April 30, 2014. This reflects an increase of \$3,450,932 over the same period of the prior fiscal year. The net surplus increase was the result of an increase in total operating revenues of \$3,755,646 offset by the increase in total maintenance and operation expenses of \$304,714 (before depreciation and amortization) for the ten-month period.

Increases have been posted in all operating revenue categories during the ten months ended April 30, 2014 except landing fees and terminal rentals. Due to the reduced landing fee rate as well as a number of airlines qualifying for the airline incentive program, even though passenger activity has increased during this period, landing fees and terminal rental revenue has decreased by \$796,338 in the aggregate. The largest increases were in parking and roadway and general aviation, which increased by \$1,844,715 and \$1,444,305, respectively. Increases in parking and roadway were reflective of the growth in passenger activity experienced by the Airport. The largest contributor to the general aviation and other revenues was the interim ground rent from Signature Flight Support, which is constructing a full service fixed base facility on the west side of the Airport. The increase can also be attributed to the land and building rent adjustments based on increases in appraised values and the consumer price index.

Total maintenance and operation expenses (before depreciation and amortization) increased by \$304,714 compared to the same period the prior fiscal year. The increase is primarily due to the increases in nonpersonnel expenses, overhead, and fees charged by the City for airport police services. The increases were largely offset by decreases in personnel expenses and costs of workers' compensation claims.

### **Management Discussion of Recent Financial Results**

**Overview.** Enplaned passengers at the Airport declined significantly between Fiscal Years 2006-07 and 2009-10. In addition to this significant reduction in air traffic, the debt service obligations of the Airport have increased significantly in recent years. In response, the City and the Airport have undertaken numerous measures, including cost-cutting and revenue enhancement initiatives. The cost cutting measures have included the elimination of employee positions, outsourcing of services (including parking and traffic control), relocation of Airport offices and reduction in police and fire related costs. The initiatives to increase revenues have included efforts to increase nonairline revenues (such as concession revenues and rental car revenues) and have included re-bidding agreements and transitioning from agreements that were based on cost-recovery rates to agreements based on market rates.

An additional measure undertaken by the Airport was the establishment of a cost per enplaned passenger ("CPE") target of \$12.00. The CPE was \$11.18 for fiscal year 2009-10, \$11.23 for fiscal year 2010-11, \$12.29 for fiscal year 2011-12 and \$11.94 for fiscal year 2012-13. The CPE is estimated to be \$11.38 for fiscal year 2013-14 and is budgeted to be \$10.50 for fiscal year 2014-15 based on a number of assumptions which may or may not materialize.

In fiscal year 2010-11, the City Council established a Council Committee (the "Airport Competitiveness Committee") to periodically consider recommendations to help ensure the success of the

Airport. The mission of the Committee is to ensure the success of the Airport by retaining current commercial air service and attracting other aviation services to the Airport.

***Airport Revenues and Expenses.*** Total operating revenues in fiscal year 2009-10 decreased by approximately 4.1%, or \$4,807,520 versus the prior fiscal year reflective of the decline in passenger and flight activities at the Airport. Decreases were posted in all revenue categories except terminal rental and general aviation/other revenues.

Total operating revenues in fiscal year 2010-11 posted a substantial increase of approximately 7.3% or \$8,191,791 over that of the prior fiscal year. The largest contributors to the increase were the terminal concessions and the parking and roadway categories, offset by a decrease in CFC Revenues. Terminal concession revenues tracked significantly higher than prior year revenues as a result of the new retail and food and beverage concessions that began operating with the minimum annual guaranteed payments. Increase in parking and roadway revenues was primarily due to the ConRAC Facility rents paid by the rental car companies. The Airport started using CFC Revenues in fiscal year 2010-11 for the debt service associated with the ConRAC and therefore, CFC Revenues were reclassified from operating to nonoperating revenues.

Total operating revenues grew by approximately 5.0% or \$6,012,412 in fiscal year 2011-12 primarily due to increases in terminal rentals and parking and roadway revenues. Terminal rentals increased due to higher terminal rental requirement as result of the increase in debt service. Parking and roadway revenues posted an increase due to the proceeds from the purchase/buyout agreement which allowed the Airport early termination of the operating lease covering 14 compressed natural gas (CNG) powered shuttle buses.

Total operating revenues in fiscal year 2012-13 decreased by approximately 3.0% or \$3,860,789 principally due to the decline in parking and roadway revenues. Lower ConRAC Facility rents were required from the rental car companies as a result of higher CFC Revenues generated. The decrease can also be attributed to the one-time revenue recorded in fiscal year 2011-12 relating to the proceeds from the purchase/buyout agreement of 14 CNG powered shuttle buses as mentioned above.

The amount of Maintenance and Operation Expenses shown in Table 11 includes depreciation and amortization and certain expenditures of projects that are treated in the Airport's audited financial statements as maintenance and operation expenses but that are paid from sources other than General Airport Revenues. Such other sources of funds include certain expenses paid from Airport capital funds that did not meet the criteria for capitalization into fixed assets. The total amount of such operating expenses paid annually from sources other than General Airport Revenues is shown in Table 12b. The majority of the expenses paid from Airport capital funds primarily related to noise mitigation projects in fiscal years 2008-09 through 2009-10 and Terminal C demolition costs in fiscal years 2009-10 and 2010-11. The operating expenses actually paid from the Airport's Maintenance and Operation Fund in fiscal years 2008-09 through 2012-13, were \$91,051,042, \$82,710,795, \$76,849,663, \$67,874,877 and \$64,974,015, respectively.

Maintenance and Operation expenses as reflected in Table 12b for fiscal years 2009-10, 2010-11, 2011-12, and 2012-13 decreased by \$8,097,976, \$1,256,917, \$8,960,213, and \$5,719,240, respectively, compared to the previous fiscal years. Significant components of these decreases include (i) the sizeable reduction of staffing levels; (ii) the decrease in overhead as a result of the reduced staffing levels and the rate reduction in fiscal years 2009-10 and 2010-11; (iii) the substantial decrease in building rent due to a reduction in leased administration spaces effective January 1, 2010, and the eventual termination of the lease effective November 30, 2010; (iv) the decreased amounts paid for parking and shuttle bus operators in fiscal year 2009-10 as a result of the reduced passenger activity; (v) the lower fees charged by the City

for ARFF services due to lower staffing requirements allowed by reduced passenger levels and reduced overhead rate in fiscal years 2009-10 and 2010-11, the capping of overhead rate at approximately 25% in fiscal years 2011-12 and 2012-13, and the matching of ARFF costs for City Fire Department staff with costs proposed if the ARFF services had been outsourced with the balance paid by the City for these services covered by the Staffing for Adequate Fire and Emergency Response grant in fiscal years 2011-12 and 2012-13; (vi) the significant reduction of the fees charged for police services as a result of the staffing model that took effect in February 2012; and (vii) the decline in the letter of credit fees associated with the commercial paper (CP) program after the City issued the Series 2011B Bonds in December 2011 to refund \$224.7 million CP notes.

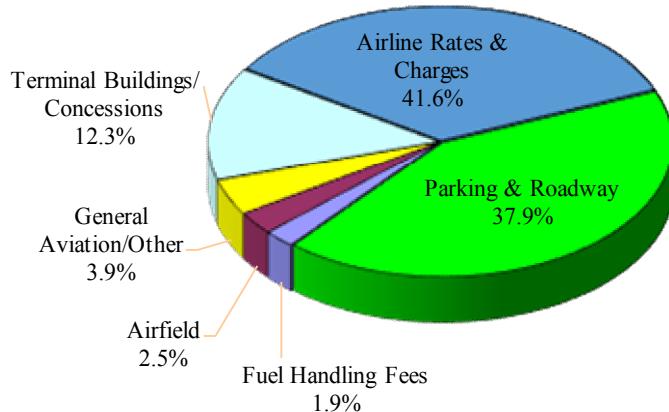
Depreciation and amortization posted a substantial increase of \$34,641,462 in fiscal year 2009-10 due to the fact that the Airport ended airline and concession operations in Terminal C on June 29, 2010 and accelerated its depreciation schedule. The demolition of Terminal C was completed in September 2010.

**Airline Rates and Charges.** The primary charges paid by the airlines are landing fees and terminal rentals for leased space. For fiscal year 2013-14, the average terminal rental rate was \$159.72 per square foot while landing fee rate was \$2.22 per 1,000 pounds of aircraft maximum gross landed weight (“MGLW”). For fiscal year 2014-15, the average terminal rental rate is \$147.68 per square foot while the landing fee rate is \$2.09 per 1,000 pounds of aircraft MGLW. See “CERTAIN FACTORS AFFECTING THE AIRPORT—Regulatory Uncertainties—Rates and Charges Regulation” in the forepart of this Official Statement.

**Parking and Roadway Revenues.** During fiscal year 2012-13, public parking revenues of approximately \$24,813,754 increased by 8.2% and concession fees and facility rent from rental car companies of approximately \$13,093,449 decreased by 0.3%, compared to fiscal year 2011-12. The Airport also derived \$3,887,641 in revenues in fiscal year 2012-13 from employee parking, dispatch and trip fees from taxi companies and other ground transportation operators and ground rental revenue and utility charges from rental car companies, compared to \$4,841,290 in fiscal year 2011-12. ConRAC Facility Rent paid by the rental car companies was \$3,320,457 in fiscal year 2012-13 and \$6,512,380 in fiscal year 2011-12. See “THE AIRPORT—Existing Facilities—Parking” and “LEASE AND OPERATING AGREEMENTS—Parking, Rental Car, Concession and Other Agreements” above.

**Revenue Diversity.** The chart below summarizes the Airport Department’s major sources of revenue for fiscal year 2012-13. As shown in the chart, the Airport Department derived approximately 41.6% of its revenues from the landing fees and terminal rentals paid by the airlines serving the Airport, compared to 37.4% in fiscal year 2011-12, and approximately 58.4% of its revenues from various sources other than the airlines (primarily parking, rental cars, terminal concessions, income from certain non-airline leases and interest income), compared to 62.6% in fiscal year 2011-12.

**Norman Y Mineta San Jose International Airport  
Major Sources of Revenues**



Percentage total does not add to 100% due to rounding.

**Source:** Norman Y. Mineta San José International Airport.

**Historical Debt Service Coverage.** The Annual Debt Service coverage ratios for the five fiscal years ended June 30, 2013, calculated in accordance with the Master Trust Agreement, are presented in Table 12b. The prior year's ending surplus, the amount that the City maintains as "rolling coverage" on the Bonds, transfers from the Rate Stabilization Fund, and the commercial paper proceeds are considered "Other Available Funds" and are added to the Net General Airport Revenues Available for Bond Debt Service under the Master Trust Agreement.

The Master Trust Agreement also provides a separate mechanism by which PFC Revenues can be applied to reduce the amount of Debt Service for purposes of the debt service coverage calculation. In fiscal year 2009-10, the City began applying PFC Revenues toward Debt Service. The City has also applied certain federal grant funds toward payment of Debt Service on the Bonds in fiscal years 2008-09 through 2011-12.

**Table 12b**  
**Norman Y. Mineta San José International Airport**  
**Historical Bond Debt Service Coverage**  
**Fiscal Years Ended June 30**

	<b>2008-09</b>	<b>2009-10</b>	<b>2010-11<sup>(3)</sup></b>	<b>2011-12</b>	<b>2012-13</b>
<b>Total Operating Revenues<sup>(1)</sup></b>	\$117,579,109	\$112,771,589	\$120,963,380	\$126,975,792	123,115,003
Adjustments to Total Operating Revenues					
Plus: Interest income and non-operating revenues	9,874,785	4,389,244	2,613,878	2,578,186	1,651,672
Less: Other revenues <sup>(2)</sup>	(7,412,558)	(6,934,991)	(39,536)	19,279 <sup>(6)</sup>	84,323 <sup>(6)</sup>
Adjusted Revenues	<u>\$120,041,336</u>	<u>\$110,225,842</u>	<u>\$123,537,722</u>	<u>\$129,573,257</u>	<u>\$124,850,998</u>
<b>Maintenance &amp; Operation Expenses</b>	\$125,380,189	\$149,493,356	\$141,436,459	\$130,322,197	\$124,427,000
Adjustments to Maintenance and Operation Expenses					
Less: Maintenance and operation expenses paid from sources other than General Airport Revenues <sup>(4)</sup>	(14,015,719)	(11,585,400)	(8,541,475)	(2,614,029)	(3,391,228)
Less: Unspent 2004 Bond Proceeds used to pay Operating Costs	0	0	0	(3,785,793)	(51,519,769)
Less: Depreciation and Amortization Expenses paid from Maintenance & Operation Fund	<u>(20,646,758)</u>	<u>(55,288,220)</u>	<u>(51,532,165)</u>	<u>(54,352,406)</u>	
Add: Interest expense	265,752	76,414	0	0	0
Add: Transfer to General Fund	103,120	0	0	115,010	0
Add: Transfer to Vehicle Maintenance & Operation Fund	205,087	14,645	0	0	0
Add: Administrative Fees on CP Program	205,087	14,645	0	0	0
Add: Bond Issuance Costs paid out of Fund 523	(240,629)	0	(4,513,156)	(4,642,739)	195,581 <u>(1,904,932)</u>
Adjusted Maintenance and Operation Expenses	<u>\$91,051,042</u>	<u>\$82,710,795</u>	<u>\$76,849,663</u>	<u>\$67,874,877</u>	<u>\$64,974,015</u>
Net General Airport Revenues	\$28,990,294	\$27,515,047	\$46,688,059	\$61,698,380	\$59,876,983
Plus: AIP grant proceeds	10,560,440	9,832,518	2,183,000	500,000	0
Commercial paper proceeds	0	741,923	0		
CFC Revenues	0	0	6,839,740	10,137,053	13,384,764
Unspent 2004 Bond Proceeds used to pay Debt Service	0	0	0	1,713,056	1,383,389
Unspent 2007 Bond Proceeds	0	0	0	0	4,418,719
Transfer from Rate Stabilization Fund	0	5,934,738	1,200,000	0	0
Prior year's ending surplus	33,101,042	29,336,101	35,458,972	33,987,539	30,642,898
Rolling coverage	<u>5,391,800</u>	<u>5,764,467</u>	<u>6,765,662</u>	<u>12,579,218</u>	<u>16,175,989</u>
Total: Other Available Funds	<u>\$49,053,282</u>	<u>\$51,609,747</u>	<u>\$52,447,374</u>	<u>\$58,916,866</u>	<u>\$66,005,759</u>
Net Revenues Available for Bond Debt Service	\$78,043,576	\$79,124,794	\$99,135,433	\$120,615,246	\$125,882,742
Revenue Bond Debt Service Requirement	\$23,036,635	\$31,367,070	\$53,889,951	\$80,725,630	\$86,324,804
Less: Available PFC Revenues	0	(4,588,000)	(21,388,340)	(21,336,421)	(22,099,631)
Net Revenue Bond Debt Service Payable from Revenues	\$23,036,635	\$26,779,070	\$32,501,611	\$59,389,209	\$64,225,173
Revenue Bond Debt Service Coverage Ratio	3.39	2.95	3.05	2.03	1.96

<sup>(1)</sup> Does not include CFC Revenues, PFC Revenues or AIP grant proceeds. AIP grant proceeds, CFC Revenues and PFC Revenues are included in the City's audited financial statements as non-operating revenues.

<sup>(2)</sup> Includes reimbursements from the Airport's tenants for improvements initially funded by the Airport. Under the Master Trust Agreement, these payments are excluded from the definition of "General Airport Revenues" and are not pledged to the payment of Bonds. See "SECURITY FOR THE BONDS—Pledge of General Airport Revenues" in the forepart of this Official Statement.

<sup>(3)</sup> CFC Revenues are used to pay for capital and related debt service associated with the ConRAC facility. CFC Revenues were reclassified from operating to non-operating revenues retroactive to fiscal year 2010-11 when the City started using them for the debt service associated with the ConRAC facility.

<sup>(4)</sup> Consists of Maintenance and Operation Expenses that were paid from available moneys other than General Airport Revenues, which consist primarily of certain capital projects that did not meet the criteria for capitalization into fixed assets that were paid from Airport capital funds and transportation expenses paid by moneys other than General Airport Revenues.

- (5) Letter of credit fees associated with the Subordinated Commercial Paper Notes, net of capitalized fees. Letter of credit fees are reflected in this Table 12b and in Table 11 as a Maintenance and Operation Expense for accounting purposes; however, fees imposed pursuant to the reimbursement agreements relating to such letters of credit are Subordinate Obligations and are not incorporated in Maintenance and Operation Expenses for purposes of calculating debt service coverage.
- (6) At the end of each of fiscal years 2011-12 and 2012-13, the Airport reimbursed certain tenants the portion of their deposits which exceeded the costs of the tenant improvements.

*Source:* Norman Y. Mineta San José International Airport.

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## CAPITAL DEVELOPMENT AT THE AIRPORT

The Airport's capital development program (the "Airport Development Program") has been formulated through a master planning process, which originally received City Council approval in 1997. The Airport Development Program consists of two phases, Phase 1 and Phase 2. The City has substantially completed Phase 1 of the Airport Development Program, which includes projects in the Terminal Area Improvement Program, as described below under "—Phase 1 of the Airport Development Program." Projects in Phase 2 of the Airport Development Program are pre-approved in the Airline Lease Agreement, but construction of the Phase 2 projects is contingent upon satisfying specified activity based triggers. See "LEASE AND OPERATING AGREEMENTS—Airline Agreements" herein and "SUMMARY OF CERTAIN PROVISIONS OF THE AIRLINE LEASE AGREEMENT—Capital Expenditures" in Appendix G.

### **Airport Master Plan**

In 1997, after extensive planning and environmental studies and reports, the City Council approved a new master plan for the Airport (the "Master Plan"). In a Record of Decision issued on December 6, 1999, the FAA conditionally approved a new Airport Layout Plan (the "ALP") displaying the Master Plan projects and unconditionally approved all of the near-term projects. Both the Master Plan and the ALP have been amended several times since 1997 and currently are intended to provide facility improvements needed to accommodate forecast demand in the year 2027 for commercial passenger service, air cargo and corporate general aviation demand. The Master Plan includes both the substantially complete Phase 1 and the planned Phase 2 of the Airport Development Program, which collectively comprise improvements to the Airport's terminal facilities, roadways, parking facilities and airfield facilities, and includes 1.075 million square feet of passenger terminal facilities comprised of up to 49 gates; parking and garage facilities comprised of up to 16,200 public parking spaces, 2,600 employee parking spaces and 10,000 rental-car parking spaces (including 2,000 ready-return spaces); air cargo facilities; ground transportation, roadway and other access improvements; and runway improvements. In the fall of 2005, and in recognition of how current market conditions were impacting passenger growth, the Airport and its airline tenants reexamined the Master Plan and developed the Terminal Area Improvement Program, a program for implementing the Master Plan by aligning ongoing and planned construction activities with available fiscal resources, taking into account revised passenger growth projections. In June 2006, the City Council approved an amendment to the Master Plan to incorporate the Terminal Area Improvement Program and other Airport Development Program revisions.

In June 2010, the City Council approved an additional amendment to the Master Plan that updated projected aviation demand and facility requirements. This amendment to the Master Plan modified specific components of the Airport Development Program. Pursuant to the amended Master Plan, the former interim long-term public parking and employee parking lots on the northwest side of the Airport (which have been relocated to the east side terminal area) are designated for development of facilities to accommodate projected growth in general aviation demand. The 29-acre Signature FBO development is located in this portion of the Airport, and an additional 15 acres north of the FAA air traffic control tower remains available for future general aviation development opportunities. See "THE AIRPORT—Existing Facilities—General Aviation Facilities."

### **Phase 1 of the Airport Development Program**

Construction of the Phase 1 projects was substantially complete in fiscal year 2010-11. The Phase 1 projects included nine new gates and approximately 366,000 square feet of new terminal space;

design and construction of the new Terminal B; improvements to the existing Terminal A, including new ticketing facilities, a new in-line baggage system that serves both Terminals A and B and security checkpoint, lobby concessions and other improvements; the phased demolition of Terminal C; design and construction of the ConRAC; realignment and improvement of existing terminal roadways; parking improvements; airfield projects, including noise mitigation and the reconstruction of Taxiway Y; and other improvements, including construction of a new belly freight facility and an ARFF facility. The Phase 1 projects also include design of certain Phase 2 projects, but under the Airline Lease Agreement the commencement of construction of the Phase 2 projects is contingent upon satisfying specified activity-based triggers.

### **Phase 2 of the Airport Development Program**

Phase 2 projects will consist primarily of the design and construction of the South Concourse of Terminal B and the second phase of Terminal B, including a total of 12 additional gates, and a new central plant facility. Under certain circumstances, the City is required to consult with the Signatory Airlines before proceeding with additional future capital developments. Phase 2 projects are pre-approved in the Airline Lease Agreement, but construction of the Phase 2 projects is contingent upon satisfying specified activity based triggers. Pursuant to the terms of the Airline Lease Agreement, the Airport must have either 217 scheduled operations on any one day or 12.2 million enplaned and deplaned passengers in any given fiscal year in order to begin the Phase 2 projects. See “SUMMARY OF CERTAIN PROVISIONS OF THE AIRLINE LEASE AGREEMENT—Capital Expenditures” in Appendix G and “PASSENGER SERVICES AND OPERATION—Landed Weight and Airport Operations” herein.

### **Costs and Funding Sources of the Airport Development Program**

Phase 1 of the Airport Development Program, which is substantially completed, was initially budgeted at \$1.3 billion (including, among other costs, design, engineering, construction, reserves, contingency, insurance and escalation for inflation). Phase 1 costs were funded from a combination of federal grants, PFC Revenues, internally generated Airport funds and the proceeds of Bonds and Subordinated Commercial Paper Notes.

Costs of Phase 2 of the Airport Development Program are currently estimated at \$400 million in 2011 dollars; however, under the Airline Lease Agreement, the commencement of construction of the Phase 2 projects is contingent upon satisfying specified activity-based triggers. See “—Phase 2 of the Airport Development Program.” The City expects sources of funding for Phase 2 projects to include (but not necessarily be limited to) federal grants, PFC Revenues, internally-generated Airport funds, and, if necessary, Airport user fees, the proceeds of additional Bonds or Subordinated Commercial Paper Notes.

### **Five Year Capital Improvement Program**

In June 2014, the City also adopted a five year, 2015-2019 Airport Capital Improvement Program primarily comprised of projects that are not part of either Phase 1 or Phase 2 of the Airport Development Program (the “CIP”). The CIP is updated annually and reflects the Airport Department’s prioritization of projects that address a variety of requirements and needs, including public safety, regulatory requirements, accommodation of air carrier and general aviation operations, and the convenience of the travelling public and that are balanced against the maintenance of competitive rates and charges imposed on the airlines. As summarized below, the estimated costs for the projects included in the CIP total approximately \$67.0 million and are subject to change. Approximately 62% of the estimated CIP costs are contingent upon the receipt of grant funding and the future availability of other Airport funds.

<b>Five Year CIP</b>	<b>Estimated Cost (millions)</b>
Southeast cargo ramp reconstruction	\$14.3
Upgrade current ARFF Facility	14.0
Extension of Taxiway H and K	6.4
Westside airfield configuration	6.0
Pavement maintenance and runway rehabilitation	4.0
Security exit control doors	3.0
ARFF vehicle replacement	2.1
Operations system replacement	1.9
Terminal building modifications	1.6
Ground transportation island – terminal A	1.4
Other Airfield Facility Projects	2.4
Other Aviation Support Projects	5.3
Other (aviation, environmental, terminal)	4.6
Total 5-Year CIP:	\$67.0

All Signatory Airlines have Majority In Interest (“MII”) participation rights with respect to airfield CIP projects; only passenger Signatory Airlines have MII participation rights with respect to terminal CIP projects. MII review of CIP projects by the Signatory Airlines only applies to projects that: (a) will affect airline rates and charges during the term of the Airline Lease Agreement; and (b) have gross project costs expected to exceed \$5 million. MII review will not apply to projects: (a) that are required by the federal government; (b) that must be rebuilt or replaced to meet the Airport’s obligations under the Airline Lease Agreement or applicable law; (c) that are required to respond to emergencies in order to keep the Airport open for public use; (d) that are undertaken in cost centers other than the airfield and terminal cost centers; (e) for the increased requirements of any Signatory Airline(s) if such Signatory Airline(s) agree to increased rentals, fees, and charges sufficient to cover the annual debt service associated with the project; or (f) that are for special purpose facilities for which the user will pay or reimburse the Airport.

The City may not proceed to design or build CIP projects that are subject to MII review without first giving the Signatory Airlines a detailed description of the purpose and expected costs of each such project and an opportunity to voice any objections to the project. If an MII review by the Signatory Airlines does not disapprove the project, the Airport may proceed with design and construction. If, within 60 days of the Airport’s notice, an MII review by the Signatory Airlines disapproves the proposed project, the Airport shall defer the project for a period of up to one year to allow for further consultation with the Signatory Airlines. At the end of the one-year deferral period, the Airport may proceed with the project notwithstanding any remaining airline objections.

The threshold for approval in the MII review process for airfield CIP projects is at least 50% of the Signatory Airlines with at least 50% of the total landing fees paid by the Signatory Airlines during the preceding fiscal year. The threshold for approval in the MII review process for terminal CIP projects is at least 50% of the Signatory Airlines who together have (a) paid at least 50% of the total Signatory Airlines’ terminal rents during the preceding fiscal year; and (b) carried at least 50% of the enplaned passengers in the preceding fiscal year.

## Environmental Matters

***Master Plan CEQA and NEPA Compliance.*** All Airport development is subject to the requirements for environmental studies and appropriate clearances under the California Environmental

Quality Act (“CEQA”) and, where federal funding or other federal actions are involved, to the requirements of the National Environmental Policy Act (“NEPA”).

An Environmental Impact Report under CEQA was prepared and certified by the City of San José (the “Master Plan EIR”) for the Master Plan adopted on June 10, 1997. Under the provisions of the San Jose Municipal Code, the Master Plan has been formally amended over time since the original 1997 adoption of the updated Master Plan. In associated conformance with CEQA, updates to the Master Plan EIR have also been approved through one Supplemental EIR and several EIR addenda. The most recent update to the Master Plan EIR (10<sup>th</sup> Addendum) was approved by the City on October 25, 2013.

An Environmental Impact Statement under NEPA was prepared by the FAA (the “Master Plan EIS”) for the updated Airport Layout Plan (“ALP”) displaying the proposed Airport Master Plan improvements, with a Record of Decision issued on December 6, 1999, providing unconditional approval of the Master Plan Phase 1 project improvements shown on the updated ALP. Projects scheduled for later phases of implementation received FAA conditional approval, indicating the potential need for subsequent NEPA clearance. As the ALP has been amended over time to reflect the City-adopted amendments to the Master Plan, the FAA has conducted applicable NEPA clearance. The most recent NEPA clearance for an ALP amendment was issued on April 15, 2014.

**Airport Noise and Capacity Act of 1990.** The Airport Noise and Capacity Act of 1990 (“ANCA”) provides for a phaseout of Stage 2 aircraft by December 31, 1999 and also limits the scope of the local airport operator’s regulatory discretion for adopting new aircraft operational restrictions for noise purposes. The FAA subsequently adopted regulations implementing ANCA under Part 161 of the Federal Aviation Regulations (“Part 161”). From 1990 forward, airport proprietors considering the adoption of restrictions or prohibitions on the operation of Stage 2 and Stage 3 aircraft are required to conduct studies that detail the economic costs and benefits of proposed restrictions, to publish proposed restrictions and to provide notice to potentially affected airlines and conduct any necessary environmental analysis, prior to enacting restrictions on the operations of Stage 2 or Stage 3 aircraft. Proposed restrictions on the operation of Stage 3 aircraft adopted after 1990 also require affirmative approval of the FAA under defined statutory criteria before they may legally be implemented. ANCA and Part 161 make the adoption of many traditional aircraft operating noise regulations by local airport proprietors infeasible without the concurrence of the airlines or other operators affected by the restrictions. Subject to certain procedural safeguards, violations of ANCA or of Part 161 could result in termination of an airport’s authority to impose and use PFCs or to receive AIP grant awards.

**California Airport Noise Regulations.** From 1972 until 2012, the Airport operated under a variance pursuant to the California Airport Noise Regulations (CCR Title 21, Division 2.5, Chapter 6) (the “Noise Regulations”). The Noise Regulations identify an exterior 65 decibel (“dB”) Community Noise Equivalent Level (“CNEL”) contour at an airport as the “Noise Impact Boundary.” The Noise Regulations provide that no proprietor of a “noise problem airport” shall operate an airport with a Noise Impact Boundary based on the standard of 65 dB CNEL, unless the operator has applied for or received a variance as prescribed by the Noise Regulations. To obtain a variance, an airport that has been deemed a noise problem airport by the county in which the airport is located must demonstrate to the State that it is making good faith efforts to eliminate incompatible land uses within the Noise Impact Boundary. Under the Noise Regulations, residential land uses may be made compatible through land acquisition, sound insulation to an interior noise level of 45 dB CNEL, or by obtaining aviation easements for the incompatible land uses. See “—ACT Program” below. Once the county determines that an airport is a noise problem airport, an airport will remain subject to the variance requirement under the Noise Regulations until such time that the county determines that the airport is no longer a noise problem airport.

The Santa Clara County Board of Supervisors designated the Airport as a noise problem airport on June 19, 1972. Since that time, the State has issued a successive series of three-year variances to the City. Because the City has eliminated incompatible land uses within the Noise Impact Boundary through completion of its ACT Program (described below), in 2011 the City requested that Santa Clara County determine that the Airport is no longer a noise problem airport. On May 24, 2012, the County of Santa Clara verified that the Airport meets the noise standard as required in Section 5012 of the State Noise Standards and no longer requires a variance. The Airport will continue to be monitored with respect to the noise impact, and a variance could be required in the future.

**Land Use Compatibility Measures.** Since the late 1960s, the City has undertaken a series of land use compatibility measures to minimize the effects of aircraft noise on neighborhoods surrounding the Airport, and to provide an airport approach zone. These measures have included land acquisition, aviation easements, noise insulation of existing residences and schools and use of planning and building code measures to increase compatibility with Airport operations.

The City began acquiring residential and other incompatible land uses in the area to the south of the Airport in the late 1960s, for both approach zone and noise compatibility purposes. All 625 parcels, totaling approximately 120 acres, within this southern acquisition area have been acquired, largely, with federal grant funds. The area is designated as Public Park/Open Space in the City's General Plan. In compliance with the conditions to the federal grants used to fund the acquisition program, any reuse of property would require approval by the FAA. See "LITIGATION—FAA Audit of Use of Airport Revenue—Guadalupe Gardens" herein.

The City has also completed the acquisition of fee interests and habitation rights in two former mobile home parks to the north of the Airport, and the uses of such properties have been converted to uses compatible with Airport operations.

**ACT Program.** In 1993, the City Council established the Acoustical Treatment Program (the "ACT Program") for the noise insulation of residences and other incompatible structures, such as schools, surrounding the Airport. The purpose of the ACT Program was to improve the living environment of eligible residences and other structures by reducing interior noise to meet an interior noise level of 45 dB CNEL, as required by the Noise Regulations. Typical treatment included the replacement of windows and doors and the installation of attic insulation, weather-stripping and air conditioning. Participation in the ACT Program was voluntary. Undertaking the ACT Program was a required noise mitigation measure included in the Master Plan approved by the City Council in 1997 and by the FAA in 1999.

The ACT program was completed in January 2010. From its inception in 1989-1990, the program treated over 2,400 dwelling units and four schools using \$139.8 million in AIP grants and PFC Revenues. The Airport continues to conduct acoustical testing on an as-requested basis.

**Airport Noise Control Program.** Since 1973, time of day operational restrictions or a scheduling "curfew" has been in effect at the Airport, when it was promulgated by the Airport Director pursuant to the authority granted under the City's Municipal Code (the "Curfew"). The Airport Noise Control Program containing these restrictions was adopted in 1984 by the City Council as a formal Airport regulation and was subsequently amended by an ordinance adopted by the City Council on October 21, 2003 (the "Curfew Ordinance"). Under the Airport Noise Control Program, as amended by the Curfew Ordinance, jet aircraft operators are prohibited from scheduling or conducting takeoffs or landings between 11:30 p.m. and 6:30 a.m. (local time), unless any such takeoff or landing is conducted by a jet aircraft that is listed on a Schedule of Authorized Aircraft issued by the Director of Aviation. If a jet aircraft is not listed on the Schedule of Authorized Aircraft, the aircraft will be allowed to operate during Curfew Hours only if the operator demonstrates in writing to the Director of Aviation that the FAA part

36 manufacturer-certificated noise level of such aircraft (using the arithmetic average of the takeoff, sideline and approach noise levels) is equal to or less than 89.0 Effective Perceived Noise Decibel Level (“EPNdB”). In addition, Stage II aircraft operators (other than certain governmental operators) may only conduct takeoffs or landings at the Airport between the hours of 7:00 a.m. and 11:00 p.m., unless the aircraft was delayed solely because of a force majeure event. Operational procedures to minimize aircraft noise on departure are implemented by the FAA through its Air Traffic Control personnel. These procedures are intended to minimize noise impact on the surrounding community. By letter dated October 2, 2003, the FAA acknowledged that the Airport Noise Control Program is “grandfathered” under ANCA because it was adopted prior to 1990, and the FAA also found that the amendments made to the Airport Noise Control Program by the Curfew Ordinance do not present a current issue of noncompliance under either ANCA or the City’s federal grant assurances. See “—Airport Noise and Capacity Act of 1990” above.

***Underground Fuel Tanks.*** Until December 22, 1998, the City and Chevron U.S.A., Inc. (“Chevron”), operated adjacent fuel storage facilities at the Airport. The City’s facilities have not been in operation since December 22, 1998, when the facilities were closed in response to the federal deadline for upgrade or closure of underground storage tanks. Chevron operated its fuel storage facility at the Airport until the opening of the new fuel storage facility owned and operated by a consortium of airlines in December 2009.

The City and Chevron entered into an agreement effective November 30, 2009, for coordinated corrective actions at the closed City and Chevron fuel storage facility sites at the Airport. Under the agreement, Chevron is the lead in coordinating and reporting to the regulators, conducting investigations, and performing remedial activities. The agreement provides for a 50/50 cost sharing responsibility for costs accrued until successful closure of the sites. In early 2014, the City applied for closure of the site with Santa Clara County. The City has also requested reimbursement from the State’s Plume Fund for the full amount of the costs incurred for these corrective actions. Any reimbursement received from the State will be split 50/50 between the Airport and Chevron. As of June 30, 2013, the Airport has accrued its 50% of the remediation costs totaling \$1,045,000, and has accrued \$1,758,000 to cover the costs of its portion of the interim remediation system. As of June 30, 2013, the City estimates that the costs to further investigate and cleanup the site will be between \$1,400,000 and \$2,000,000 depending upon the method of accomplishment and actual remediation requirements.

## OTHER MATTERS

### **Security Matters**

Since April 2014, there have been two incidents at the Airport involving Airport security. In April, a fifteen year old boy climbed over the Airport perimeter fence, climbed into the wheel well of a Hawaiian Airlines aircraft that was parked overnight at the gate, slept in the wheel well overnight, and survived the flight to Maui that departed from the Airport the next morning. The second incident in August involved a female transient who evaded TSA passenger screening and Southwest gate agents to board a Southwest flight to Los Angeles. In light of these incidents, a City Council Committee is scheduled to consider the matter of Airport security at its September 25, 2014 meeting. The TSA and the affected airlines are currently reviewing these incidents internally and with Airport staff. The City is reviewing certain perimeter security improvement recommendations that are more extensive than current regulatory requirements, but it is unknown at this time if any additional security measures will be implemented as a result of either the TSA’s or the City’s review.

## **Investment Policy and Practices of the City**

The City and its related entities are required to invest all funds under the Director of Finance's control in accordance with principles of sound treasury management and in accordance with the provisions of the California Government Code, the Charter, the City Municipal Code and the City Investment Policy (the "Policy"). The Policy was originally adopted by the City Council on April 2, 1985 (Resolution No. 58200) and is reviewed annually by the City Council.

On September 10, 2013, the City Council adopted the existing Policy that is consistent with the California Government Code. Minor revisions to the Policy are proposed, subject to approval by the City Council at its September 16, 2014 meeting. The primary objectives of the Policy, in their order of priority, are to (1) provide for the safe preservation of principal, (2) ensure that there is sufficient liquidity for operating needs, and (3) attain the maximum yield possible as long as investment practices are consistent with the first two stated objectives.

The City has not entered into any interest rate or commodity swap or hedging agreements and does not currently expect to enter into any such agreements.

## Investment Portfolio

As of June 30, 2014, the book value of the City's pooled investment fund was \$1,447,933,266 while the market value was \$1,449,219,386. The fund is classified by different types of investment securities. The composition of this fund, including the weighted average days to maturity and yield, is provided in Table 13. Airport monies invested in the fund represented approximately 11.13% of the fund.

To prevent potential loss of principal on any of the City's investments, the Policy strictly limits the composition of the holdings within the Investment Portfolio. The Finance Department's investment staff continues to focus investment decisions in accordance with the Policy's primary investment objectives as described above in "Investment Policy and Practices of the City."

**Table 13**  
**City of San José Pooled Investment Fund**  
**General Pool Investments**  
**As of June 30, 2014<sup>(1)</sup>**

	Book Value	Percent of Portfolio	Market Value	Weighted Average Days to Maturity	Weighted Average Yield
U.S. Treasury Bills and Notes	\$25,978,446	1.79%	\$25,983,870	741	0.382%
Federal Agency Securities <sup>(2)</sup>	1,083,656,057	74.84	1,084,805,885	712	0.730
Medium Term Notes (corporate)	0	0.0	0	0	0.000
Bankers Acceptance	0	0.0	0	0	0.000
Commercial Paper	190,788,763	13.18	190,919,453	73	0.200
Repurchase Agreements	0	0.0	0	0	0.000
Negotiable Certificate of Deposit	63,000,000	4.35	63,000,178	1	0.164
Money Market Mutual Fund	10,000	0.001	10,000	1	0.010
State of California Local Agency Investment Fund <sup>(3)</sup>	84,500,000	5.84	84,500,000	1	0.221
Total <sup>(4)</sup>	\$1,447,933,266	100.0%	\$1,449,219,386	556	0.592%

<sup>(1)</sup> Excludes funds invested in separate, segregated accounts as part of City held invested funds; excludes bond proceeds held by fiscal agents/trustees.

<sup>(2)</sup> Composed only of Federal Home Loan Bank (FHLB), Federal National Mortgage Association (FNMA), Federal Home Loan Mortgage Corporation (FHLMC), and Federal Farm Credit Bank (FFCB) securities.

<sup>(3)</sup> Estimated based upon City's participation in the Local Agency Investment Fund (LAIF). Weighted average yield for LAIF is based upon the most recently reported quarterly earnings rate.

<sup>(4)</sup> Totals may not add due to independent rounding.

Source: City of San José Finance Department.

In November 2012, the Airport transferred the remaining bond proceeds from Airport Revenue Bonds, Series 2007A and Series 2007B from the Trustee to the City. These proceeds funded a number of capital projects at the Airport, which are completed. The remaining proceeds of the Series 2007A Bonds were transferred to the City to pay ongoing Airport capital project costs, while proceeds of the Series 2007B Bonds were transferred to the City to pay debt service on these Bonds. The moneys are held in separate investment funds, managed and invested by the City staff. As of June 30, 2014, the book value of Series 2007A investment fund and Series 2007B investment fund were \$47,403,411 and \$26,387,462, respectively.

## **Retirement Plans**

**Overview.** With the exception of certain unrepresented employees, all regular full-time and certain part-time City employees, including employees assigned to the Airport, participate in one of two public employee defined benefit retirement plans (“Retirement Plans”) established pursuant to the City Charter: the Federated City Employees’ Retirement System (the “Federated Plan”) and the Police and Fire Department Retirement Plan (for sworn employees) (the “Police and Fire Plan”). Both Retirement Plans consist of a single-employer defined-benefit pension plan (“Pension Plan”) and a postemployment healthcare plan (“Healthcare Plan”). Each Retirement Plan is administered by its own Board of Administration (each a “Board”), and day-to-day operations are carried out by the City’s Department of Retirement Services.

The specific terms of each Retirement Plan are set forth in the City’s Municipal Code. Each Retirement Plan has different benefit tiers. The Federated Plan has Tier 1, Tier 2 and Tier 2B with the same reduced pension benefits in Tier 2 and Tier 2B as compared to Tier 1, the same retiree healthcare and dental benefits in Tier 1 and Tier 2 and no retiree healthcare and dental benefits for Tier 2B. The Police and Fire Plan has Tier 1 and Tier 2 for the police members only with reduced pension benefits for the Tier 2 police members as compared to the Tier 1 members and the same retiree healthcare and dental benefits for both tiers.

Both Pension Plans are structured as tax-qualified defined-benefit plans in which a pension benefit (an allowance paid on a monthly basis) is based upon salary and length of service. The Healthcare Plans were established under Internal Revenue Code Section 401(h) and are accounts within the Pension Plans for retiree healthcare and dental benefit funding and for the payment of these retiree benefits. In addition, the City Council has established Internal Revenue Code Section 115 Trusts as a supplement to the 401(h) accounts. The 115 Trusts and the 401(h) accounts are collectively referred to as the Healthcare Plans.

Both Pension Plans pay a monthly pension allowance and provide either fixed or index-based cost of living increases. The Healthcare Plans pay all, or a portion of, health and dental insurance premiums for qualified retirees and their survivors and dependents. Participation by covered employees in the applicable Retirement Plans is mandatory. Employees contribute a percentage of their salaries to the applicable Retirement Plans, and the City provides funding either through contributions equal to a percentage of its full-time employee covered payroll or on a lump-sum basis. The City does not participate in the Federal Social Security System.

In 2012, the City Council placed a measure on the June 2012 ballot entitled *The Sustainable Retirement Benefits and Compensation Act* and designated as Measure B (“Measure B”) which modified the provisions in the City Charter concerning the Retirement Plans and established maximum parameters for any new retirement plan for new employees. Measure B currently is the subject of litigation and administrative proceedings.

For a more detailed discussion of the City’s Retirement Plans, service retirement formulas, contributions and their calculation, funding status, other post-employment benefits, and implementation of Measure B, see “CITY OF SAN JOSE: RETIREMENT PLANS” in Appendix B.

**Funding Status and Contribution Rates.** Each Board employs the services of an actuary (Cheiron is the actuary for both Retirement Plans). The total contribution rates for employees and the City are based upon actuarial calculations that take into consideration a number of assumptions, including assumed investment earnings on the valuation assets of the Pension Plans and the Healthcare Plans that are used to pay benefits. Prior to fiscal year 2010-11 actuarial valuations for the retirement benefits of

both Pension Plans were prepared on a biennial basis. Commencing with the June 30, 2009 actuarial valuations, the valuations for both Pension Plans and both Healthcare Plans are prepared on an annual basis.

As of June 30, 2013, the actuarial funding status of the Pension Plan within the Federated Plan and the Police and Fire Plan was 59% and 78%, respectively, and the funding status of the Healthcare Plan (on a GASB basis) within the Federated Plan and the Police and Fire Plan was 18.1% and 10.7%, respectively.

In each actuarial valuation for each of the Pension Plans, Cheiron recommends contribution rates for the fiscal year beginning after the completion of that actuarial valuation. When actuarial recommended contribution rates are approved by the respective Boards of the Pension Plans, these become the City's and the employees' legally required contribution rates for the fiscal year beginning one year after the valuation date. For example, the recommended contributions contained in each of the actuarial reports for the Pension Plans as of June 30, 2013 apply to contributions by the City and the employees for the fiscal year beginning July 1, 2014.

Currently, both Pension Plans and Healthcare Plans employ a "floor" methodology for determining the City's contributions. The floor methodology requires that the annual required contribution for the City be the greater of the dollar amount reported in the actuarial valuations or the dollar amount determined by applying the percent of payroll reported in the actuarial valuation to the actual payroll for the fiscal year. This methodology ensures that adequate funding is achieved regardless of increases or decreases to the actual payroll from the actuarial assumed payroll.

For the Healthcare Plans, the City is in the process of phasing in full payment of the annual required contribution for both the City and the employees as recommended by Cheiron. The contribution rates set forth below in Table 14 are the phased in contribution rates that are capped and are not the full annual required contribution rate as calculated pursuant to GASB Statement 43 and GASB Statement 45. For a more detailed discussion of the phase in of the annual required contribution for both Healthcare Plans, including current discussions between the City and the bargaining units representing members of the Federated Plan, see "HEALTHCARE PLANS" in Appendix B.

As a department of the City, the Airport shares in the risks, rewards and costs of the Retirement Plans with the City. Employees of the City of San José Fire Department and Police Department staff the Airport's rescue and fire fighter station and provide police services at the Airport. The Airport reimburses the City's General Fund for these Police and Fire services. The Airport's share of the City's costs and liabilities associated with the Police and Fire Plan is a component of the aforementioned reimbursement, which totaled \$8,446,291 in the fiscal year ended June 30, 2012 and \$7,018,607 in the fiscal year ended June 30, 2013.

The payroll for Airport employees covered by the Federated Plan for the fiscal years ended June 30, 2013 and 2012 was \$12,931,622 and \$13,530,731, respectively. The Airport's total payroll for the fiscal years ended June 30, 2013 and 2012 was \$15,092,920 and \$15,948,673, respectively. Table 14 below shows the Airport and its employees' contribution rates to the Federated Plan for fiscal years 2011-12, 2012-13, and 2013-14 and are based on the actuarial valuations performed as of June 30, 2010, June 30, 2011, and June 30, 2012, respectively, for the Federated Plan. The rates applicable to the Airport for fiscal year 2014-15 are set forth in "CITY OF SAN JOSE: RETIREMENT PLANS – HEALTHCARE PLANS" in Appendix B.

**Table 14**  
**Airport and Airport Employee Contribution Rates**  
**Federated Plan**

Pay Period	Airport's Contribution Rate (% of covered payroll)		Employees' Contribution Rate (% of payroll)	
	Defined Benefits Pension	Postemployment Healthcare Plan	Defined Benefits Pension	Postemployment Healthcare Plan
6/26/11 through 6/23/12	28.34%	7.16%	4.68%	6.52%
6/24/12 through 6/22/13	44.45%	7.91%	5.74%	7.26%
9/30/12 through 6/22/13 <sup>(1)</sup>				
Tier 2	6.68%	7.91%	6.68%	7.26%
6/23/13 through 6/21/14				
Tier 1	50.85%	8.66%	5.97%	8.01%
Tier 2	6.68%	8.66%	6.68%	8.01%
9/27/13 through 6/21/14				
Tier 2B <sup>(2)</sup>	6.68%	10.59% <sup>(3)</sup>	6.68%	-

<sup>(1)</sup> Tier 2 became effective for employees hired on or after September 30, 2012.

<sup>(2)</sup> Tier 2B became effective for employees hired on or after September 27, 2013.

<sup>(3)</sup> Per the City's agreement with the bargaining units for the members in the Federated Plan, the City, including the Airport Department, agreed to pay the portion of the Federated Healthcare Plan's unfunded liability that the new employee in Tier 2B and the City would have paid if the employee had been eligible for participation in the Federated Healthcare Plan for retirees..

*Source:* City of San José Finance Department.

In fiscal year 2006-07 and fiscal year 2007-08, the City engaged in a process to determine whether to implement a policy to fully pre-fund the annual required contribution (ARC) as calculated under GASB Statement No. 45 for each of the Healthcare Plans. The City implemented GASB Statement No. 45 in fiscal year 2008 and elected to report a zero net Other Post Employment Benefits ("OPEB") obligation at the beginning of the transition year for both Pension Plans. Since then, the City has determined a Citywide ARC and annual OPEB cost (AOC) for the Federated Plan based upon an actuarial valuation performed in accordance with GASB Statement No. 45, Cheiron as further described under "HEALTHCARE PLANS" in Appendix B.

The City allocated to the Airport its proportionate share of the Citywide ARC and AOC for the Federated Plan based upon its percentage of retirement benefit costs for Federated Plan members. Actuarially required contributions were equal to the Airport's contributions made for retirement benefits under the Federated Plan. As shown in the table below, the difference between the cumulative AOC (Liability) allocated and the costs contributed by the Airport was \$12,076,469 and \$9,964,282 at June 30, 2013 and 2012, respectively, which is recorded as the Airport's net OPEB obligation. The Airport has earmarked funds from the unrestricted net position to pay the full amount of the net OPEB obligation. The following table sets forth the three-year trend information for the Airport's ARC, AOC, and contributions made toward the pension and health and dental components of the Federated Plan:

**Table 15**  
**Airport Contributions and Liability**  
**Federated Plan**

Fiscal Year ended June 30,	Defined Benefit Pension			Postemployment Healthcare Plan			
	ARC	Contributions	Unfunded Liability	ARC	AOC <sup>(1)</sup>	Contributions	Unfunded Liability
2011	\$4,455,031	\$4,455,031	--	\$3,164,961	\$3,227,182	\$1,436,944	\$7,529,822
2012	3,834,609	3,834,609	--	4,385,496	4,412,508	1,978,048	9,964,282
2013	5,748,106	5,748,106	--	3,691,308	3,677,300	1,565,113	12,076,469

<sup>(1)</sup> The AOC is equal to the ARC plus interest accrued on the outstanding net pension obligation at the beginning of the fiscal year and reduced by an adjustment to the ARC amount due to amortization of unfunded actuarial accrued liability.

*Source:* City of San José Finance Department.

## Labor Relations

**Overview.** The City has eleven recognized employee bargaining units, seven of which represent employees assigned to the Airport. Two of the bargaining units represent public safety employees who provide services at the Airport for which the Airport Department reimburses the City's General Fund.

The table below shows the representation and agreement dates for the eleven bargaining units. As indicated in the table, the City and nine bargaining units entered into agreements with a term expiring on June 30, 2015. The City and the San José Police Officers' Association ("POA") entered into an agreement expiring on December 31, 2015. The agreement between the City and the International Association of Firefighters ("IAFF, Local 230") expired on June 30, 2014. In addition to its represented employees, the City has approximately 259 unrepresented employees budgeted for 2014-15, fourteen (14) of which are assigned to the Airport. The Airport Department has 187 authorized positions in its budget for fiscal year 2014-15.

**Table 16**  
**City of San José**  
**Summary of Labor Agreements**

	Agreement Expiration Date	Full-Time Equivalent Employment <sup>(1)(2)</sup>	Assigned to Airport <sup>(7)</sup>
Assoc. of Building, Mechanical and Electrical Inspectors (ABMEI) <sup>(3)</sup> .....	06/30/2015	78	0
Association of Maintenance Supervisory Personnel (AMSP) ....	06/30/2015	102	19
Association of Engineers and Architects (AEA) <sup>(4)</sup> .....	06/30/2015	248	4
Association of Legal Professionals (ALP).....	06/30/2015	36	0
International Union of Operating Engineers, Local No. 3 (OE#3) .....	06/30/2015	680	36
International Brotherhood of Electrical Workers (IBEW).....	06/30/2015	75	6
City Association of Management Personnel (CAMP) .....	06/30/2015	365	29
San José Police Officers' Association (POA) <sup>(5)</sup> .....	12/31/2015	1,107	0
International Association of Firefighters (IAFF, Local 230) <sup>(6)</sup> ...	06/30/2014	671	0
Municipal Employees Federation (MEF).....	06/30/2015	1,915	58
Confidential Employees' Organization (CEO) .....	06/30/2015	224	7
Total.....		5,501	159

Full-time Equivalents (FTEs) are the combined total number of budgeted full-time positions. For example, one full-time position equals one FTE. Similarly, two half-time positions equal one FTE. *The FTE numbers presented are based upon the 2014-2015 Adopted Budget, and have been rounded to the nearest FTE.*

(1) The total number of employees does not include approximately 259 unrepresented positions budgeted in 2014-2015.

(2) Does not represent any employees paid by the Airport Department.

(3) The City has two separate agreements with AEA; the first agreement is related to employees of Unit 41 and Unit 42 and the second agreement is related to employees in Unit 43. Both agreements expire on June 30, 2015.

(4) See discussion below regarding the term of agreement with POA.

(5) Negotiations for fiscal year 2014-15 began in August 2014.

(6) Based on actual (not budgeted) data per the City's PeopleSoft payroll records as of July 28, 2014.

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

**State Law Requirements Related to Labor Negotiations.** Under California law, sworn police and fire employees are not permitted to strike. The City Charter provides that police and fire bargaining units have the right to binding interest arbitration of labor disputes once either the City or the public safety bargaining unit declares that the negotiations are at impasse, and the parties are unable to reach an agreement during the subsequent mediation. A summary of the City Charter's binding interest arbitration provisions is set forth below in “– City Charter Binding Interest Arbitration Provisions.” The agreements with the other bargaining units include “no strike” clauses during the terms of their respective agreements.

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

non-public safety bargaining group did not result in an agreement, the City Council could choose to implement the City's last, best and final offer. Implementation of terms, however, does not result in a bargaining agreement, or contract.

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

***Changes in Labor Costs over Last Decade.*** The City, including the Airport Department, has engaged in efforts to reduce labor costs. During the period from fiscal year 2003-04 through fiscal year 2013-14, the City's total compensation costs increased significantly although base payroll costs have declined due to both reductions in base pay and number of full-time equivalents ("FTEs"). From fiscal year 2003-04 through fiscal year 2013-14, the Airport Department reduced its total compensation costs by approximately 25%, as FTEs were reduced significantly during this period. As noted above, FTEs are the combined total number of budgeted full-time positions. The term "total compensation costs" refers to the City's cost of pay and benefits, including base pay, retirement contributions paid by the City to the Police and Fire Plan and Federated Plan and to the Tier 3 defined contribution retirement plan available to certain unrepresented employees, health insurance and other benefits.

The table below shows the difference in budgeted costs of total compensation of the City's FTEs from 2003-04 through 2013-14 for all of the City's funds.

**Table 17**  
**City of San José**  
**Citywide Salary and Benefits<sup>(1)</sup>**

	2003-2004	2013-2014	Difference
<b>Base Payroll</b>	<b>\$532,156,161</b>	<b>\$455,582,236</b>	(14.4%)
<b>Retirement Benefits</b>	<b>\$75,534,658</b>	<b>\$269,111,749</b>	256.3%
Federated Retirement/Other <sup>(2)</sup>	\$47,529,125	\$133,276,623	180.4%
Police/Fire Retirement	\$28,005,533	\$135,835,126	385.0%
<b>Health/Dental Benefits<sup>(3)</sup></b>	<b>\$44,138,708</b>	<b>\$66,032,442</b>	49.6%
<b>Unemployment and Other Benefits</b>	<b>\$10,273,223</b>	<b>\$7,665,541</b>	(25.4%)
<b>Total (All Benefits)</b>	<b>\$129,946,589</b>	<b>\$342,809,732</b>	163.8%
<b>Grand Total</b>	<b>\$662,102,750</b>	<b>\$798,391,968</b>	20.6%
<b>Total FTEs</b>	<b>7,213</b>	<b>5,643</b>	(21.8%)
<b>Average Total Cost Per FTE<sup>(4)</sup></b>	<b>\$91,794</b>	<b>\$141,465</b>	54.1%

<sup>(1)</sup> Does not include worker's compensation cost or overtime. The amounts are budgeted costs and include the cost of providing paid time off, such as vacation, holidays, personal/executive leave, and sick leave, to the extent that paid leave is taken during the fiscal year. The actual salary and benefit costs of individual employees vary.

<sup>(2)</sup> Other retirement benefits include retirement costs associated with part-time employees, Tier 3 retirement contributions, and the Mayor and City Council.

<sup>(3)</sup> Health/Dental Benefits are the costs budgeted for the health and dental benefits provided to FTEs.

<sup>(4)</sup> Includes total retirement costs, including unfunded liabilities.

*Source: City of San José Salary and Fringe Benefit Costs by Bargaining Unit & Fund for 2003-2004 through 2013-2014  
 Adopted Budget*

#### ***Modification to Pension and Retiree Healthcare Benefits and other Employment Benefits.***

During fiscal year 2011-12, the City and all eleven bargaining units engaged in negotiations related to retirement issues, including the terms of a ballot measure to amend the retirement provisions set forth in the City Charter. Those negotiations did not result in an agreement with any of the City's bargaining units concerning the terms of the proposed City Charter amendment or other retirement related issues. In March 2012, the City Council voted to place the Charter amendment measure, designated as Measure B, on the June 5, 2012 ballot which the voters approved by approximately 69%.

In addition to the terms of Measure B, negotiations in fiscal year 2011-12 included the Tier 2 retirement benefits for new employees, changes to healthcare benefits, and the Medicare enrollment requirement for retirees. No agreement was reached and on June 12, 2012, the City Council implemented its last, best and final offers on these matters to each of the bargaining units with members in the Federated Plan, including the availability of a new high deductible health plan for active employees on which the retiree healthcare benefit is based. The addition of the new high deductible health plan became effective as of calendar year 2013 for members of both Retirement Plans. In addition, effective January 1, 2014, the City instituted a four tier rate program for the healthcare and dental plans for both active non-sworn employees and all retirees. This means that all healthcare and dental plans available to non-sworn employees will have single, single plus spouse/domestic partner, single plus child(ren), and family rates.

The Medicare enrollment requirement became effective for members of the Federated Plan in calendar year 2013, but has not yet become effective for the Police and Fire Department Plan members.

During 2012 and 2013, the City implemented the elimination of sick leave payout upon retirement for new employees and the sick leave payout for certain employees was frozen. Sick leave payments upon retirement were eliminated for non-sworn employees hired on or after September 30, 2012 and for police sworn employees hired on or after July 7, 2013. Sick Leave payments upon retirement were frozen effective June 22, 2013 for non-sworn employees hired on or before September 29, 2012, and were frozen effective July 6, 2013 for police sworn employees hired on or before July 6, 2013. No changes have been made to sick leave payment upon retirement for fire sworn employees.

Pursuant to the City Charter, the City and POA were scheduled for binding interest arbitration on Tier 2 in the Police and Fire Department Plan for new police employees in April 2013. However, the City and POA reached agreement on a stipulated arbitration award on Tier 2 on April 26, 2013. Consistent with the impasse procedures for the public safety bargaining units, the City and IAFF, Local 230 are engaged in binding interest arbitration related to Tier 2 in the Police and Fire Department Plan for new sworn fire employees.

The significant provisions of Measure B and the status of implementing these provisions, the litigation and administrative proceedings before the California Public Employee Relations Board (“PERB”) challenging Measure B and the Tier 2 provisions of both Retirement Plans are described in “THE CITY OF SAN JOSE: RETIREMENT PLANS” in Appendix B. In addition to the matters pending before PERB as described in Appendix B, in June 2014, IAFF Local 230 filed an unfair labor practice charge with PERB related to the City’s implementation of a medical provider network for workers’ compensation claims. The City has filed its response with PERB. No action has been taken by PERB on the IAFF Local 230’s charge; however, the City cannot predict the ultimate outcome of this matter.

The following table summarizes the status of the various changes to employee compensation and benefits that the City has proposed or implemented since 2010-11.

**Table 18**  
**City of San José**  
**Status of Changes to Employee Compensation and Benefits Since 2010-11**

Employee Unit	Ongoing Total Compensation Reduction <sup>(1)</sup>	Modify Step Increases	Disability Leave Supplement	Sick leave Payout	Modify Overtime Calculation	Vacation Sellback	Healthcare Plan changes; Medicare Enrollment <sup>(2)</sup>
AEA	10%	N/A	Eliminated 06/24/12	(5)	N/A	Eliminated 12/23/12	In effect
ALP	10%	N/A	Eliminated 06/24/12	(5)	N/A	Eliminated 12/23/12	In effect
AMSP	10%	N/A	Eliminated 06/24/12	(5)	N/A	Eliminated 12/23/12	In effect
CAMP	10%	N/A	Eliminated 06/24/12	(5)	N/A	Eliminated 12/23/12	In effect
ABMEI	10%	Reduced to 2.5% per step	Eliminated 06/24/12	(5)	Status Quo	N/A	In effect
IBEW	10%	Reduced to 2.5% per step	Eliminated 07/07/13	(5)	Actual Hours Worked and Holiday Leave Only	N/A	In effect
OE#3	10%	Reduced to 2.5% per step	Eliminated 04/27/14	(5)	Actual Hours Worked and Holiday Leave Only	N/A	In effect
MEF	10% <sup>(3)</sup>	Reduced to 2.5% per step	Eliminated 07/07/13	(5)	Actual Hours Worked Only and Holiday Leave Only <sup>(7)</sup>	N/A	In effect
CEO	10% <sup>(3)</sup>	Reduced to 2.5% per step	Eliminated 07/07/13	(5)	Actual Hours Worked Only and Holiday Leave Only <sup>(7)</sup>	N/A	In effect
POA	10%	Status Quo	Status Quo	(6)	Status Quo	N/A	In effect only for healthcare plan changes for retirees <sup>(8)</sup> .
IAFF, Local 230	10%	Status Quo	Status Quo	Status Quo	Status Quo	N/A	In effect only for healthcare plan changes for retirees <sup>(8)</sup> .
Unit 99/ Unit 82 <sup>(4)</sup>	10%	N/A	Eliminated 06/24/12	(5)	N/A	Eliminated 12/23/12	In effect

<sup>(1)</sup> The City reached agreements with the POA and the non-sworn bargaining units for general wage increases for Fiscal Year 2013-2014 and Fiscal Year 2014-15.

<sup>(2)</sup> The healthcare plan changes became effective for calendar year 2013 for retirees in both Retirement Plans and for non-sworn active employees. The Medicare enrollment requirement became effective for retirees in the Federated Plan in calendar year 2013. In addition, effective calendar year 2014, all healthcare and dental care plans available to non-sworn employees have a 4-tier rate structure. Previously, employees only had the single or family rate option for healthcare. The 4-tier rate structure gave employees the option of single, single plus spouse/domestic partner, single plus child(ren), and family (which includes spouse/domestic partner and children). With a 4-tier health and dental premium rate structure, employees had more options to better fit the individual employee's specific situation. Since retirees choose among the plan options available to active employees, retirees were also able to choose among the 4-tier plan options depending on the individual retiree's specific situation.

<sup>(3)</sup> Also achieved Council direction to roll back 2% General Wage Increase received in 2010-11.

<sup>(4)</sup> Unit 99/Unit 82 are comprised of unrepresented employees whose benefits are determined by the City Council through the recommendations of the City Manager.

- (5) For employees hired on or before 09/29/12, sick leave and rate of pay for payout purposes were frozen as of 06/22/13. For employees hired on or after 09/30/12, sick leave payout is eliminated.
- (6) For employees hired on or before 07/06/13, sick leave and rate of pay for payout purposes were frozen as of 07/06/13. For employees hired on or after 07/07/13, sick leave payout is eliminated.
- (7) As part of an agreement approved by the City Council on August 5, 2014 to settle an unfair labor practice charge filed by MEF and CEO with the California Public Employment Relations Board, Holiday Leave will be counted towards the calculation of overtime effective August 17, 2014.
- (8) For a discussion of motions to compel arbitration regarding the changes to the healthcare plans offered to retirees brought by the POA and IAFF, Local 230 against the City, see “THE CITY OF SAN JOSE: RETIREMENT PLANS” in Appendix B.

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

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**Approved Bargaining Unit Agreements for 2014-15.** In spring 2014, the City began negotiations on successor agreements for fiscal year 2014-15. As of June 30, 2014, the City entered into successor agreements with its nine non-public safety bargaining units, CEO, MEF, ALP, IBEW, CAMP, ABMEI, AEA, AMSP, and OE#3. Each of these successor agreements has a term of July 1, 2014 to June 30, 2015 and contains a 3% general wage increase. The City Manager built into the Proposed 2014-15 Adopted Budget funding for potential employee compensation increases of \$24.0 million in the General Fund. A majority of this funding, \$13.5 million, is an allocation to Employee Compensation Planning Reserve for all employees other than POA, while \$7.0 million is an allocation to POA, to support the compensation increase. The Airport's portion of the increase, totaling \$733,000, was included in the Airport's budget for fiscal year 2014-15. The portion of the Employee Compensation Planning Reserve comprised of Airport Funds totaled approximately \$733,400 in the 2014-2015 Proposed Budget. The City Council allocated approximately \$445,664 as part of the 2014-2015 Adopted Budget actions, leaving a balance of approximately \$287,736 that is anticipated to be allocated in connection with the City Council's consideration and approval of the 2013-14 Annual Report in the fall of 2014.

In May 2013, the City and POA engaged in binding interest arbitration related to a successor agreement and, as part of the arbitration award issued in July 2013, no wage increase resulted due to the Charter's limitations on arbitration awards described below in "*- City Charter Binding Interest Arbitration Provisions*." Additionally, sick leave payout was eliminated for new employees and the sick leave hours and the hourly rates were frozen as described above. Subsequently, in December 2013, the City and the POA entered into a two and a half-year agreement, with a term retroactive to July 1, 2013 through December 31, 2015, containing a 4% wage increase in the fiscal year 2012-13 and 3.33% in each of the two following fiscal years and a one-time lump sum non-pensionable payment of 2% of annual base pay; other terms contained in the arbitration award remain in effect. The City entered into this agreement with the POA in part due to the retention issues in the Police Department.

Additionally, in August 2014, the City Council approved a settlement agreement with MEF and CEO to resolve an unfair labor practice charge filed by MEF and CEO with the California Public Employment Relations Board related to the implementation of the City's Last, Best and Final Offers in 2011. MEF and CEO agreed to withdraw the unfair labor practice charge with prejudice, and the City agreed to provide eligible employees additional compensatory leave time, to prospectively include holidays in the calculation of eligibility for overtime, and to amend the City's pay plan so that MEF-represented classifications will receive prospectively the same base pay as the same classification represented by CEO.

**Status of Current Negotiations for 2014-15.** The agreement with IAFF, Local 230 expired on June 30, 2014 and negotiations on a successor agreement have commenced. The City cannot predict the outcome of the negotiations with IAFF, Local 230 on a successor agreement.

Currently, IAFF, Local 230 is the only bargaining unit without a second tier of retirement benefits for new employees (Tier 2). The City and the bargaining unit were engaged in binding interest arbitration on Tier 2 in May 2014, where the City proposed the maximum permissible benefit under the City Charter limitations and agreed to reopen negotiations over Tier 2 retirement benefits in the event that there are future modifications to Measure B. On September 22, 2014, following the 10 day confidentiality period required by the City Charter, the arbitration board's decision adopting the City's proposals on Tier 2, with the exception of eliminating eligibility of Tier 2 fire members for retiree health and dental benefits, became binding and public. Under the arbitration board's decision, the Tier 2 fire members will continue to be eligible for retiree health and dental benefits. The City plans to proceed with implementation of the arbitration decision by bringing forward the corresponding amendments to the Municipal Code for the City Council's consideration and approval in the fall 2014.

Additionally, the City is in discussions with the bargaining units with members in the Federated Plan related to retiree healthcare as described in THE CITY OF SAN JOSE: RETIREMENT PLANS” in Appendix B. As of the date of this Official Statement, the City and the various bargaining units continue to meet to discuss retiree healthcare options. The City cannot predict the outcome of these discussions with any of its bargaining units.

***City Charter Binding Interest Arbitration Provisions.*** As previously noted, the Charter’s binding interest arbitration provisions apply only to the POA and IAFF, Local 230. In November 2010, the voters approved a Charter amendment to revise the Charter’s binding interest arbitration provisions for the City’s public safety bargaining units to, among other things, change the selection process for the neutral arbitrator member of the Arbitration Board (as defined below) and the factors to be weighed by the Arbitration Board in making its award, and to place limits on the Arbitration Board’s authority. The Charter’s provisions governing arbitration, as amended, are described below.

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

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

The primary factors in decisions regarding compensation shall be the City’s financial condition and, in addition, its ability to pay for employee compensation from on-going revenues without reducing City services. The Charter defines “compensation” as being all costs to the City, whether new or ongoing, for salary and benefits, including but not limited to any wages or other pays, pension, and active and retiree healthcare. No arbitration award may be issued unless a majority of the Arbitration Board determines, based upon a fair and thorough review of the City’s financial condition and a cost analysis of the parties’ last offers, that the City can meet the cost of the award from on-going revenues without reducing City services. The arbitrators shall also consider and give substantial weight to the rate of increase or decrease of compensation approved by the City Council for other bargaining units.

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

## **Insurance and Self-Insurance Programs**

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

***Citywide Insurances.*** The City self-insures for liability (other than for the Airport and the San José-Santa Clara Regional Wastewater Facility), personal injury, and workers' compensation. The City currently maintains an all-risk property insurance policy with coverage for property owned by the City, including the Airport. This policy also provides coverage for boiler and machinery exposures and loss due to business interruption resulting from a covered risk or flood. The City generally does not carry earthquake insurance as it is not reasonably available. A summary of these coverages is provided in Table 19.

**Table 19**  
**City of San José**  
**Summary of Citywide Property Insurance Coverage**  
**(For Policy Period October 1, 2014 to October 1, 2015)**

	<b>Coverage Per Occurrence</b>	<b>Deductible Per Occurrence</b>
Property, including Business Interruption <sup>(1)</sup>	\$1 billion	\$100,000
Flood:		
Flood Zones SFHA <sup>(3)</sup>	\$15 million per occurrence and annual aggregate	5% of TIV Minimum \$1 Million <sup>(2)</sup>
Flood Zone B	\$25 million per occurrence and annual aggregate	2% of TIV Minimum \$100,000 <sup>(2)</sup>
All Other Flood Zones	\$100 million per occurrence and Annual Aggregate	\$100,000 <sup>(2)</sup>

(1) Acts of terrorism are not covered.

(2) TIV: Total Insured Value; Deductible applies per affected location.

(3) SFHA: Special Flood Hazard Area.

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

**Unemployment Insurance.** The City self-insures to the limits required by State statute. The City budgets for each year's anticipated unemployment insurance claims. By policy, the City also funds a reserve of the same amount in each fiscal year.

### ***Airport Coverages.***

**Liability Coverages.** The City has airport liability policies covering the Airport, which provide a \$200 million combined single limit for bodily injury and property damage, with a sublimit of \$50 million each occurrence and in the annual aggregate for personal injury and a sublimit of \$150 million each occurrence and in the annual aggregate for war and terrorism. The City also maintains an automobile liability policy covering vehicles associated with the Airport and San José-Santa Clara Regional Wastewater Facility operations. As part of general support services, the City charges the Airport for the

cost of these liability insurance coverages. The limit of automobile liability is \$1 million for each occurrence combined as a single limit for bodily injury and property damage and the City is self-insured for physical damage, except for leased shuttle buses.

Workers' Compensation Reserve. The Airport participates in the City's self-insurance program for workers' compensation. The Airport's workers' compensation program is accounted for on a separate contribution basis under which workers' compensation claims and reserves are maintained in Airport funds, separate from the City's General Fund. Estimated workers' compensation liabilities are determined using actuarial methods. As of June 30, 2013, the Airport's liability for workers' compensation was \$1.7 million.

Additionally, all airlines operating under the Airline Lease Agreement are required to maintain certain insurance coverages. See "SUMMARY OF CERTAIN PROVISIONS OF THE AIRLINE LEASE AGREEMENT—Indemnification, Insurance and Public Liability" in Appendix G.

***Airport Coverages For Phase 1 of the Airport Development Program.***

Airport Owner-Controlled Insurance Program — North Concourse Project. On March 31, 2004, the City bound certain liability insurance coverages for the major components of the North Concourse project through an owner-controlled insurance program ("OCIP") from Chartis, formerly American International Group, AIU Holdings, Inc. and AIU LLC ("Chartis"). An OCIP is a single insurance program that provides insurance coverage for construction job site risks of the project owner, general contractors, and all subcontractors associated with construction at the designated project site. The specific coverages, limits, and deductibles are outlined in Table 20a below.

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**Table 20a**  
**City of San José**  
**Summary of Airport Owner-Controlled**  
**Insurance Program –**  
**North Concourse Project**

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<b>Coverages</b>	<b>Limit</b>	<b>Deductible Per Occurrence</b>
General Liability	\$2 million per occurrence \$4 million aggregate	\$250,000
Workers' Compensation	Statutory	\$250,000
Employers' Liability	\$2 million per accident	\$250,000
Excess Liability	\$150 million	None

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

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Due to delay in completing the North Concourse project, in March of 2007, the City was required to establish a claims loss reserve for the North Concourse Project in the aggregate principal amount of \$3.6 million with an additional \$300,000 available in a cash working fund. The claims loss reserve fund is available to Chartis to pay claims within the City's deductible, subject to an aggregate maximum loss exposure within the City's coverage limit of \$3.9 million. The full amount of the claims loss reserve was deposited with Chartis and was recorded under advances and deposits in the accompanying statement of net assets. Interest earned by the claims reserve fund is remitted to the Airport Department.

The North Concourse Project was completed in June 2010. Chartis is currently in the process of closing out the North Concourse OCIP and is auditing the project payroll and cost factors associated with the premium. The closing out process for OCIP includes an actuarial review, which examines outstanding claims. The City was able to negotiate the return of a large portion of the unused claims reserve in advance of the 10-year coverage term and in March 2010, the amount of \$2,516,719 was returned to the Airport. Chartis will continue to hold the remaining funds in the loss reserve fund until such time as the exposure to risk of claims ceases or the City opts to cash out the remaining funds in exchange for accepting responsibility for potential future claims.

Activities relating to the North Concourse OCIP claims reserve fund for the fiscal years ended June 30, 2013 and 2012 were as follows:

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**Table 20b**  
**City of San José**  
**Airport Owner-Controlled Insurance Program – North Concourse Project**  
**Summary of Claims Reserve Fund Activity**

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Coverages	<b>FY 2012-13</b>	<b>FY 2011-12</b>
Beginning Balance	\$1,028,172	\$1,065,664
Additional Deposits	-	-
Losses Paid	(80,485)	(37,492)
Ending Balance	<u>\$ 947,687</u>	<u>\$1,028,172</u>

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*Source: Norman Y. Mineta San José International Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2013.*

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Airport Owner-Controlled Insurance Program - Terminal Area Improvement Program. On March 15, 2007, the City bound certain liability insurance coverages for the major components of the Terminal Area Improvement Program through another OCIP (the “TAIP OCIP”) procured through Chartis. The terms of the TAIP OCIP require the City to fund a claims loss reserve with Chartis in the amount of \$8.9 million which Chartis has permitted the City to fund incrementally. In August 2013, Chartis refunded \$1.4 million of the loss fund to the City. The claims loss reserve had a balance of approximately \$4.0 million as of June 30, 2013. The specific coverages, limits, and deductibles for the TAIP OCIP are outlined in Table 21a.

**Table 21a**  
**City of San José**  
**Summary of Airport Owner-Controlled**  
**Insurance Program –**  
**Terminal Area Improvement Program**

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

*Source: City of San José.*

The City was obligated to maintain the TAIP OCIP through final acceptance of the Terminal Area Improvement Program, pursuant to the terms of its design-build contract with Hensel Phelps. The term of the TAIP OCIP expired on June 30, 2011. All work covered under the contract with Hensel Phelps has been completed and accepted. Chartis will continue to hold the remaining funds in the claims loss reserve fund until such time as the exposure to risk of claims ceases or the City opts to cash out the remaining funds in exchange for accepting responsibility for potential future claims.

**Owner's and Contractor's Protective Professional Indemnity, Including Contractor's Pollution Liability Policies.**

Hensel Phelps, under its design-build agreement with the City for the Terminal Area Improvement Program, has provided a contractor's protective professional liability insurance ("CPPI") policy specific to its design work on the Terminal Area Improvement Program. The CPPI affords vicarious liability coverage for the City and the contractor's pollution liability policy names the City as an additional insured. The limit on the coverage is \$5.0 million.

Activities relating to the TAIP OCIP claims reserve fund for the fiscal years ended June 30, 2012 and 2013 were as follows:

**Table 21b**  
**City of San José**  
**Airport Owner-Controlled Insurance Program – Terminal Area Improvement Program**  
**Summary of Claims Reserve Fund Activity**

<b>Coverages</b>	<b>FY 2012-13</b>	<b>FY 2011-12</b>
Beginning Balance	\$4,303,114	\$4,859,972
Additional Deposits	3,167	3,830
Losses Paid	(273,889)	(560,688)
Ending Balance	<u>\$4,032,392</u>	<u>\$4,303,114</u>

*Source: Norman Y. Mineta San José International Airport Comprehensive Annual Financial Report for Fiscal Year Ended June 30, 2013.*

## LITIGATION

There are a number of litigation matters pending against the City relating to incidents at the Airport or contractual disputes involving the Airport. These claims and suits are of a nature usually incidental to the operation and development of the Airport and, in the aggregate, in the opinion of Airport management, based upon the advice of the City Attorney, will not have a material adverse effect on the Net General Airport Revenues or financial condition of the Airport. It should be noted that a portion of the claims relating to personal injuries and property damage currently are covered by a comprehensive insurance program maintained by the City for the Airport. See “OTHER MATTERS—Insurance and Self-Insurance Programs” above.

***FAA Audit of Use of Airport Revenue.*** The FAA commenced an audit of the City’s use of Airport revenue in the spring of 2010. Federal law requires all airport owners that receive Federal assistance, such as the City, to use airport revenues for the capital or operating costs of the Airport. As a general rule, any use of airport revenues by an airport owner for costs that cannot properly be considered airport capital or operating costs is deemed to be improper revenue diversion. On June 2, 2010, auditors from the FAA provided the City with a draft audit finding improper use of Airport revenues by the City in three areas of expenditure as described below.

The City provided its response to the draft findings in June 2010. In March 2011, the FAA notified the City that the FAA was prepared to issue its final audit consistent with the draft findings, but would give the City the opportunity to comment on the final draft of the audit findings prior to issuance. The City and the FAA have engaged in subsequent discussions and exchanged further correspondence regarding the draft audit findings, with the latest correspondence from the City to the FAA in February 2014. To date, the FAA has not provided the City with a timeframe for its issuance of a final audit. In the event that the FAA issues a final audit finding improper use of Airport revenue by the City, the City will have an opportunity for an administrative hearing to contest any such determination.

The improper uses of Airport revenues alleged by the FAA are described below.

**Airport Lease Obligation.** The City purchased approximately 75 acres of real property located near the southwest corner of the Airport from the FMC Corporation between 2005 and 2006, as a strategic effort to promote economic development opportunities and to preserve the future viability of the Airport. The City acquired the property in two phases. The initial phase, consisting of the acquisition of 52 acres of the property (referred to as the “Airport West Property”) was completed in February 2005. The City completed the second phase, consisting of the acquisition of the remaining 23 acres of the property, in May 2006. The City intended to use the remaining 23 acres of the property for non-Airport economic development purposes.

The purchase of the Airport West Property was financed with lease revenue bonds issued by the City of San José Financing Authority (the “Authority”). Upon acquisition, the City leased the Airport West Property from the Authority and used a portion of the Airport West Property for construction laydown needs (including material storage and construction employee parking) to support the Terminal Area Improvement Program. The City agreed to make lease payments for the Airport West Property from Airport operating revenues available in the Maintenance and Operation Fund. At the time of the acquisition, the City contemplated other potential Airport uses for the Airport West Property, such as rental car storage, public or employee parking, flight kitchen operations, airport/airline warehouses and compatible non-aviation leaseholds. The City subsequently determined not to use the Airport West Property for these other potential Airport uses, and the City’s use of the Airport West Property for construction laydown needs ceased with the completion of the Terminal Area Improvement Program on

June 30, 2010. The City ceased using Airport operating revenues to make Airport West Property lease payments as of July 1, 2010.

In its June 2, 2010, draft audit finding, the FAA determined that the City could use Airport operating revenues to pay rent only for those portions of the Airport West Property that the City actually used for its Airport construction laydown needs and that the use of Airport operating revenues to pay rent for the remainder of the Airport West Property not actually used by the City for Airport purposes violated federal law regarding use of airport revenue. Consequently, the FAA auditors recommended that the City recalculate the rent paid from Airport operating revenues based upon actual Airport use, set the rent at fair market value, and return the remainder to the Airport enterprise fund, with interest. The City paid approximately \$2.2 million from Airport operating revenues and approximately \$10.0 million from the issuance of Subordinated Commercial Paper Notes as rent for the Airport West Property from the date of its acquisition through June 30, 2010.

The City believes that it has viable defenses to the FAA audit determination with regard to Airport West lease payments. The City further believes the acquisition of property for Airport purposes (whether by purchase or lease) necessarily requires planning and development prior to the commencement of actual Airport uses, and the use of Airport operating revenues to pay rent on property acquired for planned future Airport uses does not constitute improper use of Airport operating revenues under federal law. The City believes there is no basis under applicable federal law for the distinction made by the FAA auditors between rent payments for actual as opposed to planned airport uses. However, the City cannot predict the final outcome of the audit.

Guadalupe Gardens. In early 2002, the City Council approved a Master Plan for Guadalupe Gardens, consisting of approximately 120 acres of mostly vacant, City-owned property located south of the Airport, much of which falls within an FAA-established safety zone. The City acquired the Guadalupe Gardens properties using FAA grants for airport approach protection and noise compatibility, and the FAA grant agreements consequently required FAA approval of any planned City-use of the properties acquired with grant proceeds. By letter dated August 9, 2002, addressed to the City's Director of Aviation, the FAA San Francisco Airport District Office ("ADO") approved the City's Master Plan for reuse of Guadalupe Gardens for runway and approach protection, and the City finalized the Master Plan in reliance upon the FAA approval.

Citing provisions of federal law that require recipients of FAA grants for acquisition of land for noise compatibility purposes to dispose of any such acquired land when no longer needed by the airport owner for noise compatibility purposes, the FAA auditors determined that the FAA ADO erred in its 2002 approval of the Guadalupe Gardens Master Plan and that the City is obligated to prepare an inventory of the Guadalupe Gardens to identify those parcels that were acquired by the City with noise compatibility grant proceeds. This inventory would then be used to prepare for FAA review and approval of a disposition plan for those parcels no longer needed by the City for noise compatibility. Proceeds of the sale of the parcels proportionate to the FAA grant share of the original purchase price would be required to be used for other approved noise compatibility projects at the Airport or returned to the FAA.

The City believes that it has viable defenses to the FAA audit determination with regard to Guadalupe Gardens. The FAA ADO's 2002 approval of the Guadalupe Gardens Master Plan constituted an official FAA approval of the City's reuse of the parcels acquired with proceeds from FAA noise compatibility grants, and the approval expressly provides that the entire Guadalupe Gardens is necessary for the continuing aeronautical purpose of runway and approach protection. Having received official FAA approval of its reuse of the parcels, the City believes it is under no obligation to take any further action to secure further FAA approval of its continuing use of the Guadalupe Gardens. However, the City cannot predict the final outcome of the audit.

Cost Allocations. The FAA auditors reviewed the City's allocation of its costs to the Airport Department for services provided by the City to the Airport in fiscal year 2010-11. The City uses both direct and indirect methodologies to allocate costs to the Airport. The FAA auditors found the direct cost allocations to be acceptable.

The FAA contends that the City's indirect methodology does not correlate to the cost of services actually provided by the City to the Airport. Consequently, the auditors have recommended that the City re-allocate its costs charged to the Airport for fiscal years 2005 through 2010 using an allocation methodology that reflects services actually provided to the Airport and repay any overcharges to the Airport enterprise fund, with interest. The amount of costs allocated by the City to the Airport using the indirect methodology for fiscal years 2005 through 2010 was estimated to be \$59 million.

The City believes that its cost allocation methodologies reflect the cost of City services actually provided to the Airport and that the methodologies used by the City are consistent with applicable federal cost allocation guidance. In an effort to resolve the issue, the City capped the indirect cost allocations for certain City departments at 10%, which was the approximate rate charged to the Airport in pre-capital intensive years. This resulted in a total credit of \$5.6 million that would be applied equally to the Airport cost allocation plan over a seven year period beginning in fiscal year 2012-13. The City also proposed to adjust its indirect cost allocation methodology commencing with fiscal year 2014-15 in an effort to address the FAA concerns. To date the FAA has not responded to the City's cost allocation proposals, and the City cannot predict the final outcome of the audit.

**SJJC Aviation Services, LLC v. City of San Jose.** Between May 2013 and January 2014, SJJC Aviation Services, LLC filed three lawsuits seeking to block the Signature fixed base operation project at the Airport. SJJC Aviation Services, LLC is an incumbent tenant at the Airport that conducts fixed base operations under the name "Atlantic Aviation," and the Signature fixed base operation will be in competition with Atlantic Aviation at the Airport.

The first lawsuit (the "RFP lawsuit"), filed in May 2013 in the Superior Court of the State of California in Santa Clara County, challenged the City's RFP process and the resulting award of the lease and operating agreement to Signature. The Superior Court entered judgment dismissing the RFP lawsuit with prejudice on May 2, 2014, and SJJC Aviation Services subsequently filed an appeal to the Sixth District Court of Appeal on May 16, 2014. Briefings and a hearing date for the appeal have not yet been set.

The remaining two lawsuits filed in May and December 2013 in the Superior Court of the State of California in Santa Clara County, seek to block the Signature project under the California Environmental Quality Act ("CEQA"). In both CEQA lawsuits, SJJC Aviation Services alleges that the City violated CEQA by approving the Signature project without adequate environmental review. The Superior Court subsequently consolidated the two CEQA lawsuits, and the hearing on the merits is currently set for September 26, 2014.

The City believes that the SJJC Aviation Services challenges to the RFP process and the environmental review for the Signature project are without merit. The City is not able to predict the outcome of this litigation, but does not believe that it will adversely impact the ability of the City to pay debt service on the Series 2014 Bonds.

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**APPENDIX B**

**CITY OF SAN JOSE RETIREMENT PLANS**

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## **INTRODUCTION TO APPENDIX B**

This Appendix B provides investors with information concerning the Retirement Plans (as defined below) for the City of San José (the “City”). Investors are advised to read the entire Official Statement, including this Appendix B, to obtain information essential to making an informed investment decision.

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

This Appendix B summarizes portions of the City’s Basic Financial Statements for the Fiscal Year Ended June 30, 2013, the most recent Actuarial Valuation Reports for the City’s Federated City Employees Retirement System (the “Federated Plan”) and the City’s Police and Fire Department Retirement Plan (the “Police and Fire Plan”) (together, the “Retirement Plans”) for the fiscal year ended June 30, 2013, as well as the Federated City Employees’ Retirement System Consolidated Annual Financial Report (“Federated CAFR”) for the fiscal year ended June 30, 2013 and the CAFR for the Police and Fire Department Retirement Plan (“Police and Fire CAFR”) for the fiscal year ended June 30, 2013. In addition, other documents relevant to the Retirement Plans are referenced or discussed in this Appendix B including the experience studies and investment policies for both Retirement Plans.

Copies of documents referred to in this Appendix B are available from the Finance Department – Debt Management, City of San José City Hall, 200 East Santa Clara Street, San José, CA 95113; Phone (408) 535-7010; Fax (408) 292-6482.

The City maintains a number of websites, including a website for both Retirement Plans. However, the information presented on the City’s websites is not part of this Official Statement and should not be relied upon in making an investment decision with respect to the Series 2014 Bonds.

## **RETIREMENT PLANS IN GENERAL**

### **Overview**

All regular full-time employees of the City and certain part-time employees, with the exception of certain unrepresented employees, participate in one of two defined benefit retirement plans (“Retirement Plans”) established pursuant to the City Charter: the Federated City Employees Retirement System (the “Federated Plan”) for non-sworn employees and the Police and Fire Department Retirement Plan (the “Police and Fire Plan”) for sworn employees. Both Retirement Plans consist of a single-employer defined-benefit pension plan (“Pension Plan”) and a postemployment healthcare plan (“Healthcare Plan”). Each Retirement Plan is administered by its own Board of Administration (each a “Board”), and day-to-day operations are carried out by the City’s Department of Retirement Services staff.

The specific terms of each Retirement Plan are set forth in the City’s Municipal Code. Both Pension Plans are structured as tax-qualified defined benefit plans in which a pension benefit (an allowance paid on a monthly basis) is based upon salary and length of service. The Healthcare Plans were established under

Internal Revenue Code Section 401(h) and are accounts within the Pension Plans for retiree healthcare benefit funding and for the payment of retiree healthcare benefits. In addition, the City Council has established Internal Revenue Code Section 115 Trusts as a supplement to the 401(h) accounts. The 115 Trusts and the 401(h) accounts are collectively referred to as the Healthcare Plans.

Both Pension Plans pay a monthly pension allowance and, depending on the tier, provide either fixed or index-based cost of living increases. The Healthcare Plans pay all, or a portion of, health and dental insurance premiums for qualified retirees and their survivors and dependents. Participation by covered employees in the applicable Retirement Plans is mandatory. Employees contribute a percentage of their salaries to the applicable Retirement Plans, and the City provides funding either through contributions equal to a percentage of its full-time employee covered payroll or on a lump-sum basis. The City does not participate in the Federal Social Security System.

To achieve and maintain the appropriate funding status, the Board of each Retirement Plan retains the services of actuaries to analyze the respective assets and liabilities of the Pension Plan and Healthcare Plan to determine what level of required annual contributions are needed. The City generally has paid the Annual Required Contribution (“ARC,” defined below) for the pension benefit as presented by the actuaries for the Pension Plans. Currently, the Board for each Retirement Plan retains Cheiron as its actuary.

In addition, the Pension Plans have each included a Supplemental Retiree Benefit Reserve (“SRBR”). The SRBR was a reserve within each Pension Plan from which supplemental benefits were paid to retirees and beneficiaries in accordance with the terms applicable to each Pension Plan. As described below, the SRBR in both Pension Plans has been eliminated.

## **Board Governance**

Each Retirement Plan is administered by its own independent Board of Administration. The governance structure for each Board is described below, including a discussion of a measure on the November 2014 ballot regarding modifications to the governance of both Retirement Plans.

In August 2010, the City Council adopted ordinances to implement governance changes for each Retirement Plan’s Board to provide for the following: (1) the majority of each Board be members of the public; (2) minimum qualifications for the public members, including education and expertise related to pension plan administration; (3) geographical requirements for the public members; and (4) revising the process for removal of Board members and defining the causes for removal, including provisions for removal due to actual, potential or the appearance of a conflict of interest. The membership changes to both Boards eliminated the seats designated for City Council members, the Civil Service Commission member seat, and the City’s administration seat on the Board of the Police and Fire Plan (“Police and Fire Board”).

The governance changes to the Police and Fire Board increased the size of the Police and Fire Board from seven to nine members and changed the composition to: (1) five public members; (2) one current Fire Department employee and one current Police Department employee who are members of the Police and Fire Plan; and (3) one retired Fire Department employee and one retired Police Department employee who retired under the provisions of the Police and Fire Plan. The governance changes to the Board of the Federated Plan (the “Federated Board”) maintained the Federated Board’s size of seven members but changed the composition to: (1) four public members; (2) two current City employees who work in different City departments and who are members of the Federated Plan; and (3) one retired employee who retired under the provisions of the Federated Plan.

In 2012, the Boards for the Federated Plan and the Police and Fire Plan contracted with Cortex Applied Research, Inc. (“Cortex”) to review and evaluate the governance model of the Boards and to provide recommendations for improvement. Based on their findings, Cortex issued a report in 2013 that contained fifteen (15) recommendations. The recommendations addressed a variety of potential changes to the administration of the Retirement Plans, including: (1) providing the Boards with the authority to appoint and terminate certain positions within the Department of Retirement Services, and retain legal counsel; (2) establishing certain safeguards for stakeholders, such as appropriate compensation for independent board members and requiring that staff serving the Boards may not be members of the Retirement Plans; (3) increasing transparency and disclosure such as requiring each Board to hold an annual general meeting to inform and educate the public about the performance and activities of the Retirement Plans and additional annual disclosures, as well as increasing risk oversight by establishing an audit committee, among other things; and (4) considering consolidation of the oversight of the Retirement Plans by one board in order to address scale and efficiency of operations related to the administration of the Retirement Plans.

Cortex presented its report to the City Council in November 2013 and the City Council directed City staff to develop a workplan for implementation of the report’s recommendations. Implementation of a number of provisions based on the Cortex report requires voter approval of amendments to the City Charter.

At its August 5, 2014 meeting, the City Council approved placement of a measure on the November 4, 2014 ballot to amend the City Charter to expressly provide for the City Council’s establishment of one or more Retirement Boards with certain specified authority, including hiring of an at-will chief executive officer (CEO) to administer both Retirement Plans, retaining legal counsel, granting the CEO appointing authority over Retirement Services staff, excluding certain future Retirement Services employees from classified civil service and the City’s defined benefit Retirement Plans, and establishing a process for setting stipends paid to non-employee Retirement Board members.

Certain bargaining units have raised concerns that the ballot measure is subject to meet and confer required under State law. However, the City believes that the ballot measure does not contain items that are within the scope of mandatory bargaining. The POA has filed a grievance against the City over this issue and both parties are proceeding through the grievance process which, if not resolved, concludes with grievance arbitration. The City cannot predict whether the proposed Charter amendment will be approved by the voters or the ultimate outcome of the grievance process with the POA. For a description of State law requirements related to labor negotiations, see APPENDIX A – “The Norman Y. Mineta San José International Airport – OTHER MATTERS – Labor Relations.”

### **Internal Revenue Code Limitations on Pension Payments**

Both Retirement Plans are tax qualified plans and are subject to Internal Revenue Code requirements. The IRC places limits on the amount of compensation on which a pension may be calculated (\$260,000 for 2014) for those who became members of the Retirement Plans on or after January 1, 1996. Additionally, the IRC caps the annual maximum pension payment that is subject to periodic adjustment based on a consumer price index. For 2014, the maximum annual payment is \$210,000; however, the maximum amount is adjusted downward for non-public safety employees who retire before the age of 62, depending on the employee’s age at retirement.

The Retirement Services Department has become aware of pension overpayments to certain retirees in the Federated Plan and is developing a course of action to recommend to the Federated Board. Exceeding the maximum payment limits places a pension plan at risk of receiving unfavorable tax treatment, which in

turn, could subject the pension plan's income to the payment of income taxes that would reduce the amount available for retirement benefits. The City cannot predict the outcome of this matter although it is not anticipated that any remedial action with respect to the overpayments will have a significant impact on Airport revenues.

### **Accounting Changes for Pension Plans**

In June 2012, the Government Accounting Standards Board (“GASB”) approved Statement No. 67, *Financial Reporting for Pension Plans, an amendment of GASB Statement No. 25*, and Statement No. 68, *Accounting and Financial Reporting for Pensions, an amendment of GASB Statement No. 27*. GASB Statement No. 67 addresses reporting by pension plans and is effective for financial statements for periods beginning after June 15, 2013. GASB Statement No. 68, which primarily relates to reporting by governments that provide pensions to their employees, is effective for fiscal years beginning after June 15, 2014.

In its Management Letter to the City dated November 19, 2012 (“2012 Management Letter”), Macias, Gini & O’Connell (“Macias”), the City’s independent auditing firm, informed the City that these two new statements include the following key changes:

- Separating how the accounting and financial reporting is determined from how pensions are funded.
- Employers with defined-benefit pension plans will recognize a net pension liability, as defined by the standard, in their government-wide, proprietary and fiduciary fund financial statements.
- Incorporating ad hoc cost-of-living adjustments and other ad hoc postemployment benefit changes into projections of benefit payments, if an employer’s past practice and future expectations of granting them indicate they are essentially automatic.
- Using a blended discount rate that applies both the expected long-term rate of return on pension plan investments to projected benefit payments for which plan assets are expected to be available to make projected benefit payments, and the interest rate on a tax-exempt 20-year AA/Aa- or higher rated municipal bond index to projected benefit payments for which plan assets are not expected to be available for long-term investment in a qualified trust.
- Adopting a single actuarial cost allocation method – entry age normal – rather than the current choice among six actuarial cost methods.
- Requiring more extensive note disclosures and required supplementary information.

Both Pension Plans are subject to the provisions of GASB Statement No. 67 beginning with the fiscal year ended June 30, 2014. The City will be subject to the provisions of GASB Statement No. 68 beginning with the fiscal year ending June 30, 2015. In its 2012 Management Letter, Macias also advised the City of the likelihood that GASB Statement No. 68 will dramatically change the City’s financial statements and disclosures and will result in the recognition of a net pension liability. Macias recommended consulting with the Pension Plans’ actuary to develop a better understanding of and to quantify the impact of these new accounting and reporting standards on the City’s current financial statements. The City recognizes the likely significant impact of GASB Statement No. 68 on the City’s financial statements and disclosures to be brought on by the new accounting and reporting standards. The City plans on coordinating the implementation of GASB Statement No. 68 with the Pension Plans’ actuary.

In its June 2014 presentations to the Boards for both Retirement Plans, Cheiron noted that GASB no longer defines an “Annual Required Contribution” or “ARC.” In its place, a recommended contribution

determined in accordance with actuarial standards of practice is referred to as an “Actuarially Determined Contribution” or an “ADC.” For accounting and financial reporting purposes, however, the annual amount reported is simply referred to as the pension expense.

Cheiron also noted that the contribution policy of each plan was sufficient to satisfy the requirements under GASB 67 and 68 to use the expected return on assets as the discount rate. Furthermore, the other assumptions and methods used in the actuarial valuation are consistent with the requirements of GASB 67 and 68, so absent any assumption or plan changes, there will not be a significant difference between the actuarial liability reported in the funding valuation and the GASB 67 and 68 measure of the plan’s total pension liability. The net pension liability reported under GASB 67 and 68 will be similar to the unfunded actuarial liability based on the market value of assets that is reported in the funding valuation. Finally, the annual pension expense under GASB 68 recognizes changes from one year to the next over much shorter periods than are used in actuarially determined contribution amounts. As a result, the annual pension expense will be largely unrelated to actuarially determined contribution amounts and is likely to be much more volatile.

## **APPENDIX B DEFINITIONS**

The following terms will be used in this Appendix B:

***Actuarial Accrued Liability (the “AAL”):*** That portion of the present value of future benefits not provided for by future normal costs. The AAL can be thought of as the value of benefits already earned (under the applicable plan’s funding method) in exchange for employees’ past service.

***Actuarial Value of Assets:*** The value of cash, investments, and other property belonging to the applicable plan as used by the actuary for the purpose of an actuarial valuation. The purpose of an actuarial value of assets is to smooth out fluctuations in market values so long-term costs are not distorted by short-term fluctuations in the market.

***Amortization Payment:*** The portion of the pension plan contribution which is designed to pay interest and principal on the unfunded actuarial liability in a given number of years.

***Annual Required Contribution (the “ARC”):*** The annual required contribution is defined by GASB as the employer’s required contributions calculated in accordance with parameters established by GASB. The ARC has two principal components: the “Normal Cost” and the amortized amount of the unfunded actuarial liability (the “UAL”). The amortization of the UAL represents the current year’s payment toward the unfunded actuarial liability (i.e., the UAL) and must be based on an amortization period no longer than 30 years. The allocation of these cost components between the employer and the employees is determined by the governing documents of the particular plan.

***Entry Age Normal (“EAN”) Actuarial Cost Method:*** A method under which the actuarial present value of the projected benefits of each individual included in an actuarial valuation is allocated as a level percentage of pay from the individual’s date of entry into the plan to the individual’s assumed cessation of employment.

***Market Value of Assets:*** The market value of assets is the estimated amount for which an asset should exchange on the date of valuation between a willing buyer and a willing seller in an arm’s-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently, and without compulsion. The market value of assets is adjusted for accruals at the end of each fiscal year and is reported in the Comprehensive Annual Financial Report of the plan.

**Normal Cost:** Normal Cost is the portion of the contribution that is expected to cover the present value of benefits that are attributable to current service by covered employees under the actuarial cost method adopted by the applicable plan.

**Smoothing:** When measuring assets for determining the UAL, many pension plans, including each of the Pension Plans, “smooth” gains and losses to reduce the volatility of contribution rates. Specific smoothing methodologies for the respective plans are discussed below in “PENSION PLANS – Pension Plans’ Actuarial Valuations – Smoothing Methodology.”

**Unfunded Actuarial Liability (the “UAL”):** The UAL is the excess of the AAL over the actuarial value of assets. The UAL is an estimate based on a series of economic and demographic assumptions associated with the pension plan’s membership. The UAL typically results from investment losses and gains and changes in actuarial assumptions, benefit improvements and other experiences that differ from those anticipated by the actuarial assumptions. The purpose of the UAL calculation is to determine, as of the date of the calculation, the sufficiency of the assets in the Retirement Plans for funding the accrued costs attributable to currently active, vested terminated (i.e., the deferred members) and retired employees. The funding sufficiency is typically expressed as the ratio of the actuarial valuation of assets to the AAL. If the actuarially calculated funding level of a plan is less than 100%, the plan has a UAL.

For a description of assumptions relating to the actuarial valuations of the Pension Plans and Healthcare Plans, see “PENSION PLANS – Pension Plans’ Actuarial Valuations” and “HEALTHCARE PLANS – Healthcare Plans’ Actuarial Valuations”.

## **RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS**

### **Measure B – Charter Amendment Related to Retirement Plans**

Since 2007, the City has examined the costs associated with the Retirement Plans. Following the enactment of Government Accounting Standards Board Statements No. 43 and 45 (“GASB 43/45”) related to the Healthcare Plans, the City and its bargaining units engaged in a phased-in transition to fully fund the annual required contribution by the City and City employees. Although the funding policy then in effect required contributions by both the City and its employees to the annual required contribution for retiree healthcare and dental costs, the funding was not then nor is it currently sufficient to fully fund the required annual contribution for retiree healthcare and dental costs. See “SUMMARY OF RETIREMENT PLANS” below for more information.

In 2010, in light of substantial projected increases to the City’s contribution for both pension and retiree health and dental benefits, the City Council directed the City’s internal auditor (the “City Auditor”) to review and make recommendations regarding the City’s Pension Plans. In September 2010, the City Auditor released a report entitled “Pension Sustainability: Rising Pension Costs Threaten the City’s Ability to Maintain Service Levels – Alternatives for a Sustainable Future” (the “Pension Report”). The Pension Report made a number of recommendations to the City Council that included cost containment strategies for the retirement benefits provided by both Retirement Plans.

During 2011 and 2012, the City and its bargaining groups engaged in negotiations related to modifications of the benefits provided by both Retirement Plans, including the terms of a ballot measure amending the City’s Charter provisions related to retirement benefits. Those negotiations did not result in an agreement with any of the bargaining groups.

The City Council placed a measure on the June 5, 2012 ballot entitled *The Sustainable Retirement Benefits and Compensation Act* and designated as Measure B (“Measure B”) which the voters approved. Measure B modified the City’s Retirement Plans and established the maximum parameters for any new retirement plan for new employees. Measure B’s specific components included:

- Contributions. Prior to the enactment of Measure B, the City Charter required the City and employees to make contributions towards the pension benefit’s Normal Cost in a ratio of 8 (City) to 3 (employee). With the exception of 2010-2011, during which a number of bargaining groups made contributions towards the pension UAL pursuant to negotiated agreements, the City has historically funded most of the UAL associated with the pension benefit. Under Measure B, effective June 23, 2013, employees are required to make additional contributions towards the UAL, phased in at a rate of 4% of pensionable pay per year, up to a maximum of 16% per year, but no more than half the yearly cost of the UAL. Measure B also specifies that if this contribution provision is held by a court to be unenforceable, equivalent savings to the City are to be obtained through compensation reductions. In connection with the litigation related to Measure B, on April 23, 2014, the City entered into a further stipulation to delay implementation of the increased contribution to a date no sooner than July 1, 2015.
- Alternative Plan. Measure B requires the City to adopt a Voluntary Election Program (“VEP”), subject to Internal Revenue Service (“IRS”) approval. The VEP would generally provide reduced pension benefits as compared to the existing Pension Plans; however, employees who “opt into” the VEP would not be required make the additional contributions to the UAL. In the event the VEP is not implemented, employees will be required to make the additional contributions towards the UAL of each Pension Plan as described in the preceding paragraph.
- Disability Retirements. Measure B limits disability retirements to cases where the employee cannot perform the work the employee performed prior to the disability or any other work in the City’s classification plan or, in the case of sworn public safety employees, in the employee’s department. Prior to the enactment of Measure B, the Federated Plan provided for an offset against a disability pension allowance for workers’ compensation paid for the same disability. Measure B also requires that these offset provisions be incorporated in the Police and Fire Plan.
- Cost of Living Adjustments for Retirees. Prior to the enactment of Measure B, both Pension Plans provided automatic annual cost of living (“COLA”) increases of 3% to the allowances paid to retirees and beneficiaries. Measure B authorizes the City Council to temporarily suspend the COLA if the City Council adopts a resolution declaring a fiscal and service level emergency.
- Supplemental Retiree Benefit Reserve (“SRBR”). Measure B requires the elimination of the SRBR in each of the Pension Plans. Prior to the enactment of Measure B, the City suspended payments under SRBR. Since the passage of Measure B, the City Council has adopted ordinances to eliminate the SRBR held in each Pension Plan. On December 4, 2012, the City Council approved an ordinance change, which eliminated the SRBR for the Federated Plan, and on January 29, 2013, the City Council approved an ordinance change which eliminated the SRBR for the Police and Fire Plan.
- Retiree Healthcare. Measure B codifies the preexisting Municipal Code requirements that employees contribute a minimum of 50% of the cost of retiree healthcare, including both the Normal Cost and the UAL. For health benefits, the preexisting Municipal Code provisions provided that both Healthcare Plans pay that portion of the premium that is equivalent to the premium for the lowest-priced medical plan with which the City contracts for medical benefits for City employees. Measure B codified the definition of “Low Cost Plan” for these purposes. Measure B also provides for a “reservation of rights” for the City to terminate or modify any retiree healthcare plan. See “HEALTHCARE

PLANS” for additional information related to the calculation of the Annual Required Contribution for both Healthcare Plans.

- Actuarial and Investment Standards. Measure B requires the Boards for both Retirement Plans to adhere to specified actuarial and investment standards, including that the Retirement Plans must be actuarially sound.
- New Employees. Measure B requires the adoption of a retirement plan for new employees with specified limitations on the benefits and the City’s contributions (“Tier 2”). On August 28, 2012, the City Council adopted a Tier 2 plan within the Federated Plan for employees hired on or after September 30, 2012. See discussion in “Tier 2 and Tier 2B in the Federated Plan,” below. A stipulated arbitration award related to a Tier 2 plan for police members in the Police and Fire Plan was approved on April 26, 2013. See discussion below in “Tier 2 for Police Members in the Police and Fire Plan.” To date, no Tier 2 plan has been established for fire members but the City and the bargaining unit representing sworn fire employees are engaged in binding arbitration on this issue pursuant to the City Charter. See APPENDIX A – “THE NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT – OTHER MATTERS – Labor Relations” for additional information.
- Voter Approval. Measure B reserves to the voters any future change to retirement benefits.

Significant portions of Measure B are currently subject to legal challenge by members of the Retirement Plans. Additionally, various bargaining units representing members of the Retirement Plans have filed unfair labor practice charges with the California Public Employment Relations Board (“PERB”) related to Measure B.

### **Measure B Litigation and Administrative Proceedings and Other Litigation Related to Retirement Benefits**

#### Measure B Litigation

Individual employees, bargaining groups and retirees filed actions in the California Superior Court challenging Measure B or aspects of Measure B in which the plaintiffs allege, among other causes of action, violation of vested rights, due process rights, and impairment of contract. The Measure B provisions related to Tier 2 plans were not challenged.

Six cases have been consolidated under the caption of *San José Police Officers’ Association v. City of San José, Board of Administration for Police and Fire Department* (the “SJPOA Caption”). The seventh case, filed by a retiree in one of the City’s retirement plans (the Police and Fire Plan), which challenged the elimination of the SRBR, has been dismissed without prejudice.

For the cases under the SJPOA Caption, the court trial occurred during the summer of 2013, and the judge took the case under submission in October, 2013 after hearing final arguments and motions by the parties. On April 30, 2014, a consolidated judgment for the cases under the SJPOA Caption was filed (“Consolidated Judgment”), following the judge’s filing of a Statement of Decision on February 20, 2014 and a Tentative Decision on December 20, 2013.

The Consolidated Judgment is summarized as follows:

- The 4% increase in employee pension contributions towards the UAL, up to a maximum of 16% (or 50% of the total liability, whichever is less) was found to be invalid as were the alternative plans to

which existing employees could elect to opt in the VEP. However, the savings provision specifying a mandatory compensation reduction in lieu of additional employee pension contributions was upheld.

- The disability retirement provisions were upheld.
- The elimination of the SRBR in both Pension Plans was upheld.
- The minimum contribution toward retiree healthcare was upheld with respect to the inclusion of unfunded liabilities, but the judgment modified Measure B's language to delete the term "minimum of" to reflect that employees are required to only pay 50% of the cost as opposed to a higher percentage.
- The definition of Low Cost Plan as applied to the retiree healthcare benefit was upheld.
- The ability to suspend the retirement COLA provisions for up to five years in a fiscal and service level emergency was found to be invalid.
- The provision related to voter approval of retirement benefit increases and the severability provision were upheld.

Various parties challenging Measure B under the SJPOA Caption have filed notices of appeal of the Consolidated Judgment and the City Council has authorized filing a notice of appeal. The City anticipates that an appellate decision could be rendered in late 2015 or the first half of 2016.

On April 23, 2014, the City entered into a further stipulation with the parties in the cases under the SJPOA Caption to delay implementation of the increased employee retirement contribution component of Measure B to a date no sooner than July 1, 2015. The stipulation also delays implementation of other aspects of Measure B to a date no sooner than July 1, 2015. The stipulation, however, does not impact new employees in Tier 2 of either of the Retirement Plans.

In addition to these cases, the San José Police Officers' Association ("POA") filed a petition for a writ of mandamus alleging that the City violated the Meyers-Milius-Brown Act by failing to meet and confer in good faith with respect to the City's placement of Measure B on the ballot in June 2012. The POA sought an order preventing the City from proceeding with the Charter changes approved in Measure B, but that request was denied by the Court. This case remains pending in the Superior Court.

On April 15, 2013, the California Attorney General issued an opinion granting the POA's application to bring a *Quo Warranto* action on behalf the People of the State of California alleging that the City violated the Meyers-Milius-Brown Act by failing to meet and confer in good faith with respect to the City's placement of Measure B on the ballot in June 2012. The POA filed its complaint in the *Quo Warranto* action on April 29, 2013. The City has filed its answer and the parties currently are engaged in discovery. The City anticipates a trial date in 2015.

In light of the number of cases and the complexity of the issues presented, the City is unable to predict the ultimate outcome of any of these cases challenging Measure B.

### Administrative Actions Related to Labor Issues Surrounding Retirement

The California Public Employment Relations Board (“PERB”) oversees the implementation of the Meyers-Milias-Brown Act which governs collective bargaining by certain public employers and their employees. PERB acts as an appellate body to hear challenges to dismissals of unfair labor practices charges that are issued by PERB staff, as well as proposed decisions issued by administrative law judges.

In March 2013, PERB staff issued complaints against the City arising from:

1. Unfair labor practice charges filed by the American Federation of State, County and Municipal Employees (“AFSCME”) on behalf of the Municipal Employees Federation (“MEF”) and the Confidential Employees Organization (“CEO”); the International Association of Fire Fighters (“IAFF, Local 230”); and International Federation of Professional and Technical Engineers, Local 21 on behalf of the Association of Engineers and Architects (“AEA”), the Association of Maintenance Supervisory Personnel (“AMSP”), and the City Association of Management Personnel (“CAMP”) alleging that the City failed to meet and confer in good faith on the placement of Measure B on the June 2012 ballot.
2. Unfair labor practice charge filed by the International Union of Operating Engineers, Local No. 3 (“OE#3”) related to the negotiations concerning a successor agreement in 2011 that resulted in the City Council’s approval of the implementation of the City’s last, best final offer in May 2011, and related to the negotiations on retirement issues. It should be noted, however, that the portion of this unfair labor practice charge regarding the negotiations concerning a successor agreement in 2011 that resulted in the City Council’s approval of the implementation of the City’s last, best final offer in May 2011, only, has been withdrawn by OE#3.

These charges were issued pursuant to State regulations governing PERB procedures. Under these provisions, the bargaining unit, an individual, or the employer may file unfair labor practice charges with PERB, and PERB is required to issue a complaint “if the charge...is sufficient to establish a prima facie case.” PERB accepts the allegations of the charging party as true in determining whether to issue the complaint and there is no factual determination by PERB of the accuracy or validity of the allegations prior to the issuance of a complaint. Following the issuance of a complaint, the subject of the complaint files an answer and the matter is assigned to a PERB administrative law judge for a hearing and proposed decision. Both parties have the right to appeal the administrative law judge’s decision to the PERB Board, and the right to seek subsequent appellate review in the Court of Appeals and California Supreme Court.

Hearings before a PERB administrative law judge were held earlier this year on the complaints described above in numbered paragraph 1 and 2 (regarding the negotiations on retirement issues only) with no decision issued to date.

The City cannot predict the outcome of any these matters or the time frame in which they will be resolved. In the case of the PERB complaints alleging the City’s failure to meet and confer in good faith regarding the City’s placement of Measure B on the June 2012 ballot, it is unclear whether PERB has jurisdiction to overturn the results of the election approving Measure B.

### Other Litigation Related to Retirement Benefits

In July 2014, The San Jose Retired Employees Association (the “Association”), along with four individually named retirees, filed a verified complaint against the City in the Santa Clara County Superior Court. The complaint alleges that the City changed the basic retiree healthcare benefit to a new plan that “fundamentally alters” the nature and quality of the benefit provided to retirees, because the plan has

increased co-pays and deductibles. The complaint further alleges that the affected retirees had a vested right to the plan in existence when they were employed by the City, and to the premium amount paid by the City for their healthcare benefit. The action seeks monetary damages for the increase in co-pays, deductibles and premium payments made by the affected retirees, as well as injunctive and writ relief prohibiting the City from continuing to provide the new health benefit to retirees.

The City has been served with the Complaint, and anticipates that it will file a responsive pleading seeking a dismissal of the action on the grounds that the decision in the Measure B litigation, to which the Association was a party, upheld the change in the retiree healthcare benefit.

### **Private Letter Ruling Request to IRS Regarding VEP**

Measure B provides an option for current employees to choose a new tier of benefits. However, the City's outside tax counsel recommended that the City seek a letter ruling from the IRS for this option. The reason stated by the City's outside tax counsel is that the IRS has a number of applications involving employee pension choice currently pending. The question raised in the applications involve whether the election would disqualify the affected plans (thus eliminating their current tax exempt status) and whether the employee contributions should all be taxed to the employee as the contributions are made.

Based on the advice of outside tax counsel, the City Council filed a request for private letter ruling with the IRS on June 13, 2012. Most importantly, that request included asking for the following:

- A ruling that mandatory employee contributions to the Pension Plans would be able to continue to be non-taxable until distributed from the respective Pension Plans (rather than being taxed as the contributions are deposited into each Pension Plan).
- A ruling that the mandatory employee contributions to the Pension Plans would not be subject to income tax withholding as they are deposited into the Pension Plans.
- A ruling that the Pension Plans will not be disqualified, which means that taxes could be payable on their earnings.

As of the date of this Official Statement, the IRS has not taken action on the City's requested ruling. It is not known how the City's request for a private letter ruling will be impacted by the trial court's decision in the Measure B litigation which found the VEP invalid (as described above) or the pending appeals, as described above in "Measure B Litigation."

### **Proposed Amendments to City Charter Regarding Measure B**

In June 2014, the City Council authorized its City Manager to initiate negotiations with the City's employee unions over two possible adjustments, as listed below, to the Measure B pension modifications approved by voters in 2012.

- Allow employees who have left city employment to return to work for the City with the same retirement benefit they had when they left should said employees return before January 1, 2017.
- If a police officer or fire fighter is seriously injured and could not work for a year, they would qualify for a disability retirement should the police officer or fire fighter suffer a serious bodily

injury from a single event, even if the police officer or fire fighter may be able to do other work for the City.

The proposed changes require voter approval of an amendment to the City Charter. The City Council at its August 5, 2014 meeting considered but did not take the required action to place a Charter amendment to implement these changes on the November 2014 ballot and the deadline for doing so has passed. Under current State law, the City may not place a Charter amendment altering retirement benefits on the ballot until the next statewide general election in November 2016.

### **Negotiations Related to Extension of Measure B Stipulation and Additional Changes to Retirement Plans**

At its meeting on September 16, 2014, the City Council considered a recommendation of the City Council's Rules and Open Government Committee and directed (1) the City Manager and the City Attorney in conjunction with the City's outside counsel to enter into negotiations with the parties in the Measure B litigation under the SJPOA Caption to extend the stipulation for implementation of Measure B's provisions requiring increased pension contributions from employees or alternatively, the corresponding reduction in compensation for at least an additional year beyond July 1, 2015; and (2) City staff to enter into negotiations with the POA to create a "Patrol Staffing Retention Plan" ("Retention Plan") that would allow police officers with 25 years or more experience to remain on the force as paid employees, at the rank of officer or sergeant, performing patrol responsibilities, while at the same time receiving a pension from the Police and Fire Plan. The Retention Plan may be considered to be a form of a deferred retirement option program ("DROP" program") under which pension payments are distributed to an account for the employee's benefit while the employee continues to work for the employer and receive a salary without the deductions for pension contributions. The City Council's motion specified that the Retention Plan was to avoid guaranteeing a rate of return for the deferred pension payments as has been the case for other DROP programs.

The City Council's direction related to the stipulation extension was made in order to alleviate the concern of employees in Tier 1 of both Pension Plans about reduction in compensation required by Measure B and upheld by the trial court in the Consolidated Judgment described above in "Measure B Litigation". The City Council's direction regarding the Retention Plan was given in order to address retention of experienced police officers who would be eligible for retirement in 2015.

The City cannot predict the outcome of these negotiations, including the specific elements of any resulting Retention Plan and the cost of implementing such a plan. With respect to the extension of the stipulation related to implementation of Measure B, the City would continue to bear the cost of the UAL, as determined by the actuary for the Pension Plans. See "SUMMARY OF RETIREMENT PLANS – Summary of Retirement Plans Historic and Projected Contributions", below. The City also cannot predict whether there will be other initiatives in addition to those described above to modify Measure B or the Retirement Plans.

### **Tier 2 and Tier 2B in the Federated Plan**

On August 28, 2012, the City Council adopted an ordinance to provide Tier 2 pension benefits for new Federated Plan members hired on or after September 30, 2012. The new tier includes significant benefit changes from the existing Federated Plan ("Tier 1") including, but not limited to, a decrease in the benefits multiplier from 2.5% per year to 2.0% per year; an increase from 55 years to 65 years of age for retirement eligibility at full benefits; a consumer price index-driven cost-of-living increase with a

maximum of 1.5% instead of the existing annual fixed 3.0% increase; a decrease in maximum benefit to 65% of final average salary from 75%; no survivor benefits for death after retirement unless the member elects a reduced benefit; pensionable compensation to be based on base salary only rather than on base compensation plus premium pays; members to contribute 50% of the total Normal Cost, any accrued unfunded actuarial liability and administrative costs of the Federated Plan; year of service credit to require 2,080 hours of regular time worked (including paid leave, but not including overtime) rather than 1,739 hours of regular time worked; and final average compensation based on the highest consecutive three years of compensation instead of on the highest one year.

On August 27, 2013, the City Council adopted an ordinance to exclude Tier 2 members hired on or after September 27, 2013 from retiree medical and dental benefits (“Tier 2B”) but the City shall bear and pay an amount equal to the additional costs incurred by this retirement system for that portion of the unfunded liability as determined by the actuary for the retirement system that the City and Tier 2B members would have otherwise paid as contributions had those employees been eligible for the retiree healthcare defined benefit. With respect to pension benefits and liabilities, references in this Appendix B to Tier 2 in the Federated Pension Plan include Tier 2B.

Tier 2 members (excluding Tier 2B members) in the Federated Plan may participate in the Federated Healthcare Plan. However, in addition to the changes to pension benefits outlined above, at age 65, members will be required to enroll in Medicare Parts A and B. If a member does not meet this requirement within six months of the date the member turns 65, healthcare benefits will cease until such time the member becomes compliant.

### **Tier 2 for Police Members in the Police and Fire Plan**

An arbitration proceeding with the POA on Tier 2 in the Police and Fire Plan was scheduled on April 26, 2013. At this arbitration hearing, the Arbitration Board approved the Tier 2 terms agreed to by the City and the POA as a stipulated arbitration award which has been implemented by the City per the stipulated award’s terms. The new tier includes benefit changes from the existing Police and Fire Plan including, but not limited to, a decrease in the benefits multiplier from 2.5% per year (for first 20 years and 4% for years after that) to 2.0% per year; an increase from 50 years to 60 years of age for retirement eligibility at full benefits; a consumer price index-driven cost-of-living increase with a maximum of 1.5% instead of the existing annual fixed 3.0% increase; a decrease in maximum benefit to 65% of final average salary from 90%; pensionable compensation to be based on base salary only rather than on base compensation plus premium pays; members to contribute 50% of the total Normal Cost, any accrued unfunded actuarial liability and administrative costs of the Police and Fire Plan; and final average compensation based on the highest consecutive three years of compensation instead of on the highest one year.

Tier 2 members participate in the existing Police and Fire Healthcare Plan unless otherwise modified through the meet and confer process.

### **Tier 2 for Fire Members in the Police and Fire Plan**

An arbitration proceeding with the IAFF, Local 230 on Tier 2 in the Police and Fire Plan was held on May 13, 2014, pursuant to the City Charter’s provisions regarding binding interest arbitration. Both the City and the IAFF, Local 230 submitted last offers for settlement for arbitration for consideration by the arbitration board. On September 22, 2014, following the 10 day confidentiality period required by the City Charter, the arbitration board’s decision adopting the City’s proposals on Tier 2, with the exception of eliminating eligibility of Tier 2 fire members for retiree health and dental benefits, became binding and

public. Under the arbitration board's decision, the Tier 2 fire members will continue to be eligible for retiree health and dental benefits. The City plans to proceed with implementation of the arbitration decision by bringing forward the corresponding amendments to the Municipal Code for the City Council's consideration and approval in the fall 2014. See APPENDIX A – "THE NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT – OTHER MATTERS – Labor Relations" for additional information concerning the City Charter provisions regarding binding interest arbitration.

### **Tier 3 for Unrepresented Employees ("Unit 99")**

Tier 3 is an option for new unrepresented management and professional employees hired into Unit 99 (the unit of City's unrepresented management and professional employees) on or after February 3, 2013. Tier 3 provides for a defined contribution plan in lieu of participating in the Tier 2 or Tier 2B defined benefit plan of the Federated Plan. An eligible employee must not have previously been a member of a City retirement system and must sign an irrevocable election form on his or her first day of employment with the City electing to participate in Tier 3. If no irrevocable election form is signed, the employee will be automatically placed into Tier 2, or Tier 2B if hired on or after September 27, 2013, of the Federated Plan. Tier 3 members are not eligible for retiree healthcare or retiree dental benefits. The Tier 3 benefit represents an employee contribution of 3.75% of salary into an Internal Revenue Code Section 401(a) defined contribution plan and a City contribution of 3.75% of salary. Maximum contribution amounts for 2014 are \$52,000 and are subject to future cost of living adjustments by the IRS.

## SUMMARY OF RETIREMENT PLANS

### Service Retirement Formulas for the Pension Plans

The service retirement formulas for calculation of the monthly pension allowance for the Federated Plan and the Police and Fire Plan are described in the tables below:

**Table B-1a**  
**Federated Plan Service Pension Formulas**

	<b>Age/Years of Service</b>	<b>Deferred Vested</b>	<b>Pension Allowance</b>
<b>Tier 1</b>	55 with 5 years service	55 with 5 years service. (This applies to members who separate from City service before retirement and leave their contributions in the Federated Plan.)	2.5% x years of service x final compensation (75% max).
	30 years service at any age		If separation takes place prior to July 1, 2001, final compensation is highest average monthly salary during 36 consecutive months. If after July 1, 2001, final compensation is highest average monthly salary during 12 consecutive months <sup>(1)</sup> .
<b>Tier 2 and Tier 2B</b>	65 with 5 years service	55 with 5 years service with actuarial equivalent reduction. (This applies to members who separate from City service before retirement and leave their contributions in the Federated Plan.)	2.0% x years of service x final compensation (65% max).
	55 with 5 years service with actuarial equivalent reduction		Final compensation is highest average monthly salary during 36 consecutive months. <sup>(2)(3)</sup>

<sup>(1)</sup> Final compensation not to exceed 108% of compensation paid to the member during the second highest consecutive 12-month period, excluding the months used to calculate the highest 12 months. Final average salary excludes overtime pay and expense allowances. In addition, the pension allowance is adjusted for an annual cost of living allowance (COLA) of 3% per year.

<sup>(2)</sup> Final average salary excludes overtime pay and expense allowances. In addition, the pension allowance is adjusted for an index-based annual cost of living allowance (COLA) of a maximum of 1.5% per year.

<sup>(3)</sup> Tier 2 and Tier 2B members have the same pension benefits, however Tier 2B members have no retiree healthcare benefits.

*Source: City of San José Office of Employee Relations; Federated CAFR.*

**Table B-1b**  
**Police and Fire Plan Service Pension Formulas**

<b>Age/Years of Service</b>		<b>Early Retirement</b>	<b>Deferred Vested</b>	<b>Pension Allowance</b>
<b>Police</b>	50 with 25 years service	50-54 with 20 years of service (discounted pension)	55 with 10 years service <u>only</u> if 20 years have elapsed from date of membership.	First 20 years of Service: 2.5% x years of service x final compensation (50% max).
	55 with 20 years service	Allowance reduced pursuant to Municipal Code Section 3.36.810	Benefits can be received at age 50 with at least 25 years of service.	21-30 yrs service: 4% per year of service x final compensation (40% max) <sup>(1)</sup>
	30 years service at any age (with reciprocity must be 50 years of age)			Maximum total benefit is 90% of final compensation
	Mandatory retirement at 70 years of age			
<b>Police Tier 2</b>	60 with 10 years service	Not applicable	55 with 10 years service. Benefits can be received at age 50 with actuarial equivalent reduction.	2.0% x years of service x final compensation (65% max).
	50 with 10 years service and actuarial equivalent deduction			Final compensation is highest average monthly salary during 36 consecutive months. <sup>(2)</sup>
<b>Fire<sup>(3)</sup></b>	50 with 25 years service	50-54 with 20 years of service (discounted pension)	55 with 10 years service only if 20 years have elapsed from date of membership.	First 20 years of service: 2.5% x years of service (50% max)
	55 with 20 years service	Allowance reduced pursuant to Municipal Code Section 3.36.810	Benefits can be received at age 50 with at least 25 years of service.	Beginning 21 <sup>st</sup> year of service: 3% x years of service x final compensation (90% max). All years convert to 3% after 20 years <sup>(1)</sup> .
	30 years service at any age (with reciprocity must be 50 years of age)			
	Mandatory retirement at 70 years of age			

<sup>(1)</sup> Final average compensation is the average monthly salary during the highest 12 consecutive months of service. However, if any of the highest period is within the last 12 months of work, that highest year will be capped at 108% of the 12 months before the last 12 months of service. In addition, the pension allowance is adjusted for an annual cost of living allowance (COLA) of 3% per year.

<sup>(2)</sup> Final average salary excludes overtime pay and expense allowances. In addition, the pension allowance is adjusted for an index-based annual cost of living allowance (COLA) of a maximum of 1.5% per year.

<sup>(3)</sup> As noted above, there is currently no Tier 2 in place for Fire members of the Police and Fire Plan, but arbitration on this matter is currently ongoing.

*Source: City of San José Office of Employee Relations; Police and Fire CAFR.*

## Retirement Plans Membership

As shown in Table B-2a below, total membership in the Federated Pension Plan increased slightly by 159 members from 2012 to 2013. For the Police and Fire Pension Plan, total membership also increased slightly by 104 members from 2012 to 2013. As of June 30, 2013, both Retirement Plans had total active member populations below the combined populations of retirees and terminated vested members.

**Table B-2a  
Retirement Plans' Membership**

	June 30, 2013		June 30, 2012	% Change
	Tier 1	Tier 2	Tier 1	
<b>Pension Plan Membership</b>				
Federated Plan				
Retirees & beneficiaries receiving benefits*	3,711	0	3,602	3.03%
Terminated vested members not yet receiving benefits	994	7	969	3.30%
Active members	2,856	238	3,076	0.59%
<b>Total</b>	<b>7,561</b>	<b>245</b>	<b>7,647</b>	<b>2.08%</b>
Police and Fire Plan				
Retirees & beneficiaries receiving benefits*	1,995	0	1,943	2.68%
Terminated vested members not yet receiving benefits	229	0	166	38.0%
Active members	1,707	0	1,718	(0.64%)
<b>Total</b>	<b>3,931</b>	<b>0</b>	<b>3,827</b>	<b>2.72%</b>
<b>Healthcare Plan Membership</b>				
Federated Plan				
Retirees & beneficiaries receiving benefits*	3,125	0	3,062	2.06%
Terminated vested members not yet receiving benefits	121	0	111	9.00%
Active members	2,856	238	3,076	0.59%
<b>Total</b>	<b>6,102</b>	<b>238</b>	<b>6,249</b>	<b>1.46%</b>
Police and Fire Plan				
Retirees & beneficiaries receiving benefits*	1,893	0	1,855	2.05%
Terminated vested members not yet receiving benefits	7	0	5	40.00%
Active members	1,707	0	1,718	(0.64%)
<b>Total</b>	<b>3,607</b>	<b>0</b>	<b>3,578</b>	<b>0.81%</b>

\* The combined domestic relations orders are not included in the count above as their benefit is included in the member count.

Source: Member data from Federated CAFR and Police and Fire CAFR.

As shown in Table B-2b below, total payroll for active members in the Federated Plan remained fairly constant and the average pay per active member decreased by 0.6%. The Police and Fire Plan also saw a reduction in total payroll for both Police and Fire active members caused by a decrease in both the number of overall active members and a decrease in average pay per member.

**Table B-2b**  
**Retirement Plans' Active Member and Payroll Data**  
*(Payroll amounts in millions)*

	<u>June 30, 2013</u>	<u>June 30, 2012</u>	<u>% Change</u>
<b>Federated Plan Payroll Data</b>			
Active Federated Member Payroll	\$ 225.8	\$ 225.9	(0.0%)
Average pay per Active Federated Member	\$ 72,973	\$ 73,426	(0.6%)
<b>Police and Fire Plan Payroll Data</b>			
Active Member Payroll Police	\$ 109.8	\$ 116.5	(5.7%)
Active Member Payroll Fire	74.9	71.5	4.7%
Total Active Member Payroll <sup>(1)</sup>	<u>\$ 184.6</u>	<u>\$ 188.0</u>	(1.8%)
Average Pay per Active Member Police	\$ 106,793	\$ 108,228	(1.3%)
Average Pay per Active Member Fire	\$ 110,253	\$ 111,378	(1.0%)
Average Pay Per Active Member	\$ 108,169	\$ 109,405	(1.1%)

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

*Source: Payroll/pay data from Cheiron 2013 Federated Actuarial Report, Cheiron 2013 Police and Fire Actuarial Report.*

### **Summary of Retirement Plans Historic and Projected Contributions**

Investors are cautioned that the amount of the UAL, the funded ratio, and the calculations of Normal Cost as reported by the Retirement Plans and the resulting pension and healthcare contributions is “forward looking” information prepared by the Retirement Plans for their own purposes. Such “forward looking” information reflects the judgment of the Boards of the respective Retirement Plans and their actuaries as to the amount of assets which the Retirement Plans will be required to accumulate to fund future benefits over the lives of the currently active employees, vested terminated employees, existing retired employees, and their beneficiaries. These judgments are based upon a variety of assumptions, one or more of which may prove to be inaccurate or that may change with the future experience of the Retirement Plans. The actuarial methods and assumptions could be changed by the Boards of the respective Retirement Plans at anytime. Such changes could cause the City’s obligations to the Retirement Plans to be higher or lower in any particular year.

As shown in Table B-3a, the City’s annual dollar contribution to the Pension Plans and Healthcare Plans has been increasing since 2007-2008. The decline in the City’s contributions for the Police and Fire Plan in 2012-2013 from the amount paid in 2011-2012 is primarily attributed to the plan experience including a significant reduction in payroll.

**Table B-3a**  
**Federated and Police and Fire Retirement Plans**  
**City Pension and Healthcare Contributions**  
*(Amounts in thousands)*

<b>Fiscal Year</b>	<b>Federated Plan<sup>(1)(2)</sup></b>			<b>Police and Fire Plan<sup>(3)(4)</sup></b>			<b>Grand Total</b>
	<b>Pension</b>	<b>Healthcare</b>	<b>Total</b>	<b>Pension</b>	<b>Healthcare</b>	<b>Total</b>	
2007-08	\$54,958	\$11,560	\$66,518	\$56,372	\$10,618	\$66,990	\$133,508
2008-09	57,020	16,368	73,388	53,103	9,888	62,991	136,379
2009-10	54,566	17,027	71,593	52,315	11,284	63,599	135,192
2010-11	59,180	17,146	76,326	77,918	17,001	94,919	171,245
2011-12	87,082	25,834	112,916	121,009	21,205	142,214	255,130
2012-13	103,109	21,251	124,360	105,234	15,808	121,042	245,402
2013-14 <sup>(5)</sup>	102,470	24,484	126,954	119,561	17,073	136,673	263,627
2014-15 <sup>(5)</sup>	116,333	25,438	141,771	128,822	19,441	147,641	289,412

- <sup>(1)</sup> The annual employer pension contributions provided above (2007-2008 thru 2012-2013) are based on the Board adopted pension contribution rates adjusted for the timing of actual contributions including year-end contributions receivable and prior year contribution adjustments. In addition, in fiscal year ended June 30, 2011, the contribution has been reduced to reflect the additional employee contributions pursuant to MOAs with certain bargaining units.
- <sup>(2)</sup> The actual healthcare contributions provided above (2007-2008 thru 2012-2013) include year-end contributions receivable and prior year contribution adjustments.
- <sup>(3)</sup> The annual employer pension contributions provided above (2007-2008 thru 2012-2013) are based on the Board adopted pension contribution rates adjusted for the timing of actual contributions including year-end contributions receivable and prior year contribution adjustments. In addition, in fiscal year ended June 30, 2011, the contribution has been reduced to reflect the additional employee contributions.
- <sup>(4)</sup> The actual healthcare contributions include year-end contributions receivable and prior year contribution adjustments. In addition, beginning with fiscal year 2011, the implicit subsidy amounts have also been included in actual contributions. Actual contributions for the fiscal years ended June 30, 2008 through 2012 were made to the Postemployment Healthcare 401(h) Plan. All employer contributions to the Postemployment Healthcare Plans were made to the new Section 115 subtrusts in fiscal year 2012-2013.
- <sup>(5)</sup> Fiscal years 2013-2014 and 2014-2015 amounts are based on actuarial projections assuming contributions paid at beginning of the year.

Sources: *City of San José, Retirement Services Department, Federated CAFR and Police and Fire CAFR (for years 2007-2008 through 2012-2013), Cheiron 2013 Federated Pension Plan Actuarial Report and Cheiron 2013 Police & Fire Pension Plan Actuarial Report (for years 2013-2014 and 2014-2015).*

In January 2014, as directed by the Retirement Plans, Cheiron provided five-year budget projections for the City's contributions for the Pension Plans and Healthcare Plans based on the June 30, 2013 actuarial valuations. The five-year budget projections provided by Cheiron also included projections of the City's contributions to both Pension Plans for twenty years through 2034. The projections assume that all valuation assumptions were exactly met and are exactly met each and every year for the projection period. In addition, the projections assume that the active population remains level and plan provisions remain unchanged. In reality, actual experience will deviate from the assumptions with the expectation that overall favorable deviations will be offset by unfavorable deviations over time. For both Pension Plans, Cheiron's projections also include the elimination of the SRBR for the forecast period. In addition, for both Healthcare Plans, Cheiron's projections include changes to the healthcare plans offered to active employees as described in APPENDIX A – “THE NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT – OTHER MATTERS – Labor Relations – Modification to Pension and Retiree Healthcare Benefits and other Employment Benefits.” For additional information and discussion regarding the funding policy of both Healthcare Plans, please refer to “HEALTHCARE PLANS – Funding Policy” below.

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

<b>Fiscal Year</b>	<b>Federated Payroll</b>	<b>Amount for Pension</b>	<b>Pension Rate</b>	<b>Healthcare Amount</b>	<b>Healthcare Rate</b>	<b>Total Amount</b>	<b>Total Rate</b>
2015	\$230.3	\$120.5	52.31%	\$26.3	11.44%	\$146.8	63.75%
2016	234.9	120.9	51.49	31.7	13.51	152.7	65.00
2017	239.6	123.0	51.35	33.0	13.76	156.0	65.11
2018	244.4	127.8	52.30	33.7	13.80	161.5	66.10
2019	249.3	129.2	51.82	34.5	13.83	163.7	65.66

*Source: Data from Cheiron 5-Year Budget Projections for Federated Plan, January 15, 2014.*

Please note that for the Police and Fire Plan projections below, the City has negotiated agreements regarding the Healthcare Plan funding policy which includes a provision that if the City or member rates exceed 11% and 10% of payroll respectively, the parties are to meet and confer on how to address any contributions above those two percentages. As the five-year projection illustrates, the rates for Police are projected to reach those levels in fiscal year 2015, and Cheiron was directed to cap the City contribution rates to this limit in the forecast.

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

<b>Fiscal Year</b>	<b>Police &amp; Fire Payroll</b>	<b>Amount for Pension</b>	<b>Pension Rate</b>	<b>Healthcare Amount</b>	<b>Healthcare Rate</b>	<b>Total Amount</b>	<b>Total Rate</b>
2015	\$188.4	\$133.3	70.79%	\$19.4	10.30%	\$152.7	81.09%
2016	192.1	133.5	69.48	20.9	10.85	154.4	80.32
2017	198.8	136.9	68.83	21.7	10.89	158.6	79.72
2018	205.8	144.0	69.97	22.5	10.89	166.5	80.87
2019	213.0	147.5	69.28	23.2	10.89	170.7	80.17

*Source: Data from Cheiron 5-Year Budget Projections for Police and Fire Plan, February 26, 2014*

In addition to the five-year projected contributions for the Pension and Healthcare Plans, as directed by and for the benefit of the Retirement Plans, Cheiron provided the following 20-year projections of contributions for the Pension Plans. For the Federated Pension Plan, the 20-year projections show contribution rates after 2017-2018 gradually declining to about 45.3% of pay in fiscal year 2032, reflecting the gradual impact of Tier 2's lower Normal Cost rate. In fiscal year 2033, the contribution rate drops further to about 38.1% when the impact of the 2011 assumption changes is fully amortized. For the Police and Fire Pension Plan, the 20-year projections show contribution rates gradually declining as Tier 2 and its lower Normal Cost rate are phased in. In 2027 and 2028, there is a significant drop as the

experience losses and assumption changes from 2009 and 2010 are fully amortized. The variability in the remainder of the projection reflects the expiration of additional amortizations established after 2010.

It is certain that not all assumptions will be exactly met each and every year. There is a significant range of uncertainty in these 20-year projections due primarily, but not exclusively, to the assumed rates of investment return. Actual investment returns that vary from the assumption can result in significantly different contribution rates. In the short-term, the five-year asset smoothing method combined with the amortization period (20 years for the Federated Plan and 16 years for the Police and Fire Plan) act to dampen the immediate effect on contribution rates of changes in the unfunded liability.

**Table B-3d**  
**20-Year Projections of City Pension Contributions**  
*(Amounts in thousands)*

<b>Fiscal Year</b>	<b>Federated Plan</b>		<b>Police and Fire Plan</b>	
	<b>Projected City Contribution</b> <b>Amount</b>	<b>Projected Total Contribution Rate</b> <b>(% of Payroll)</b>	<b>Projected City Contribution</b> <b>Amount</b>	<b>Projected Total Contribution Rate</b> <b>(% of Payroll)</b>
2015	\$120,476	52.3%	\$133,333	70.8%
2016	120,943	51.5	133,466	69.5
2017	123,026	51.3	136,847	68.8
2018	127,813	52.3	143,999	70.0
2019	129,186	51.8	147,550	69.3
2020	131,137	51.1	151,434	68.7
2021	133,073	50.5	155,367	68.1
2022	135,046	49.8	159,191	67.4
2023	137,174	49.2	149,094	61.0
2024	139,507	48.6	152,329	60.2
2025	142,026	48.1	167,720	64.1
2026	144,647	47.7	171,886	63.4
2027	147,331	47.2	115,509	41.2
2028	150,100	46.8	77,127	26.6
2029	152,912	46.3	116,674	38.8
2030	155,749	45.9	103,802	33.4
2031	158,640	45.4	93,667	29.1
2032	162,739	45.3	101,990	30.6
2033	140,779	38.1	96,772	28.1
2034	133,516	35.1	76,711	21.5

*Source: Data from Cheiron 2014 5-Year Budget Projections for Federated Plan dated January 15, 2014, and Police and Fire Plan dated February 26, 2014.*

## PENSION PLANS

### **Summary of Historic UAL and Funded Ratios**

The current funding status of the pension benefits provided by both Pension Plans is summarized in Table B-4a. The funded ratio in the following tables for pension benefits does not take into account the assets and liabilities related to retiree healthcare benefits or, prior to 2011, the SRBR for each Pension Plan. The current funding status of the Healthcare Plans is summarized in “HEALTHCARE PLANS.”

The schedules of the funding progress for both Pension Plans are set forth in the Required Supplementary Information Section of the City’s Basic Financial Statements for the fiscal year ended June 30, 2013. However, it is important to note that the funding progress schedules referred to in the City’s Basic Financial Statements for the fiscal year ended June 30, 2013 reflect actuarial data as of June 30, 2012. The most recent actuarial valuations for the Federated Plan and the Police and Fire Plan, both as of June 30, 2013, represent the current data available for the funding progress for both Pension Plans as shown below in Tables B-4b and B-4c.

Table B-4a below shows the historical dollar amount of the UAL for both Pension Plans and the funded ratio as of the last eight valuation dates calculated using the actuarial (smoothed) value of assets. Over the past several years, both Pension Plans have experienced steady and significant increases in the UAL, primarily attributable to changes in actuarial assumptions and recognition of prior unfavorable investment returns.

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**Table B-4a**  
**Federated Plan and Police & Fire Plan**  
**Historical Pension UAL and Funded Ratio**  
*(Amounts in thousands)*

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<b>Fiscal Year</b>	<b>Federated Plan - Pension</b>		<b>Police &amp; Fire Plan - Pension</b>		<b>Total</b>
	<b>UAL</b>	<b>Funded Ratio</b>	<b>UAL</b>	<b>Funded Ratio</b>	
6/30/2003	\$ 30,972	98%	\$ (3,087)	100%	\$ 27,885
6/30/2005	326,916	81	44,342	98	371,258
6/30/2007	338,092	83	6,596	100	344,688
6/30/2009	729,597	71	393,913	87	1,123,510
6/30/2010	780,945	69	653,751	80	1,434,696
6/30/2011	981,567	65	510,286	84	1,491,853
6/30/2012 <sup>(1)</sup>	1,078,027	62	694,253	80	1,772,280
6/30/2013	1,230,493	59	806,107	78	2,036,600

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<sup>(1)</sup> June 30, 2012 results reflect the elimination of the Supplemental Retiree Benefit Reserve.

*Source: Data from Cheiron 2013 Federated Pension Plan and Police and Fire Pension Plan Actuarial Reports (2005-2012 only), Retirement Services Department.*

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The UAL as a percentage of covered payroll is a measure of the relative magnitude of the UAL. As illustrated in the table below, the Federated Plan’s UAL was 545% of total covered annual payroll in 2013. It would require contributing approximately five and a half times the 2013 covered payroll to fund all of the Federated Plan’s accrued actuarial liability.

**Table B-4b**  
**Federated Plan - Schedule of Pension Funding Progress**  
*(Amounts in thousands)*

<b>Valuation Date</b>	<b>Actuarial Value of Assets</b>	<b>Actuarial Liability</b>	<b>UAL</b>	<b>Funded Ratio</b>	<b>Covered Payroll</b>	<b>UAL as % of Covered Payroll</b>
6/30/2005	\$ 1,384,454	\$ 1,711,370	\$ 326,916	81%	\$ 286,446	114%
6/30/2007	1,622,851	1,960,943	338,092	83	291,405	116
6/30/2009	1,756,558	2,486,155	729,597	71	323,020	226
6/30/2010	1,729,413	2,510,358	780,945	69	300,811	260
6/30/2011	1,788,660	2,770,227	981,567	65	228,936	429
6/30/2012 <sup>(1)</sup>	1,762,973	2,841,000	1,078,027	62	225,859	477
6/30/2013	1,782,629	3,013,763	1,231,134	59	225,779	545

(1) June 30, 2012 results reflect the elimination of the Supplemental Retiree Benefit Reserve.

(2) The Tier 2 assets were omitted from this table.

*Source: Cheiron 2013 Federated Pension Plan Actuarial Report*

As illustrated below for the Police and Fire Plan, the UAL was 437% of total covered annual payroll in 2013. It would require contributing approximately four times the 2013 covered payroll to fund all of the Police and Fire Plan's accrued actuarial liability.

**Table B-4c**  
**Police and Fire Plan - Schedule of Pension Funding Progress**  
*(Amounts in thousands)*

<b>Valuation Date</b>	<b>Actuarial Value of Assets</b>	<b>Actuarial Liability</b>	<b>UAL</b>	<b>Funded Ratio</b>	<b>Covered Payroll</b>	<b>UAL as % of Covered Payroll</b>
6/30/2005	\$ 1,983,090	\$ 2,027,432	\$ 44,342	98%	\$ 210,018	21%
6/30/2007	2,365,790	2,372,386	6,596	100	227,734	3
6/30/2009	2,569,569	2,963,482	393,913	87	255,223	154
6/30/2010	2,576,705	3,230,456	653,751	80	251,058	260
6/30/2011	2,685,721	3,196,007	510,286	84	190,726	268
6/30/2012	2,703,539	3,397,792	694,253	80	187,959	369
6/30/2013	2,771,924	3,578,031	806,107	78	184,645	437

*Source: Cheiron 2013 Police and Fire Pension Plan Actuarial Report*

### Pension Plans' Actuarial Valuations

Prior to 2010-2011, actuarial valuations for the pension benefits of both Pension Plans were prepared on a biennial basis. Commencing with the June 30, 2009 actuarial valuations, the valuations for both Pension Plans are prepared on an annual basis, and in each actuarial valuation for each of the Pension Plans, the corresponding actuary recommends contribution rates for the fiscal year beginning after the completion of that actuarial valuation. When actuarial recommended contribution rates are approved by the respective Boards of the Pension Plans, these become the City's and the employees' legally required contribution rates for the fiscal year beginning one year after the valuation date. For example, the recommended

contributions contained in each of the actuarial reports for the Pension Plans as of June 30, 2013 apply to contributions by the City and the employees for the fiscal year beginning July 1, 2014.

The required contribution rates determined by the Pension Plans' actuary anticipate that the City will make contributions on a bi-weekly basis throughout the fiscal year. The City has elected since 2008-2009 to prefund all or part of its total annual required contributions to the Pension Plans at the beginning of each fiscal year and the Pension Plans' actuary applies an interest discount to the required contributions to account for the fact that contributions are made at the beginning of the year instead of throughout the year. The "prefunded" annual contributions are made on the basis of estimated bi-weekly payroll for the fiscal year and are trued up at the end of the fiscal year based on actual bi-weekly payroll. Generally, both Pension Plans employ a "floor" methodology for determining contributions. The floor methodology requires that the contribution for the City be the greater of the dollar amount reported in the actuarial valuations or the dollar amount determined by applying the percent of payroll reported in the actuarial valuation to the actual payroll for the fiscal year. This methodology ensures that adequate funding is achieved regardless of increases or decreases to the actual payroll from the actuarial assumed payroll.

Below are highlights of several of the Pension Plans' actuarial assumptions:

***Actuarially Assumed Investment Rates of Return.*** The net rate of return assumed by each Pension Plan represents the long-term expected rate of return on the applicable Pension Plan's investments that, together with current assets and future contributions, would generate sufficient funds to pay benefits. For the June 30, 2013 valuations, the Federated Board reduced its assumed investment rate of return from 7.5% to 7.25% while the Police and Fire Board reduced its assumed investment rate of return from 7.25% to 7.125%. The Boards for the Pension Plans have incrementally reduced their respective assumed rates of return from 8.25% since July 1, 2009 for the Federated Plan and from 8.0% since July 1, 2010 for the Police and Fire Plan.

***"Smoothing" Methodology.*** When measuring assets for determining the UAL, many pension plans, including each of the Pension Plans, "smooth" gains and losses to reduce the volatility of contribution rates. Both Pension Plans utilize a smoothing or spreading of that shortfall or excess over a five-year period. If in the one-year period prior to the annual actuarial valuation, the actual net investment return on the Pension Plan's market value of assets is lower or higher than the actuarial assumed net rate of return, then 20% of the shortfall or excess is recognized each year when determining the recommended contribution rates for that actuarial valuation. The impact of this will result in smoothed assets which are lower or higher than the market value of assets depending upon whether the remaining amount to be smoothed is either a net gain or a net loss. For the Police and Fire Plan only, past practice has been to limit the smoothing of assets to be no greater than 120% and no less than 80% of the market value of assets. Under this practice, any investment gains or losses that would cause smoothed assets to fall outside of this 80%-120% market value corridor would be recognized immediately rather than smoothed over five years.

***Amortization Method and Period.*** Various plans use different amortization periods for paying off or amortizing a UAL. Prior to June 30, 2009, the Federated Plan used a 30-year open or rolling amortization period which meant that in each actuarial valuation, the entire UAL was re-amortized over a new 30-year period following each valuation period. Subsequent to June 30, 2009, the UAL for the Federated Plan as of June 30, 2009 is amortized over a 30-year closed period, and changes in the UAL in future years will be amortized over a 20-year closed period, with a separate amortization schedule set up for each change in UAL in each year for pension benefits.

With respect to the UAL attributable to periods on or before June 30, 2003, the Police and Fire Plan uses a closed amortization period which ends on June 30, 2017. With respect to all UAL attributable to

periods after June 30, 2003, the Police and Fire Plan amortizes it through a layered amortization method in which the UAL experienced between annual valuation dates are amortized over a period ending 16 years following each applicable valuation date. The contribution to the UAL as of the end of a given year (as reflected in an actuarial valuation report) is amortized as a level percentage of payroll.

Tables B-5a and B-5b summarize actuarial assumptions used by both Pension Plans for the 2013 valuations:

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**Table B-5a**  
**Federated Plan – Pension Actuarial Assumptions**

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Valuation Date	June 30, 2013
Actuarial funding method	Entry Age
Amortization method	Level percent of pay, closed, layered
Equivalent single amortization period	25.8 Years
Asset valuation method	5-year smoothing of return over or under expected returns
Actuarial Assumptions:	
Investment Rate of Return	7.25%
Projected salary increases due to wage inflation <sup>(1)</sup>	2.00% for 5 years, and 2.85% thereafter
Cost-of-living Adjustments <sup>(2)</sup>	Tier 1-3.0% per year; Tier 2-1.5% per year

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<sup>(1)</sup> Additional merit salary increases of 0.25% to 4.50% based on a participant's years of service are also assumed. These increases are not used in the amortization of the UAL.

<sup>(2)</sup> Cost-of-living adjustments are fixed at 3% by the plan provisions for Tier 1 and do not fluctuate with actual inflation. For Tier 2, adjustments fluctuate with actual inflation and are capped at 1.5%.

*Source: Data from Cheiron 2013 Federated Pension Plan Actuarial Report*

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**Table B-5b**  
**Police and Fire Plan – Pension Actuarial Assumptions**

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Valuation Date	June 30, 2013
Actuarial funding method	Entry Age
Amortization method	Level percent of pay, closed, layered
Equivalent single amortization period	13.4 Years
Asset valuation method	5 year smoothing of return
Actuarial Assumptions:	
Investment Rate of Return	7.125%
Wage inflation <sup>(1)</sup>	2.00% for two years and 3.50% thereafter
Cost-of-living Adjustments <sup>(2)</sup>	3.0% per year, 1.5% for Police Tier 2

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<sup>(1)</sup> Excludes merit increases.

<sup>(2)</sup> Cost-of-living adjustments are fixed at 3% by the plan provisions for Tier 1 and do not fluctuate with actual inflation. For Tier 2, adjustments fluctuate with actual inflation and are capped at 1.5%.

*Source: Data from Cheiron 2013 Police and Fire Pension Plan Actuarial Report*

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### Federated Pension Plan 2013 Valuation Summary

The most recent actuarial valuation of the Federated Pension Plan, as of June 30, 2013, was performed by Cheiron (“Cheiron” or, alternatively, the “Actuary”) and summarized in its report dated December 13, 2013 entitled: “Federated City Employees’ Retirement System June 30, 2013 Actuarial Valuation” (the “Cheiron 2013 Federated Pension Plan Actuarial Report”) and included both Tier 1 and Tier 2. The Federated Pension Plan’s actuarial value is calculated by recognizing the deviation of actual investment returns compared to the expected return (7.25% for 2013-2014, 7.5% for 2011-2013, 7.95% for 2010-2011, 7.75% for 2009-2010) over a five-year period. The dollar amount of the expected return on the market value of assets is determined using actual contributions, benefit payments and administrative expenses during the year. Any difference between this amount and the actual net investment earnings is considered a gain or loss.

In the Cheiron 2013 Federated Pension Plan Actuarial Report, the Actuary concluded that as of June 30, 2013:

- The funded ratio based on the actuarial value of assets for the Federated Plan was 59.2%, down from 62.1% as of June 30, 2012.
- The funded ratio based on the market value of assets remains constant at 58%.
- The UAL was approximately \$1,230.5 million as compared to a UAL of \$1,078.0 million as of June 30, 2012.
- The actuarial value of assets was equal to \$1,783.3 million and the actuarial accrued liability was \$3,013.8 million. The Federated Pension Plan’s total actuarial liability increased by 6.1% and the market value of assets increased by 6.8% when compared to the June 30, 2012 valuation.
- Total deferred investment gains and losses for the past four years net to a loss of \$21.7 million. Any future investment gains or losses will impact the Federated Pension Plan’s future funded percentage and contribution rate requirements. Deferred losses are the result of smoothing.
- The ratio of the actuarial value of assets to the market value of assets decreased from 107% to 101% from the prior valuation, indicating that the deferred losses are now slightly greater than the deferred gains.

### Police and Fire Pension Plan 2013 Valuation Summary

The most recent actuarial valuation of the Police and Fire Pension Plan, as of June 30, 2013, was performed by Cheiron and summarized in its report dated January 7, 2014 (the “Cheiron 2013 Police and Fire Pension Plan Actuarial Report”). The Cheiron 2013 Police and Fire Pension Plan Actuarial Report did not directly value Tier 2 police members as the tier’s effective date occurred after the valuation date; however, contribution rates for Tier 2 police members for the fiscal year ending June 30, 2015 were included. The Police and Fire Pension Plan’s actuarial value of assets is calculated by recognizing the deviation of actual investment returns compared to the expected return (7.125% for 2013-2014, 7.25% for 2012-2013, 7.5% for 2011-2012, 7.75% for 2010-2011, 8.00% for prior years) over a five-year period. The dollar amount of the expected return on the market value of assets is determined using the actual contributions and benefit payments during the year. Any difference between this amount and the actual net investment earnings is considered a gain or a loss.

In the Cheiron 2013 Police and Fire Pension Plan Actuarial Report, Cheiron concluded that as of June 30, 2013:

- The funded ratio based on the actuarial value of assets was 77.5%, down from 79.6% as of June 30, 2012. This is due primarily to recognition of prior investment losses and the reduction of the investment return assumption from 7.25% to 7.125%.
- The funded ratio based on the market value of assets was 78.0%, increased from 75.9% as of June 30, 2012.
- The UAL was approximately \$806.1 million as compared to the UAL of approximately \$694.3 million reported as of June 30, 2012.
- The decrease in the funded ratio, and corresponding increase in UAL, is primarily attributable to changes in actuarial assumptions and recognition of prior unfavorable investment returns.
- The actuarial value of pension assets was equal to approximately \$2,771.9 million and actuarial accrued liabilities of approximately \$3,578.0 million. For the Police and Fire Pension Plan, the total actuarial liability increased by 5.3% and the market value of assets increased by 8.2% compared to the prior valuation.
- Total deferred investment gains and losses for the past four years net to a gain of \$17.6 million. Any future investment gains or losses will impact the Police and Fire Plan’s future funded percentage and contribution rate requirements. Deferred gains are the result of smoothing.
- The ratio of the actuarial value of assets to the market value of assets decreased from 105% to 99% from the prior valuation, indicating that the deferred losses are greater than the deferred gains.

## Pension Plan Assets and Liabilities

Table B-6 compares the assets, liabilities, UAL and funding ratios between the June 30, 2013 valuation and the June 30, 2012 valuation for the pension assets and liabilities of both Pension Plans.

**Table B-6**  
**Pension Assets & Liabilities**  
*(Amounts in millions)*

	<b>June 30, 2013</b>	<b>June 30, 2012<sup>(1)</sup></b>	<b>% Change</b>
<b>Federated Plan</b>			
Total Actuarial Liability	\$ 3,013.8	\$ 2,841.0	6.1%
Market Value Assets	\$ 1,761.5	\$ 1,649.2	6.8%
Actuarial Value Assets	\$ 1,783.3	\$ 1,763.0	1.2%
Unfunded Actuarial Liability	\$ 1,230.5	\$ 1,078.0	14.1%
Funding Ratio – Market Value	58%	58%	0.4%
Funding Ratio – Actuarial Value	59%	62%	(2.9%)
<b>Police &amp; Fire Plan</b>			
Total Actuarial Liability	\$ 3,578.0	\$ 3,397.8	5.3%
Market Value Assets	\$ 2,789.5	\$ 2,578.9	8.2%
Actuarial Value Assets	\$ 2,771.9	\$ 2,703.5	2.5%
Unfunded Actuarial Liability	\$ 806.1	\$ 694.3	16.1%
Funding Ratio – Market Value	78.0%	75.9%	2.8%
Funding Ratio – Actuarial Value	77.5%	79.6%	(2.6%)

<sup>(1)</sup> June 30, 2012 results reflect the elimination of the Supplemental Retiree Benefit Reserve.

Source: Data from Cheiron 2013 Federated Pension Plan Actuarial Report; Cheiron 2013 Police and Fire Pension Plan Actuarial Report

To determine on-going funding requirements for pension benefits, most pension plans utilize an actuarial value of pension assets that differs from the market value of those assets. The actuarial value of pension assets is based on smoothing year-to-year market value returns for purposes of reducing the resulting volatility on contributions. The market value represents the value of the pension assets if they were liquidated on the valuation date. Tables B-7 and B-8 below show the calculation of the market value of the pension assets of each Pension Plans and provide the applicable actuarial value for purposes of comparison.

**Table B-7**  
**Federated Plan - Market and Actuarial Value of Pension Assets**  
*(Amounts in thousands)*

	<b>June 30, 2013</b>	<b>June 30, 2012</b>
<b>Market Value, Beginning of Year</b>	\$ 1,649,249	\$ 1,760,617
Contributions		
Member	\$ 12,652	\$ 10,554
City	103,109	87,082
Contributions Total	\$ 115,762	\$ 97,637
Net Investment Earnings*	146,366	(68,901)
Benefit Payments	(146,807)	(136,798)
Administrative Expenses	(3,024)	(3,306)
<b>Market Value, End of Year</b>	<b>\$ 1,761,546</b>	<b>\$ 1,649,250</b>
Actuarial Value of Assets	\$ 1,783,270	\$ 1,762,973

\* Gross investment earnings less investment expenses

Source: Cheiron 2013 Federated Pension Plan Actuarial Report

**Table B-8**  
**Police and Fire Plan - Market and Actuarial Value of Pension Assets**  
*(Amounts in thousands)*

	<b>June 30, 2013</b>	<b>June 30, 2012</b>
<b>Market Value, Beginning of Year</b>	\$ 2,578,929	\$ 2,627,728
Contributions		
Member	\$ 20,228	\$ 19,345
City	105,234	121,008
Contributions Total	\$ 125,462	\$ 140,353
Net Investment Earnings*	248,258	(33,877)
Benefit Payments	159,702	151,720
Administrative Expenses	3,422	3,556
<b>Market Value, End of Year</b>	<b>\$ 2,789,524</b>	<b>\$ 2,578,929</b>
Actuarial Value of Assets	\$ 2,771,924	\$ 2,703,539

\* Gross investment earnings less investment expenses

Source: Cheiron 2013 Police and Fire Pension Plan Actuarial Report

## Components of Actuarial Liability

The actuarial liability illustrated in Table B-9 represents the expected amount of money needed to pay for pension benefits attributed to employee service rendered prior to the valuation date. It is the difference between the present value of future pension benefits and the present value of future Normal Costs. In addition, retired Federated Plan members in Tier 1 receive an annual fixed 3% cost of living adjustment which, as Table B-9 illustrates, primarily accounts for approximately \$1.07 billion of the actuarial liability for the June 30, 2013 valuation. For the Police and Fire Plan, the annual 3% cost of living adjustment for Tier 1 members accounts for approximately \$1.40 billion of the actuarial liability.

**Table B-9**  
**Pension Actuarial Liability**  
*(Amounts in thousands)*

	June 30, 2013			June 30, 2012
	Basic	Cost of Living	Total	Total
<b>Federated Plan<sup>(1)</sup></b>				
Total Actuarial Liability	\$ 1,943,093	\$ 1,070,671	\$ 3,013,764	\$ 2,841,000
<b>Police &amp; Fire Plan<sup>(2)</sup></b>				
Total Actuarial Liability	\$ 2,181,383	\$ 1,396,648	\$ 3,578,031	\$ 3,397,792

<sup>(1)</sup> The valuation for 2013 includes the Federated Pension Plan Tier 2.

<sup>(2)</sup> The valuation for 2013 does not directly value the Tier 2 police members.

*Source: Data from Cheiron 2013 Federated Pension Plan Actuarial Report and Cheiron 2013 Police and Fire Pension Plan Actuarial Report*

## Pension Plans' Contribution

The Pension Plans' contribution for the City and employees are based upon actuarial calculations that take into consideration a number of economic and demographic assumptions, including assumed investment earnings on the valuation assets of the Pension Plans that are used to pay benefits. The actuarial process can employ various funding methodologies to determine annual contribution levels. Currently, Cheiron, the actuarial firm retained by the respective Boards of both Pension Plans, employs the entry age normal actuarial cost method. Under this method, there are two components to the pension contribution: the Normal Cost and the UAL contribution.

Normal Costs for the Police and Fire Pension Plan Tier 1 and the Federated Pension Plan Tier 1, as governed by the City Charter and the Municipal Code, are shared by the City and the active employee members of the Pension Plans with a contribution ratio of 8/11 for the City and 3/11 for the employee. For the Police and Fire Pension Plan Tier 2 and the Federated Pension Plan Tier 2, the City's portion of the total contribution rate is 50% and the employee's portion of the total contribution rate is 50%. Historically, the City has been responsible for funding the cost of amortizing most of the UAL and other miscellaneous costs of the Pension Plans. As discussed above in "RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS – Measure B – Charter Amendment Related to Retirement Plans," effective June 23, 2013, Measure B would require City employees to be responsible for up to 50% of the cost of amortizing the cost of the UAL subject to the cap of 16% of pensionable pay. However, in connection with the litigation challenging Measure B, the City has entered into a further stipulation to delay implementation of this aspect of Measure B to a date no sooner than July 1, 2015. See "RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS – Measure B

Litigation and Administrative Proceedings and Other Litigation Related to Retirement Benefits – Measure B Litigation.”

As discussed above in “RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS – Measure B – Charter Amendment Related to Retirement Plans”, after June 30, 2012, the City Council amended the provisions of both Retirement Plans to eliminate the SRBR. The results for the current valuation reflect the elimination of the SRBR.

#### Federated Plan Pension Contribution

Table B-10 shows a reconciliation of the change in the Federated Plan Tier 1 contribution rate, and the Federated Plan Tier 1 contribution amount for the pension benefit from the rate and amount calculated in the prior actuarial valuation report. As depicted in Table B-10, the pension contribution rate reflects various components.

The employee member pension contribution rate for Federated Plan Tier 1 is a proportion (3/11ths) of the Normal Cost (including administrative expenses) with the remaining 8/11ths of the Normal Cost allocated to the City. The decrease in the Normal Cost and accordingly the member employee contribution rate is primarily the result of economic assumption changes.

In addition to the 8/11ths of the Normal Cost (including administrative expenses), the City is allocated all of the Reciprocity Normal Cost (the cost of funding reciprocity with other California pension plans) plus an amortization payment on the UAL. The increase in the City’s Tier 1 contribution rate is primarily due to economic assumption changes, investment losses and the decreased payroll over which the UAL is spread. Payroll for Tier 1 is expected to decrease over time as members leave the system and new entrants join Tier 2.

**Table B-10**  
**Federated Plan - Tier 1 City Contribution Reconciliation**  
*(Amounts in millions)*

	<b>Member</b>	<b>City</b>			<b>Total</b>
		<b>Normal</b>	<b>UAL</b>	<b>Total</b>	<b>Total City \$</b>
2014 Tier 1 Pension Contribution Rate	5.97%	16.12%	34.73%	50.85%	\$100.7
Investment experience	0.00	0.00	2.97	2.97	5.9
Other experience	0.00	0.01	(0.11)	(0.10)	(0.2)
Payroll change	0.00	0.00	2.19	2.19	1.4
Economic Assumption Change	(0.33)	(0.94)	5.28	4.34	6.8
2015 Tier 1 Pension Contribution Rate	5.64%	15.19%	45.06%	60.25%	\$114.6

*Source: Cheiron 2013 Federated Pension Plan Actuarial Report*

Table B-11 below summarizes the pension contribution rates for both the City and the employee members of the Federated Plan for Federated Pension Plan Tier 2. The decrease in the City's Tier 2 contribution rate can be attributed to the actual demographic characteristics of the new entrants into Tier 2 differing from what was previously assumed for the initial contribution rates. As of the prior valuation date, there were no Tier 2 members. These characteristics may change in the short-term as new employees are hired into Tier 2.

**Table B-11**  
**Federated Plan - Tier 2 City Contribution Reconciliation**  
*(Amounts in millions)*

	<b>Member</b>	<b>City</b>			<b>Total</b>	<b>Total</b>
		<b>Normal</b>	<b>UAL</b>	<b>Total</b>		<b>City \$</b>
2014 Tier 2 Pension Contribution Rate	6.68%	6.68%	0.00%	6.68%	\$1.8	
Investment experience	0.00	0.00	0.00	0.00	-	
Other experience	(1.13)	(1.14)	0.01	(1.13)	(0.3)	
Payroll change	0.00	0.00	0.00	0.00	0.3	
Economic assumption change	(0.02)	(0.02)	0.00	(0.02)	(0.0)	
2015 Tier 2 Pension Contribution Rate	5.53%	5.52%	0.01%	5.53%	\$1.8	

*Source: Cheiron 2013 Federated Pension Plan Actuarial Report*

Table B-12 illustrates the City's contribution dollar amounts for the Federated Plan's pension benefit for 2014-2015 and 2013-2014 assuming the City contribution is made at the beginning of the year. See "RECENT CHANGES TO THE RETIREMENT PLANS AND RETIREE BENEFITS – Measure B Litigation and Administrative Proceedings and Other Litigation Related to Retirement Benefits – Measure B Litigation."

**Table B-12**  
**Federated Plan**  
**City Contribution Amounts For Pension Benefit (Beginning of Year)**  
*(Amounts in thousands)*

	July 1, 2014			July 1, 2013 <sup>(4)</sup>		
	Basic	COLA	Total	Basic	COLA	Total
<b>Tier 1</b>						
City Service Normal Cost	\$ 21,636	\$ 6,940	\$ 28,576	\$ 23,956	\$ 7,543	\$ 31,500
City Reciprocity Normal Cost <sup>(1)</sup>	209	95	304	317	99	416
<b>Total City Normal Cost</b>	<b>\$21,845</b>	<b>\$ 7,035</b>	<b>\$ 28,880</b>	<b>\$24,273</b>	<b>\$ 7,642</b>	<b>\$ 31,915</b>
City Deficiency Cost <sup>(2)</sup>	\$ 40,730	\$43,488	\$ 84,218	\$ 31,095	\$36,329	\$ 67,424
City Golden Handshake Cost <sup>(3)</sup>	1,169	284	1,453	1,071	261	1,332
<b>Total City UAL Cost</b>	<b>\$ 41,899</b>	<b>\$43,772</b>	<b>\$ 85,671</b>	<b>\$32,166</b>	<b>\$36,590</b>	<b>\$ 68,756</b>
<b>City Contribution</b>	<b>\$ 63,744</b>	<b>\$50,807</b>	<b>\$114,551</b>	<b>\$56,440</b>	<b>\$44,232</b>	<b>\$100,671</b>
<b>Tier 2</b>						
City Normal Cost	\$ 1,603	\$ 177	\$ 1,780	\$ 1,651	\$ 148	\$ 1,799
City UAL Cost	2	N/A	2	N/A	N/A	N/A
<b>City Contribution</b>	<b>\$ 1,605</b>	<b>\$ 177</b>	<b>\$ 1,782</b>	<b>\$ 1,651</b>	<b>\$ 148</b>	<b>\$ 1,799</b>

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

(2) The deficiency rate is the amortization of the funding deficiency.

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

(4) July 1, 2013 results reflect the elimination of the SRBR.

Source: Cheiron 2013 Federated Pension Plan Actuarial Report

#### Police and Fire Plan Pension Contribution

Table B-13 shows a reconciliation of the change in the Police and Fire Plan's contribution rate, and the Police and Fire contribution amount for the pension benefit from the rate and amount calculated in the prior actuarial valuation report. As depicted in Table B-13, the pension contribution rate reflects various components.

For Tier 1 members of the Police and Fire Plan, the employee member contribution rate is a proportion (3/11ths) of the Normal Cost (excluding reciprocity) plus the employee member's historic share of assumed administrative expenses. In addition employee members pay a portion of the UAL attributable to certain benefit improvements. The remaining 8/11ths of the Normal Cost is allocated to the City. In addition to the 8/11ths of the Normal Cost (including administrative expenses), the City is allocated all of the Reciprocity Rate (the cost of funding reciprocity with other California pension plans) and the

remaining portion of the UAL rate.

For Tier 2 Police members of the Police and Fire Plan, members and the City share the total contribution rate equally. Tier 2 became effective after the June 30, 2013 valuation date, therefore no Tier 2 members were directly valued, but Tier 2 contribution rates are developed by Actuary for fiscal year 2014-2015.

Cheiron has concluded as of June 30, 2013 that contribution requirements are expected to increase through the fiscal year ending June 30, 2015 as a result of deferred investment losses under the actuarial value of asset smoothing method and because the Police and Fire Board reduced the actuarially assumed net rate of return to 7.125%. The City's contribution was expected to increase to \$132.7 million for 2015, but due to a combination of investment and demographic experience (including a reduction in payroll), the City's contribution only increased to \$128.2 million.

**Table B-13**  
**Police and Fire Plan**  
**Reconciliation of Changes in Tier 1 Pension Contribution Rates (% of Payroll) and Amounts<sup>(1)</sup>**  
*(Amounts in millions)*

	<b>Member Rate</b>	<b>City Normal Cost</b>	<b>City UAL Rate</b>	<b>City Total Rate</b>	<b>Projected Payroll</b>	<b>City Contribution Amount</b>
2014 Pension Contribution	11.7%	31.6%	34.3%	65.9%	\$ 188.0	\$ 119.6
Expected 2015 Pension Contribution	11.7%	31.6%	39.0%	70.6%	\$ 194.5	\$ 132.7
Changes Due to Plan Experience:						
Investment Experience	0.0%	0.0%	(0.5%)	(0.5%)	\$ 194.5	\$ (0.9)
Demographic Experience	0.0	0.0	(0.5)	(0.5)	194.5	(0.9)
Payroll Change	0.0	0.0	1.4	1.4	187.4	(2.1)
Assumption Change	(0.3)	(0.3)	1.9	1.6	182.5	(0.5)
Subtotal	(0.2%)	(0.2%)	2.3%	2.1%	\$ 182.5	\$ (4.5)
2015 Pension Contribution	11.4%	31.4%	41.3%	72.7%	\$ 182.5	\$ 128.2

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

Source: Cheiron 2013 Police and Fire Pension Plan Actuarial Report

Table B-14 below shows the estimated dollar amounts of the City's contribution amounts for 2014-2015 and 2013-2014 assuming contributions are made at the beginning of the fiscal year.

**Table B-14**  
**Police and Fire Plan**  
**City Contribution Amounts (Beginning of Year)**

Source	July 1, 2014			July 1, 2013		
	Pension	COLA	Total	Pension	COLA	Total
<b><u>Police (Tier 1)</u></b>						
Normal Cost	\$ 22,376,449	\$ 9,474,469	\$ 31,850,917	\$ 24,896,327	\$ 10,565,852	\$ 35,462,179
UAL	18,150,669	24,002,231	42,152,900	15,692,238	22,288,130	37,980,368
Total	\$ 40,527,117	\$ 33,476,700	\$ 74,003,817	\$ 40,588,565	\$ 32,853,982	\$ 73,442,547
<b><u>Police (Tier 2)</u></b>						
Normal Cost	\$ 522,290	\$ 83,175	\$ 605,465	N/A	N/A	N/A
UAL	0	0	0	N/A	N/A	N/A
Total	\$ 522,290	\$ 83,175	\$ 605,465	N/A	N/A	N/A
<b><u>Fire</u></b>						
Normal Cost	\$ 16,576,465	\$ 6,900,798	\$ 23,477,263	\$ 15,531,829	\$ 6,388,951	\$ 21,920,780
UAL	13,370,275	17,365,470	30,735,745	10,280,678	13,916,826	24,197,504
Total	\$ 29,946,741	\$ 24,266,268	\$ 54,213,009	\$ 25,812,507	\$ 20,305,777	\$ 46,118,284
<b><u>Total</u></b>						
Normal Cost	\$ 39,475,204	\$ 16,458,442	\$ 55,933,646	\$ 40,428,156	\$ 16,954,803	\$ 57,382,959
UAL	31,520,944	41,367,701	72,888,645	25,972,916	36,204,956	62,177,872
Total	\$ 70,996,148	\$ 57,826,143	\$ 128,822,291	\$ 66,401,072	\$ 53,159,759	\$ 119,560,831

Source: Cheiron 2013 Police and Fire Pension Plan Actuarial Report.

## Investments

The State Constitution and the Municipal Code provide that the Board of each Retirement Plan has exclusive control over the investment of the assets of the respective Pension Plans. As discussed above in "RETIREMENT PLANS IN GENERAL", assets within the 401(h) account in each Pension Plan is designated for the payment of the applicable Healthcare Plan benefits. The Municipal Code also specifies that each Board is to manage the investments for the purpose of providing benefits to its members and beneficiaries, maintaining the actuarial soundness of the Pension Plan, and defraying reasonable expenses of administering the Pension Plan. The Boards for both Retirement Plans have retained investment consultants to advise them.

Table B-15a below illustrates the historic annual returns gross of fees for both Pension Plans for the last ten fiscal years as reported in their respective CAFRs. Table B-15b reflects the historic investment returns for both Pension Plans for three years, five years, ten years and as of June 30, 2014 consultant reports.

**Table B-15a  
Historical Annual Investment Returns (Gross) Since 2003-2004**

Fiscal Year	Federated Plan	Police and Fire Plan
2003-04	16.8%	16.4%
2004-05	8.9	10.9
2005-06	10.2	11.5
2006-07	16.2	19.3
2007-08	(3.1)	(5.1)
2008-09	(16.7)	(18.0)
2009-10	14.0	14.3
2010-11	19.0	18.4
2011-12	(3.0)	(0.1)
2012-13	8.1	9.9
2013-14	14.3 <sup>(1)</sup>	13.9 <sup>(2)</sup>

<sup>(1)</sup> Data for the Federated Plan is provided by the Meketa Investment Group's San José Federated City Employees' Retirement System Quarterly Review dated June 30, 2014 and represents performance which is gross of fees for public market managers and net of fees for private market.

<sup>(2)</sup> Data for the Police and Fire Plan is provided by the NEPC LLC's Investment Performance Analysis Report dated June 30, 2014 and represents performance gross of fees.

*Source: City of San José, Retirement Services Department (Federated CAFR, Police and Fire CAFR) For fiscal years 2003-2004 through 2012-2013.*

**Table B-15b  
Historical Investment Returns At Various Intervals as of June 30, 2014**

Time Frame	Federated Plan <sup>(1)</sup>	Police and Fire Plan <sup>(2)</sup>
Fiscal Year/ 1 Year	14.3%	13.9%
3 Years <sup>(3)</sup>	6.2	7.8
5 Years <sup>(3)</sup>	10.2	11.1
10 Years <sup>(3)</sup>	6.2	6.9

<sup>(1)</sup> Data for the Federated Plan is provided by the Meketa Investment Group's San José Federated City Employees' Retirement System Quarterly Review dated June 30, 2014 and represents performance which is gross of fees for public market managers and net of fees for private market managers. Fiscal Year begins on July 1 and ends June 30.

<sup>(2)</sup> Data for the Police and Fire Plan is provided by the NEPC LLC's Investment Performance Analysis Report dated June 30, 2014 and represents performance gross of fees.

<sup>(3)</sup> These returns are annualized from the prior period for the duration indicated.

*Source: City of San José, Retirement Services Department*

Potential investment returns and the subsequent risk associated with those returns are partially a function of the underlying assets of the respective Pension Plan. Each Board, as part of its fiduciary responsibilities, adopts asset allocation targets commensurate with the applicable Board's diversification goals and risk tolerance. Tables B-16a and B-16b below illustrate each Pension Plan's approved asset allocation targets. It is important to note that the stated asset allocation targets for both Pension Plans represent the ultimate allocation goal of the Pension Plans; however, during periods of allocation transition, asset allocation target objectives may not be achieved. For detailed asset class holdings and for further information on plan assets and allocation refer to the Federated CAFR and Police and Fire CAFR for the year ended June 30, 2013. In addition, the investment policies of both Pension Plans provide more detailed information on allowable asset classes and constraints.

Both Pension Plans utilize hedge fund strategies and have adopted absolute return asset classes as part of their asset allocation diversification strategy. In addition, both Pension Plans may utilize hedge fund strategies within their equity and fixed income asset classes. For the Federated Plan, as of August 21, 2014, an 11% target allocation has been apportioned to absolute return strategies in addition to 10% of hedge fund strategies within the equity (6%) and fixed income (4%) asset classes. For the Police and Fire Plan, a 16% target allocation has been apportioned to the absolute return asset class, which includes a 6% allocation to hedge fund strategies. Additionally, the Police and Fire Plan as of September 4, 2014 had 9.5% of hedge strategies within the fixed income asset class and 2% of hedge fund within the equity asset class.

**Table B-16a  
Federated Plan Target Asset Allocation**

Asset Class	Minimum	Target	Maximum
Equity & Real Estate	30%	37%	44%
Fixed Income	14%	24%	34%
Absolute Return Strategies	6%	11%	16%
Real Assets	15%	23%	30%
Strategic Partner	0%	5%	7%
Cash	0%	0%	5%

*Source: Board adopted asset allocation as of August 21, 2014 per San José Federated City Employees' Retirement System Asset Allocation Review as presented by Meketa Investment Group.*

**Table B-16b  
Police and Fire Plan Target Asset Allocation**

Asset Class	Minimum	Target	Maximum
Equity	25%	39%	50%
Fixed Income	15%	27%	35%
Inflation-linked Asset	12%	17%	25%
Absolute Return Strategies	10%	16%	30%
Cash	0%	1%	5%

*Source: Board adopted asset allocation as of September 4, 2014 per City of San José Police and Fire Plan 2014 Asset Allocation Review as presented by NEPC.*

Annually, the Boards for both Pension Plans receive projections from their respective investment consultants for the expected net rates of return based on the respective approved target asset allocations. The expected returns are derived from the investment consultants' annual review of capital market assumptions, which include expectations for asset class returns, volatility and correlations. The investment consultants for both Pension Plans currently project expected long-term annualized net rates of return in excess of Board adopted investment returns based on the respective target asset allocations for both Pension Plans.

## **HEALTHCARE PLANS**

### **General**

As discussed above in “RETIREMENT PLANS IN GENERAL,” each Retirement Plan includes a Healthcare Plan which provides eligible retirees, their dependents, and survivors with health and dental benefits. For retiree health benefits, both Healthcare Plans pay that portion of the premium that is equivalent to the premium for the lowest-priced medical plan with which the City contracts for medical benefits for City employees. If the retiree elects a medical plan that is not the lowest priced plan, the eligible retiree or survivor pays the difference between the portion paid for the applicable Healthcare Plan and that charged by the medical care provider. In the case of dental benefits, both Healthcare Plans pay the entire premium.

In April 2004, GASB issued Statement No. 43, Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans (“GASB 43”). GASB 43 establishes uniform financial reporting standards for postemployment healthcare and other non-pension benefits (“OPEB”) plans. The approach followed in GASB 43 is generally consistent with the approach adopted for defined benefit pension plans with modifications to reflect differences between pension plans and OPEB plans. GASB 43 became effective for the City’s OPEB Plans for the fiscal year ended June 30, 2007.

Additionally, in June 2004, GASB issued Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions (“GASB 45”), which addresses how state and local governments should account for and report their costs and obligations related to OPEB. GASB 45 generally requires that employers account for and report the annual cost of OPEB and the outstanding obligations and commitments related to OPEB in essentially the same manner as they currently do for pensions. GASB 45’s provisions may be applied prospectively and do not require governments to fund their OPEB plans. An employer may establish its net OPEB liability at zero as of the beginning of the initial year of implementation; however, the unfunded actuarial accrued liability is required to be amortized over future periods. GASB 45 also establishes disclosure requirements for information about the plans in which an employer participates, the funding policy followed, the actuarial valuation process and assumptions, and, for certain employers, the extent to which the plan has been funded over time. The City implemented GASB 45 in fiscal year 2008 and elected to report a zero net OPEB obligation at the beginning of the transition year for both Healthcare Plans.

### **Funding Policy**

The annual contribution for the Healthcare Plans’ benefits are allocated to both the City and the active employee members. For the Federated Healthcare Plan (for Tier 1 and Tier 2 members), the annual contributions for retiree health costs are shared 50/50, and the contributions for retiree dental costs are shared in a ratio of 8/11 for the City and 3/11 for the employee. For the Federated Plan, Tier 2B, the active employee members make no contribution for the Federated Healthcare Plan’s benefits as they are not eligible for these benefits. The City and the bargaining groups in the Federated Plan are in discussions about retiree healthcare costs, however, the City agreed to pay the cost attributable to the unfunded liability of the Federated Healthcare Plan that the City and the employee in Tier 2B would have paid if the employee had been eligible for the retiree healthcare benefit. The retiree healthcare discussions are ongoing.

For the Police and Fire Healthcare Plan, the annual contribution for retiree health costs is shared 50/50 and the annual contributions for retiree dental costs are shared in a ratio of 75/100 for the City and 25/100 for the employee.

Until the City entered into agreements with various bargaining groups as described below, contributions for the health and dental benefits for both the City and the participating employees of both Healthcare Plans were based upon an actuarially determined percentage of employees' base salary sufficient to provide adequate assets to pay benefits when due over the next 10 years for the Police and Fire Plan and the next 15 years for the Federated Plan.

In 2007 and 2008, the City engaged in a process to determine whether to implement a policy to fully pre-fund the annual required contribution as calculated under Statement No. 45 for each of the Healthcare Plans. In connection with this process, the City retained outside counsel to provide advice regarding the legal restrictions on making changes to the health and dental benefits of both retirees and active employees. Based on the outside counsel's opinion that was publicly released, in March 2008, the City Manager issued a memorandum to City employees and retirees, which stated that because the health and dental benefits can be considered a "vested" benefit, the City Administration would not recommend a change in these benefits as specified in the Municipal Code at that time.

As discussed below, the City is in the process of phasing in payment of the annual required contribution for the retiree health and dental benefits provided by both Healthcare Plans as calculated pursuant to GASB Statements 43 and 45. Under GASB 43 and GASB 45, an implicit subsidy for health and dental benefits exists because the medical experience for retirees under age 65 are pooled with the experience for active employees thereby resulting in a lowering of the premium paid for retirees under age 65. The liabilities for the implicit subsidy have been included in the GASB 43 and GASB 45 disclosure calculations reported in the financial statements of both Healthcare Plans and the City and in the phase-in contribution rates for the Federated Healthcare Plan's members. However, the implicit subsidies have not been included in the phase-in contribution rate calculations for the Police and Fire Healthcare Plan.

#### Federated Healthcare Plan Funding Policy

In June 2009, the City and the bargaining units with members in the Federated Plan and unrepresented employees began phasing into fully funding the annual required contribution over a period of five years ending as of June 30, 2013. The terms of the agreements with the bargaining units provide that the initial unfunded retiree healthcare liability as of June 30, 2009 will be fully amortized over a 30-year period as a level percentage of payroll so that it will be paid by June 30, 2039. In December 2010, the Federated Board, acting upon advice from its actuary, adopted a 20-year closed amortization period for each annual change in unfunded actuarial liability on or after June 30, 2010. Effective with the June 30, 2013 valuations, the amortization method was changed from a level percent of payroll to a level dollar amortization reflecting that the plan is closed to new entrants and GASB's requirements for an annual required contribution. This change increases the contribution amounts in the short-term, but produces lower expected contributions later in the amortization period. The increase for the fiscal year ending June 30, 2015 for employees and the City, before application of any caps in the bargaining agreement, is approximately \$9 million (out of a total employee and City contribution amount of approximately \$54 million). Since the caps are set to expire, only contributions after the expiration date are actually affected. The following table shows the date each amortization base was established, the remaining period, the remaining principal, and the amortization payment as of June 30, 2013.

**Table B-17**  
**Federated Healthcare Plan Amortization Schedule – Funding Basis**

<b>Date Established</b>	<b>Remaining Period</b>	<b>Outstanding Balance</b>	<b>Amortization Payment</b>		
			<b>Medical</b>	<b>Dental</b>	<b>Total</b>
6/30/2009	26	\$ 757,224,741	\$ 57,679,649	\$ 5,583,402	\$ 63,263,051
6/30/2010	17	88,142,290	8,086,296	782,755	8,869,051
6/30/2011	18	(28,500,078)	(2,539,561)	(245,830)	(2,785,391)
6/30/2012	19	(204,167,194)	(17,718,393)	(1,715,144)	(19,433,537)
6/30/2013	20	(111,351,291)	(9,434,120)	(913,225)	(10,347,345)
Total		\$ 501,348,468	\$ 36,073,871	\$ 3,491,958	\$ 39,565,829

*Source: Cheiron 2013 Federated Postemployment Healthcare Plan Actuarial Valuation Report.*

The 2009 agreements also provide that the five-year phase-in of the annual required contribution will not have an incremental increase of more than 0.75% of pensionable pay in each fiscal year for the employee contributions and the City cash contribution rate will not have an incremental increase of more than 0.75% of pensionable pay in each fiscal year. Notwithstanding these limitations on incremental increases, the agreements further provide that by the end of the five-year phase-in the City and the employee members “shall be contributing the full Annual Required Contribution in the ratio currently provided” in the relevant sections of the Municipal Code.

#### *Modifications to Federated Healthcare Plan Funding Agreement and Federated Healthcare Plan*

In June 2013, the City and its bargaining units with members in the Federated Plan reached an agreement related to the Federated Healthcare Plan and modified the 2009 agreements.

Following are key elements of the June 2013 agreement:

- Phase-in. Extends the ramp up to the annual required contribution. Employee and City contribution rates will increase by 0.75% in 2013-2014 and 2014-2015, with the contribution rates to the full annual required contribution to begin on December 21, 2014, and all subsequent Fiscal Years.
- New Employees. Provides that new full-time employees will not be eligible for the existing retiree healthcare benefit and will not be required to make the contributions towards the existing plan (Tier 2B).
- UAL. The City will pay the portion of the unfunded liability the new employee in Tier 2B and the City would have contributed towards the UAL for the Federated Healthcare Plan.
- New Rate Program. Effective January 1, 2014, the City instituted a four tier rate program for the healthcare and dental plans for both active non-sworn employees and all retirees. This means that all healthcare and dental plans available to non-sworn employees will have single, single plus spouse/domestic partner, single plus child(ren), and family rates.
- Meet and Confer. Provides for an opportunity to meet and confer at any time upon request of the City or the bargaining units to discuss solutions that could reduce healthcare costs for both the City and employees.

- IRS Limitations. Provides an opportunity to continue exploring retiree healthcare benefit options for current employees based on IRS limitations.
- 115 Employee Contributions. Employee contributions will start being deposited into the 115 trust in time to avoid any potential of reaching the IRS limits on the 401(h) account. In addition, AFSCME withdrew an outstanding unfair labor practice charge related to the City's creation of the 115 trust that was filed on behalf of the MEF and CEO bargaining units.

Furthermore, in recognition that controlling retiree healthcare costs is a mutual issue facing both the City and its employees, the City and its Federated bargaining units are continuing discussions in the form of a Retiree Healthcare Stakeholder Solutions Working Group, with the goal of developing options that lead to long-term solutions to the retiree healthcare issue. The Working Group has discussed options, including but not limited to: benchmarking the benefit to a certain dollar amount per month with an escalator, a transition benefit to increase the number of years necessary to receive the full benefit, and closing the plan. Each of these options is being considered as possible cost-saving solutions.

Preliminary cost estimates for various scenarios have been provided by an actuarial firm hired by both the City and Federated bargaining units to facilitate the retiree healthcare discussions. These estimates were not developed based on a full actuarial valuation and, ultimately, the Board's actuary would determine the costs. The City and Federated bargaining units have jointly requested the Board's actuary to provide cost-estimates on the various scenarios. The City and Federated bargaining units have reached agreement, subject to the ratification of the members and approval by the City Council, to extend the expiration of the phase-in to paying the full annual required contribution, currently scheduled for December 2014 through June 20, 2015, to allow the discussion to continue on reducing retiree healthcare costs. It is anticipated that ratification votes of the bargaining units' membership and the City Council consideration of the extension agreement will occur in fall 2014. The City cannot predict whether the extension agreement will be approved or the costs for implementing any of the scenarios under discussion.

As referenced in APPENDIX A – “THE NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT – OTHER MATTERS – Labor Relations,” the changes to retiree healthcare benefits implemented as of January 1, 2013 are subject to motions to compel arbitration by the public safety bargaining units the POA and IAFF, Local 230. Each of these bargaining units brought separate Superior Court actions to compel arbitration and seeking Writ relief to prevent the City from continuing to provide the new lowest cost health plans for police and fire retirees. Those actions have not been actively pursued by the bargaining units because the health plan changes were upheld by the trial judge in the Measure B litigation. The City understands that they will not agree to dismiss these cases, and instead want to hold them in abeyance pending an appellate decision on the retiree health care issue in the Measure B litigation. The City is unable to predict whether the public safety units will prevail in these motions to compel or the results of any arbitration proceeding.

#### Police and Fire Healthcare Plan Funding Policy

In February 2009, the City reached an agreement with the POA to fully fund the annual required contribution with respect to the sworn police department employees over a period of five years ending on June 30, 2013, subject to the limitations described below. The agreement provides that the initial unfunded retiree healthcare liability, or UAL, will be fully amortized over a 30-year closed (decreasing) period starting July 1, 2009 so that it will be paid by June 30, 2039.

The City and the bargaining unit representing Fire Department members, IAFF, Local 230, entered into a labor agreement in March 2011. The agreement provides for a five-year phase-in of the annual required contribution, ending on June 30, 2015, subject to the limitations described below. The agreement also

provides that the initial UAL will be fully amortized over a 30-year closed (decreasing) period so that it will be paid by June 30, 2041. From time to time, the Police and Fire Plan's actuary will update the contributions required to fully fund the liabilities for retiree healthcare.

The following table shows, for each amortization base, the remaining period, the remaining principal and the amortization payment due on July 1, 2013.

The agreements with the POA and IAFF, Local 230 both provide that the five-year phase-in of the annual required contribution for Police and Fire Department employees in the Police and Fire Healthcare Plan will not have an incremental increase of more than 1.25% of pensionable pay in each fiscal year for the employee contributions and City cash contribution will not have an incremental increase of more than 1.35% of pensionable pay in each fiscal year. If at any time the employee's cash contribution rate exceeds 10% of pensionable pay or the City cash contribution rate exceeds 11% of pensionable pay, the City and the applicable bargaining unit will meet and confer on how to address any retiree healthcare contributions above 10% of pensionable pay for employees or 11% of pensionable pay for the City. Such discussions will include alternatives to reduce retiree healthcare costs. These limitations will preclude full funding of the annual required contribution within the applicable five-year period.

Since the police members' contribution rate has exceeded the cap instituted by the agreement, the POA and the City will be engaging in the meet and confer process to discuss reducing retiree healthcare costs. It is expected that these will begin in fall of 2014. Although the contribution rate exceeds 10%, the police members' contributions are calculated at the 10% capped rate. The City cannot predict the outcome of this meet and confer process or an arbitration of this matter in the event the POA and the City do not reach agreement.

**Table B-18**  
**Police and Fire Healthcare Plan Amortization Schedule - Funding Basis**

<b>Amortization Base</b>	<b>Remaining Period</b>	<b>Outstanding Balance</b>	<b>Amortization Payment</b>	<b>Amortization Rate</b>
Police Department – Medical	25	\$ 247,361,015	\$ 16,081,766	14.36%
Police Department – Dental	25	23,180,212	1,507,023	1.35
Fire Department – Medical	27	151,573,225	9,396,167	12.31
Fire Department – Dental	27	<u>14,849,853</u>	<u>920,556</u>	1.21
Totals		\$ 436,964,305	\$ 27,905,512	

*Source: Cheiron 2013 Police and Fire Postemployment Healthcare Plan Actuarial Valuation Report.*

## Summary of Healthcare Plans' UAL and Funded Ratios

As shown in Table B-19, in 2006, the Retirement Plans' actuaries initiated actuarial studies of the health and dental assets and liabilities complying with GASB 43 and GASB 45 for both Healthcare Plans. Implementation of GASB 43 and GASB 45 as of June 30, 2006 resulted in significantly lower discount rates for both Healthcare Plans and resulted in a significantly higher measure of liabilities as compared to the prior valuation as of June 30, 2005 that had not been prepared, nor required to be prepared, in accordance with GASB 43 and GASB 45.

**Table B-19**  
**Historical Healthcare Plan UAL and Funded Ratio - GASB Basis**  
*(Amounts in thousands)*

<b>Fiscal Year</b>	<b>Federated Healthcare Plan</b>		<b>Police and Fire Healthcare Plan</b>		<b>Total UAL</b>
	<b>UAL</b>	<b>Funded Ratio</b>	<b>UAL</b>	<b>Funded Ratio</b>	
6/30/2005	\$ 235,700	24.6%	\$ 136,600	20.9%	\$ 372,300
6/30/2006	621,700	11.6	812,837	5.0	1,434,537
6/30/2007	520,148	16.0	620,834	7.0	1,140,982
6/30/2009	710,884	11.0	705,986	7.0	1,416,870
6/30/2010	818,360	12.0	887,722	6.0	1,706,082
6/30/2011	1,009,905	12.0	943,086	6.0	1,952,991
6/30/2012	958,822	13.0	930,936	7.0	1,889,758
6/30/2013	713,177	18.0	625,490	11.0	1,338,667

Shaded data represents valuation data prior to the implementation of GASB 43 and GASB 45.

Source: *Data from 2013 Cheiron Federated Postemployment Healthcare Plan Actuarial Valuation Report; 2013 Cheiron Police and Fire Postemployment Healthcare Plan Actuarial Valuation Report.*

As shown in Tables B-20a and B-20b, the City's contribution amount has increased for both Healthcare Plans in comparison to fiscal year ending 2009 as the actuarial liability has grown and funding policies were adopted to phase-in to the full annual required contribution.

The increases in the actuarial liability have resulted in increased annual OPEB funding costs for both the employer and employee. Until the Healthcare Plans receive payment of the full Annual OPEB Cost ("AOC") on a GASB basis, the Net OPEB Obligation will continue to increase as evidenced below. The Net OPEB Obligation is the accumulated difference between the AOC and the amount actually paid.

**Table B-20a**  
**Federated Healthcare Plan Schedule of City Contributions**  
*(Amounts in thousands)*

Fiscal Year Ending	Annual OPEB Cost (AOC)	City Contributions Plus Implicit Subsidy	Percentage of AOC Contributed	Net OPEB Obligation
2009	\$ 33,725	\$ 15,918	47	\$ 44,760
2010	39,414	21,585	55	62,589
2011	44,834	21,072	47	86,351
2012	68,028	25,833	38	128,456
2013	57,202	20,923	37	164,825
2014	49,664	TBD	TBD	TBD

TBD refers to the Net OPEB Obligation being calculated as part of the City's CAFR production for 2013-2014 which will occur in the fall of 2014.

*Source: Data from 2013 Cheiron Federated Postemployment Healthcare Plan Actuarial Valuation Report*

**Table B-20b**  
**Police and Fire Healthcare Plan Schedule of City Contributions**  
*(Amounts in thousands)*

Fiscal Year Ending	Annual OPEB Cost (AOC)	City Contributions Plus Implicit Subsidy	Percentage of AOC Contributed	Net OPEB Obligation
2008	\$ 48,191	\$ 13,624	28%	\$ 34,138
2009	50,651	13,063	26	71,314
2010	51,734	15,546	30	106,990
2011	64,105	17,001	27	154,566
2012	65,747	21,205	32	198,108
2013	56,913	15,807	28	239,213
2014	35,791	TBD	TBD	TBD

TBD refers to the Net OPEB Obligation being calculated as part of the City's CAFR production for 2013-2014 which will occur in the fall of 2014

*Source: Data from 2013 Cheiron Police and Fire Postemployment Healthcare Plan Actuarial Valuation Report*

## **Healthcare Plans' Actuarial Valuations**

Actuarial assumptions used for the valuations for the health and dental benefits provided by the Federated Healthcare Plan and the Police and Fire Healthcare Plan are generally the same as are used for the valuations of the Pension Plans, but also include assumptions with respect to future healthcare utilization and inflation. Below are the significant actuarial valuation methods and assumptions used for the June 30, 2013 valuations of the Federated Healthcare Plan and Police and Fire Healthcare Plan. Both Healthcare Plans also employ the “floor” methodology described above in “– PENSION PLANS – Pension Plans’ Actuarial Valuations.”

**Table B-21a**  
**Federated Plan – Healthcare Actuarial Assumptions**

Valuation Date	June 30, 2013
Actuarial funding method	Individual Entry Age
Amortization method	Level Dollar Closed
Equivalent single amortization period	26.4 Years
Asset valuation method	Market Value
Actuarial Assumptions:	
Payroll Growth Rate	2% for first 5 years, 2.85% thereafter
Discount Rate	5.30%
Ultimate Rate of Medical Inflation	4.25%

*Source: Data from 2013 Cheiron Federated Postemployment Healthcare Plan Actuarial Valuation Report*

**Table B-21b**  
**Police and Fire Plan – Healthcare Actuarial Assumptions**

Valuation Date	June 30, 2013
Actuarial funding method	Individual Entry Age
Amortization method	Level percent of pay open
Equivalent single amortization period	30 Years
Asset valuation method	Five-year smoothed value
Actuarial Assumptions:	
Payroll Growth Rate	3.50%
Discount Rate	6.00%
Ultimate Rate of Medical Inflation	4.25%

*Source: Data from 2013 Cheiron Police and Fire Postemployment Healthcare Plan Actuarial Valuation Report*

### Federated 2013 Healthcare Plan Valuation

Cheiron performed an actuarial valuation, as of June 30, 2013, of the Federated Healthcare Plan. Utilizing the City's current phase-in funding policy, the actuarial liability as of June 30, 2013, on a "funding basis" as opposed to a GASB basis, was \$659.0 million with \$157.7 million in assets, which resulted in a UAL of \$501.3 million, a reduction of approximately \$103.3 million from the prior valuation. The decrease in the UAL from the previous valuation is primarily due to change in expected current and future healthcare claims and expense costs and the adoption of the four-tier rate structure effective January 1, 2014 as discussed above in "- Funding Policy – Federated Healthcare Plan Funding Policy – Modifications to Federated Healthcare Plan Funding Agreement and Federated Healthcare Plan." See APPENDIX A – "NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT – OTHER MATTERS – Labor Relations – Modification to Pension and Retiree Healthcare Benefits and other Employment Benefits." The reduction in UAL from the prior valuation resulted in the funding ratio for this valuation increasing to 24% from 19%.

**Table B-22a**  
**Federated Healthcare Plan Funding Valuation Basis**  
*(Amounts in thousands)*

<b>Valuation Date</b>	<b>6/30/2013</b>	<b>6/30/2012</b>
Discount Rate	7.25%	7.50%
Actuarial Liability	\$659,043	\$742,466
Assets	157,695	137,798
UAL	501,348	604,668
Funding Ratio	24%	19%
<b>Fiscal Year Ending</b>	<b>6/30/2015</b>	<b>6/30/2014</b>
<u>Through December 21, 2014</u>		
Member Contribution Rate	8.76%	8.01%
City Contribution Rate – Member with coverage	9.41%	8.66%
City Contribution Rate – Member without coverage	12.66%	10.59%
<u>After December 21, 2014<sup>(2)</sup></u>		
Member Contribution Rate	11.55%	N/A
City Contribution Rate – Member with coverage	12.56%	N/A
City Contribution Rate – Member without coverage	18.60%	N/A
City Contribution Amount (BOY) <sup>(1)</sup>	\$25,438	\$24,484

<sup>(1)</sup> This is the amount of the City's contribution if paid at the beginning of the fiscal year "BOY".

<sup>(2)</sup> The City and Federated bargaining units have reached agreement, subject to the ratification of the members and approval by the City Council, to extend the expiration of the phase-in to paying the full annual required contribution, currently scheduled for December 2014 through June 20, 2015.

*Source: Data from 2013 Cheiron Federated Postemployment Healthcare Plan Actuarial Valuation Report*

The City has negotiated agreements with its labor unions that require both employee and City contributions to fund the Federated Plan. The agreements call for contributing the full annual required contribution under GASB 43 and 45 beginning on December 21, 2014. As discussed above, this implementation date is anticipated to be extended through June 20, 2015. During the phase-in period, contribution rates are limited to an incremental increase to 0.75% of pay for the Federated Plan members

and City for each fiscal year. The contribution rates for fiscal year 2013-2014 as shown in Table B-22b reflect the caps. For the fiscal year ending June 30, 2015, the limited contribution rates will apply for the first part of the fiscal year. The full annual required contribution rates that were expected to apply for the second part of the fiscal year will not be in effect if the agreement to extend the phase-in period through June 20, 2015 is approved as described above.

**Table B-22b**  
**Federated Healthcare Plan Contribution Rates – Funding Basis (% of Payroll)**

	2015			2014
	Medical	Dental	Total	Total
Normal Cost	4.92%	0.59%	5.51%	6.08%
Amortization Payment	16.78	1.62	18.40	16.59
<b>Total</b>	<b>21.70%</b>	<b>2.21%</b>	<b>23.91%</b>	<b>22.67%</b>
<b>Contribution Amount Without Caps (applies after December 21, 2014)</b>				
Employees	10.85%	0.60%	11.45%	N/A
City (Employees with coverage)	10.85	1.61	12.46	N/A
City (Employees without coverage)	16.78	1.62	18.40	N/A
<b>Contribution Amount With Caps (applies through December 21, 2014<sup>(1)</sup>)</b>				
Employees	8.37%	0.39%	8.76%	8.01%
City (Employees with coverage)	8.37	1.04	9.41	8.66
City (Employees without coverage)	11.82	0.84	12.66	10.59

<sup>(1)</sup> The City and Federated bargaining units have reached agreement, subject to the ratification of the members and approval by the City Council, to extend the expiration of the phase-in to paying the full healthcare contribution, currently scheduled for December 2014 through June 20, 2015.

*Source: Data from 2013 Cheiron Federated Postemployment Healthcare Plan Actuarial Valuation Report*

On a GASB basis, Cheiron has calculated that the actuarial accrued liability of the Federated Healthcare Plan as of June 30, 2013 is \$870.9 million, which is a decrease from the \$1.1 billion the previous year. With \$157.7 million in assets, the resulting GASB UAL for the valuation period is \$713.2 million with a plan funded ratio of 18%. The annual required contribution calculated in accordance with GASB, and based on a 5.3% discount rate, is \$52.4 million. Since 2007, the actuarial liability has grown, reflecting the accumulation of total projected benefits attributed to an employee, rising health care costs, reductions in the discount rate, and changes to other assumptions.

For OPEB plans where the contribution equals the annual required contribution under GASB 43 based on a discount rate equal to the expected return on plan assets, the discount rate for GASB purposes is also the actuarial assumed investment rate. When the contribution equals the pay-as-you-go (annual benefit payments), the discount rate for GASB purposes is equal to the expected return on the City's unrestricted assets. However, where the contribution amount is between these two amounts, GASB requires the use of a blended discount rate that is prorated between the actuarial assumed investment rate and the expected return on City assets. Since the City currently pays less than the full annual required contribution under GASB but more than the annual benefit payments, its valuations are subject to the blended discount rate methodology. The discount rate on a GASB basis increased from 4.8% to 5.3% in this valuation period. However, plan experience and changes, due to the changes to the healthcare plans offered to active

employees described above, resulted in the net decrease in the UAL of approximately \$245.6 million from the prior valuation.

**Table B-22c**  
**Federated Plan Healthcare Plan - GASB Basis**  
*(UAL in millions)*

	<b>2007</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>
Funded Ratio	15.7%	10.7%	11.7%	11.8%	12.6%	18.1%
UAL	\$ 520.1	\$ 710.9	\$ 818.4	\$ 1,009.9	\$ 958.8	\$ 713.2
Discount Rate	6.6%	6.7%	6.7%	6.1%	4.8%	5.3%

*Source: Data from 2013 Cheiron Federated Postemployment Healthcare Plan Actuarial Valuation Report*

In its valuation report, Cheiron projected that the actuarial liability on a GASB basis will decline from about \$0.9 billion to approximately \$0.7 billion over the next two years assuming the full annual required contribution is contributed beginning December 21, 2014 (which as described above is not anticipated to occur). Then, the actuarial liability is projected to increase, reaching approximately \$1.1 billion in 20 years with assets increasing from \$158 million to approximately \$800 million over the same period. The City's contribution is expected to increase from 8.66% in fiscal year 2014 to approximately 13.8% of pay in fiscal year 2018, then expected to decrease to approximately 8.4% of pay in fiscal year 2033 before increasing to 13.3% in fiscal year 2034. When the primary amortization base for the UAL is fully paid in fiscal year 2041, there is a significant projected decrease in contribution rates,

### Police and Fire 2013 Healthcare Plan Valuations

Cheiron performed an actuarial valuation, as of June 30, 2013, of the Police and Fire Healthcare Plan, which was presented to the Police and Fire Plan Board at its February 2014 meeting.

Utilizing the City's current funding policy, the actuarial liability on a "funding basis" as of June 30, 2013 was approximately \$512.0 million with approximately \$75.0 million in assets resulting in a UAL of approximately \$437.0 million, a reduction of approximately \$93 million from the prior valuation. The decrease in the UAL from the previous valuation is primarily due to change in expected current healthcare claims and expense costs, changes to assumed rates of increase in future healthcare claims and expenses, and the adoption of the four-tier rate structure effective January 1, 2014 for retirees in the Police and Fire Healthcare Plan. The reduction in UAL from the prior valuation resulted in the funding ratio increasing to 14.7% from 11.1%.

**Table B-23a**  
**Police and Fire Healthcare Plan Funding Valuation Basis<sup>(1)</sup>**  
*(Amounts in thousands)*

	<b>6/30/2013</b>	<b>6/30/2012</b>
Discount Rate	7.125%	7.25%
Actuarial Liability (AL)	\$ 511,999	\$ 596,223
Actuarial Value of Assets (AVA)	75,035	66,385
Unfunded Actuarial Liability (UAL)	436,964	529,839
AVA Funding Ratio	14.7%	11.1%
Market Value of Assets (MVA)	\$ 74,716	\$ 62,978
Unfunded Liability (MVA Basis)	437,283	533,245
MVA Funded Ratio	14.6%	10.6%
	<b>6/30/2015</b>	<b>6/30/2014</b>
Member Contribution Rate	9.83%	8.69%
City Contribution Rate	10.69%	9.42%
City Contribution Amount (BOY) <sup>(2)</sup>	\$ 19,441	\$ 17,073

<sup>(1)</sup> Excludes implicit subsidy

<sup>(2)</sup> This is the amount of the City's contribution if paid at the beginning of the fiscal year "BOY".

*Source: Data from 2013 Cheiron Police and Fire Postemployment Healthcare Plan Actuarial Valuation Report*

The table below illustrates contribution rates for the Police and Fire Healthcare Plan without the caps on the contribution rates of the City and the members.

**Table B-23b**  
**Police and Fire Healthcare Plan Preliminary Contribution Amounts - Funding Basis**  
**(% of Payroll)**

	2015		2014
	Medical	Dental	Total
<b>Police Department</b>			
Normal Cost	6.17%	0.53%	6.70%
Amortization Payment	14.36	1.35	15.71
<b>Total</b>	<b>20.53%</b>	<b>1.88%</b>	<b>22.41%</b>
Contribution Allocation without Phase-In			
Member	10.27%	0.47%	10.74%
City	10.26	1.41	11.67
<b>Total</b>	<b>20.53%</b>	<b>1.88%</b>	<b>22.41%</b>
<b>Fire Department</b>			
Normal Cost	5.97%	0.51%	6.48%
Amortization Payment	12.31	1.21	13.52
<b>Total</b>	<b>18.28%</b>	<b>1.72%</b>	<b>20.00%</b>
Contribution Allocation without Phase-In			
Member	9.14%	0.43%	9.57%
City	9.14	1.29	10.43
<b>Total</b>	<b>18.28%</b>	<b>1.72%</b>	<b>20.00%</b>

*Source: Data from 2013 Cheiron Police and Fire Postemployment Healthcare Plan Actuarial Valuation Report*

Tables B-23c and B-23d below illustrate the contribution rates for the Police and Fire Healthcare Plan implementing the phase-in and annual increase limits for the City, the police members and the fire members. As discussed above, the Healthcare Plan funding policy includes a provision that caps the City or member rates at 11% and 10% of payroll respectively, as shown below, after applying the phase-in and the annual increase limits, the Fire contribution rates are below the caps. However, the Police contribution rates exceed the caps.

**Table B-23c**  
**Police Contribution Rates for Police and Fire Healthcare Plan - Funding Basis**  
**(% of Payroll) Reflecting Annual Caps<sup>(1)</sup>**

	<b>Medical</b>	<b>Dental</b>	<b>Total</b>
Calculated FYE 2015 Contribution Rate			
Member	10.27%	0.47%	10.74%
City	10.26	1.41	11.67
Total	20.53%	1.88%	22.41%
FYE 2014 Contribution Rates			
Member	9.11%	0.40%	9.51%
City	9.12	1.19	10.31
Total	18.23%	1.59%	19.82%
Capped FYE 2015 Contribution Rates			
Member	10.27%	0.47%	10.74%
City	10.26	1.40	11.66
Total	20.53%	1.87%	22.40%

<sup>(1)</sup> The Annual Caps limit the annual increase in the City and member contribution rates to 1.35% and 1.25% of payroll respectively.

*Source: Data from 2013 Cheiron Police and Fire Postemployment Healthcare Plan Actuarial Valuation Report*

**Table B-23d**  
**Fire Contribution Rates for Police and Fire Healthcare Plan - Funding Basis**  
**(% of Payroll) Reflecting Phase-In and Annual Caps<sup>(1)</sup>**

	Medical	Dental	Total
Phased-In FYE 2015 Contribution Rates			
Member	8.10%	0.39%	8.49%
City	8.09	1.18	9.27
Total	16.19%	1.57%	17.76%
FYE 2014 Contribution Rates			
Member	7.05%	0.30%	7.36%
City	7.05	0.91	7.97
Total	14.11%	1.21%	15.32%
Capped FYE 2015 Contribution Rates			
Member	8.10%	0.39%	8.49%
City	8.09	1.18	9.27
Total	16.19%	1.57%	17.76%

<sup>(1)</sup> The Annual Caps limit the annual increase in the City and member contribution rates to 1.35% and 1.25% of payroll respectively.

*Source: Data from 2013 Cheiron Police and Fire Postemployment Healthcare Plan Actuarial Valuation Report*

On a GASB basis, Cheiron has calculated that the actuarial accrued liability as of June 30, 2013 was approximately \$700.5 million, a decrease of approximately \$296.8 million from the previous valuation. With approximately \$75.0 million in assets, the resulting GASB UAL was approximately \$625.5 million, with a funded ratio of 10.7%. The annual required contribution calculated in accordance with GASB, and based on a 6.0% actuarially assumed net rate of return, was \$32.8 million.

As discussed above, GASB 43 and GASB 45 require a blended discount rate be utilized when the contributions to an OPEB plan are more than annual benefit payments but less than the full annual required contribution. The discount rate on a GASB basis increased from 4.4% to 6.0% in this valuation period, which resulted in a decrease in the UAL of approximately \$12.0 million from the prior valuation.

**Table B-23e**  
**Police and Fire Plan Postemployment Healthcare – GASB Basis**  
*(UAL in millions)*

	2007	2009	2011	2012	2013
Funded Ratio	6.8%	7.3%	6.0%	6.7%	10.7%
UAL	\$620.8	\$706.0	\$943.1	\$930.9	\$625.5
Discount Rate	6.4%	6.7%	5.7%	4.4%	6.0%

*Source: 2013 Cheiron Police and Fire Postemployment Healthcare Plan Actuarial Valuation Report.*

In its valuation report, Cheiron projected that the actuarial liability on a GASB basis will increase from approximately \$0.7 billion to approximately \$1.4 billion over the next 20 years with assets increasing

from \$75 million to approximately \$1.0 billion over the same period. However, these projections disregarded the cap currently in place on contributions of 11% for the City and 10% for members, showing contributions of approximately 11.4% of pay for the City and 10.5% of pay for members for most of the projection period.

## **Investments**

Most of the assets reserved for both Healthcare Plans are held in the Pension Plans of both Retirement Plans. As such the Boards of both Healthcare Plans currently utilize the investment policies and asset allocations of the respective Pension Plans for the 401(h) portion of the Healthcare Plans.

In addition, the City has established Internal Revenue Code Section 115 Trusts as a supplement to the 401(h) accounts. City contributions and employee contributions have been deposited into the Federated 115 Trust as of July 1, 2011 and December 22, 2013, respectively. City contributions have been deposited into the Police and Fire 115 Trusts as of July 1, 2012. Employee contributions continue to be deposited in the 401(h) account of the Police and Fire Plan.

Due to the smaller asset size of the 115 Trusts, the Investment Managers of the respective Boards advised the use of different asset allocations than the allocations applicable to the Pension Plans' investments including the 401(h) accounts. The Federated Board at its March 2013 meeting adopted a separate asset allocation and investment policy for the Federated 115 Trust, which formalized the existing investment policy. The Police and Fire Board at its June 2013 meeting adopted an initial separate asset allocation and investment policy for the Police and Fire 115 Trusts which was revised in August 2014. Tables B-24a and B-24b below illustrate the current asset allocation of both the Federated 115 Trust and the Police and Fire 115 Trusts.

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**Table B-24a**  
**Federated Healthcare Plan 115 Trust Target Asset Allocation**

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<b>Asset Class</b>	<b>Minimum</b>	<b>Target</b>	<b>Maximum</b>
Global Equity	53%	59%	65%
Fixed Income	23%	28%	33%
Real Assets	8%	13%	18%

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*Source: Federated City Employees' Retiree Healthcare 115 Trust Investment Policy Statement*

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**Table B-24b**  
**Police and Fire Healthcare Plan 115 Trust Target Asset Allocation**

<b>Asset Class</b>	<b>Minimum</b>	<b>Target</b>	<b>Maximum</b>
Equity	25%	43%	50%
Fixed Income	5%	15%	25%
Inflation-Linked	12%	22%	25%
Absolute Return/ Global Asset Allocation	0%	20%	25%
Cash	0%	0%	5%

*Source: Board adopted asset allocation as of August 7, 2014 per City of San José Police and Fire Department Retirement Plan Health Care Trust Asset Allocation Recommendation as presented by NEPC.*

## **ESTABLISHMENT OF 115 TRUSTS FOR HEALTHCARE PLANS; TAX LIMITATIONS**

The Internal Revenue Code Section 401(h) permits a pension plan to provide retiree healthcare benefits under certain conditions, including: (1) a separate account (the “401(h) account”) is maintained for the healthcare benefits and (2) the healthcare benefits are subordinate to the pension benefits. Under IRS regulations, subordination means that the contributions for healthcare benefits do not exceed 25% of the aggregate contributions excluding contributions to fund past service credits. Exceeding the subordination limit puts a pension plan at risk of unfavorable tax treatment by the IRS, which in turn, could subject the pension plan’s income to the payment of income tax and reduce the assets available for the payment of benefits.

To avoid exceeding the subordination limit for the 401(h) accounts held in both Pension Plans, the City Council enacted an ordinance to establish a separate trust under Internal Revenue Code Section 115 for the Federated Plan effective June 2011 (the “Federated 115 Trust”). For the Police and Fire Plan, the City Council enacted an ordinance, effective in June 2012 to establish separate trusts under Internal Revenue Code Section 115 for the police members (the “Police 115 Trust”) and the fire members (the “Fire 115 Trust” and together with the Police 115 Trust, the “Police and Fire 115 Trusts”). The Board for each Retirement Plan also serves as the board of trustees for the corresponding 115 Trust. On June 11, 2013, the City Council adopted amendments to the City’s Municipal Code provisions applicable to the Police and Fire 115 Trusts for the Police 115 Trust and the Fire 115 Trust to allow two wholly separate subtrusts of a single trust.

Both the Federated Board and the Police and Fire Board have sought and received private letter rulings from the IRS on the tax exempt status of the respective 115 Trusts. Additionally, on August 6, 2013, in response to the City’s request, the IRS issued a private letter ruling indicating that employee contributions into the Federated 115 Trust and the Police and Fire 115 Trusts may be made as employer contributions and therefore are excludable from the employee’s gross income and are not subject to income or other employment taxes.

Both Boards have been advised that the contributions made to the 115 Trust must be treated as non-refundable in order to maintain the 115 Trust’s tax exempt status. Both Retirement Plans permit return of employee pension and retiree healthcare contributions held in the 401(h) accounts, although the retiree healthcare contributions have been refunded from each Pension’s Plan’s pension fund and not the 401(h) account within each pension fund.

## APPENDIX C

### SUMMARY OF CERTAIN PROVISIONS OF THE MASTER TRUST AGREEMENT

#### DEFINITIONS

*The following are definitions of certain terms used in this Official Statement, including in the summaries of the Master Trust Agreement and the Tenth Supplemental Trust Agreement. This summary does not purport to be complete and is qualified in its entirety by reference to the full terms of the Master Trust Agreement and the Tenth Supplemental Trust Agreement.*

##### Accreted Value

“Accreted Value” means, with respect to any Capital Appreciation Bonds, as of any date of calculation, the sum of the amount set forth in a Supplemental Agreement as the amount representing the initial principal amount of such Capital Appreciation Bond plus the interest accumulated, compounded and unpaid thereon as of the most recent compounding date (plus, if such calculation is between compounding dates, the amount of interest accumulated at the original offering yield of the Capital Appreciation Bond from the most recent compounding date) as determined in accordance with the provisions of the Supplemental Agreement authorizing the issuance of such Capital Appreciation Bonds.

##### Act

“Act” means Section 9110 of the Aviation Safety and Capacity Expansion Act of 1990 (codified at 49 U.S.C. App. 1513(e)), as amended or any successor or similar federal statute.

##### Additional Bonds

“Additional Bonds” means Bonds issued pursuant to the Master Trust Agreement with a parity claim with Bonds previously issued thereunder as to General Airport Revenues.

##### Allocated General Airport Revenues

“Allocated General Airport Revenues” has the meaning set forth under “SECURITY FOR THE BONDS — Flow of Funds — Surplus Revenue Fund — Rate Stabilization Fund” in the forepart of this Official Statement.

##### Annual Debt Service

See definition of “Debt Service.”

##### Available PFC Revenues

“Available PFC Revenues” means PFC Revenues made available to pay Debt Service in any period as described under “SECURITY FOR THE BONDS — Other Available Funds, CFC Revenues and Available PFC Revenues” in the forepart of this Official Statement.

##### Balloon Bond

“Balloon Bond” means any Bond (including commercial paper notes and bond anticipation notes), 25% or more of the principal of which matures or is payable on the same date and

which is not required by the instrument pursuant to which such Bond was incurred, to be amortized by payment or redemption prior to such date.

Beneficial Owner

“Beneficial Owner” means the Person who has an ownership interest in any Bond which is held in custodial deposit by DTC and registered in the name of Cede & Co., the nominee of DTC, or by any other institution designated to act as depository or nominee pursuant to the Master Trust Agreement.

Bond Counsel

“Bond Counsel” means a counsel of recognized national standing in the field of law relating to municipal bonds and the exemption from federal income taxation of interest thereon, appointed and paid by the City.

Bondholder; Bondowner, Owner

“Bondholder,” “Bondowner” or “Owner” means any person who shall be the registered owner of any Outstanding Bond.

Bonds

“Bonds” means all of the bonds authorized by, and at any time Outstanding pursuant to, the Master Trust Agreement or any Supplemental Agreement, including any Additional Bonds authorized by, and at any time Outstanding pursuant to, the Master Trust Agreement and any Supplemental Agreement, but not including Subordinate Obligations.

Book-Entry Bonds

“Book-Entry Bonds” means Bonds issued under the book-entry system pursuant to the Master Trust Agreement.

Business Day

“Business Day” means any day other than a Saturday, Sunday or day upon which banks in San Francisco, California, or New York, New York are authorized or required to be closed.

Capital Appreciation Bonds

“Capital Appreciation Bonds” means Bonds all or a portion of the interest on which is compounded and accumulated at the rates and on the dates set forth in a Supplemental Agreement and is payable only upon redemption or on the maturity date of such Bonds. Bonds which are issued as Capital Appreciation Bonds, but later convert to Bonds on which interest is paid periodically shall be Capital Appreciation Bonds until the conversion date and from and after such conversion date shall no longer be Capital Appreciation Bonds, but shall be treated as having a principal amount equal to their Accreted Value on the conversion date.

CFC Law

“CFC Law” means Section 1936.5 of the California Civil Code, as amended, and Ordinance No. 26063 adopted by the Council on March 7, 2000 and codified as Part 6 of Chapter 25.08 of the San José Municipal Code, as amended, or any successor legislation.

## CFC Revenues

“CFC Revenues” means all amounts received by the City from the payment of any customer facilities fees or charges and customer transportation fees or charges by customers of automobile rental companies, including but not limited to fees or charges pursuant to certain sections of the CFC Law. CFC Revenues also include all interest, profits or other income derived from the deposit or investment of any CFC Revenues.

## Code

“Code” means the Internal Revenue Code of 1986, as amended, and any successor to the Code.

## Continuing Disclosure Agreement

“Continuing Disclosure Agreement” means, with regard to any Bonds, the agreement signed by the City and acknowledged by the Trustee on the date such Bonds are issued in form and substance satisfactory to the purchaser of such Bonds, pursuant to the requirements of Securities and Exchange Commission Rule 15c2-12.

## Current Interest Bonds

“Current Interest Bonds” means Bonds interest on which is payable at least annually pursuant to the Supplemental Agreement under which they are issued.

## Debt Service; Annual Debt Service; Maximum Annual Debt Service

“Debt Service” means for any specified period the sum of (1) the interest falling due on any then Outstanding Current Interest Bonds, assuming that all Principal Installments are paid when due, but excluding any interest funded from the proceeds of any series of Bonds and applied toward the payment of interest on such Bonds, and (2) the Principal Installments payable on any then Outstanding Bonds. For the purpose of determining Debt Service on any Bonds, the following shall apply:

To determine the interest payable on Variable Rate Bonds, the interest rate used shall be (except to the extent that either subsection (2) relating to Hedged Bonds or subsection (4) relating to Balloon Bonds applies), at the option of the City either (a) for purposes of the calculations required by the rate maintenance covenant (see “SECURITY FOR THE BONDS — Rate Maintenance Covenant” in the forepart of this Official Statement), the actual interest rates which were in effect for the relevant period of calculation, or (b), for all other purposes, the current average annual fixed rate of interest on securities of similar quality, subject to similar federal and state income tax treatment and having a similar maturity date, all as certified by a financial advisor, plus 25 basis points (0.25%). With respect to any Guaranteed Obligations, Debt Service shall include the Guaranteed Obligation Requirements, if any.

With respect to any Hedged Bonds, the interest on such Hedged Bonds during the term of any Qualified Hedge and for so long as the related Qualified Hedge Provider has not defaulted on its payment obligations thereunder, shall be calculated by adding (a) the amount of interest payable by the City on such Hedged Bonds pursuant to their terms, and (b) the amount of payments payable by the City under the related Qualified Hedge, and subtracting (c) the amount of payments payable to the City under the Qualified Hedge by the Qualified Hedge Provider at the rate specified in the related Qualified Hedge; provided, however, that to the extent that the related Qualified Hedge Provider is in default under the Qualified Hedge, the amount of interest payable by the City on the related Hedged Bonds shall be the

interest calculated as if such Qualified Hedge had not been executed. In determining the amount of payments by or receipts of the City under a Qualified Hedge for any future period that are not fixed throughout the term thereof (i.e., which are variable), such payments or receipts for any period of calculation (the “Determination Period”) shall be computed by assuming that the variables comprising the calculation (e.g., indices) applicable to the Determination Period are equal to the average of the actual variables which were in effect for the most recent 12-month period immediately preceding the date of calculation for which such information is available (or shorter period if such information is not available for a 12-month period).

For the purpose of calculating the Debt Service on Balloon Bonds which do not constitute Short-Term Obligations excluded from the calculation of Debt Service pursuant to clause (6) below, such Balloon Bonds shall be treated as if the principal amount thereof were amortized from the date originally incurred in substantially equal installments of principal and interest over a term of 25 years (provided, however, that the full principal amount of such Balloon Bonds shall be included in making such calculation if such principal amount is due within one year of the date such calculation is being made); and, if interest accrues under such Balloon Bonds at other than a fixed rate, the interest rate used for such computation shall be the rate at which the City could borrow (as of the time of calculation) for such period, as certified by a certificate of a Financial Advisor delivered to the City. With respect to any Guaranteed Obligations, Debt Service shall include the Guaranteed Obligation Requirements, if any.

The principal of and interest on Bonds, Guaranteed Obligation Requirements and payments under a Qualified Hedge shall be excluded from the determination of Debt Service to the extent that the same were or are expected to be paid with amounts on deposit on the date of calculation (or Bond proceeds to be deposited on the date of issuance of proposed Bonds) in a fund under the Master Trust Agreement or any Supplemental Agreement.

For purposes of computing the Debt Service of Paired Obligation Bonds, the applicable rate of interest payable thereon shall be the net interest rate payable pursuant to the offsetting indices.

For purposes of calculating the Debt Service of Short-Term Obligations which are or will be payable only from General Airport Revenues of the Fiscal Year in which such Short-Term Obligations are incurred, such Short-Term Obligations shall be disregarded and shall not be included in calculating Debt Service.

Notes which are issued in anticipation of the receipt of grants shall not be included in calculating Debt Service.

“Annual Debt Service” means the Debt Service for the Fiscal Year to which reference is made less the Available PFC Revenues for such Fiscal Year.

“Maximum Annual Debt Service” means the largest Annual Debt Service amount for a Fiscal Year ending after the date of calculation.

#### Designated Debt

“Designated Debt” means a specific indebtedness, designated by the City, in which such debt shall be offset with a Qualified Hedge, such specific indebtedness to include all or any part of a series of Bonds.

## Enterprise

“Enterprise” means the San José International Airport, now located partially within and partially without the City, including runways, taxiways, landing pads, navigational and landing aids, control towers, facilities for storage of aircraft and for parking of automobiles, roadways, passenger and freight terminals, land, easements and rights in land for clear zone and approach purposes, maintenance hangars and related facilities and all equipment, buildings, grounds, facilities, utilities and structures owned, leased or operated by the City in connection with or for the promotion or the accommodation of air commerce and air navigation and services in connection therewith, together with all additions, betterments, extensions and improvements thereto, to the fullest extent permitted by the Charter and the Law. The term “Enterprise”, unless otherwise specifically limited in any Supplemental Agreement, shall also include all other airports, airfields, landing places, heliports or places for the take-off and landing of aircraft, and all airport facilities appurtenant thereto, wheresoever situated, hereafter owned or operated by the City.

## Event of Default

“Event of Default” means an event of that name described under “Events of Default” below.

## Federal Securities

“Federal Securities” means any of the investments described in subsections (1), (2), (3), (4) or (11) of the definition of Permitted Investments below.

## Financial Advisor

“Financial Advisor” means an investment banking or financial advisory firm, commercial bank, or any other Person who or which is retained by the City for the purpose of passing on questions relating to the availability and terms of specified types of Bonds and is actively engaged in and, in the good faith opinion of the City, has a favorable reputation for skill and experience in underwriting or providing financial advisory services in respect of similar types of securities.

## Fiscal Year

“Fiscal Year” means the period beginning on July 1 of each year and ending on the next succeeding June 30, or such other fiscal year as may be adopted by the Council for the City.

## General Account

“General Account” means the General Account within the Bond Reserve Fund.

## General Airport Revenues

“General Airport Revenues” means all revenues, income, receipts and moneys derived by the City from the operation of the Enterprise, including (i) income derived from landing fees and the sale or use of airplane fuel, (ii) all other rents and charges made to or for the account of airplanes making use of the Enterprise, (iii) receipts from agriculture, automobile service stations and automobile parking on airport land, (iv) proceeds of loss of use or business interruption insurance, and (v) all receipts from leases and concessions, including rents, percentages of income or receipts for business conducted on any

property in the Enterprise or from services performed by the City in connection with or incidental to the operation of the Enterprise, but excluding –

(1) any money received by or for the account of the City from the levy or collection of taxes,

(2) moneys received from the State of California and the United States of America to the extent required to be deposited in restricted funds and/or used for purposes inconsistent with their use as General Airport Revenues under the terms of the Master Trust Agreement,

(3) lease deposits and security deposits,

(4) moneys required to be paid to the State of California and the United States of America pursuant to agreements with the City,

(5) moneys received from insurance proceeds or settlements (except as otherwise provided in the Master Trust Agreement) or the sale of or upon the taking by or under the threat of eminent domain of all or any part of the Enterprise,

(6) proceeds from Bonds or Subordinate Obligations issued by the City or proceeds from loans, indebtedness or other obligations entered into by the City,

(7) moneys or securities received by the City as gifts or grants, to the extent the use of such moneys or securities is restricted by the donor or grantor to purposes inconsistent with their use as General Airport Revenues under the terms of the Master Trust Agreement,

(8) CFC Revenues,

(9) PFC Revenues,

(10) Special Facility Revenues,

(11) Unrealized Items,

(12) Qualified Hedge Termination Payments, and

(13) Cargo facility charges or similar fees imposed on any of cargo operators, cargo facilities or cargo parcels.

“General Airport Revenues” also includes all interest, profits or other income derived from the deposit or investment of any moneys in the General Revenue Fund or any account therein except as otherwise provided under the Master Trust Agreement.

#### Guaranteed Obligation Requirements

“Guaranteed Obligation Requirements” means, with respect to any Guaranteed Obligations pertaining to any series of Bonds, for purposes of any calculation for the Fiscal Year in which such calculation is made and for each subsequent Fiscal Year, the amount required to be paid by the City to the Qualified Bank during such Fiscal Year (whether by reason of scheduled payments, payments required to be made at the option or demand of the Qualified Bank, or otherwise) as compensation (to the extent not taken into account in Maintenance and Operation Costs of the Enterprise) or reimbursement in accordance with the terms of the Letter of Credit Agreement, if on or prior to the date of calculation, the

Letter of Credit shall have been drawn upon in whole or in part to pay the principal of and/or interest on the Guaranteed Obligations and such draw shall not have been reimbursed. In such case the repayment obligations under the Letter of Credit Agreement shall be on a parity with all Outstanding Bonds.

#### Guaranteed Obligations

“Guaranteed Obligations” means Bonds becoming due on one fixed maturity date, the payment of which is additionally secured by a Letter of Credit issued by a Qualified Bank pursuant to a Letter of Credit Agreement. Nothing prevents any series of Bonds from having two or more maturities of Guaranteed Obligations if the Guaranteed Obligations are not stated to mature in consecutive annual installments.

#### Hedged Bonds

“Hedged Bonds” means Bonds for which the City shall have entered into a Qualified Hedge.

#### Independent Certified Public Accountant

“Independent Certified Public Accountant” means any certified public accountant or firm of such accountants appointed and paid by the City, and who, or each of whom –

- (1) is in fact independent and not under domination of the City;
- (2) does not have any substantial interest, direct or indirect, with the City; and
- (3) is not connected with the City as an officer or employee of the City, but who may be regularly retained to make annual or other audits of the books of or reports to the City.

#### Investment Agreement

“Investment Agreement” means:

(1) an uncollateralized investment agreement that is provided by (i) a domestic FDIC-insured commercial bank or a US branch of a foreign bank, rated at least “Aa2” by Moody’s and “AA” by Standard & Poor’s; (ii) a domestic insurance company rated “Aaa” by Moody’s and “AAA” by Standard & Poor’s; (iii) a domestic structured investment company approved by each Municipal Bond Insurer and rated “Aaa” by Moody’s and “AAA” by Standard & Poor’s; or (iv) a guaranteed corporation or a monoline financial guaranty insurance company approved by each Municipal Bond Insurer, provided that the long-term debt or claims-paying ability rating of the company or the guarantor is “Aaa” by Moody’s and “AAA” by Standard & Poor’s; and

(2) a collateralized investment agreement that is provided by (i) a registered broker/dealer subject to SPIC jurisdiction rated “A1” or better by Moody’s and “A+” or better by Standard & Poor’s; (ii) a domestic FDIC-insured commercial bank or a US branch of a foreign bank, rated at least “A1” by Moody’s and “A+” by Standard & Poor’s; (iii) a domestic insurance company rated at least “A1” by Moody’s and “A+” by Standard & Poor’s; (iv) a domestic structured investment company approved by each Municipal Bond Insurer and rated “Aaa” by Moody’s and “AAA” by Standard & Poor’s; or (v) a guaranteed corporation or a monoline financial guaranty insurance company approved by each Municipal Bond Insurer, provided that

the long-term debt or claims-paying ability rating of the company or the guarantor is “Aaa” by Moody’s and “AAA” by Standard & Poor’s.

Notwithstanding the foregoing, both that certain Series 2007 Collateralized Investment Agreement, dated as of September 13, 2007, by and between the Trustee and Citigroup Global Markets Inc., and that certain Series 2004 Collateralized Investment Agreement, dated as of September 13, 2007, by and between the Trustee and Citigroup Global Markets Inc., shall be Investment Agreements under the Master Trust Agreement.

#### Law

“Law” means the City of San José Airport Revenue Bond Law (Chapter 4.38 of the San José Municipal Code).

#### Letter of Credit

“Letter of Credit” means an irrevocable and unconditional letter of credit, a standby purchase agreement, a line of credit or other similar credit arrangement issued by a Qualified Bank to secure payment of Guaranteed Obligations or Variable Rate Bonds.

#### Letter of Credit Agreement

“Letter of Credit Agreement” means an agreement between the City and a Qualified Bank pursuant to which such Qualified Bank agrees to issue a Letter of Credit and which sets forth the repayment obligation of the City to such Qualified Bank on account of any draw under the Letter of Credit, which agreement shall be authorized by the City in a Supplemental Agreement. Said Supplemental Agreement shall also authorize the issuance or remarketing of the Guaranteed Obligations or Variable Rate Bonds secured by such Letter of Credit.

#### Maintenance and Operation Costs of the Enterprise

“Maintenance and Operation Costs of the Enterprise” means the costs of maintaining and operating the Enterprise, calculated on sound accounting principles, including (among other things) salaries and wages, benefits, fees for services, costs of materials, supplies and fuel, expenses of management, repairs and other expenses necessary to maintain and preserve the Enterprise in good repair and working order, and amounts for administration, overhead, insurance, taxes (if any), letter of credit fees, broker-dealer fees, auction agent fees, trustee fees, bond administration expenses, arbitrage rebate calculation and payment requirements and other similar costs, but excluding in all cases depreciation and obsolescence charges or reserves therefor, amortization of intangibles or other bookkeeping entries of a similar nature, costs of capital additions, replacements, betterments, extensions or improvements to the Enterprise, which under generally accepted accounting principles are chargeable to a capital account or to a reserve for depreciation, Qualified Hedge Termination Payments, Unrealized Items, costs associated with any Special Facility otherwise paid pursuant to a Special Facility Agreement, and charges for the payment of principal and interest on any indebtedness heretofore or hereafter issued for airport purposes.

#### Maximum Annual Debt Service

See definition of “Debt Service.”

### Minimum Sinking Fund Account Payments

“Minimum Sinking Fund Account Payments” means the aggregate amounts required by the Master Trust Agreement and any Supplemental Agreement to be deposited in Sinking Fund Accounts for the payment of Term Bonds.

### Municipal Bond Insurer

“Municipal Bond Insurer” means any insurance company or companies which has or have issued a policy of municipal bond insurance insuring payment of the principal of and interest on any of the Bonds of any series and are designated as such in a Supplemental Agreement providing for the issuance or sale of the Bonds of such series.

### Net General Airport Revenues

“Net General Airport Revenues” means General Airport Revenues less all Maintenance and Operation Costs of the Enterprise, but not including such Maintenance and Operation Costs as may be paid by the City from available moneys other than General Airport Revenues.

### Opinion of Counsel

“Opinion of Counsel” means a written opinion of counsel (who may be counsel for the City) retained by the City and who is acceptable to the Trustee.

### Other Available Funds

“Other Available Funds” means amounts (other than General Airport Revenues or PFC Revenues) made available to pay Debt Service in any period as described under “SECURITY FOR THE BONDS – Other Available Funds, CFC Revenues and Available PFC Revenues” in the forepart of this Official Statement.

### Outstanding

“Outstanding,” when used as of any particular time with reference to Bonds, means (subject to certain exceptions) all Bonds theretofore executed, issued and delivered by the City under the Master Trust Agreement except --

- (1) Bonds theretofore cancelled by the Trustee or surrendered to the Trustee for cancellation;
- (2) Bonds for the payment or redemption of which funds or securities in the necessary amount shall have theretofore been deposited with the Trustee (whether upon or prior to the maturity or redemption date of such Bonds), provided that, if such Bonds are to be redeemed prior to the maturity thereof, notice of such redemption shall have been given as provided in the Master Trust Agreement satisfactory to the Trustee shall have been made for the giving of such notice; and
- (3) Bonds in lieu of or in substitution for which other Bonds shall have been executed, issued and delivered by the City pursuant to the Master Trust Agreement.

For purposes of this definition, Bonds the principal of or interest on which has been paid by a Municipal Bond Insurer shall not be deemed paid by or on behalf of the City, shall not be defeased and shall remain Outstanding under the Master Trust Agreement until paid by the City.

For purposes of determining the percentage of consenting Owners of Capital Appreciation Bonds required by the Master Trust Agreement on any date, the Outstanding aggregate principal amount of Capital Appreciation Bonds shall be equal to the Accreted Value of such Capital Appreciation Bonds on such date.

#### Outstanding Subordinate Notes

“Outstanding Subordinate Notes” means the City’s outstanding San José International Airport Subordinated Commercial Paper Notes, Series A, B and C and any other Subordinated Commercial Paper Notes that are issued and Outstanding from time to time.

#### Paired Obligation Bonds

“Paired Obligation Bonds” means Bonds issued by the City which consist of an arrangement in which two inversely related Variable Rate Bonds are issued with interest based on offsetting indices or other mechanism resulting in a combined payment which is economically equivalent to a fixed rate.

#### Payment Date

“Payment Date” means any interest, or interest and principal, payment date on which payment of the Principal Installments of or interest on the Bonds is due.

#### Permitted Investments

“Permitted Investments” means any of the following, unless provided otherwise in a Supplemental Agreement with regard to a series of Additional Bonds, but only to the extent then permitted by the City’s Investment Policy, as amended from time to time by the Council:

(1) Cash (insured at all times by the Federal Deposit Insurance Corporation or otherwise collateralized with obligations described under subsection (2) below).

(2) Direct obligations of the United States of America (including obligations issued or held in book-entry form on the books of the Department of the Treasury, and CATS and TIGRS) or obligations the principal of and interest on which are unconditionally guaranteed by the United States of America.

(3) Bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following federal agencies and provided such obligations are backed by the full faith and credit of the United States of America:

- (i) U.S. Export-Import Bank (Eximbank);
- (ii) Farmers Home Administration (FmHA);
- (iii) Federal Financing Bank;
- (iv) Federal Housing Administration Debentures (FHA);

- (v) General Services Administration;
- (vi) Government National Mortgage Association (GNMA or “Ginnie Mae”);
- (vii) U.S. Maritime Administration; and
- (viii) U.S. Department of Housing and Urban Development (HUD).

(4) Bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following non-full faith and credit U.S. government agencies:

- (i) Federal Home Loan Bank System;
- (ii) Federal Home Loan Mortgage Corporation (FHLMC or “Freddie Mac”);
- (iii) Federal National Mortgage Association (FNMA or “Fannie Mae”);
- (iv) Student Loan Marketing Association (SLMA or “Sallie Mae”);
- (v) Resolution Funding Corp. (REFCORP) obligations; and
- (vi) Farm Credit System.

(5) Money market funds registered under the Federal Investment Company Act of 1940, whose shares are registered under the Federal Securities Act of 1933, and rated “AAAm-G,” “AAA-m” or better by Standard & Poor’s Corporation (and the equivalent by Moody’s), and including funds for which the Trustee and its affiliates provide investment advisory or other management services.

(6) Certificates of deposit secured at all times by collateral described in subsections (2) or (3) above. Such certificates must be issued by commercial banks, savings and loan associations or mutual savings banks. The collateral must be held by a third party and the Bondholders must have a perfected first security interest in the collateral.

(7) Certificates of deposit, savings accounts, deposit accounts or money market deposits which are fully insured by FDIC, including BIF and SAIF.

(8) Commercial paper rated, at the time of purchase, “Prime-1” by Moody’s and “A-1” or better by Standard & Poor’s.

(9) Bonds or notes issued by any state or municipality which are rated by Moody’s and Standard & Poor’s in one of the two highest rating categories assigned by such agencies.

(10) Federal funds or bankers acceptances with a maximum term of one year of any bank which has an unsecured, uninsured and unguaranteed obligation rating of “Prime-1” or “A3” or better by Moody’s and “A-1” or “A” or better by Standard & Poor’s.

- (11) Pre-refunded Municipal Obligations;
- (12) The Local Agency Investment Fund of the State of California;
- (13) Investment Agreements; and

(14) Repurchase Agreements.

Person

“Person” means a corporation, firm, other body corporate (including, without limitation, the United States of America, the State of California, or any other body corporate and politic other than the City), partnership, limited liability company, association, or individual, and also includes an executor, administrator, trustee, receiver, or other representative appointed according to law.

PFC Revenues

“PFC Revenues” means passenger facility charges collected by the City pursuant to the Act and the Regulations, as amended from time to time, and interest earnings thereon, net of amounts that collecting air carriers are entitled to retain for collecting, handling and remitting such passenger facility charge revenues.

Pre-refunded Municipal Obligations

“Pre-refunded Municipal Obligations” means any bonds or other obligations of any state of the United States of America or of any agency, instrumentality or local governmental unit of any such state which are not callable at the option of the obligor prior to maturity or as to which irrevocable instructions have been given by the obligor to call on the date specified in the notice; and

(1) which are rated, based on an irrevocable escrow account or fund, in the highest rating category by at least two Rating Agencies; or

(2) (i) which are fully secured as to principal and interest and redemption premium, if any, by an escrow consisting only of cash or obligations described under paragraph (2) of the definition of Permitted Investments, which escrow may be applied only to the payment of such principal of and interest and redemption premium, if any, on such bonds or other obligations on the maturity date or dates thereof or the specified redemption date or dates pursuant to such irrevocable instructions, as appropriate, and (ii) which escrow is sufficient, as verified by a nationally recognized independent certified public accountant, to pay principal of and interest and redemption premium, if any, on the bonds or other obligations described in this paragraph on the maturity date or dates specified in the irrevocable instructions referred to above, as appropriate.

Principal Installment

“Principal Installment” means, with respect to any Bond, the amount of principal or Accrued Value payable on a Payment Date, whether by reason of the maturity of a Bond or the mandatory redemption thereof from Minimum Sinking Fund Account Payments.

Project

“Project” means any additions, enlargements, betterments, extensions and other improvements or expenditures to or related to, and the equipping of, the Enterprise, including, without limitation, the acquisition of land therefor, passenger terminal facilities and related aircraft aprons, automobile parking, runways, utility plants and systems, terminal roadway systems, other transportation systems, rental car facilities, parking facilities and systems related thereto, landscaping, noise control improvements or expenditures (including such expenditures on private property) and related facilities, all as authorized in and described by the Master Trust Agreement or any Supplemental Agreement.

Qualified Bank

“Qualified Bank” means a state or national bank or trust company or savings and loan association or a foreign bank with a domestic branch or agency which is organized and in good standing under the laws of the United States or any state thereof or any foreign country, which is legally authorized to provide a Letter of Credit with respect to Guaranteed Obligations.

Qualified Hedge

“Qualified Hedge” means any financial arrangement (including any option obtained by the City to enter into such arrangement in the future) between the City and a Qualified Hedge Provider (a) which provides that each of the parties shall pay to the other an amount or amounts calculated as if such amount were interest accruing during the term of the arrangement at a specified rate (whether fixed or variable rate or measured against some other rate) on a Designated Debt, and payable from time to time or at a designated time or times (whether before, during or after the term of the arrangement), including a swap, cap, floor or collar; (b) which provides that if such amount is to be paid before it is deemed to have accrued, the amount paid shall reflect the present value of such future amount (i.e., an upfront premium), while an amount to be paid after it is deemed to have accrued shall reflect the time value of such funds; (c) which provides that payment dates and calculated accrual rates need not be the same for each payor, but to the extent payment dates coincide, the arrangement may (but need not) provide that one shall pay to the other any net amount due under such arrangement, (d) which relates to Designated Debt consisting of all or part of a particular series of Bonds; (e) the provider of which is a Qualified Hedge Provider or has been a Qualified Hedge Provider within the 60 day period preceding the date on which the calculation of Annual Debt Service is being made; (f) which has a term not greater than the term of the Designated Debt or to a specified mandatory tender or redemption of such Designated Debt; and (g) which has been designated in writing to the Trustee by the City as a Qualified Hedge with respect to such Bonds.

Qualified Hedge Provider

“Qualified Hedge Provider” means a financial institution whose senior long-term debt obligations, or whose obligations under any Qualified Hedge are guaranteed by a financial institution, or subsidiary of a financial institution, whose senior long-term debt obligations are rated in either of the two highest rating categories by at least two Rating Agencies, or the equivalent thereto in the case of any successor thereto.

Qualified Hedge Termination Payment

“Qualified Hedge Termination Payment” means an amount payable by the City or a Qualified Hedge Provider, in accordance with a Qualified Hedge, to compensate the other party to the Qualified Hedge for any losses and costs that such other party may incur as a result of an event of default or the early termination of the obligations, in whole or in part, of the parties under such Qualified Hedge.

Qualified Independent Airport Consultant

“Qualified Independent Airport Consultant” means a person or a firm who or which engages in the business of advising the management of airports concerning the operation and financing of airports, including consultation and advice with respect to leases and agreements with airline companies and concessionaires of all types and character, and also including advice and consultation generally concerning the use and operation of airports, and which person or firm, by reason of his or its knowledge and experience, has acquired a reputation as a recognized airport consultant. Such Qualified Independent Airport Consultant may include a person or firm rendering professional engineering or accounting

services in addition to his or its occupation as an airport consultant and may include any person or firm regularly employed by the City as an airport consultant to the City.

Qualified Reserve Facility

“Qualified Reserve Facility” means (i) a surety bond or similar instrument issued by a Municipal Bond Insurer, obligations insured by which have a rating of “AAA” (or the equivalent) by at least two Rating Agencies (one of which must be Moody’s) on the date the Qualified Reserve Facility is issued, or (ii) a Letter of Credit issued by a Qualified Bank which has a rating of “AA” (or the equivalent) by at least two Rating Agencies (one of which must be Moody’s) on the date the Qualified Reserve Facility is issued.

Rating Agency

“Rating Agency” or “Rating Agencies” means Moody’s Investors Service Inc., Standard & Poor’s Rating Service, Fitch, Inc. or any other nationally recognized securities rating agency providing a rating on the Bonds.

Regularly Scheduled Hedge Payments

“Regularly Scheduled Hedge Payments” means the regularly scheduled payments under the terms of a Qualified Hedge which are due absent any termination, default or dispute in connection with such Qualified Hedge.

Regulations

“Regulations” means the regulations promulgated under and pursuant to the Act including 14 CFR Part 158, and also means the terms of any written notification approving the City’s use of PFC Revenues given by the Administrator of the Federal Aviation Administration pursuant to said regulations.

Repurchase Agreement

“Repurchase Agreement” means a repurchase agreement with

- (1) a primary dealer on the Federal Reserve reporting dealer list which is rated “A” or better by Standard & Poor’s and Moody’s; or
- (2) a bank rated “A” or better by Standard & Poor’s and Moody’s; or
- (3) a domestic structured investment company approved by each Municipal Bond Insurer and rated “Aaa” by Moody’s and “AAA” by Standard and Poor’s; or
- (4) a guaranteed corporation or a monoline financial guaranty insurance company approved by each Municipal Bond Insurer, provided that the long-term debt or claims-paying ability rating of the company or the guarantor is “Aaa” by Moody’s and “AAA” by Standard & Poor’s,

that require the delivery of investments described in clauses (2), (3), (4)(i), (4)(ii), (4)(iii) or (4)(vi) of the definition of Permitted Investments. Such collateral must be delivered to the City, the Trustee (if the Trustee is not supplying the collateral) or a third party acting as agent for the Trustee (if the

Trustee is supplying the collateral) before or simultaneously with payment (perfection by possession of certificated securities). Such collateral must be valued weekly, marked-to-market at current market price plus accrued interest. The value of such collateral must equal 104% of the amount of cash transferred by the City or the Trustee to the counterparty under the repurchase agreement, plus accrued interest. If the value of such collateral is at any time below 104% of the value of the cash transferred by the City or the Trustee, then additional cash and/or acceptable collateral must be provided. Notwithstanding the foregoing, if the securities provided as collateral are investments described in clauses (4)(i), (4)(ii), (4)(iii) or (4)(vi) of the definition of Permitted Investments, then the value of such collateral must equal 105%.

#### Required Reserve

“Required Reserve” means, with respect to any series of Bonds, the amount required to be maintained in the reserve fund, if any, for such series of Bonds pursuant to the Supplemental Agreement authorizing the issuance of such series of Bonds. The Required Reserve for the Series 2001A Bonds, the Series 2002 Bonds, the Series 2011A-1 Bonds, the Series 2011A-2 Bonds, and the Series 2014 Bonds (the “Existing General Account Bonds”), and any Additional Bonds issued on a parity therewith and secured by the General Account within the Bond Reserve Fund, shall be the lesser of (i) the Maximum Annual Debt Service on all Existing General Account Bonds and such Additional Bonds, or (ii) the amount permitted to be held in the General Account within the Bond Reserve Fund by the arbitrage bond regulations issued by the United States Department of the Treasury under Section 148 of the Code, as such regulations are, at the time, applicable and in effect; provided, however, that any Required Reserve may be provided in whole or in part by one or more Qualified Reserve Facilities.

#### Rolling Coverage Amount

“Rolling Coverage Amount” means the uncommitted amounts in the Maintenance and Operation Fund or the General Revenue Fund, in an amount not to exceed 25% of Annual Debt Service in any Fiscal Year, that are available to pay Maintenance and Operation Costs of the Enterprise or Debt Service on Bonds and that are designated as the Rolling Coverage Amount by the City.

#### Serial Bonds

“Serial Bonds” means Bonds designated as Serial Bonds in the Supplemental Agreement providing for the issuance of such series and for which no Minimum Sinking Fund Account Payments are provided.

#### Short-Term Obligations

“Short-Term Obligations” means bonds, notes or other evidences of indebtedness that have a claim on the General Airport Revenues and a total maturity of not more than 12 months.

#### Sinking Fund Account

“Sinking Fund Account” means any special account or accounts established by the Master Trust Agreement or any Supplemental Agreement for the payment of Term Bonds.

#### Special Facility

“Special Facility” means buildings and facilities incident or related to the Enterprise, which are designated as Special Facilities pursuant to a Special Facility Agreement subject to the provisions of the Master Trust Agreement. See “Special Facilities” below.

Special Facility Agreement

“Special Facility Agreement” has the meaning specified under “Special Facilities” below.

Special Facility Revenues

“Special Facility Revenues” means revenues with respect to any Special Facility to the extent they are excluded from General Airport Revenues as provided in a Special Facility Agreement.

Subordinate Obligations

“Subordinate Obligations” means bonds, notes or other evidences of indebtedness which have a claim on the General Airport Revenues that is subordinate to the claim of the Bonds.

Supplemental Agreement

“Supplemental Agreement” means any trust agreement then in full force and effect which has been duly approved, executed and delivered by the City and the Trustee under and in conformity with the Law, and which is amendatory of or supplemental to the Master Trust Agreement; but only if and to the extent that such Supplemental Agreement is specifically authorized thereunder.

Term Bonds

“Term Bonds” means Bonds designated as Term Bonds in the Supplemental Agreement providing for the issuance of such series that are payable at or before their specified maturity date or dates from Minimum Sinking Fund Account Payments established for that purpose and that are calculated to retire such Bonds on or before their specified maturity date or dates.

Trustee

“Trustee” means BNY Western Trust Company, appointed as Trustee pursuant to the Master Trust Agreement, its successors and assigns, and any other corporation or association which may at any time be substituted in its place.

Unrealized Items

“Unrealized Items” mean, with respect to the calculation of Maintenance and Operation Costs of the Enterprise or General Airport Revenues for any period, any revenues or expenses recognized in accordance with generally accepted accounting principles which are due to unrealized gains or losses caused by marking assets or liabilities of the Enterprise to market.

Variable Rate Bonds

“Variable Rate Bonds” means Bonds which bear interest at a variable rate of interest.

Yield

“Yield” shall have the meaning ascribed to such term by the Code.

## **THE MASTER TRUST AGREEMENT**

*The following is a summary of certain provisions of the Master Trust Agreement, as amended by the Tenth Supplemental Trust Agreement. This summary does not purport to be complete and is qualified in its entirety by reference to the full terms of the Master Trust Agreement.*

### **Pledge of Revenues**

All of the General Airport Revenues are irrevocably pledged to the payment of the Maintenance and Operation Costs of the Enterprise and to the principal of and interest on the Bonds, and the General Airport Revenues may not be used for any other purpose while any of the Bonds remain Outstanding; except that the General Airport Revenues may be used for such purposes as are expressly permitted by the Master Trust Agreement. Said pledge shall constitute a lien on the General Airport Revenues for the payment of the Maintenance and Operation Costs of the Enterprise and the Bonds in accordance with the terms of the Master Trust Agreement, which lien shall be prior to any other lien or claim against the General Airport Revenues.

The City covenants and agrees that all General Airport Revenues will be received and held by the City in trust as provided by the Master Trust Agreement and will be accounted for through the General Revenue Fund. All such General Airport Revenues, whether held as trustee by the City or deposited with the Trustee, shall nevertheless be disbursed, allocated and applied solely to the uses and purposes set forth as provided by the Master Trust Agreement, and shall be accounted for separate and apart from all other moneys, funds, accounts or other resources of the City. All General Airport Revenues at any time paid into the General Revenue Fund shall be held by the City in trust for the benefit of the Owners at any time of the Bonds issued under the Master Trust Agreement and entitled to be paid therewith, and the City shall have no beneficial right or interest in any of such moneys, except only as in the Master Trust Agreement provided. All General Airport Revenues deposited with the Trustee shall be held, disbursed, allocated and applied as provided in the Master Trust Agreement by the Trustee.

### **Liability of City Limited to General Airport Revenues and Other Available Funds**

Notwithstanding anything in the Master Trust Agreement to the contrary, the City shall not be required to advance any moneys derived from the proceeds of any taxes collected in the City, or from any source of income other than the General Airport Revenues pledged to the payment of any Bonds under the Master Trust Agreement and the Other Available Funds and Available PFC Revenues made available therefor, for the payment of the principal of or interest on such Bonds, for the maintenance and operation of the Enterprise, for the performance of any covenants or for the payment of any obligations, including indemnification. The City may, however, advance funds for any such purpose, provided that such funds are derived from a source legally available for such purpose and may be used by the City for such purpose without incurring indebtedness.

The Bonds shall be revenue bonds, payable exclusively from the General Airport Revenues, Other Available Funds and Available PFC Revenues, as in the Master Trust Agreement provided. The general fund of the City is not liable, and the credit or taxing power of the City is not pledged, for the payment of the Bonds or their interest. The Owners of the Bonds shall never have the right to compel the exercise of the taxing power of the City or the forfeiture of any property of the City. The principal of and interest on the Bonds and any premiums upon the redemption of any thereof shall not be a debt of the City, nor a legal or equitable pledge, charge, lien or encumbrance upon any property of the City or upon any of its income, receipts or revenues except the amounts pledged to the payment thereof as provided in the Master Trust Agreement.

## **Issuance of Bonds under the Master Trust Agreement**

Bonds may be issued from time to time under the Master Trust Agreement, the Charter and the Law for any airport purpose, including for the purpose of financing and refinancing the acquisition, construction, expansion, improvement of one or more Projects and the Enterprise. The aggregate principal amount of Bonds which may be issued is not limited (subject, however, to the right of the City to limit or restrict the aggregate principal amount of Bonds which may at any time be issued and Outstanding) and may consist of one or more series of varying denominations, dates, maturities, interest rates and other provisions, all issued and to be issued pursuant to the Master Trust Agreement and the Law, subject to certain limitations (see "SECURITY FOR THE BONDS — Additional Series of Bonds" in the forepart of this Official Statement). The Master Trust Agreement constitutes a continuing agreement with the Owners of all of the Bonds issued or to be issued and Outstanding thereunder to secure the full and final payment of the principal of and the premiums, if any, and the interest on all Bonds, subject to the covenants, agreements, provisions and conditions therein contained.

Transfer of Bonds. Any Bond may, in accordance with its terms, be transferred, upon the books required to be kept pursuant to the Master Trust Agreement, by the person in whose name it is registered, in person or by his duly authorized attorney, upon surrender of such Bond for cancellation, accompanied by delivery of a duly executed written instrument of transfer in a form approved by the Trustee. Whenever any Bond or Bonds shall be surrendered for transfer, the City shall execute and the Trustee shall authenticate and deliver a new Bond or Bonds of the same series and maturity, for a like aggregate principal amount. The Trustee shall require the payment by any Bondowner requesting any such transfer of any tax or other governmental charge required to be paid with respect to such transfer. No transfer of Bonds shall be required to be made by the Trustee after the fifteenth day of the month next preceding each Payment Date.

Exchange of Bonds. Bonds may be exchanged at the principal corporate trust office of the Trustee in San Francisco, California, for a like aggregate principal amount of Bonds of other authorized denominations of the same series and maturity. The Trustee shall require the payment by the Bondowner requesting such exchange of any tax or other governmental charge required to be paid with respect to such exchange. No exchange of Bonds shall be required to be made by the Trustee after the fifteenth day of the month next preceding each Payment Date.

Bonds Mutilated, Lost, Destroyed or Stolen. If any Bond shall become mutilated, the City, at the expense of the Owner of said Bond, shall execute, and the Trustee shall thereupon authenticate and deliver a new Bond of like tenor and number in exchange and substitution for the Bond so mutilated (except that such number may be preceded by a distinguishing prefix), but only upon surrender to the Trustee of the Bond so mutilated. Every mutilated Bond so surrendered to the Trustee shall be cancelled by it and delivered to, or upon the order of, the City. If any Bond shall be lost, destroyed or stolen, evidence of such loss, destruction or theft may be submitted to the City and the Trustee and, if such evidence be satisfactory to both and indemnity satisfactory to them shall be given, the City, at the expense of the Owner, shall execute, and the Trustee shall thereupon authenticate and deliver a new Bond in lieu of and in substitution for the Bond so lost, destroyed or stolen (except that such number may be preceded by a distinguishing prefix). The City may require payment of a sum not exceeding the actual cost of preparing each new Bond and of the expenses which may be incurred by the City and the Trustee in the premises. Neither the City nor the Trustee shall be required to treat both the original Bond and any duplicate Bond as being Outstanding for the purpose of determining the principal amount of Bonds which may be issued or for the purpose of determining any percentage of Bonds Outstanding, but both the original and duplicate Bond shall be treated as one and the same.

## **Proceedings for the Issuance of Series of Additional Bonds**

Whenever the City shall determine to issue a series of Additional Bonds, the City shall authorize, and cause to be executed and delivered a Supplemental Agreement providing for the issuance of such series of Additional Bonds, setting forth the terms of such Additional Bonds in a new appendix to the Master Trust Agreement. Such Supplemental Agreement may also provide that the proceeds, funds and accounts relating to such Additional Bonds may be invested in investments other than those set forth in the definition of Permitted Investments.

None of the limitations or restrictions on the issuance of Additional Bonds set forth in the Master Trust Agreement are applicable to any series of Additional Bonds which are to be issued solely for the purpose of refunding and retiring all of the Bonds issued and then Outstanding, and nothing in the Master Trust Agreement limits the issuance of any Additional Bonds if, after the issuance and delivery of such Additional Bonds, none of the Bonds theretofore authorized will be Outstanding or the City shall have discharged the entire indebtedness on all such Bonds Outstanding in one of the ways authorized by the Master Trust Agreement.

## **Qualified Hedges**

The obligation of the City to make Regularly Scheduled Hedge Payments under a Qualified Hedge with respect to a series of Bonds may be on a parity with the obligation of the City to make payments with respect to such series of Bonds and other Bonds issued on a parity with such Bonds, except as otherwise provided by a Supplemental Agreement and in the Master Trust Agreement with respect to any Qualified Hedge Termination Payments. The City may provide in any Supplemental Agreement that Regularly Scheduled Hedge Payments under a Qualified Hedge shall be secured by a pledge of or lien on the General Airport Revenues on a parity with the Bonds of such series and all other Bonds on a parity therewith, regardless of the principal amount, if any, of the Bonds of such series remaining Outstanding. In the event that a Qualified Hedge Termination Payment or any other amounts other than as described in the preceding two sentences are due and payable by the City under a Qualified Hedge, the obligation of the City to pay such Qualified Hedge Termination Payment and any such other amounts shall be subordinate to all other obligations payable from the General Airport Revenues, unless otherwise specified in a Supplemental Agreement.

## **Special Facilities**

Anything in the Master Trust Agreement to the contrary notwithstanding, the City may enter into contracts, leases, subleases or other agreements pursuant to which the City or the other parties to such agreements will agree to construct or cause to be constructed a Special Facility on land constituting part of the Enterprise or will agree to acquire or construct a Special Facility on land not then constituting part of the Enterprise (which land if not then owned or leased by the City may be acquired for such purpose), or to acquire and remodel, renovate or rehabilitate a building, structure or other facility (including the site thereof) for a Special Facility (a "Special Facility Agreement") under the following conditions:

- (1) No Special Facility may be constructed or acquired and subject to a Special Facility Agreement under the provisions of the Master Trust Agreement summarized under this heading if the result of the use or occupation of such Special Facility under the Special Facility Agreement would result in a reduction of Net General Airport Revenues and Other Available Funds below the minimum amount of Net General Airport Revenues and Other Available Funds covenanted to be produced and

maintained in accordance with the Master Trust Agreement as determined by a certificate of the Director of Finance; and

- (2) Any financing for the Special Facility shall be secured as provided in the Special Facility Agreement and shall not be secured by or payable from the General Airport Revenues or any of the funds or accounts held under the Master Trust Agreement. The Special Facility Agreement may provide the terms and conditions under which any revenues of the Special Facility will become General Airport Revenues.

### **Certain Covenants of the City**

Payment of Principal and Interest. The City will punctually pay or cause to be paid the principal and interest (and premium, if any) to become due in respect of every Bond, in strict conformity with the terms of the Bonds and of the Master Trust Agreement, but solely from the General Airport Revenues pledged to the payment of said Bonds and any Other Available Funds made available for the payment of Debt Service.

Against Encumbrances. Subject to any rights of the United States of America or the State of California, except as expressly authorized under the Master Trust Agreement, the City will not mortgage or otherwise encumber, pledge or place any charge upon the Enterprise or any part thereof, or upon any General Airport Revenues, or issue any bonds or obligations payable from such revenues, prior to or on a parity with the Bonds (except as provided under the Master Trust Agreement), provided that Letter of Credit Agreements entered into in connection with Guaranteed Obligations or Variable Rate Bonds and any Regularly Scheduled Hedge Payments may be payable on a parity with the Bonds.

Nothing in the Master Trust Agreement shall prevent the City from authorizing and issuing bonds, notes, warrants, certificates or other obligations or evidences of indebtedness which as to principal or interest, or both, (1) are payable from General Airport Revenues after and subordinate to the payment of the principal of and interest on the Bonds, or (2) are payable from moneys which are not General Airport Revenues.

Sale or Other Disposition of Property. The City will not sell or otherwise dispose of the Enterprise or any part thereof essential to the proper operation of the Enterprise or to the maintenance of any General Airport Revenues except as expressly permitted under the Master Trust Agreement. The City will not enter into any lease or agreement which impairs the operation of the Enterprise or impedes the rights of the Owners of the Bonds with respect to the General Airport Revenues or the operation of the Enterprise, but the City may enter into any lease or agreement concerning all or any part of the Enterprise for airport or non-airport uses if such lease or agreement will not impair the operation of the Enterprise or impede the rights of the Owners of the Bonds with respect to the General Airport Revenues or the operation of the Enterprise.

Any real or personal property which has become nonoperative or which is not needed for the efficient and proper operation of the Enterprise, or any material or equipment which has worn out, may be sold if such sale (togeth er with all other sales theretofore made in the calendar year in which such sale is described in this paragraph) will not reduce annual General Airport Revenues in an amount which would cause the City to be unable to comply with the provisions described earlier in the Official Statement under "SECURITY FOR THE BONDS – Rate Maintenance Covenant" and if all of the net proceeds of such sale (less any amounts payable to the United States of America or the State of California or required by the United States of America or the State of California to be deposited in a restricted fund) are deposited in the General Revenue Fund.

The City has reserved the right to sell all or a portion of the Enterprise, and to enter into and execute agreements for and to complete such sale, but subject to the following specific conditions, which are conditions precedent to such sale:

(1) The City shall be in compliance with all covenants set forth in the Master Trust Agreement, and in all Supplemental Agreements theretofore executed and delivered by the City.

(2) The Council shall have determined by resolution that the net proceeds of the sale (less any amounts payable to the United States of America or the State of California or required to be deposited in a restricted fund) are to be used (i) for the redemption of Bonds, or (ii) for the making of additions or improvements to or extensions of the Enterprise.

(3) If the City shall have determined that the net proceeds of the sale (less any amounts payable to the United States of America or the State of California or required to be deposited in a restricted fund) are to be used for the redemption of Bonds, such proceeds of the sale shall be deposited with the Trustee, and the following conditions shall have been satisfied:

(i) The Council shall have authorized and caused to be executed and delivered a Supplemental Agreement providing for the redemption of the maximum principal amount of Bonds which can be redeemed from such proceeds of such sale, or, in the event that no Bonds are subject to redemption on the next succeeding interest payment date, directing the Trustee (A) to hold such proceeds in trust, (B) to invest such proceeds in the investments permitted in the Master Trust Agreement until any such Bonds shall become redeemable, subject to any restrictions imposed by the Master Trust Agreement, (C) to deposit the interest and income on such proceeds in the General Revenue Fund as such interest and income is received, and (D) to use such proceeds to redeem Bonds in the amount and manner specified in the Master Trust Agreement and any Supplemental Agreement on the first interest payment date on which the Bonds can be redeemed; and a certified copy of such Supplemental Agreement shall have been filed with the Trustee.

(ii) If such proceeds are not to be immediately used for the redemption of Bonds but instead are to be held by the Trustee until such Bonds become redeemable, the City shall have filed with the Trustee a written report of an independent certified public accountant stating (A) the amount of proceeds to be deposited with the Trustee from such sale, (B) an estimate of the total amount of Bonds and the amount of such Bonds of each maturity which could be redeemed from such proceeds on the first interest payment date on which such Bonds are redeemable, and (C) the estimated annual interest and income to be earned on such proceeds while held and invested by the Trustee. Such interest and income on such proceeds upon receipt by the Trustee shall be deposited in the General Revenue Fund and shall be treated as General Airport Revenues for all purposes of the Master Trust Agreement, including determining whether the City is in compliance with the covenant described earlier in the Official Statement under "SECURITY FOR THE BONDS — Rate Maintenance Covenant."

(iii) If such proceeds of such sale are to be immediately used to redeem Bonds, the Net General Airport Revenues for the last Fiscal Year or last recorded twelve-month period preceding the date of the adoption by the Council of the resolution authorizing such sale, less a deduction for the portion of such Net General Airport Revenues attributable to the portion of the Enterprise to be sold, all as shown by a certificate or opinion of an independent certified public accountant or a written report of a Qualified Independent Airport Consultant, shall be at least equal to 125% of Maximum Annual Debt Service for Bonds to be Outstanding following the redemption of Bonds from the proceeds of such sale.

(iv) If such proceeds are not to be immediately used for the redemption of Bonds but instead are to be held by the Trustee until such Bonds become redeemable, the Net General Airport Revenues for the last Fiscal Year or last recorded twelve-month period preceding the date of adoption by the Council of the resolution authorizing such sale, less a deduction for the portion of such Net General Airport Revenues attributable to the portion of the Enterprise to be sold, plus an allowance for the estimated annual interest or income to be earned on the invested proceeds of such sale while held and invested by the Trustee, all as shown by a certificate or opinion of an independent certified public accountant or a written report of a Qualified Independent Airport Consultant, shall be at least equal to 125% of Maximum Annual Debt Service on Bonds Outstanding at the time of such sale.

If the City shall have determined that the net proceeds of the sale (less any amounts payable to the United States of America or the State of California or required to be deposited in a restricted fund) are to be used for the making of additions or improvements to or extensions of the Enterprise, such proceeds of the sale shall be deposited by the Director of Finance in a special fund in trust to be used for the making of additions or improvements to or extensions of the Enterprise, and there shall have been filed with the Trustee a certificate of the City to the effect that, after such sale and application of funds, the General Airport Revenues will be sufficient to allow the City to continue to be in compliance with the covenant described earlier in the Official Statement under "SECURITY FOR THE BONDS — Rate Maintenance Covenant."

Notwithstanding any other provision of the Master Trust Agreement, the City shall be permitted to sell or transfer the Enterprise in its entirety to another public agency with (i) the consent of each Municipal Bond Insurer which insures the Outstanding Bonds, (ii) the consent of a majority in aggregate principal amount of Outstanding Bonds not insured by a Municipal Bond Insurer, (iii) the delivery to the Trustee of an opinion of Bond Counsel to the effect that such sale or transfer will not adversely affect the exclusion from gross income for federal income tax purposes of interest on the Tax-Exempt Bonds, (iv) the delivery to the Trustee of a confirmation from each Rating Agency then rating the Bonds that such sale or transfer will not adversely affect the rating on the Bonds, and (v) the full and complete assumption by such public agency of the obligations of the City under the Master Trust Agreement and under the Bonds.

Maintenance and Operation of Enterprise. The City will maintain and preserve the Enterprise in good repair and working order at all times from the General Airport Revenues available for such purposes, in conformity with standards customarily followed in the aviation industry for airports of like size and character. The City will not take any action or omit to take any action that would cause the Federal Aviation Administration, the Department of Transportation or any other state or federal agency to suspend or to revoke the City's operating certificates for the Enterprise. The City will at all times use reasonable efforts to keep the Enterprise open for take-offs and landings.

Liens and Claims. Subject to any rights of the United States of America or the State of California, the City shall keep the Enterprise and all parts thereof free from judgments, from mechanics' and materialmen's liens and from all liens and claims of whatsoever nature or character, to the end that the security provided pursuant to the Master Trust Agreement may at all times be maintained and preserved, and the City shall keep the Enterprise and the General Airport Revenues free from any liability which, in the judgment of the Trustee (and its determination thereof shall be final), might hamper the City in conducting its business or operating the Enterprise.

Insurance. The City shall procure or cause to be procured, and maintain or cause to be maintained, at all times while any of the Bonds are Outstanding, insurance on the Enterprise against such risks (including accident to or destruction of the Enterprise) as are usually insured against in connection

with similar enterprises. Any proceeds of any such insurance shall be used as set forth in the Master Trust Agreement.

The City may adopt alternative risk-management programs to insure against any of the risks required to be insured against under the Master Trust Agreement, including a program of self-insurance, in whole or in part. Any such alternative risk management program must be approved as reasonable and appropriate by a risk management consultant designated by the City, who may be an employee of the City. The approval of the risk management consultant shall be in the form of a report on the nature of the program and the adequacy of its funding which shall be prepared and filed with the Trustee within 90 days of implementation of such program and thereafter annually no later than 90 days following the renewal of the City's insurance policies in each year in which such program is in effect.

The City will deliver to the Trustee no later than 90 days following the date of renewal of the City's insurance policies in each year a schedule, in such detail as the Trustee in its discretion may request, setting forth specified information on the insurance policies then in force. Each such insurance policy shall require that the Trustee be given thirty (30) days' notice of any intended cancellation thereof or reduction of the coverage provided thereby.

Books and Accounts; Financial Statements; Reporting and Notice Requirements. The City will keep proper books of record and accounts of the Enterprise, separate from all other records and accounts of the City, in which complete and correct entries shall be made of all transactions relating to the Enterprise. Such books of record and accounts shall at all times during business hours be subject to the inspection of the Trustee or of any Owner of Bonds then Outstanding or their representatives authorized in writing, at reasonable hours and under reasonable conditions.

The City will prepare and file with the Trustee annually within six months after the close of each Fiscal Year so long as any of the Bonds are Outstanding:

(1) financial statements of the Enterprise for the preceding Fiscal Year, prepared in accordance with generally accepted accounting principles applied on a consistent basis from year to year, including a balance sheet (which shall include a statement showing the balances in each fund required to be established under the provisions of the Master Trust Agreement), statement of income, statement of retained earnings, and statement of changes in financial position, including separate accounts as required pursuant to generally accepted accounting principles for CFC Revenues, PFC Revenues, Other Available Funds and Available PFC Revenues, which financial statements shall be examined by and include the certificate or opinion of an independent certified public accountant, such certificate or opinion to include a statement as to the manner and extent to which the City has complied with the provisions of the Master Trust Agreement as it relates to said financial statements;

(2) a general statement of the physical condition of the Enterprise; and

(3) a statement as to all insurance carried by the City on the Enterprise as of the end of such Fiscal Year, including a brief description of the amount and coverage of each insurance policy and the name of the insuring company.

The City will furnish a copy of the aforesaid statements to any Bondowner upon request, and will furnish to the Trustee such reasonable number of copies thereof (not exceeding 100 copies) as may be required by the Trustee for distribution to investment bankers, security dealers and others interested in the Bonds and to the Owners of Bonds requesting copies thereof. The Trustee shall not be required to incur any nonreimbursable expenses in making such distribution.

City Budgets. The City shall prepare and adopt an annual budget for the Enterprise for each Fiscal Year setting forth in reasonable detail the General Airport Revenues and Other Available Funds anticipated to be derived in such Fiscal Year and the expenditures anticipated to be paid or provided for therefrom in such Fiscal Year. The City shall supply to the Trustee and to any Bondholders who shall so request in writing a copy of the annual budget for the Fiscal Year covered by such budget. Such budget shall be open for inspection by any Owner during normal business hours. If the City shall at any time adopt a revised annual budget for the Enterprise, the City shall supply a copy to the Trustee and to any Bondholder who shall so request in writing.

Maintenance of General Airport Revenues. The City will promptly collect all rents and charges due for the occupancy or use of the Enterprise, if any, as the same become due, and will promptly and vigorously enforce its rights against any tenant or other person who does not pay such rents or charges as they become due. The City will at all times maintain and vigorously enforce all of its rights under any leases or other contracts relating to any part of the Enterprise, if any.

Payment of Taxes, Etc. The City will pay and discharge, or cause to be paid and discharged, all taxes, assessments and other governmental charges which may hereafter be lawfully imposed upon the City on account of the Enterprise, if any, or any portion thereof or upon any General Airport Revenues and which, if unpaid, might impair the security of any Bonds, when the same shall become due, but nothing contained in the Master Trust Agreement shall require the City to pay any such tax, assessment or charge so long as it shall in good faith contest the validity thereof.

Eminent Domain Proceeds. If all or any part of the Enterprise shall be taken by or under threat of eminent domain proceedings, the net proceeds realized by the City therefrom (excluding any portion thereof payable to the United States of America or the State of California or required by the United States of America or the State of California to be deposited in a restricted fund) shall be deposited by the Director of Finance in a special fund in trust and applied and disbursed by the Director of Finance subject to the following conditions:

(1) If such proceeds are sufficient to provide for the payment of the entire amount of principal due or to become due upon all of the Bonds, together with all of the interest due or to become due thereon and any redemption premiums, so as to enable the City to retire all of the Bonds then Outstanding, either by redemption at the then-current redemption prices or by payment at maturity or partly by redemption prior to maturity and partly by payment at maturity, the Director of Finance shall transfer such moneys to the Trustee who shall apply such moneys to such retirement and to the payment of such interest. The balance of such moneys, if any shall be transferred back to the City and shall be available for use by the City for any lawful purpose.

(2) If such proceeds are insufficient to provide the moneys required for the purposes set forth in the foregoing subsection (1), the Council shall by resolution determine to apply such proceeds for one of the following purposes, subject to the conditions hereinafter in this subsection (2) set forth:

(a) The City may determine to apply such proceeds to the purchase or redemption of Bonds then Outstanding on the dates and at the prices the Bond are subject to redemption. In that event, the Director of Finance shall transfer such proceeds to the Trustee who shall apply such proceeds to the redemption or purchase of Bonds of each series then Outstanding as set forth in a Written Request of the City.

(b) The City may determine to apply such proceeds to the cost of additions or improvements to or extensions of the Enterprise, if (A) the City first secures and files with the

Trustee a written certificate of a Qualified Independent Airport Consultant showing (i) the annual losses, if any, in General Airport Revenues, suffered, or to be suffered, by the City by reason of such eminent domain proceedings, (ii) a general description of the additions, improvements or extensions then proposed to be acquired by the City from such proceeds, and (iii) an estimate of the additional amount of General Airport Revenues to be derived from such additions, improvements or extensions; and (B) such written report concludes that such additional amounts of General Airport Revenues will sufficiently offset the loss of General Airport Revenues resulting from such eminent domain proceedings so that the ability of the City to meet its obligations under the Master Trust Agreement will not be substantially impaired. The conclusion of the Qualified Airport Consultant accepted by the City shall be final and conclusive. The City shall then promptly proceed with the construction of the additions, improvements or extensions substantially in accordance with such written certificate. Payments for such construction shall be made by the City from such proceeds. Any balance of such proceeds not required by the City for the purposes aforesaid shall be deposited in the General Revenue Fund.

(3) If such eminent domain proceedings have had no material effect upon the General Airport Revenues and the security of the Bonds, and a Qualified Independent Airport Consultant so concludes in a written certificate filed with the Trustee, and the Municipal Bond Insurers concur in writing, the Trustee may so determine. Such determination by the Trustee shall be final and conclusive, and, upon notice thereof, the City may determine to apply such proceeds to the costs of additions or improvements to or extensions of the Enterprise, or may deposit such proceeds in the General Revenue Fund as deemed appropriate by the Director of Finance.

Observance of Laws and Regulations. The City shall comply promptly, fully and faithfully with and abide by any statute, law, ordinance, order, rule or regulation, judgment, decree, direction or requirement now in force or hereafter enacted, adopted or entered by any competent governmental authority or agency applicable or with respect to or affecting the Enterprise; subject to the City's right to contest the applicability or validity thereof as further described in the Master Trust Agreement.

Prosecution and Defense of Suits. The City shall promptly from time to time take such action as may be necessary or proper to remedy or cure any defect in or cloud upon the title to the Enterprise hereafter developing, and shall prosecute all such suits, actions and other proceedings as may be appropriate for such purposes and, to the extent permitted by law, shall indemnify and save the Trustee and every Bondowner harmless from all loss, cost, damage and expense, including attorneys' fees, which they or any of them may incur by reason of any such defect, cloud, suit, action or proceeding.

The City shall defend against every suit, action or proceeding at any time brought against the Trustee or any Bondowner upon any claim arising out of the receipt, application or disbursement of any General Airport Revenues or involving the rights and duties of the Trustee or the rights of any Bondowner under the Master Trust Agreement; provided, that the Trustee or any Bondowner at its or his election may appear in and defend any such suit, action or proceeding. The City shall, to the extent permitted by law, indemnify and hold harmless the Trustee and the Bondowners against any and all liability claimed or asserted by any person arising out of such receipt, application or disbursement, and shall indemnify and hold harmless the Bondowners against any attorneys' fees or other expenses which any of them may incur in connection with any litigation to which any of them may become a defendant by reason of his ownership of Bonds. The City, to the extent permitted by law, shall promptly reimburse any Bondowner in the full amount of any attorneys' fees or other expenses which he may incur in litigation or otherwise in order to enforce his rights under the Master Trust Agreement or the Bonds, provided that such litigation shall be concluded favorably to such Bondowner's contentions therein. Notwithstanding

any contrary provision in the Master Trust Agreement, this covenant shall remain in full force and effect, even though all indebtedness and obligations issued under the Master Trust Agreement may have been fully paid and satisfied, until the City shall have been dissolved.

Tax Covenants. The City will take no action that would cause the interest on the Tax-Exempt Bonds to be included in federal gross income and the non-preference status of such interest for federal alternative minimum income tax purposes with respect to Tax-Exempt Bonds that are not “qualified private activity bonds” under the Code. To that end, and without limiting the scope of the foregoing, the City will comply with any tax certificates or agreements entered into in connection with the issuance of any Tax-Exempt Bonds. To the extent necessary or desirable to maintain the exclusion of interest on the Tax-Exempt Bonds from federal gross income, the City may direct the Trustee to invest any funds held under the Master Trust Agreement or any Supplemental Agreement in yield-restricted investments.

Governmental Approvals. The City will perform (or cause to be performed) any construction, reconstructions and restorations of, improvements, betterments and extensions to, and equippings and furnishings of, and will operate and maintain (or cause to be operated and maintained) the Enterprise at standards required in order that the same may continue to be approved by the proper and competent authority or authorities of the United States of America for the landing and taking off of aircraft operating in scheduled service, and as a terminal point for the receipt and dispatch of passengers, property and mail by aircraft.

Compliance With Terms of Grants-in-Aid. The City shall comply with the requirements of any grants-in-aid received by the City.

### **Investment of Moneys**

All moneys held by the City or the Trustee in the Funds and accounts established or continued under the Master Trust Agreement shall be held in time or demand deposits (including certificates of deposit) in any bank or trust company (including the Trustee) authorized to accept deposits of public funds, and shall be secured at all times by such obligations, and to the fullest extent, as is required by law, and may at the written direction of the City be invested in Permitted Investments, maturing not later than the date on which such moneys are required for payment by the Director of Finance or the Trustee, as the case may be. Moneys in the Bond Reserve Fund may be deposited or invested in time or demand deposits or Permitted Investments which mature not more than five years from the date of investment; provided, however, that any Permitted Investment with a nominal term greater than five years but which permits withdrawal of the entire principal amount of such investment at par, without penalty and at such times as shall be required under the Master Trust Agreement, shall be deemed to have a maturity for purposes of this sentence of the first such permitted withdrawal date. For the purpose of determining the amount of money in the Bond Reserve Fund, all investments of moneys therein shall be valued annually, or more frequently upon Written Request of the City, not to exceed semiannually (or any other frequency agreed upon by the City and the Trustee), at face value if such investments mature within twelve months from the date of valuation, and if such investments mature more than twelve months after the date of valuation, at the price at which such investments are redeemable by the holder at the holder's option, if so redeemable, or, if not so redeemable, at the lesser of (i) the cost of such investments minus the amortization of any premium or plus the amortization of any discount, or (ii) market value of such investments; provided that, prior to making any transfers to the Interest Fund, pursuant to the Master Trust Agreement, or to the General Revenue Fund of amounts on deposit in an account within the Bond Reserve Fund in excess of the Required Reserve, the Trustee shall (i) submit the calculations it used to determine the value of investments held in the Bond Reserve Fund to the City and (ii) obtain written approval of such calculations from the City.

The Trustee may sell or present for redemption any obligations so purchased by it whenever it shall be necessary in order to provide moneys to meet any payment, and the Trustee shall not be liable or responsible for any loss resulting from such investment. The Trustee may act as principal or agent in the acquisition or disposition of any investment. The Trustee may commingle any of the moneys held by it pursuant to the Master Trust Agreement for investment purposes only; provided, however, that the Trustee shall account separately for the moneys belonging to each fund or account established pursuant to the Master Trust Agreement and held by it.

Unless otherwise provided in a Supplemental Agreement, (i) investment earnings on amounts in each of the accounts within each Improvement Fund shall be retained in said accounts and funds, and (ii) investment earnings on amounts in the General Revenue Fund and all accounts therein shall be deposited in the General Revenue Fund.

### **Events of Default; Acceleration; Waiver of Default**

If one or more of the following events (each an "Event of Default") shall happen, that is to say--

(1) if default shall be made in the due and punctual payment of the principal of, or the premium (if any) on, any Bond when and as the same shall become due and payable, whether at maturity as therein expressed, by proceedings for redemption, by declaration or otherwise, or if default shall be made in the redemption or payment at maturity from any Sinking Fund Account of any Term Bonds in the amounts and at the times provided therefor;

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

(3) if default shall be made by the City in the observance of any of the other covenants, agreements or conditions on its part in the Master Trust Agreement or in the Bonds contained, and such default shall have continued for a period of sixty days after written notice thereof, specifying such default and requiring the same to be remedied, shall have been given to the City by the Trustee or by a Municipal Bond Insurer, or to the City and the Trustee by the Owners of not less than twenty-five per cent (25%) in aggregate principal amount of the Bonds at the time Outstanding; or

(4) if the City shall file a petition or answer seeking reorganization or arrangement under the federal bankruptcy laws or any other applicable law of the United States of America, or if a court of competent jurisdiction shall approve a petition, filed with or without the consent of the City, seeking reorganization under the federal bankruptcy laws or any other applicable law of the United States of America, or if, under the provisions of any other law for the relief or aid of debtors, any court of competent jurisdiction shall assume custody or control of the City or of the whole or any substantial part of its property;

then, and in every such case, the Owner of any Bond at the time Outstanding shall be entitled to proceed to protect and enforce the rights vested in such Owner by the Master Trust Agreement by such appropriate judicial proceeding as such Owner shall deem most effectual to protect and enforce any such right, either by suit in equity or by action at law, whether for the specific performance of any covenant or agreement contained in the Master Trust Agreement, or in aid of the exercise of any power granted in the Master Trust Agreement, or to enforce any other legal or equitable right vested in the Owners of Bonds by the Master Trust Agreement or by law; provided, however, that no such Bondowner shall have the right to institute any such judicial proceeding unless (a) such Owner shall have previously given to the Trustee written notice of the occurrence of an Event of Default; (b) the Owners of at least ten per cent

(10%) in aggregate principal amount of the Bonds then Outstanding shall have made written request to the Trustee to exercise the powers granted in the Master Trust Agreement or to institute such action, suit or proceeding in its own name; (c) such Owner or said Owners shall have tendered to the Trustee reasonable indemnity against the costs, expenses and liabilities to be incurred in compliance with such request; (d) the Trustee shall have refused or omitted to comply with such request for a period of sixty days after such written request shall have been received by, and said tender of indemnity shall have been made to, the Trustee; and (e) the Trustee shall not have received contrary directions from the Owners of a majority in aggregate principal amount of the Bonds Outstanding. The provisions of the Master Trust Agreement shall constitute a contract with the Owners of the Bonds, and, subject to the foregoing sentence, such contract and duties of the City and of the Council members, officers and employees thereof shall be enforceable by any Bondowner by mandamus or other appropriate suit, action or proceeding in any court of competent jurisdiction.

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

Notwithstanding any other provision of the Master Trust Agreement, an Event of Default with respect to the payment of or the performance of a covenant or the satisfaction of any other condition or requirement with respect to any Subordinate Obligation shall not be deemed, in and of itself, an Event of Default with respect to the Bonds unless such Event of Default is also an Event of Default with respect to such Bonds.

Nothing in the Master Trust Agreement or in the Bonds shall affect or impair the obligation of the City, which is absolute and unconditional, to pay the principal of and the interest (and premium, if any) on the Bonds to the respective Owners of the Bonds at the respective dates of maturity, or upon call for redemption, as provided in the Master Trust Agreement, but only out of the General Airport Revenues and other funds and accounts pledged in the Master Trust Agreement for such payments and any Other Available Funds, or affect or impair the right of action, which is also absolute and unconditional, of such Owners to institute suit to enforce such payment by virtue of the contract embodied in the Bonds.

A waiver of any default or breach of duty or contract by any Bondholder shall not affect any subsequent default or breach of duty or contract, or impair any rights or remedies on the subsequent default or breach. No delay or omission of the Trustee or of any Owner of any of the Bonds to exercise any right or power arising upon the happening of any Event of Default shall impair any such right or power or shall be construed to be a waiver of any such Event of Default or an acquiescence therein, and every power and remedy given by applicable law or the Master Trust Agreement to the Trustee or to the Owners of Bonds may be exercised from time to time and as often as shall be deemed expedient by the Trustee or the Owners of Bonds.

**Actions by Trustee as Attorney-in-Fact.** Any suit, action or proceeding which any Owner of Bonds shall have the right to bring to enforce any right or remedy under the Master Trust Agreement may be brought by the Trustee for the equal benefit and protection of all Owners of Bonds similarly situated (notwithstanding any conditions upon the bringing of any such action, suit or proceeding set forth above) and the Trustee is appointed (and the successive respective Owners of the Bonds issued under the Master Trust Agreement, by taking and holding the same, shall be conclusively deemed so to have appointed it) the true and lawful attorney-in-fact of the respective Owners of the Bonds for the purpose of bringing any such suit, action, or proceeding and to do and perform any and all acts and things for and in behalf of the respective Owners of the Bonds as a class or classes, as may be necessary or advisable in the opinion of the Trustee as such attorney-in-fact.

Remedies Not Exclusive. No remedy conferred in the Master Trust Agreement upon or reserved to the Trustee or to the Owners of Bonds is intended to be exclusive of any other remedy. Every such remedy shall be cumulative and shall be in addition to every other remedy given under the Master Trust Agreement or now or hereafter existing, at law or in equity or by statute or otherwise and may be exercised without exhausting and without regard to any other remedy conferred by the Law or any other law.

### The Trustee

So long as there is no Event of Default, the City may remove the Trustee by giving written notice to such Trustee and by giving Bondholders notice by mail, and any successor thereto, and may appoint a successor or successors thereto; provided that any such successor shall be a bank or trust company which singly or together with its corporate parent, shall have a combined capital and surplus of at least fifty million dollars (\$50,000,000), and shall be subject to supervision or examination by federal or state authority.

The Trustee may at any time resign by giving written notice of resignation to the City and the Bondholders as provided in the Master Trust Agreement. Upon receiving such notice of resignation or upon removal of the Trustee, the City is required to appoint a successor trustee within 60 days in accordance with the Master Trust Agreement.

The Trustee may be removed at any time, at the request of the Municipal Bond Insurers insuring a majority in principal amount, including any Accreted Value, of Bonds Outstanding under the Master Trust Agreement, for any breach of the trust by the Trustee set forth in the Master Trust Agreement. No removal, resignation or termination of the Trustee shall take effect until a successor, acceptable to the Municipal Bond Insurers insuring a majority in principal amount, including any Accreted Value, of the Bonds Outstanding under the Master Trust Agreement, shall be appointed.

The Trustee shall, prior to an Event of Default, and after the curing of all Events of Default which may have occurred, perform such duties and only such duties as are expressly and specifically set forth in the Master Trust Agreement and no implied covenants or duties shall be read into the Master Trust Agreement against the Trustee. The Trustee shall, during the existence of any Event of Default (which has not been cured), exercise such of the rights and powers vested in it by the Master Trust Agreement, and use the same degree of care and skill in their exercise, as a prudent person would exercise or use under the circumstances in the conduct of such person's own affairs.

The Trustee shall not be required to inquire into or take notice, or be deemed to have notice, or any Event of Default under the Master Trust Agreement or any other event which, with the passage of time, the giving of notice or both, would constitute an Event of Default unless the Trustee shall have actual knowledge or be specifically notified in writing of such Event of Default or event by the City or by the Owners of at least twenty-five percent (25%) in aggregate principal amount of the Bonds then Outstanding. Except as otherwise expressly provided herein, the Trustee shall not be bound to ascertain or inquire as to the performance or observance by the City, or any other party to the transaction contemplated in the Master Trust Agreement, of any of the terms, conditions, covenants or agreements herein or any of the documents executed in connection with the Bonds.

The Trustee shall not be liable with respect to any action taken or omitted to be taken by it in good faith in accordance with the direction of the Owners of a majority in aggregate principal amount of the Bonds Outstanding relating to the time, method and place of conducting any proceeding or any remedy available to the Trustee, or the exercise of any trust or power conferred upon the Trustee, under the Master Trust Agreement. The Trustee shall be under no obligation to exercise any of the rights or

powers vested in it by the Master Trust Agreement at the request, order or direction of any of the Owners or the City unless such Owners or the City shall have offered to the Trustee security or indemnity reasonably satisfactory to it against the fees, costs, expenses and liabilities (including reasonable attorneys' fees) which may be incurred by the Trustee.

No provision of the Master Trust Agreement shall require the Trustee to expend or risk its own funds or otherwise incur any financial liability in the performance of any of its duties hereunder, or in the exercise of any of its rights or powers.

### **Modification of Trust Agreement and Payment Agreement**

Modification without Consent of Bondholders. The Master Trust Agreement, any Supplemental Agreement and the rights and obligations of the City and of the Owners of the Bonds may also be modified or amended at any time by a Supplemental Agreement which shall become binding upon execution and delivery by the parties thereto, without the consent of any Bondholders or any Municipal Bond Insurer, but only to the extent permitted by law and only for any one or more of the following purposes –

(1) to add to the covenants and agreements of the City in the Master Trust Agreement contained other covenants and agreements thereafter to be observed or to surrender any right or power reserved to or conferred upon the City;

(2) to cure, correct or supplement any ambiguous or defective provision contained in the Master Trust Agreement or in regard to questions arising under the Master Trust Agreement, as the City may deem necessary or desirable and not inconsistent with the Master Trust Agreement, and which shall not materially adversely affect the interests of the Owners of the Bonds;

(3) to provide for the issuance of Additional Bonds, and to provide the terms and conditions under which such Additional Bonds may be issued, subject to and in accordance with the provisions of the Master Trust Agreement and any applicable Supplemental Agreement; and

(4) to amend provisions of the Master Trust Agreement relating to the Surplus Revenue Fund.

Modification with Consent of Bondholders. Subject to the limitations imposed under any Supplemental Agreement providing for the issuance of Subordinate Obligations, the Master Trust Agreement, any Supplemental Agreement, and the rights and obligations of the City and of the Owners of the Bonds and of the Trustee may be modified or amended at any time by a Supplemental Agreement which shall become binding when the written consents of (i) a majority, of the Owners in aggregate principal amount of the Bonds then Outstanding, exclusive of Bonds disqualified as provided in the Master Trust Agreement, and (ii) each Municipal Bond Insurer insuring such Bonds (so long as such Municipal Bond Insurer is not in default under the policy of municipal bond insurance issued by it in connection with any series of Bonds) shall have been filed with the Trustee (provided, that no such Municipal Bond Insurer shall unreasonably withhold consent to such modification or amendment).

Subject to the limitations imposed under any Supplemental Agreement providing for the issuance of Subordinate Obligations, the Master Trust Agreement and the rights and obligations of the City and of the Owners of the Bonds and of the Trustee may also be modified or amended at any time by a Supplemental Agreement which shall become binding when the written consents of each Municipal Bond Insurer insuring such Bonds shall have been filed with the Trustee, following prior written notification thereof to Rating Agencies, provided that at such time the payment of the principal of and

interest on all Bonds Outstanding shall be insured by a policy or policies of municipal bond insurance issued by a Municipal Bond Insurer or Insurers.

No such modification or amendment shall (A) extend the fixed maturities of the Bonds, or extend the time for making any Minimum Sinking Fund Account Payments, or reduce the rate of interest thereon, or extend the time of payment of interest, or reduce the amount of principal thereof, or reduce any premium payable on the redemption thereof, without the consent of the Owner of each Bond so affected, or (B) reduce the aforesaid percentage of Owners of such Bonds whose consent is required for the execution of any amendment or modification of the Master Trust Agreement, or (C) modify any of the rights or obligations of the Trustee without its written consent thereto.

The Council may at any time authorize and cause to be executed and delivered a Supplemental Agreement amending the provisions of the Bonds, the Master Trust Agreement or any Supplemental Agreement, to the extent that such amendment is permitted by the Master Trust Agreement. A copy of such Supplemental Agreement, together with a request to Bondholders and to each Municipal Bond Insurer for their consent thereto, shall be mailed by the City to each Owner of Bonds and to each Municipal Bond Insurer, but failure to mail copies of such Supplemental Agreement and request shall not affect the validity of the Supplemental Agreement when assented to as described below. Notice of the authorization, execution and delivery of such Supplemental Agreement (stating that a copy thereof is available for inspection at the principal office of the Trustee) shall be mailed to each Bondholder.

Such Supplemental Agreement shall not become effective unless there shall be filed with the Trustee the required written consents of the Owners of the Bonds and of each Municipal Bond Insurer, as described above, and a notice shall have been mailed. Each such consent shall be effective only if accompanied by proof of ownership of the Bonds for which such consent is given, which proof shall be such as is permitted by the Master Trust Agreement. Any such consent shall be binding upon the Owner of the Bonds giving such consent and on any subsequent Owner (whether or not such subsequent Owner has notice thereof) unless such consent is revoked in writing by the Owner giving such consent or a subsequent Owner by filing such revocation with the Trustee prior to the date when the notice described below has been given.

After the Owners of the required percentage of Bonds and each Municipal Bond Insurer shall have filed their consents to the Supplemental Agreement, the City shall mail a notice to the Bondholders in the manner provided and the notice of authorization, execution and delivery thereof, stating in substance that the Supplemental Agreement has been consented to by the Owners of the required percentage of Bonds and each Municipal Bond Insurer and will be effective as described above (but failure to mail copies of said notice shall not affect the validity of the Supplemental Agreement or consents thereto). The Supplemental Agreement shall become effective upon the execution and delivery thereof.

In lieu of obtaining any demand, request, direction, consent or waiver in writing, the Trustee may call and hold a meeting of the Bondholders upon such notice and in accordance with such rules and regulations as the Trustee considers fair and reasonable for the purpose of obtaining any such action.

Any proceedings whereby the consent of the Owners is to be obtained at a time when all Outstanding Bonds are Book-Entry Bonds, the Trustee shall establish a record date upon which any action shall become effective pursuant to such consent under the Master Trust Agreement. The Trustee shall give notice of such record date to all Owners not less than 15 calendar days in advance of such record date, to the extent possible.

## **Discharge of the Master Trust Agreement**

If the City shall pay and discharge the entire indebtedness on all Bonds Outstanding in any one or more of the following ways--

(1) by well and truly paying or causing to be paid the principal of (including redemption premiums, if any) and interest on all such Bonds Outstanding, as and when the same become due and payable (but this clause shall not include Bonds the principal of or interest on which has been paid by a Municipal Bond Insurer until said principal and interest shall have been paid by the City); or

(2) by depositing with the Trustee, in trust, at or before maturity, money which, together with the amounts then on deposit with the Trustee for the payment of Debt Service on such Bonds, including any reserve funds, is fully sufficient to pay or redeem all such Bonds Outstanding, including all principal, interest and redemption premiums, if any; or

(3) by delivering to the Trustee, for cancellation by it, all such Bonds Outstanding; or

(4) by depositing with the Trustee, in trust, Federal Securities in such amount which, in the determination of an independent certified public accountant, who shall certify such determination to the Trustee, shall, together with the income or increment to accrue thereon and any other moneys of the City made available for such purpose, be fully sufficient to pay and discharge the indebtedness on all such Bonds (including all principal, interest and redemption premiums, if any) at or before their respective maturity dates;

and if the City shall also pay or cause to be paid all other sums payable by the City, then and in that case, at the election of the City (evidenced by a certificate of the City signifying its intention to pay and discharge all such indebtedness and that the Master Trust Agreement and all other obligations of the City under the Master Trust Agreement with respect to such Bonds shall cease and terminate, which shall be filed with the Trustee), and notwithstanding that any such Bonds shall not have been surrendered for payment, the pledge of the General Airport Revenues and other funds provided for in the Master Trust Agreement and all other obligations of the City under the Master Trust Agreement with respect to such Bonds shall cease, terminate and be completely discharged, and the Owners of such Bonds not so surrendered and paid shall thereafter be entitled to payment only out of the money or Federal Securities deposited with the Trustee as aforesaid for their payment; subject, however, to the provisions of the Master Trust Agreement. The discharge of the obligations of the City under the Master Trust Agreement shall be without prejudice to the rights of the Trustee to charge for and be reimbursed by the City for any expenditures which it may thereafter incur in connection herewith.

The City may at any time surrender to the Trustee for cancellation by it any Bonds previously issued and delivered, which the City may have acquired in any manner whatsoever, and such Bonds, upon such surrender and cancellation, shall be deemed to be paid and retired.

Discharge of Liability on Bonds. Upon the deposit with the Trustee, in trust, at or before maturity, of money or Federal Securities in the necessary amount to pay or redeem any Outstanding Bonds (whether upon or prior to their maturity or the redemption date of such Bonds), provided that if such Bonds are to be redeemed prior to the maturity thereof, notice of such redemption shall have been given as in Master Trust Agreement provided or provision satisfactory to the Trustee shall have been made for the giving of such notice, then all liability of the City in respect of such Bonds shall cease, determine and be completely discharged and the Owners thereof shall thereafter be entitled only to

payment out of the money or Federal Securities deposited with the Trustee as aforesaid for their payment, subject, however, to the provisions of the Master Trust Agreement.

Payment of Bonds after Discharge of Master Trust Agreement. Any moneys deposited with the Trustee in trust for the payment of the principal of, or interest or premium on, any Bonds and remaining unclaimed for two years after the principal of all the Outstanding Bonds has become due and payable (whether at maturity or upon call for redemption or by declaration as provided in the Master Trust Agreement) shall then be repaid to the City, and the Owners of such Bonds shall thereafter be entitled to look only to the City for payment thereof, and all liability of the Trustee with respect to such moneys shall thereupon cease. In such event, the Owners of the Bonds in respect of which such moneys were deposited shall thereafter be deemed to be general creditors of the City for amounts equivalent to the respective amounts deposited for the payment of such Bonds and so repaid to the City (without interest thereon).

## **THE TENTH SUPPLEMENTAL TRUST AGREEMENT**

*The following is a summary of certain provisions of the Tenth Supplemental Trust Agreement. This summary does not purport to be complete and is qualified in its entirety by reference to the full terms of the Tenth Supplemental Trust Agreement.*

### **Terms of the Series 2014 Bonds**

The Tenth Supplemental Trust Agreement sets forth the terms of the Series 2014A Bonds, the Series 2014B Bonds, and the Series 2014 C Bonds (collectively, the “2014 Bonds”), most of which are described earlier in the Official Statement under “DESCRIPTION OF THE SERIES 2014 BONDS.”

### **Establishment of Funds**

Certain funds and accounts relevant to the Series 2014 Bonds are established under the Tenth Supplemental Trust Agreement as follows:

2014A Costs of Issuance Fund for the deposit of proceeds from the sale of the Series 2014A Bonds to pay the costs of issuing the Series 2014A Bonds.

2014B Costs of Issuance Fund for the deposit of proceeds from the sale of the Series 2014B Bonds to pay the costs of issuing the Series 2014B Bonds.

2014C Costs of Issuance Fund for the deposit of proceeds from the sale of the Series 2014C Bonds to pay the costs of issuing the Series 2014C Bonds.

2014A Interest Account within the Interest Fund, for the deposit of such amounts as are necessary to make the required payments of interest on the Series 2014A Bonds on each Payment Date.

2014B Interest Account within the Interest Fund, for the deposit of such amounts as are necessary to make the required payments of interest on the Series 2014B Bonds on each Payment Date.

2014C Interest Account within the Interest Fund, for the deposit of such amounts as are necessary to make the required payments of interest on the Series 2014C Bonds on each Payment Date.

2014A Principal Account within the Principal Fund, for the deposit of such amounts as are necessary to make the required payments of principal, if any, of the Series 2014A Bonds on each Payment Date.

2014B Principal Account within the Principal Fund, for the deposit of such amounts as are necessary to make the required payments of principal, if any, of the Series 2014B Bonds on each Payment Date.

2014C Principal Account within the Principal Fund, for the deposit of such amounts as are necessary to make the required payments of principal, if any, of the Series 2014C Bonds on each Payment Date.

2014A Redemption Fund for the deposit of proceeds for the purpose of redeeming the bonds to be refunded by the 2014A Bonds on the date of delivery of the 2014A Bonds, as directed in writing by the City.

2014B Redemption Fund for the deposit of proceeds for the purpose of redeeming the bonds to be refunded by the 2014B Bonds on the date of delivery of the 2014B Bonds, as directed in writing by the City.

2014C Redemption Fund for the deposit of proceeds for the purpose of redeeming the bonds to be refunded by the 2014C Bonds on the date of delivery of the 2014C Bonds, as directed in writing by the City.

2014A Rebate Fund for the deposit of proceeds received from the City for purposes of ultimate rebate to the United States, all as more particularly described in the Tax Certificate related to the 2014A Bonds.

2014B Rebate Fund for the deposit of proceeds received from the City for purposes of ultimate rebate to the United States, all as more particularly described in the Tax Certificate related to the 2014B Bonds.

2014C Rebate Fund for the deposit of proceeds received from the City for purposes of ultimate rebate to the United States, all as more particularly described in the Tax Certificate related to the 2014C Bonds.

The proceeds from the sale of the Series 2014 Bonds are to be deposited into certain of the funds and accounts as set forth in the front of this Official Statement under “PLAN OF REFUNDING” and “ESTIMATED SOURCES AND USES OF PROCEEDS.”

**APPENDIX D**

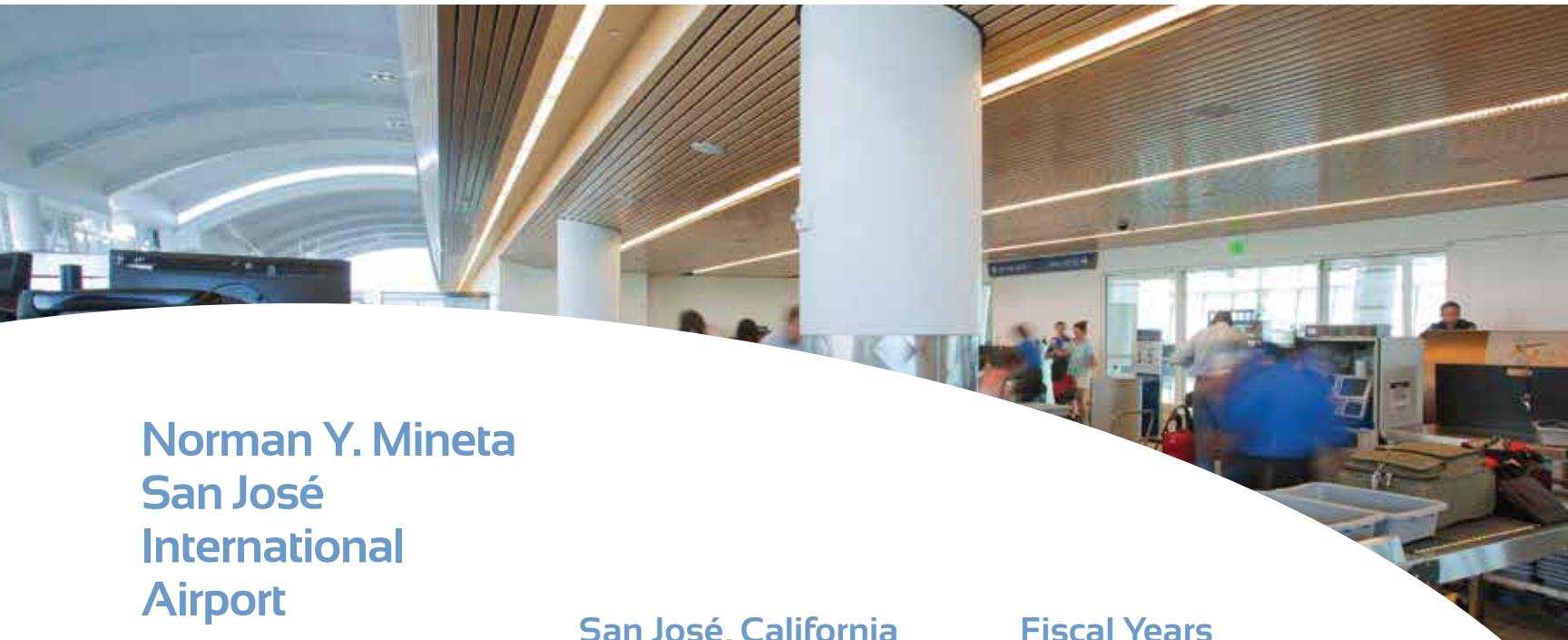
**AUDITED FINANCIAL STATEMENTS OF THE NORMAN Y. MINETA SAN JOSE  
INTERNATIONAL AIRPORT FOR FISCAL YEAR ENDED JUNE 30, 2013**

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# COMPREHENSIVE

## Annual Financial Report



Norman Y. Mineta  
San José  
International  
Airport

San José, California  
A Department of the  
City of San José

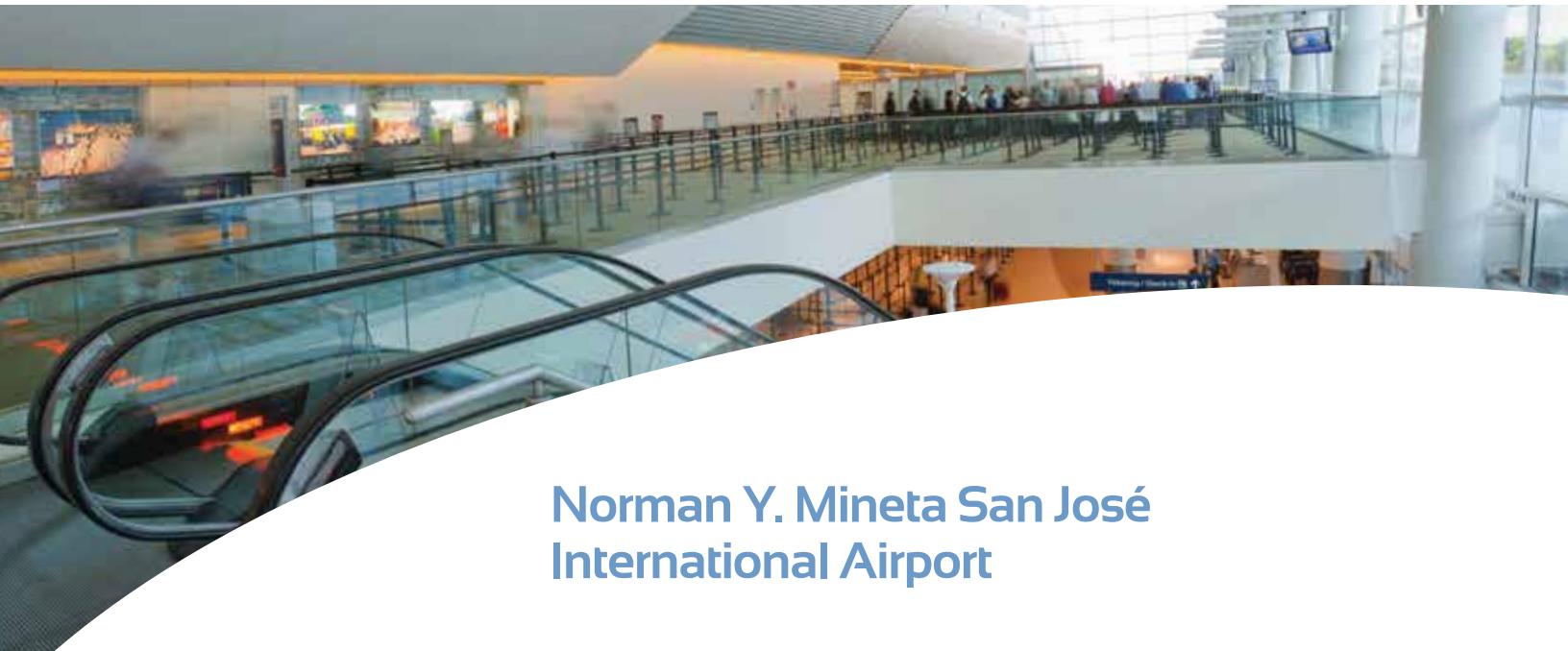
Fiscal Years  
Ended June 30,  
2013 and 2012





# COMPREHENSIVE

## Annual Financial Report



Norman Y. Mineta San José  
International Airport

San José, California  
A Department of the  
City of San José  
  
Fiscal Years  
Ended June 30,  
2013 and 2012

Prepared by:  
Finance and Administration  
  
Terri A. Gomes, CPA  
Deputy Director



**Norman Y. Mineta San José International Airport  
(A Department of the City of San José)  
Comprehensive Annual Financial Report  
Fiscal Year Ended June 30, 2013**

Kim Becker Aguirre  
Director of Aviation

John Aitken  
Acting Assistant Director of  
Aviation & Deputy Director of  
Aviation - Operations

Terri A. Gomes, CPA  
Deputy Director of Aviation  
– Finance & Administration

**Prepared by:  
Airport Department  
Finance & Administration Division - Accounting Section**

Evelyn M. Slotnick  
Principal Accountant

Laura Luu  
Senior Accountant

Steven Lam  
Senior Accountant

Elsa Jacobo  
Senior Accountant

Mary Soo  
Senior Accountant

Kristy Tricoli  
Accountant I

Corrie Konatsu  
Accounting Technician

Peter Romero  
Accounting Technician

Kim Lingenfelter  
Senior Account Clerk

Janet Kuang  
Senior Account Clerk

Claudia Molina  
Senior Account Clerk

Lanie Prestosa  
Senior Account Clerk

**Special Assistance**

Bonnie Cromartie, Finance & Administration  
Division

Sandra Gates, Finance & Administration  
Division

Sylvia Kang, Finance & Administration Division

Dave Maas, Planning & Development  
Division

Danielle Kenealey, City Attorney's Office

Michael Zimmerman, Planning &  
Development Division

Steve McChesney, Public Works Department



# INTRODUCTORY



NORMAN Y. MINETA  
**SAN JOSE**  
INTERNATIONAL  
AIRPORT  
SILICON VALLEY'S AIRPORT

CITY OF  
**SAN JOSE**  
CAPITAL OF SILICON VALLEY

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT  
(A Department of the City of San José)**

**COMPREHENSIVE ANNUAL FINANCIAL REPORT**

**FISCAL YEAR ENDED JUNE 30, 2013**

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**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT  
(A Department of the City of San José)**

**COMPREHENSIVE ANNUAL FINANCIAL REPORT**

**FISCAL YEAR ENDED JUNE 30, 2013**

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# GEO LOCATOR MAP



## Norman Y. Mineta San José International Airport

San José, California  
A Department of the  
City of San José  
Fiscal Years Ended  
June 30, 2013 and 2012

- Primary Service Area
- Secondary Service Area
- ✈ Norman Y. Mineta San José International Airport



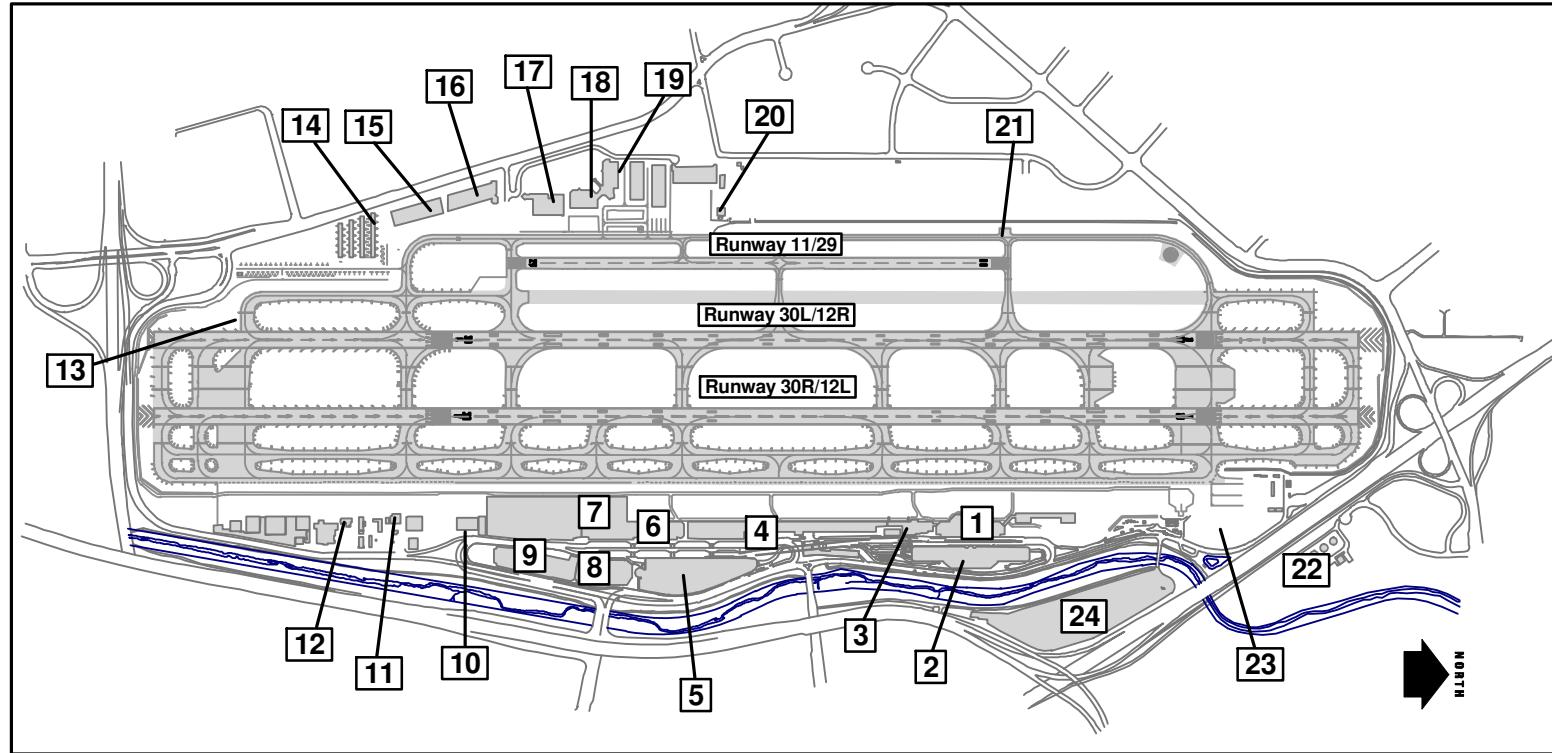
Reduced  
View of  
Service  
Areas



NORMAN Y. MINETA  
**SAN JOSE**  
INTERNATIONAL  
AIRPORT  
SILICON VALLEY'S AIRPORT

CITY OF  
**SAN JOSE**  
CAPITAL OF SILICON VALLEY

# Norman Y. Mineta San José International Airport



## Map Legend

1. Terminal A
2. Terminal A Parking Garage
3. Interim Federal Inspection Services
4. Terminal B
5. Consolidated Rental Car Center
6. Hourly Lot 5
7. Daily Lot 6
8. Hourly Lot 3
9. Daily Lot 4
10. Air Freight
11. Fire Station 20
12. SJPD Airport Division
13. VOR Checkpoint
14. GA West
15. AvBase Aviation
16. ACM
17. HP Aviation (Corporate)
18. FAA-FSDO
19. Atlantic San Jose (Fueling & Transient Services)
20. FAA Air Traffic Control Tower
21. VOR Checkpoint
22. Fuel Farm Location
23. North Air Cargo
24. Economy Lot 1

## LOCATOR MAP

*September 2013*



NORMAN Y. MINETA  
SAN JOSE  
INTERNATIONAL  
AIRPORT



Coordinate System: Airport Grid  
Airfield Elevation: 58' MSL  
Airfield Lat: N37 21.7  
Airfield Long: W121 55.7



November 12, 2013

CITIZENS OF THE CITY OF SAN JOSE  
HONORABLE MAYOR AND CITY COUNCIL

The Comprehensive Annual Financial Report (CAFR) of the Norman Y. Mineta San José International Airport (Airport), a department of the City of San José (City), for the fiscal years ended June 30, 2013 and 2012, is hereby submitted. Responsibility for both the accuracy of the data, and the completeness and fairness of the presentation, including all disclosures, rests with the Airport's management. We believe the data, as presented, is accurate in all material aspects and presented in a manner designed to fairly set forth the financial position and changes in financial position of the Airport, and that all disclosures necessary to enable the reader to gain the maximum understanding of the Airport's financial affairs have been included. This transmittal letter provides a summary of the Airport's background, economic condition and outlook, and major initiatives.

Management's discussion and analysis (MD&A) immediately follows the independent auditor's report and provides a narrative introduction, overview, and analysis of the financial statements. MD&A complement this letter of transmittal and should be read in conjunction with it.

#### **REPORTING ENTITY**

The City Charter created the Airport Department (Department) in 1965 as a department within the City.<sup>1</sup> The City is a charter city that operates under a council-manager form of government. The eleven members of the City Council serve as the governing body that oversees the operation of the Airport. The Director of Aviation is responsible for the operation of the Department and reports directly to the City Manager. The Department operates the Airport, which is currently classified as a medium-hub domestic airport with some international service. The Department's mission is to meet the air transportation needs of the business and public communities in a safe, efficient, and effective manner.

The primary area served by the Airport consists of Santa Clara County, which is also the San José Primary Metropolitan Statistical Area (MSA) and is commonly referred to as Silicon Valley. Furthermore, the primary service area includes the adjacent counties of Monterey, San Benito, and Santa Cruz and portions of two adjacent counties, Alameda and San Mateo (collectively, the "Air Service Area"). The Air Service Area is part of the larger San Francisco/San José/Oakland Area. The nearby counties of Merced, Stanislaus, and San Joaquin comprise a secondary service area. Three of the six Air Service Area counties belong to the Association of Bay Area Governments (ABAG) regional planning agency and rank within the top five most populated counties of the ABAG

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<sup>1</sup> The San José City Charter was put into effect in May of 1965.

Region, with Santa Clara and Alameda Counties ranking first and second, and the County of San Mateo ranking fifth. In addition to the Airport, two other commercial airports serve the San Francisco/San José/Oakland area: San Francisco International Airport and Oakland International Airport. A separate unit of local government operates each of the three facilities independently.

## ECONOMIC CONDITION AND OUTLOOK

Aviation demand nationwide and globally is primarily a function of population and economic growth, developments within the airline industry, and airport and airspace capacity. Airline traffic at airports principally serving origin-destination passengers is most responsive to local economic and population growth. As a predominantly origin-destination, medium-hub airport, the Airport is dependent upon the regional economy, national and international economic conditions, airline service, airfare levels, and population for the passengers who produce its revenue base.

Passenger activity at the Airport increased at a compound annual growth rate of 1.4% between fiscal years 2003 and 2006, the most recent recovery period for the Airport. Since 2006, the Airport had seen a substantial decline in the number of passengers, from 10.9 million in fiscal year 2006 to 8.3 million in fiscal year 2012, which in turn had reduced Airport revenues and resources. Several notable events occurred during this period (both locally and nationwide), most notably a nationwide recession from December 2007 to June 2009, as well as a peak in oil prices, and significant airline capacity cuts at most medium hub airports nationwide. In fiscal year 2013, a total of approximately 8.5 million passengers travelled through the Airport resulting in passenger traffic growth of approximately 2.8%.

In response to the declining activity in recent years, the Airport has taken many steps to reduce its operating budget costs including, among others, (a) elimination of more than 200 positions since 2008, (b) outsourcing of custodial, and parking and traffic control services, (c) relocation of the off-Airport administrative offices, and (d) reductions in police and fire-related costs. By reducing operating costs, the Airport is able to offer services at competitive prices to attract and retain airlines, flights, and passengers. In addition, the Airport has aggressively sought to increase revenues for the past several years. Through its new concessions program, the Airport has increased the number of shops and restaurants in the new terminal, and its contracts with concessionaires require a minimum annual guarantee that results in higher revenues when the new terminal opened. The recently approved lease with Signature Flight Support, to develop and operate a first-class general aviation facility on the west side of the Airport, is estimated to provide \$2.6 million in annual ground rent as well as minimum annual guarantee of \$400,000 for flowage fees.

The City and the Airport continue to work with the Silicon Valley Leadership Group and the San Jose Silicon Valley Chamber of Commerce to help attract new airlines and routes. In an effort to increase service and restore lost flights, the Airport and airports across the nation have been developing and enhancing air service incentive programs. Since its original adoption in 2006, the Airport's incentive program has evolved from a basic one-year waiver for any new route to a flexible program that associates the length of a waiver period to the length of a flight. It also includes incentives for underserved markets, as well as unserved markets and international flights. In addition, on December 1, 2009, the City Council adopted a separate resolution establishing a Focus City Promotional Fee Waiver Incentive Program. This program encourages carriers to increase their overall commitment to the Airport by agreeing to incremental growth in flights for two full consecutive years. A Focus City Airline would agree to add a minimum of four new year-round daily flights to a minimum of at least two unserved cities each year. As a return on investment, these incentive programs will stimulate revenue from parking, concessions, and other Airport services, which will directly offset the short-term loss of revenue from waived airline fees and charges for qualifying new service.

The enhanced incentive programs resulted in additional flights. Past participants included Southwest Airlines with service to Austin, jetBlue Airways with service to Boston, Hawaiian Airlines with service to Kahului (Maui), and Alaska Airlines, with service to Austin, Kona and Kahului (Maui), Lihue (Kauai), and Cabo San Lucas. Virgin America and Delta Airlines, both with service to Los Angeles, and All-Nippon Airways, with service to Tokyo-Narita, are current participants.

### **Population and Income**

The City is the county seat of Santa Clara County. It is the tenth largest city in the United States and the third largest in California behind Los Angeles and San Diego. According to the California Department of Finance estimates, San José has an estimated population of 984,299 as of January 1, 2013, reflecting a growth of 1.5% over the prior year. San José is located in Santa Clara Valley, at the southern end of the San Francisco Bay Area, a region referred to as Silicon Valley. Santa Clara County is the sixth largest county in California and the largest in Northern California. The population of Santa Clara County grew 1.6% from 2012 to 2013, with the population increasing to 1,842,254 as of January 1, 2013. The six counties comprising the primary area for the Airport grew 1.0% from 2012, in line with the State growth rate of 0.8%. In total, the population of the primary area increased by 58,698 from the prior year and accounts for 12.8% of the State's population.<sup>2</sup>

The per capita income information described below is the information available from the Bureau of Economic Analysis as updated on November 26, 2012.

Total personal income and per capita personal income (PCPI) are highly relied upon measures of economic standing. These indicators are a composite measurement of market potential and indicate the general ability to purchase available products or services. As personal income increases, air travel becomes more affordable and can be used more frequently.

According to the U.S. Bureau of Economic Analysis, in 2011 Santa Clara County had a PCPI of \$61,833 and was 142% of the state average of \$43,647, and 145% of the national average of \$42,693, and it ranked 4<sup>th</sup> in the State of California. Within the Air Service Area, the remaining counties personal income and PCPI were as follows:

<b>Personal Income and Per Capita Personal Income within the Air Service Area</b>							
<b>County Name</b>	<b>Personal Income</b> <b>(Millions of Dollars)</b>			<b>Per Capita Personal Income</b> <b>(Dollars)</b>			
	<b>2010</b>	<b>2011</b>	<b>% Change</b>	<b>2010</b>	<b>2011</b>	<b>% Change</b>	<b>2011 Rank</b>
Alameda	\$72,025	\$75,908	5.4%	\$47,603	\$49,617	4.2%	9
Monterey	16,678	17,356	4.1%	40,055	41,138	2.7%	22
San Benito	1,882	1,964	4.4%	33,904	35,029	3.3%	37
San Mateo	47,947	50,597	5.5%	66,629	69,577	4.4%	3
Santa Cruz	12,247	12,920	5.5%	46,586	48,883	4.9%	11
Santa Clara	102,590	111,880	9.1%	57,433	61,833	7.7%	4
California	\$1,564,209	\$1,645,138	5.2%	\$41,893	\$43,647	4.2%	

<sup>2</sup> California Department of Finance

Per capita income increased by 7.7% from 2010 in Santa Clara County compared to an increase of 4.2% and 6.9% for California and the nation, respectively.<sup>3</sup>

## **Employment**

Both the California and U.S. unemployment rates remain high in comparison to pre-recession levels but are on a downward trend. In 2013, the unemployment rate in Santa Clara and San Benito counties declined from the previous year for the second time since 2006. Employment growth in this region had declined sharply after growing at a solid pace between 2006 and 2007. California's economic problems originated in the housing and financial sectors, spread into the consumer economy, and subsequently into the rest of the economy.<sup>4</sup>

Santa Clara County's unemployment rate at June 2013 was 6.8%, with 63,000 unemployed, an increase of 5,600 from May 2013.<sup>3</sup> Likewise, the unemployment rate in the San José-Sunnyvale-Santa Clara MSA was 6.9% in June 2013, up from a revised 6.3% in May 2013, and below the yearago estimate of 8.9%. This compares with an unadjusted unemployment rate of 9.6% in San Benito County, 8.8% for California, and 7.8% for the nation during the same period.<sup>3</sup>

San José-Sunnyvale-Santa Clara MSA	May-2013	Jun-2013	Change	Jun-2012	Jun-2013	Change
	Revised	Prelim			Prelim	
Total Employment Numbers, All Industries	933,500	942,000	8,500	917,100	942,000	24,900
Total Farm	4,800	5,100	300	5,100	5,100	-
Total Nonfarm	928,700	936,900	8,200	912,000	936,900	24,900
Mining and Logging	200	200	-	200	200	-
Construction	37,800	39,500	1,700	35,400	39,500	4,100
Manufacturing	156,300	158,300	2,000	158,900	158,300	(600)
Trade, Transportation & Utilities	131,900	133,900	2,000	130,700	133,900	3,200
Information	51,800	53,000	1,200	50,600	53,000	2,400
Financial Activities	34,200	34,500	300	33,900	34,500	600
Professional & Business Services	188,400	190,200	1,800	181,300	190,200	8,900
Educational & Health Services	122,500	119,500	(3,000)	117,700	119,500	1,800
Leisure & Hospitality	87,900	89,200	1,300	83,200	89,200	6,000
Other Services	24,100	24,600	500	25,200	24,600	(600)
Government	93,600	94,000	400	94,900	94,000	(900)

<sup>3</sup> U.S. Department of Commerce, Bureau of Economic Analysis

<sup>4</sup> Employment Development Department – State of California

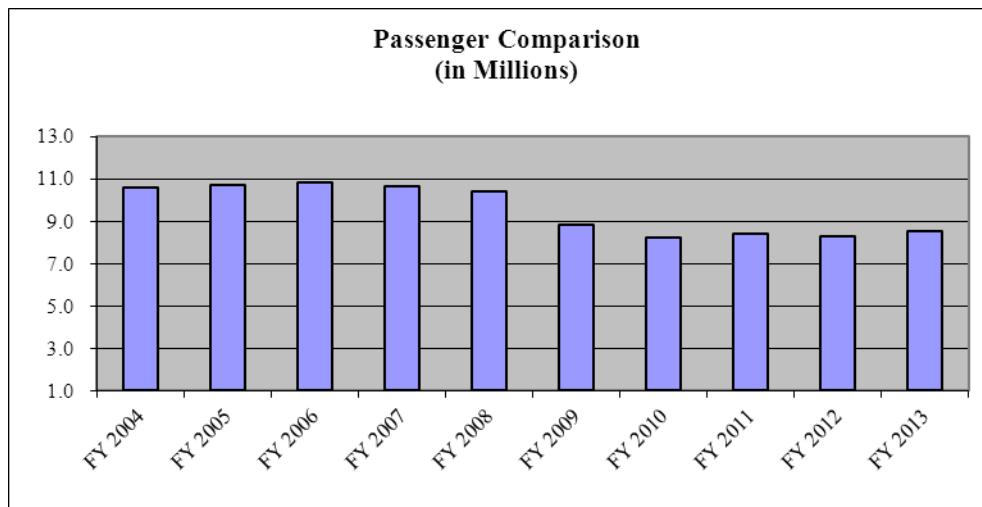
Professional and business services lead the way in posting a monthly increase in jobs on a year-over basis, increasing by 8,900 jobs, while leisure and hospitality increased by 6,000 jobs. Other industries with significant year-over-year job additions included: construction by 4,100 jobs, trade, transportation, and utilities increased 3,200 jobs, and information increased by 2,400 jobs. In contrast, government decreased by 900 jobs from last June.

#### **Norman Y. Mineta San José International Airport: Passenger and Air Traffic**

The Airport is classified as a medium hub airport by the Federal Aviation Administration (FAA) and ranked as the 46<sup>th</sup> busiest airport in the nation in terms of total passengers according to Airports Council International-North America statistics, as of calendar year 2012. As of June 30, 2013, 14 carriers provided scheduled passenger service to 29 destinations, including nine mainline carriers, three regional/commuter carriers, and two international carriers. In addition, two all-cargo carriers provided scheduled cargo service at the Airport.

For FY 2013, the Airport enplaned and deplaned 8.5 million passengers, which represents an increase of 2.8% from the previous fiscal year.

The graph below displays fiscal year-to-date passenger comparison for the last ten fiscal years.



For FY 2013, the Airport experienced an overall increase of 0.4% in traffic operations due to gains in the following categories: passenger carriers (an increase of 1,030 operations or 1.2%) and General Aviation Itinerant (an increase of 1,350 or 5.3%).

### **Airport Master Plan**

In 1997, after extensive planning and environmental studies and reports, the City Council approved a new master plan for the Airport (the “Master Plan”). In a Record of Decision issued on December 6, 1999, the FAA conditionally approved a new Airport Layout Plan (the “ALP”) displaying the Master Plan projects and unconditionally approved all of the near-term projects. Both the Master Plan and the ALP have been amended several times since 1997 and currently are intended to provide facility improvements needed to accommodate forecast demand in the year 2027 for commercial passenger service, air cargo and corporate general aviation demand. The Master Plan includes both the substantially complete Phase 1 and the planned Phase 2 of the Airport Development Program, which collectively comprise improvements to the Airport’s terminal facilities, roadways, parking facilities and airfield facilities and includes 1.075 million square feet of passenger terminal facilities comprised of up to 49 gates; parking and garage facilities comprised of up to 16,200 public parking spaces, 2,600 employee parking spaces and 10,000 rental-car parking spaces (including 2,000 ready-return spaces); air cargo facilities; ground transportation, roadway and other access improvements; and runway improvements. In the fall of 2005, and in recognition of how current market conditions were impacting passenger growth, the Airport and its airline tenants reexamined the Master Plan and developed the Terminal Area Improvement Program, a program for implementing the Master Plan by aligning ongoing and planned construction activities with available fiscal resources, taking into account revised passenger growth projections. In June 2006, the City Council approved an amendment to the Master Plan to incorporate the Terminal Area Improvement Program and other Airport Development Program revisions. In June 2010, the City Council approved an additional amendment to the Master Plan that updated projected aviation demand and facility requirements, and modified specific components of the Airport Development Program. Pursuant to the amended Master Plan, the former interim long-term public parking and employee parking lots on the northwest side of the Airport (which have been relocated to the east side terminal area) will be gradually converted to new general aviation leasehold facilities.

Construction of the Phase 1 projects was substantially complete in FY 2011. The Phase 1 projects included nine new gates and approximately 366,000 square feet of new terminal space; design and construction of the new Terminal B; improvements to the existing Terminal A, including new ticketing facilities, a new in-line baggage system that serves both Terminals A and B and security checkpoint, lobby concessions and other improvements; the phased demolition of Terminal C; design and construction of the Consolidated Rental Car (ConRAC) facility; realignment and improvement of existing terminal roadways; parking improvements; airfield projects, including noise mitigation and the reconstruction of Taxiway Y; and other improvements, including construction of a new belly freight facility and an aircraft rescue and fire fighting facility. Additional program elements of Phase 1 that were completed in FY 2013 included the common use lounge, a taxi staging building, Terminal A/A+ space refurbishment, and building system upgrades. Ongoing projects include Terminal A baggage system ceiling protection, relocation of northeast electrical services, and completion of the northeast area (formerly the rental car fueling and wash site). Construction of the northeast area began in August 2013 and will provide for a fuel truck maintenance facility, shuttle bus staging and storage, and adjacent employee parking. In April 2013, the City completed a request for proposal process to provide for new general aviation aeronautical services facilities on the west side of the Airport and the City Council approved the proposal to award the contract to the successful proposer, Signature Flight Support. It is anticipated that negotiation with Signature will be completed in the fall of 2013 with issuance of a site development permit allowing for the start of construction to follow

in early 2014. Signature will be funding the costs related to this project. Lawsuits were filed by Atlantic Aviation against the City challenging the environmental clearance for the facilities and the selection process in which the City Council awarded the lease to Signature.

Phase 2 projects will consist primarily of the design and construction of the South Concourse of Terminal B and the second phase of Terminal B, including a total of 12 additional gates, and a new central plant facility. Under certain circumstances, the City is required to consult with the Signatory Airlines before proceeding with additional future capital developments. Phase 2 projects are preapproved in the Airline Lease Agreement, but construction of the Phase 2 projects is contingent upon satisfying specified activity based triggers. Pursuant to the terms of the Airline Lease Agreement, the Airport must have either 217 scheduled operations on any one day or 12.2 million enplaned and deplaned passengers in any given fiscal year in order to begin the Phase 2 projects.

## **MAJOR INITIATIVES**

The Airport's mission is to meet the air transportation needs of the business and public communities in a safe, efficient, and effective manner. In concert with the City's move towards a more customer-focused service delivery government, the Airport embraced the following Vision Statements:

*Norman Y. Mineta San José International Airport will be the region's gateway and first choice for air transportation services.*

It will be a place where travelers want to come, and people want to work. It will be easy to get into, around, and out of the Airport. Because the Airport will be an innovator in its use of technology and delivery of services, it will create an exciting environment to visit and use.

*Travelers will feel the anticipation and sense of adventure that air travel should generate.*

Business travelers will have a hassle free experience. Families and leisure travelers will feel their vacation has begun when they arrive at the Airport. People will leave the Airport feeling like guests who have been treated well, and will want to come back.

*The Airport will be a partner with businesses working to drive the regional economy.*

The airlines and other tenants will feel the Airport provides opportunities for their business to succeed.

*The Community will be proud to have the Airport in their midst, seeing it as a good neighbor and understanding its benefits to the region.*

The Airport will be a landmark representing San José and the Silicon Valley.

*The Airport will be a great place to work for all employees.*

The Airport organization will be a place where an individual can enjoy building a career. Each employee will feel they have made a meaningful contribution and their efforts are valued. It will be a place where all employees are recognized for their contributions and where a "can-do" attitude prevails. Norman Y. Mineta San José International Airport will be the employer of choice. Employees will be proud to be a part of the Airport organization and proud to tell their friends and neighbors they are part of this vision.

These Vision Statements are used by the Airport as a guide in making better decisions and sound management practices.

Highlights of the Airport's activities and accomplishments for the fiscal year ended June 30, 2013, include the following:

- Air Service Development

The much anticipated international flight to Narita International Airport in Tokyo on All Nippon Airways (ANA) began on January 11, 2013. Issues with the grounding of all Boeing 787 aircraft temporarily suspended service. ANA resumed the five-weekly flights on June 1 and soon thereafter, announced increased service to daily flights effective July 10, 2013. The Airport became the first local airport to have regularly scheduled international Boeing 787 Dreamliner air service.

A favorite of tech savvy travelers and recently recognized as the nation's best performing airline by the annual Airline Quality Rating, Virgin America launched nonstop service to Los Angeles International Airport with four daily flights. Delta Airlines also resumed service to Los Angeles in June 2013 with four daily nonstop flights. Delta previously served this market until 2008.

In December 2012, Alaska Airlines increased service to both Guadalajara and Cabo San Lucas, Mexico to year-round daily service from the previous three times-weekly and twice-weekly flights, respectively.

- \$82 Million Corporate Aviation Facility to be Built at the Airport

Airport staff is finalizing negotiations on a 50-year lease for Signature Flight Support, a global leader in corporate aviation, to build and operate a private development on 29 acres on the Airport's west side. Signature will service, most notably, the personal aircraft of the principals at Google, as well as other clients in the Silicon Valley business community. Signature will construct a full-service, world-class fixed base operation (FBO) to support based and itinerant corporate and general aviation aircraft operations at the Airport. The 270,000 square foot facility will be LEED gold-certified and include: an executive passenger terminal, seven hangars, ramp space accommodating large business jets and aircraft servicing facilities.

- Taxiway W Grant

The Airport received a \$5.2 million grant from the FAA to fund the fifth phase of construction of the Taxiway W extension. The project will enhance safety and reduce the risk of accidents on the airfield. The long-term plan to complete the new taxiway also will help support the future development of the west side of the Airport for general and corporate aviation services.

- The Club

The Airport and Airport Lounge Development opened *The Club at SJC*, a "common use" VIP lounge open to all airline passengers, on January 10, 2013. By purchasing a day pass for \$35, travelers have access to all the amenities of an airport lounge where they can escape the hustle and bustle of the terminals to work quietly, meet with clients, or freshen up during their journey. Priority Pass members have access to the lounge and some airlines offer their premium class or high-mileage status passengers access, at no additional cost.

- New Taxi Staging Business Facility Now Open at Silicon Valley's Airport

A newly-constructed taxi staging building and associated 1.6 acre parking lot, located at 2470 Airport Boulevard has been opened. This permanent and professional business facility supports the needs of Taxi San Jose (TSJ), the taxi dispatch service contractor, and on-demand taxi and door-to-door shuttle permitted operators. The building is appropriately-sized at 1,900 square feet, and offers basic amenities for TSJ staff and permitted drivers.

- Airport Information at Travelers' Fingertips with the FlySmart App

The Airport launched a smartphone app from FlySmart™ giving customers another reason to choose tech-savvy and customer friendly SJC for their travel plans. The free app (FlySmartapp.com) offers real-time flight notifications and airport information, and features listings for concessions, all available to iPhone, iPad, Android and Blackberry users. The FlySmart app gives travelers free access to information about the Airport and over 100 U.S. and international airports before and during their journey, all at their fingertips via smartphones and tablets. Detailed maps offer quick links to airport driving directions, on-airport parking information, ground transportation options, and terminal layout. Passengers can access the airline directory and visually locate check-in counters, restaurants and shops. Other important features are real-time push alerts to update itinerary changes and departure notifications, as well as the ability to track flight itinerary on one screen, enabling travelers to manage their time more efficiently.

- Faster and Free Wi-Fi for Airport Travelers

The Airport completed an upgrade to the passenger free wi-fi network providing faster speed, new hardware and the elimination of all advertising. Airport travelers can enjoy the fastest and easiest-to-use wi-fi system among U.S. airports. Fast and free wi-fi is offered in all public locations at the Airport. Providing faster and free wi-fi gives high-tech travelers another reason to choose the Airport for their travel plans.

- The First and Only Bay Area Airport to Offer Zipcar

The Airport now offers Zipcar, the world's largest car sharing service. It's easy for the travelers who are Zipcar members to use a car. By simply accessing the Zipcar app or website and reserving a vehicle, travelers can go directly to the reserved Zipcar in Airport's ConRAC facility, located across from Terminal B. Travelers do not have to stop at a counter. Once arriving at the reserved car, travelers can simply use the Zipcard to open the car and drive off. Upon return, travelers return the Zipcar to the same location. The Airport is the first and only airport in the Bay Area to offer this ground transportation service.

- Airport Participates in Golden Guardian 2013 Exercise, Simulating the Response to a Catastrophic Earthquake

Earthquake aftershocks, steel rods protruding from a runway, piles of broken glass inside and outside Terminal B, roadway closures and press briefings are just a few of the many stressful and simulated situations that staff had to contend with as part of the Airport's participation, along with the City of San José, in the statewide Golden Guardian 2013 Exercise held in May 2013. Emergency Operations Centers (EOC) for both the City and the Airport were activated as part of Santa Clara County's biennial participation in this annual state-sponsored exercise. The drill involved the response and recovery during day No. 3 of a catastrophic earthquake along the San Andreas Fault. Numerous Airport staff played a role in the EOC, the simulation cell – where scenario injects were coordinated and disseminated - or the Joint

Information Center (JIC) throughout the day. With the completion of this exercise, the Airport continues to reaffirm its commitments to safety and customer service as the first priorities for passengers and personnel.

- Annual Emergency Tabletop Exercise

The Airport completed its annual emergency tabletop exercise in March 2013, to meet FAA requirements and to evaluate the effectiveness of the Airport Emergency Plan. The scenario involved an air carrier aircraft arriving at the Airport that experienced landing gear failure resulting in injuries to passengers and crew members. Role players included representatives of the Airport Department, San José Fire, San José Police, FAA and an Airport-based airline. The audience included evaluators from other air carrier airports. With the completion of this drill, the Airport has reaffirmed its commitment to safety as the first priority through compliance with Federal Aviation Regulation Part 139 and the Airport Operating Certificate.

- Airport Passes Annual FAA Inspection with Flying Colors

The Airport passed its annual FAA inspection in January with a finding of no discrepancies. The three-day inspection included: a briefing with airport management; an examination of airport records; inspections of the airfield, rescue and firefighting vehicles, and fueling facilities; and a review of night-time safety operations. The FAA performs these operational safety inspections on all commercial service airports each year, and has once again reaffirmed the Airport's commitment to safety as the first priority through compliance with Federal Aviation Regulation Part 139, the Airport Certification Manual, and the Airport Operating Certificate.

- Issuance of Series 2012A Airport Revenue Bonds

In November 2012, the Airport refunded the Series 2002A Bonds in the amount of \$49,140,000 by issuing the Series 2012A Bonds. The Series 2012A bonds were purchased as direct placement with Banc of America Public Capital Corp with an interest rate of 1.53%. The refunding provides approximately \$6,152,462 in aggregate debt service savings or \$5,905,688 on a present value basis.

- Standard & Poor's Affirms Rating for the Airport

Standard & Poor's (S&P) affirmed its underlying rating of "A-" on outstanding senior-lien debt issued by the Airport and maintained an outlook of "stable" on February 27, 2013. S&P cited the strong regional economic base and the Airport's proactive management as credit strengths justifying the "A-" rating. The stable outlook reflects S&P's view that Airport management will be able to maintain adequate liquidity and debt service coverage over the next two years, and that passenger activity will remain constant or improve modestly due to actual and announced additional airline service routes on All Nippon Airways, Delta Air Lines and Virgin America.

- Moody's Revises Rating Outlook to Stable for the Airport

Moody's Investors Service has affirmed the A2 rating on the Airport's general airport revenue bonds, and has revised the rating outlook to stable from negative. The A2 rating is based on a number of factors: The Airport's large and economically diverse service area combined with a strong passenger traffic base, improved financial position achieved through aggressive operating cost reductions, as well as increased revenue from rental car operations, food and beverage and retail concessions, and more revenue anticipated from a new corporate

aviation facility; and a fully funded capital improvement program with no additional planned borrowing. The change in outlook to stable from negative is due to the rating agency's expectation that the number of passengers departing the Airport will continue to stabilize and, in fact, grow due to general economic improvement in the region and actual and announced additional airline service routes, on All Nippon Airways, Delta Air Lines and Virgin America.

- Incentive Reward for the Airlines

The lease agreement with the airlines has a built-in incentive provision, which reduces the Airport's share of indirect overhead expenses allocated to it by the City for support services the City provides to the Airport. Because the operation and management of the Airport are supported by a number of City departments, employees, and resources that are not directly charged to the Airport operating budget, the City allocates a percentage of its total indirect overhead expenses to the Airport operating budget. If in any year during the term of the airline agreement the percentage growth in enplaned passengers at the Airport exceeds the growth in enplaned passengers nationwide (as measured by data published in the FAA Aviation Forecast or similar report/forecast if the FAA Aviation Forecast is no longer available), then the City agrees to reduce the amount of its indirect overhead expenses that would otherwise be allocated to the Airport's operating budget for the next fiscal year by a corresponding percentage.

The Airport's enplanements grew by 2.7% in FY 2013. The FAA projected enplanement growth of 0.0% in FY 2013. As a result, the City will reduce the amount of its indirect overhead expenses allocated to the Airport in FY 2014 by \$419,833.

- Airport Recognized for Marketing Excellence Among Industry Peers

The Airport received a third place award in the Airports Council International – North America (ACI-NA) 2013 Excellence in Marketing and Communications Contest in the *Video & Film Productions* category. SJC: This is the Silicon Valley Opportunity is the Air Service Development video created to showcase the Airport as Silicon Valley's airport of choice, highlight the region as home to many of the world's largest global technology companies within a close proximity of the Airport, and illustrate San José as the gateway to Northern California to new and existing airlines. The video, shared at international air service networking conferences, captures the spirit of Silicon Valley and San José by highlighting the cultural diversity of the area, the global crossroads of high technology and innovation, and world-famous destinations surrounding the Airport.

- Airport Named as a Top 10 Airport Globally Where Travelers Will Welcome a Layover

Mother Nature Network, a website sharing advice on eco-tourism, named the Airport as one of the world's 10 best airports for a layover. Reasons cited for the Airport's distinction as a place that offers passengers plenty to do if stuck for a few hours include: tech-themed art installations throughout the terminals such as the Space Observer, and the competitively-priced *Club at SJC*, the new VIP Lounge open to all passengers and located conveniently between both terminals, which features works of local artists.

- Airport Named Nation's No. 3 Airport for Kids

Travelnerd.com, a blog site dispensing advice on air travel, named the Airport the nation's third best airport for traveling with kids. Reasons cited for this distinction include six dedicated nursing rooms and Airport's free and fast Wi-Fi, allowing kids to entertain themselves on their tech gadgets. The Airport and tenants offer numerous other kid-friendly amenities, including family restrooms; child-friendly restrooms offering diaper changing stations and wall-mounted seats in each stall to secure little ones; the Space Observer and Dreaming F.I.D.S., aka the fish tank, public art works; children's play tables and seating in holdrooms for Southwest Airlines and Alaska Airlines; and Hicklebee's Children's Bookstore within the Authors retail concession in Terminal A.

- Airport Received Transportation Security Administration (TSA) Partnership Award

This award recognized the Airport's accomplishments and excellence in performance that distinctly benefit the interests of the U.S. and clearly advance the TSA's mission to protect the nation's transportation systems while significantly enhancing TSA's ability to achieve its strategic goals.

- The Airport's Concessions Program Recognized by Airport Peers at Industry Conference

The Airport received a third place award in the Best Food & Beverage Program – Medium Airport category at the Airports Council International – North America 2012 Airport Concessions Conference held in Denver in November 2012. The Airport's Terminal B food and beverage concessions program was recognized for aesthetics and the variety of menu items and price points to appeal to a broad audience with varying tastes, requirements and budgets.

- Best On-Time Performance

The Airport is ranked the best airport in California for on-time performance for medium to large size airports, according to data from the Bureau of Transportation Statistics. Oakland ranked 5<sup>th</sup> while San Francisco International Airport (SFO) came in last with the worst on-time performance for airports throughout California. For medium to large size airports in the U.S., the Airport was tied with Minneapolis-St. Paul for fourth overall. Performance rankings of other Bay Area airports included Oakland at 17<sup>th</sup>, Sacramento International at 20<sup>th</sup>, and SFO at 64<sup>th</sup> out of the 65 major airports in the U.S.

- Airport Facilities Division Received National Honor

The Airport's Facilities Division was awarded by the Maintenance Solution Magazine the 2012 Maintenance Solutions Achievement Award in the area of Renovations and Retrofits. The Facilities Division was recognized for their work in upgrading the Airport's central plant operating system during the Airport's modernization program. The central plant operating system is critical in providing cooling, heating, temperature control for building occupants 24 hours a day, seven days a week. The result of the upgrade of the central plant resulted in 170,000kWh less energy consumption, reduced the carbon dioxide output by 173,000 pounds, and provided \$32,000 in cost savings. The Facilities Division was one of two maintenance and facilities departments at a commercial or institutional facility in the U.S. to receive this honor.

## OUTLOOK FOR THE FUTURE

San José's economic development strategy identifies the Airport's role in providing an important infrastructure resource to support the economy. Businesses need Airport infrastructure and services in order to successfully market goods and services. Global economic demands mean that it is critical that Airport infrastructure be developed and services continue to meet emerging needs.

The Airport works in partnership with various City departments, such as the Department of Transportation, Police and Public Works Departments, to improve the transportation systems to benefit the residents of San José as well as support successful business development. These partnerships allow the City to focus coordination efforts on critical transportation projects. The synergy from these efforts is promoted by the Transportation and Aviation City Service Area (CSA), where the Airport Operating Budget is organized and reported.

The mission of the CSA is to provide the community with safe, secure, and efficient surface and air transportation systems that support San José's livability and economic vitality. The following are the Transportation and Aviation Services CSA desired outcomes:

- Provide safe and secure transportation systems
- Provide viable transportation choices that promote a strong economy
- Travelers have a positive, reliable and efficient experience
- Preserve and improve transportation assets and facilities
- Provide a transportation system that enhances community livability

In May 2010, the City Council directed the City Manager and Director of Aviation to take steps necessary to ensure the ability of the Airport to successfully compete for air service and continue to keep costs to airlines at a nationally competitive level. This direction led to a comprehensive Airport Competitiveness Strategy, as well as the development of a standing City Council Committee focused on Airport Competitiveness. The Airport Competitiveness Committee's purpose is to ensure the success of the Airport by: 1) facilitating the implementation of the Airport Competitiveness Strategic Plan; 2) retaining air carriers; and 3) attracting new air service to the Airport.

The need to carefully manage expenditures and reduce ongoing operating costs is especially critical due to the higher debt service costs associated with the new facilities and the limited growth in the number of enplaned passengers. The focus of the direction for the Operating Budget has been on evaluating alternatives for providing Airport services in the most cost-effective manner and implementing those alternative service delivery models that create efficiencies and ongoing savings as well as improve customer service experience.

The 2013-14 Adopted Budget contains several ongoing cost reduction elements. The largest operating savings for 2013-2014 have been accomplished by revisions to the commercial paper-letter of credit program and the associated fees, renegotiation of the on-demand ground transportation dispatch services agreement with allocation of administrative tasks to the contractor rather than the City, and elimination of funding for an airport lounge operator and customer cart delivery services which were implemented in alternative ways. Reductions to utilities budgets for gas and electricity reflect the development of history in operation of the new facilities heating and air conditioning needs. Several years of consistent utility expenditures enables the refinement of budgeted funds.

The Airport continues to analyze and identify other potential cost reduction measures. The long-term key to success is increasing the number of passengers and flights, allowing costs to be distributed over a larger enplanement base thus reducing the cost per enplaned passenger (CPE). City leadership

from the Mayor and Council, with the support from Silicon Valley Leadership Group and the San José Silicon Valley Chamber of Commerce, is actively engaged in efforts to help attract new air carriers and routes. Enplanement growth is the key, not only to making the Airport more price competitive to the airlines, but also increased passengers generate non-airline revenues such as parking fees, concession sales and rental car fees.

Creation of a Business Development Division in the Department supports revenue generation strategies by dedicating staff to explore and develop new revenue sources and pursue air service development strategies to retain and increase airline passengers. The Mayor acknowledged the importance of collaborating with airline partners to achieve successful launches of new service and directed that \$500,000 be used in marketing efforts focused on new flights, destinations and airlines.

Several capital projects currently under development have also been determined to be key elements to the Airport's competitiveness strategy. To accommodate future international air traffic, extension of the Federal Inspection Facility (FIS) Sterile Corridor at Terminal B Gates 17 and 18 provides flexibility to use the gates for domestic flights or supports the simultaneous arrival of multiple international aircraft. Construction of the final Phase of Taxiway W, anticipated for completion around the end of the year, results in a full length parallel taxiway to serve large aircraft operating on the west side of the Airport.

Conservative budget and fiscal policies have led to a surplus for FY 2013. For the fiscal year ended June 30, 2013, Airport's revenues exceeded its expenses and other reserve requirements by \$29.7 million which was \$5.8 million greater than the \$23.9 anticipated and utilized in the preparation of the Adopted 2013-14 Rates and Charges (as computed pursuant to the Airline-Airport Lease and Operating Agreement). The additional \$5.8 million surplus will assist in balancing the budget and achieving the targeted CPE of \$12 in future years.

The Airport's 2014-2018 Adopted Capital Improvement Program (CIP) totals \$280.7 million and reflects a shift in focus from the many projects comprising the Terminal Area Improvement Program (TAIP) to the maintenance and preservation of the Airport infrastructure. Airport staff has been working with the Finance Department, City Attorney's Office, and bond counsel to evaluate legally allowable uses for unspent bond proceeds associated with the 2007A and 2007B bonds. Uses include prospective projects such as completion of projects that were deferred from the original TAIP program due to funding issues during the construction phase of the program. The projects include Terminal A arrivals roadway repairs, Terminal A bag system ceiling protection, and completion of the northeast area (formerly the rental car fueling and wash site). The northeast area will provide for a fuel truck maintenance facility, shuttle bus staging and storage, adjacent employee parking in addition to the completed taxi staging building. The remaining funds are anticipated to be used to maintain the CPE at \$12 for the next five years.

The 2014-2018 Adopted Capital Improvement Program (CIP) provides funding of \$280.7 million, of which \$167.0 million is allocated in FY 2014. The majority of project funding (\$159.6 million) is set aside to pay debt service on outstanding bonds. An additional \$2.4 million funds general non-construction activities, leaving \$87.4 million for capital construction over the next 5 years.

The Airport Capital Program is guided chiefly by the Airport Master Plan. The many projects comprising the \$1.3 billion TAIP are largely complete and the Airport has shifted its focus to the redevelopment of the non-terminal areas, including the Airport's west side.

On April 16, 2013 the City Council authorized the execution of an agreement with a fixed base operator for a 50-year land lease to develop and operate a first-class general aviation facility on 29-

acres of Airport west side property. The proposed development will bring in \$82 million in private capital investment and is expected to generate roughly \$3 million annually in new revenues for the Airport. An additional 15 acres north of the FAA air traffic control tower remains available for future development opportunities. The phased extension of Taxiway W, addresses FAA recommendations on the Airport's Runway Safety Action Plan and is the first step in providing the infrastructure to support development on the Airport's west side. Additional airfield projects are programmed in the out years of the CIP and, like the Taxiway W Improvements project, are contingent upon the receipt of \$31.3 million in FAA grant funding.

Highlights of the Airport's 2014-2018 Adopted CIP are as follows:

#### Airfield Facilities

The Adopted CIP allocates \$34.9 million towards projects that will maintain and improve airfield infrastructure to accommodate the demands for air carrier and general aviation operations. The timing and completion of Airfield improvement projects are largely contingent upon the receipt of AIP grants. Below are the highlights of the Airfield Facilities over the next five years:

- \$11.8 million for the Taxiway W Improvements, which includes the closeout of Phases III and IV and the construction of Phase V, which will construct the final phase of Taxiway W from Taxiway D to Taxiway G. Upon completion, the Airport will have a full length parallel taxiway to serve large aircraft operating on the west side of the Airport. The award of grant funding in the amount of \$5.2 million from the FAA was received in July 2013. The contract was awarded in August 2013.
- \$6.8 million for the design and construction of two cross taxiways at Taxiway E and Taxiway F from Runway 30L to Taxiway V. This project requires environmental clearance.
- \$6.4 million for the design and construction of the extension of Taxiway H from Runway 30L to Taxiway V, and Taxiway K from Taxiway W to Taxiway V to accommodate large aircraft (Group IV taxiways).
- \$3.0 million for the initial implementation of projects on the west side of the Airport that may be necessary once studies to evaluate the existing airfield against new FAA design standards are complete. These projects could include removal of Runway 11-29 and relocation of Taxiway V. If modifications are not needed, this funding would be used to rehabilitate the existing Taxiway V and Runway 11-29.

#### Aviation Support Facilities - General

The Adopted CIP provides \$25.7 million to fund various new infrastructure improvements and to renovate, maintain, or upgrade existing facilities. The largest project in this category, the Airport Rescue and Fire Fighting (ARFF) Facility, is programmed in the final year of the CIP and is dependent upon the receipt of FAA grant funding. The Vehicle Replacement program begins to address deferred replacement of the Airport's aging fleet of vehicles and rolling stock.

Significant projects in Aviation Support Facilities – General are highlighted below:

- \$14 million upgrade of the current ARFF Facility, known as Fire Station 20, to correct building deficiencies, address diversity in the workforce, and increase vehicle capacity and training capabilities. The timing and completion of this project are contingent upon the receipt of grant funding from the FAA.
- \$2.6 million for the Pavement Maintenance that includes repair, replacement, or reconstruction of asphalt and concrete pavement, including striping and markings, at various locations throughout the Airport to meet airfield and roadway safety requirements.
- \$2.4 million for the Operations System Replacement, which includes as needed capital renewal and replacement to maintain various operations' systems throughout the Airport including access control, security, noise and curfew, shared use and parking, revenue systems.
- \$1.6 million for Vehicle Replacement Program. The Airport currently has an aging fleet of 122 vehicles and rolling stock. The average age of the Airport's 92 street legal vehicles is over 15 years old and the acquisition of new and replacement vehicles are needed to maintain a reliable and cost-effective fleet.
- \$1.1 million for Coleman Entrance Landscaping. This project funds approximately 32,000 square feet of landscape at the Coleman Avenue entrance to the Airport in 2017-2018.

#### Passenger Terminal Facilities

A total of \$21.3 million funds various new infrastructure improvements and to maintain, renovate, or upgrade existing facilities, including the deferred maintenance of Airport elevators and the Terminal A Baggage Claim escalators. Significant projects in Passenger Terminal Facilities are highlighted below:

- \$14.2 million is allocated for project close-out and improvements in the northeast quadrant of the campus including fuel truck maintenance facility, shuttle bus staging, employee parking lot and relocation of electrical services.
- \$2.0 million is allocated for terminal building modifications and other minor alterations to accommodate expansions or changes at all Airport buildings and terminals.
- \$1.9 million for the FIS Sterile Corridor Extension to construct a secure interior corridor connecting Terminal B Gates 17 and 18 to accommodate up to three international airport arrivals simultaneously.
- \$1.5 million refurbishment of two escalators located in the Terminal A Baggage Claim area. This project was originally programmed to begin in 2008-2009 but was deferred due to scheduling and limited resources, and will start in 2015-2016.

#### Other Support Facilities and General Non-Construction

Additional funding of \$7.9 million is included in the Adopted CIP for various Aviation Support Environmental and Transportation Facilities, as well as Non-Construction projects. To continue the assessment and clean up of the former fuel farm site, funding of \$1.9 million is included in Aviation Environmental Facilities. Funding of \$1.9 million is also

included for the design and renovation of the Terminal A Ground Transportation Island to increase operational efficiency and to match the appearance of the Terminal B Ground Transportation Island. Funding of \$1.0 million is included in the General Non-Construction to continue the Advanced Planning project which funds preliminary planning, programming, special studies, and surveys for the Airport.

## **FINANCIAL INFORMATION**

The management staff of the Airport is responsible for establishing and maintaining an internal control system designed to safeguard the assets of the Airport from loss, theft, or misuse, and allow the compilation of adequate accounting data for the preparation of financial statements in conformity with accounting principles generally accepted in the United States of America. The internal control system is designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that the cost of a control should not exceed its likely benefits, and that the evaluation of costs and benefits is subject to management estimates and judgments.

### **Single Audit**

As a recipient of federal funds, the Airport is also responsible for providing assurance that an adequate internal control system is in place to ensure compliance with applicable laws and regulations relating to federal award programs. This internal control system is subject to periodic evaluation by management, the City Auditor, and the City's outside independent certified public accountants.

As part of the City's Single Audit procedures, tests are made to determine compliance with the internal control system in place, including those controls relating to Federal award programs, and whether the Airport has complied with all applicable laws and regulations. The City's Single Audit for the year ended June 30, 2013 is still in progress.

The Airport was authorized to impose Passenger Facility Charges (PFCs) effective September 1, 1992. Legislation authorizing the collection of PFCs prescribes reporting and control requirements and restricts the use of PFC revenue to the acquisition of specified assets or payment of PFC eligible debt service. At least annually, during the period in which the PFC is collected, held, or used, the Airport must provide for an audit of its PFC accounts. The audit must be conducted by an independent certified public accountant. The scope of the audit must include evaluation of the Airport's internal accounting controls to account for the collection and use of PFCs. The audit can be performed separately for the PFC account or as part of the Single Audit. For FY 2013, the audit of the Airport's PFC accounts was performed as part of the Single Audit. The audit is complete and there were no noted material weaknesses in the Airport's internal accounting controls or instances of noncompliance with applicable PFC regulations.

### **Budgetary Controls**

Each year, the Airport prepares an operating budget and a capital budget. These documents are presented to the City Council and included in the City's annual appropriated budget. The approved budgets serve as an approved plan to facilitate control and operational evaluation.

The Airport and the City maintain budgetary controls to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the San José City Council. The level of

budgetary control, at which expenses cannot legally exceed the budgeted amount, is at the appropriation level.

The Airport, as with the City, also uses encumbrance accounting as another technique of accomplishing budgetary control of the Airport funds. Purchase commitments are earmarked for particular purposes and become unavailable for general spending.

Appropriations that are not encumbered lapse at the end of the fiscal year. Year-end encumbrances are carried forward and become part of the following year's budget. For budget purposes, expenses are recognized in the year encumbered. For financial statement purposes, expenses are recognized when incurred.

Certain budgetary and fund provisions are stipulated in the Airline–Airport Lease and Operating Agreement and the Master Trust Agreement. Both operating and capital budgets comply with the provisions or restrictions set forth within these agreements.

The Airport continues to meet its responsibility for sound financial management as demonstrated by the statements included in the financial section of this report.

## **OTHER INFORMATION**

### **Independent Audit**

In accordance with Sections 805(a) and 1215 of the City Charter, the annual audit of Airport funds was completed by Macias Gini & O'Connell LLP, Certified Public Accountants for the fiscal year ended June 30, 2013. In addition to meeting the requirements set forth in the City Charter, the City's audit was also designed to meet the requirements of the Federal Single Audit Act Amendments of 1996 and the related Office of Management and Budget Circular A-133. The Airport's federal awards programs are included in the City-wide Single Audit Report. The auditor's report on the Airport's financial statements is included in the financial section of this report.

### **Awards**

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to Norman Y. Mineta San José International Airport for its CAFR for the fiscal year ended June 30, 2012. This was the sixteenth consecutive year that the Airport has achieved this prestigious award. In order to be awarded a Certificate of Achievement, the Airport must publish an easily readable and efficiently organized CAFR. This report must satisfy both accounting principles generally accepted in the United States of America and applicable legal requirements.

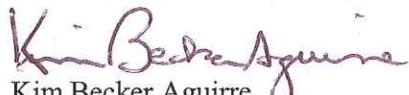
A Certificate of Achievement is valid for a period of one year only. We believe that our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements and we are submitting it to the GFOA to determine its eligibility for another certificate.

### Acknowledgments

The preparation of the CAFR was made possible by the dedicated service and efforts of the Airport's Finance and Administration Division. Each member of the division has our sincere appreciation for the contributions made in the preparation of this report.

In addition, staff in all Airport divisions should be recognized for responding quickly and positively to requests for detailed information which accompany each annual audit. The role of Macias Gini & O'Connell LLP should also be acknowledged as a significant contribution to a fine product.

Respectfully submitted,



Kim Becker Aguirre  
Director of Aviation



Terri A. Gomes, CPA  
Deputy Director  
Finance and Administration Division



Government Finance Officers Association

**Certificate of  
Achievement  
for Excellence  
in Financial  
Reporting**

Presented to

**Norman Y. Mineta  
San Jose International Airport  
California**

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended

**June 30, 2012**

A handwritten signature in black ink that reads "Jeffrey R. Emen". The signature is fluid and cursive, with "Jeffrey" on top and "R. Emen" below it.

Executive Director/CEO

**Norman Y. Mineta San José International Airport**  
**(A Department of the City of San José)**  
**Listing of Principal Officials**  
**June 30, 2013**

**ELECTED OFFICIALS:**

Chuck Reed .....	Mayor
Pete Constant .....	Council Member, District 1
Ash Kalra.....	Council Member, District 2
Sam Liccardo.....	Council Member, District 3
Kansen Chu .....	Council Member, District 4
Xavier Campos.....	Council Member, District 5
Pierluigi Oliverio.....	Council Member, District 6
Madison Nguyen .....	Council Member, District 7
Rose Herrera.....	Council Member, District 8
Donald Rocha .....	Council Member, District 9
Johnny Khamis.....	Council Member, District 10

**AIRPORT COMMISSION:**

Keith Ian Graham.....	Chairperson
Andrés Quintero.....	Vice-Chairperson
E. Ronald Blake.....	Member
AJ Borade.....	Member
Matt Domenici.....	Member
Alain Dussau.....	Member
George Gange.....	Member
Spencer Horowitz.....	Member
Julie Riera Matsushima.....	Member
Stephen McMinn.....	Member
Robert Varich.....	Member
Donald Rocha.....	Council Member, Airport Liaison

**CITY OFFICIAL**

Debra Figone.....	City Manager
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**AIRPORT DEPARTMENT:**

Kim Becker Aguirre.....	Director of Aviation
John Aitken.....	Acting Assistant Director of Aviation & Deputy Director, Operations
Terri A. Gomes, CPA .....	Deputy Director, Finance & Administration
Patrick R. Tonna.....	Deputy Director, Facilities & Engineering
David Maas, P.E.....	Deputy Director, Planning & Development
Cheryl Marcell.....	Deputy Director, Air Service Development
Diane Mack-Williams .....	Division Manager, Airport Technology Services
Jim Webb.....	Assistant to Director, Government Relations
Vicki L. Day.....	Program Manager - Customer Services & Interim Air Service Manager
Rosemary Barnes .....	Public Information Manager
Lieutenant Loyd Kinsworth	San José Police Dept. – Airport Division

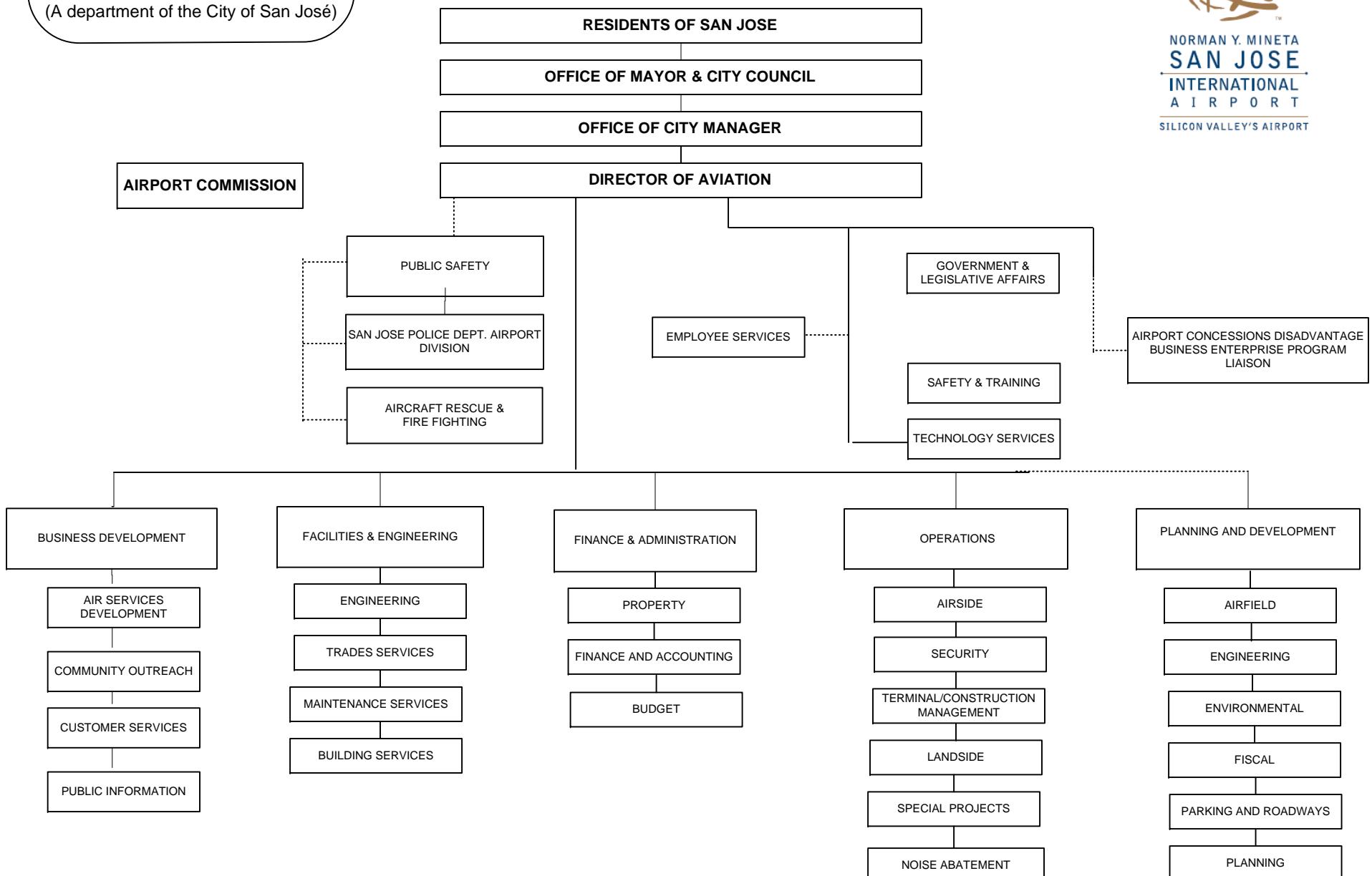


NORMAN Y. MINETA  
**SAN JOSE**  
INTERNATIONAL  
AIRPORT

SILICON VALLEY'S AIRPORT

XXX

NORMAN Y. MINETA SAN JOSE  
INTERNATIONAL AIRPORT  
(A department of the City of San José)





# FINANCIAL



Signature Flight Support, a global leader in corporate aviation, will construct a full service, world class fixed base operation (FBO) to support based and itinerant corporate and general aviation aircraft operations at the Airport.

The 270,000 square foot facility will be LEED gold-certified and include: an executive passenger terminal, seven hangars, ramp space accommodating large business jets, and aircraft servicing facilities.



## **Independent Auditor's Report**

Honorable City Council  
City of San José, California

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Norman Y. Mineta San José International Airport (Airport), a department of the City of San José, California (City), as of and for the fiscal years ended June 30, 2013 and 2012, and the related notes to the financial statements, as listed in the table of contents.

#### ***Management's Responsibility for the Financial Statements***

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

#### ***Auditor's Responsibility***

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

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

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

#### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Airport as of June 30, 2013 and 2012, and the changes in its financial position and its cash flows for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America.

## ***Emphasis of Matters***

### ***Basis of Presentation***

As discussed in Note 1, the financial statements of the Airport are intended to present the financial position, the changes in financial position and, where applicable, cash flows of only that portion of the business-type activities and major fund of the City that is attributable to the transactions of the Airport. They do not purport to, and do not, present fairly the financial position of the City as of June 30, 2013 and 2012, the changes in its financial position, or, where applicable, its cash flows for the fiscal years then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

### ***Changes in Accounting Principles***

As described in Note 1, effective July 1, 2011, the Airport adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position* and GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*. Our opinion is not modified with respect to this matter.

## ***Other Matters***

### ***Required Supplementary Information***

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

### ***Other Information***

Our audits were conducted for the purpose of forming an opinion on the Airport's financial statements. The introductory, statistical and bond disclosure sections are presented for purposes of additional analysis and are not a required part of the financial statements. The introductory, statistical and bond disclosure sections have not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

## ***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated November 12, 2013 on our consideration of the Airport's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters for the fiscal year ended June 30, 2013. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Airport's internal control over financial reporting and compliance.

*Macias Gini & Company LLP*

Walnut Creek, California  
November 12, 2013

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

This section of the Norman Y. Mineta San José International Airport's (Airport) Comprehensive Annual Financial Report (CAFR) presents a narrative overview and analysis of the financial activities of the Airport for the fiscal years ended June 30, 2013 and 2012.

### **AIRPORT ACTIVITIES HIGHLIGHTS**

A total of approximately 8.5 million passengers travelled through the Airport in 2013 compared to approximately 8.3 million in 2012, resulting in passenger traffic growth of 2.8%. The Airport faced a decline of 1.6% in 2012 after experiencing a slight increase in passenger traffic of 1.9% in 2011.

As of June 30, 2013, Airport carriers served 29 nonstop markets with 135 daily departures compared to 29 nonstop markets with 126 daily departures as of June 30, 2012 and 30 nonstop markets with 128 daily departures as of June 30, 2011.

The following shows major air traffic activities at the Airport during the last three fiscal years:

	<u>2013</u>	<u>2012</u>	<u>2011</u>
Flight operations	120,575	120,105	122,091
	0.4%	-1.6%	-7.2%
Landed weight (passenger carriers)	5,213,194	5,125,391	5,221,002
	1.7%	-1.8%	-3.5%
Landed weight (cargo carriers)	248,067	268,748	319,185
	-7.7%	-15.8%	-1.0%
Total enplaned and deplaned passengers	8,488,459	8,256,223	8,389,050
	2.8%	-1.6%	1.9%
Enplaned passengers	4,234,753	4,124,885	4,189,223
	2.7%	-1.5%	2.0%
Deplaned passengers	4,253,706	4,131,338	4,199,827
	3.0%	-1.6%	1.8%
Domestic passengers	8,265,327	8,092,059	8,232,103
	2.1%	-1.7%	1.6%
International passengers	223,132	164,164	156,947
	35.9%	4.6%	21.6%
Cargo tonnage (in tons)	43,184	41,883	47,327
	3.1%	-11.5%	-11.0%
Parking (vehicles) exits	996,029	956,259	1,073,622
	4.2%	-10.9%	7.1%

The Airport continues to offer several air service incentive programs to support the development of new passenger air service at the Airport, including a program aimed at increasing service to unserved or underserved cities (the “New Service Program”), another program aimed at encouraging airlines to add additional service to designated cities (the “Focus City Program”) and a program that reduces the Airport’s share of indirect overhead expenses allocated to it by the City for support services the City provides to the Airport (the “Municipally-Funded Air Service Incentive Program”).

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

As part of the New Service Program, the Director of Aviation designates certain unserved or underserved cities as either qualifying short-haul domestic cities, medium-range domestic or international cities or long-haul international cities. The Director has the authority to change the cities on the list from time to time depending on market conditions, passenger data, market research, route feasibility studies and community feedback. Under the New Service Program, an airline providing new nonstop service between the Airport and an airport in a qualifying short-haul domestic city, medium-range domestic or international city or long-haul international city will receive credits against landing fees, eligible facility rental charges, gate use fees, aircraft parking charges and Airport imposed international passenger processing fees (excluding Passenger Facility Charges) that the airline would otherwise have incurred for the new service, for a promotional period ranging from one to three years from the commencement of the service. All eligible fees are waived during the one-year promotional period for new nonstop service to qualifying short-haul domestic cities. New nonstop service to qualifying medium-range domestic or international cities is eligible for a two-year promotional period, with all eligible fees waived during the first year and fifty percent (50%) of eligible fees waived during the second year of the promotional period. New nonstop service to qualifying long-haul international cities is eligible for a three-year promotional period, with all eligible fees waived during the first year, sixty-six percent (66%) of eligible fees waived during the second year, and thirty-three (33%) of eligible fees waived during the third year. All airlines, including both new and incumbent carriers, are eligible to participate in the program. Past participants have included Southwest Airlines with service to Austin, jetBlue Airways with service to Boston, Hawaiian Airlines with service to Kahului (Maui), and Alaska Airlines with service to Austin, Kona, Kahului (Maui), Lihue (Kauai), and Cabo San Lucas. Virgin America and Delta, both with service to Los Angeles, and All-Nippon Airways, with service to Tokyo-Narita, are current participants. To receive the fee waiver credits, the airline must agree to begin new nonstop service between the Airport and an airport in a qualifying domestic or international city, and the qualifying service must be continuously operated during the length of the promotional period. In addition, an airline will qualify for the fee waiver only if the new service is not offset by a reduction in service by that airline on an existing nonstop route.

The Focus City Program is designed to encourage airlines to add new air service at the Airport. Compared to the New Service Program, the Focus City Program offers longer incentive periods to any airline that designates the City as a focus city and commits to two consecutive years of incremental growth at the Airport, adding a minimum number of new qualifying routes and frequencies. Under the Focus City Program, an airline would qualify for a waiver of fees for two years if it adds at least four flights each year, with at least two of those flights to currently unserved or underserved cities. Additional flights to destinations that are already well served would not receive the fee waiver, but those flights would count toward meeting the remaining Focus City Program incentive threshold of four new flights per year.

The Municipally-Funded Air Service Incentive Program reduces the Airport's share of indirect overhead expenses allocated to it by the City for support services the City provides to the Airport. Because the operation and management of the Airport are supported by a number of City departments, employees, and resources that are not directly charged to the Airport operating budget, the City allocates a percentage of its total indirect overhead expenses to the Airport operating budget. If in any year during the term of the airline agreement the percentage growth in enplaned passengers at the Airport exceeds the growth in enplaned passengers nationwide (as

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

measured by data published in the FAA Aviation Forecast or similar report/forecast if the FAA Aviation Forecast is no longer available), then the City agrees to reduce the amount of its indirect overhead expenses that would otherwise be allocated to the Airport's operating budget for the next fiscal year by a corresponding percentage. The airline agreement also provides that in no event will the City's indirect overhead expenses allocated to the Airport operating budget exceed twenty-five percent (25%) or be less than fifteen percent (15%) during the term of the airline agreement.

### **FINANCIAL HIGHLIGHTS**

The Airport continues to remain vigilant in its efforts to maintain reasonable airline costs and to meet the cost per enplaned passenger of under \$12 as directed by the City Council. The Airport posted a decrease in net position for the 2013 fiscal year.

- Operating revenues decreased by 3.0% from \$127.0 million in 2012 to \$123.1 million in 2013.
- Operating expenses before depreciation and amortization decreased by 11.1% from \$78.8 million in 2012 to \$70.1 million in 2013.
- Operating income before depreciation and amortization increased from \$48.2 million in 2012 to \$53.0 million in 2013.
- Depreciation and amortization increased from \$51.5 million in 2012 to \$54.4 million in 2013.
- The above resulted in operating loss before nonoperating revenues and expenses of \$1.3 million in 2013 and \$3.3 million in 2012.
- Nonoperating expenses, net of nonoperating revenues, increased from \$43.7 million 2012 to \$43.8 million in 2013.
- Capital contributions received in the form of grants from the federal government decreased from \$7.4 million in 2012 to \$7.0 million in 2013.
- Net position was a decrease of \$38.2 million in 2013 compared to a decrease of \$39.6 million in 2012. This was the result of the increases in depreciation and amortization and nonoperating expenses and decreases in operating revenues and capital contributions, offset by the decrease in operating expenses.

In addition, the Airport posted a decrease in net position at the end of 2012 fiscal year.

- Operating revenues increased by 0.5% from \$121.0 million in 2011 to \$127.0 million in 2012.
- Operating expenses before depreciation and amortization decreased by 12.3% from \$89.9 million in 2011 to \$78.8 million in 2012.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

- Operating income before depreciation and amortization increased from \$31.1 million in 2011 to \$48.2 million in 2012.
- Depreciation and amortization was \$51.5 million in both fiscal years.
- The above resulted in operating loss before nonoperating revenues and expenses of \$3.3 million in 2012 and \$20.5 million in 2011.
- Nonoperating expenses, net of nonoperating revenues, increased from \$26.5 million 2011 to \$43.7 million in 2012.
- Capital contributions received in the form of grants from the federal government decreased from \$10.9 million in 2011 to \$7.4 million in 2012.
- Net position was a decrease of \$39.6 million in 2012 compared to a decrease of \$36.1 million in 2011. This was the result of the increases in nonoperating expenses and decrease in capital contributions, offset by the increase in operating revenues and decrease in operating expenses.

### **HIGHLIGHTS IN CHANGES IN NET POSITION**

The following table reflects a condensed summary of the changes in net position (in thousands) for fiscal years ended June 30, 2013, 2012, and 2011:

	<b><u>2013</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
Operating revenues	\$ 123,115	\$ 126,975	\$ 120,963
Operating expenses before depreciation and amortization	<u>(70,074)</u>	<u>(78,802)</u>	<u>(89,904)</u>
Operating income before depreciation and amortization	53,041	48,173	31,059
Depreciation and amortization	<u>(54,353)</u>	<u>(51,520)</u>	<u>(51,532)</u>
Operating loss	<u>(1,312)</u>	<u>(3,347)</u>	<u>(20,473)</u>
Nonoperating revenues and expenses, net	<u>(43,816)</u>	<u>(43,650)</u>	<u>(26,527)</u>
Loss before capital contributions	<u>(45,128)</u>	<u>(46,997)</u>	<u>(47,000)</u>
Capital contributions	<u>6,954</u>	<u>7,399</u>	<u>10,862</u>
Decrease in net position	<u>(38,174)</u>	<u>(39,598)</u>	<u>(36,138)</u>
Net position - beginning, as previously reported	371,077	416,626	452,764
Change in accounting principle	-	(5,951)	-
Net position - beginning, as restated	<u>371,077</u>	<u>410,675</u>	<u>452,764</u>
Total net position - ending	<u>\$ 332,903</u>	<u>\$ 371,077</u>	<u>\$ 416,626</u>

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

### **NET POSITION SUMMARY**

Net position serves over time as a useful indicator of the Airport's financial position. The Airport adopted the provisions of Governmental Accounting Standards Board Statement No. 65, *Items Previously Reported as Assets and Liabilities*, as of July 1, 2011. The Airport restated the July 1, 2011 net position to write off unamortized bond issuance costs previously reported as an asset and included in the deferred amounts on refunding of debt. The 2011 financial statements were not restated.

The Airport's assets plus deferred outflows of resources exceed liabilities plus deferred inflows of resources by \$332.9 million, \$371.1 million, and \$410.7 million at June 30, 2013, 2012 and 2011, respectively, a \$38.2 million decrease from June 30, 2012 to June 30, 2013 and a \$39.6 million decrease from June 30, 2011 to June 30, 2012.

A condensed summary of the Airport's net position (in thousands) at June 30, 2013, 2012 and 2011 is shown below:

	<b><u>2013</u></b>	<b><u>2012</u></b>	<b><u>2011</u></b>
<b>Assets:</b>			
Unrestricted assets	\$ 99,976	\$ 94,842	\$ 70,452
Restricted assets	273,238	291,882	290,294
Capital assets	1,443,362	1,483,245	1,517,327
Other assets	13,016	13,831	12,061
<b>Total assets</b>	<b>1,829,592</b>	<b>1,883,800</b>	<b>1,890,134</b>
<b>Deferred outflow of resources:</b>			
Loss on refundings of debt	698	1,758	-
<b>Liabilities:</b>			
Current liabilities – unrestricted	55,600	59,385	422,312
Current liabilities payable from restricted assets	49,924	41,805	36,543
<b>Noncurrent liabilities</b>	<b>1,389,759</b>	<b>1,413,291</b>	<b>1,020,604</b>
<b>Total liabilities</b>	<b>1,495,283</b>	<b>1,514,481</b>	<b>1,479,459</b>
<b>Deferred inflows of resources:</b>			
Gains on refundings of debt	2,104	-	-
<b>Net position:</b>			
Net investment in capital assets	209,381	242,916	272,598
Restricted	65,408	69,350	64,128
Unrestricted	58,114	58,811	79,900
<b>Net position</b>	<b>\$ 332,903</b>	<b>\$ 371,077</b>	<b>\$ 416,626</b>

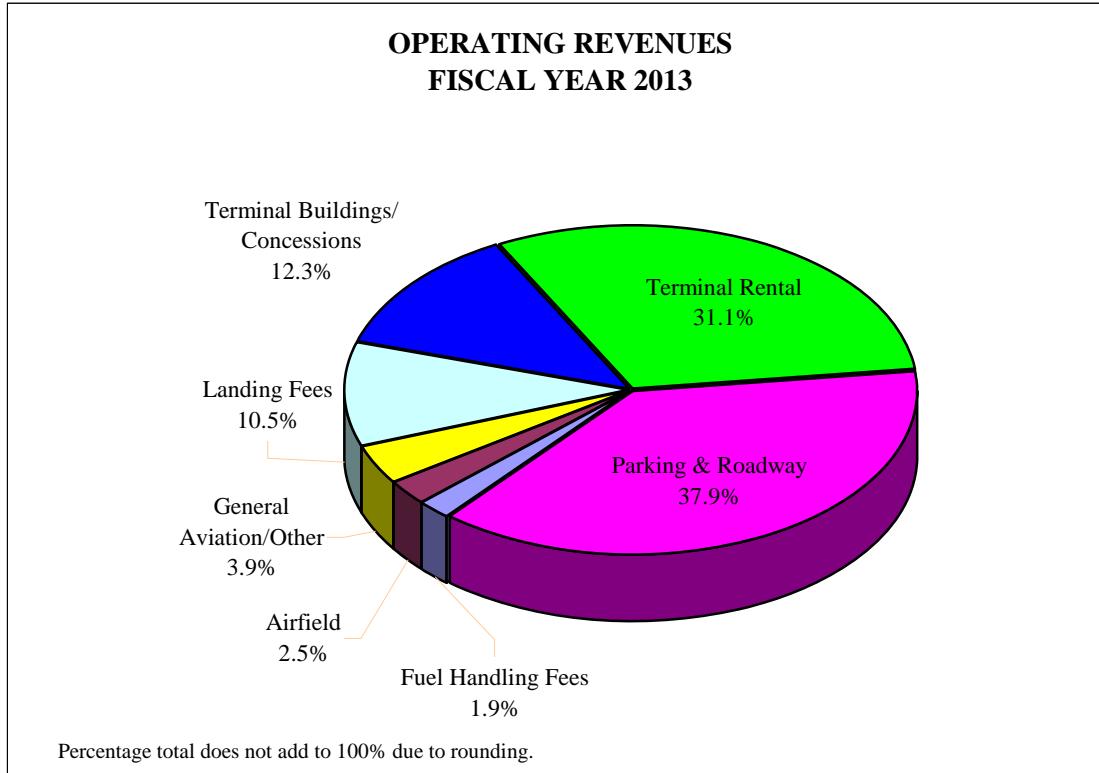
The largest portion, 62.9%, 65.5%, and 66.4% of the Airport's net position at June 30, 2013, 2012, and 2011, respectively, represents its investment in capital assets (e.g. land, buildings, improvements and equipment), less the debt outstanding used to acquire those capital assets. The Airport uses these capital assets to provide services to its passengers and visitors to the Airport; consequently these assets are not available for future spending.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)**

A portion of the Airport's net position represents amounts that are subject to restrictions under the Airline Lease Agreement, the Master Trust Agreement, and the rental car agreement, and passenger facility charges (PFC) and customer facility charges (CFC) that are restricted by Federal regulations and Civil Code §1936, respectively.

### **REVENUES**

The following chart reflects the major sources and the percentage of operating revenues for the fiscal year ended June 30, 2013:



As illustrated in the above chart, parking and roadway revenue represents 37.9% of the total operating revenues. Parking and roadway revenues include public parking, utility and concession fees from rental cars, employee parking, taxicab and other ground transportation fees, and facility and ground rents from rental car companies for use of the Consolidated Rental Car facility (ConRAC) located at the Airport. Facility rent is equal to the sum of annual debt service associated with the ConRAC plus coverage amounts and reserve fund requirements applicable to the ConRAC-related debt service, less revenues from CFCs plus operating costs for any transportation system operated by the Airport to transport passengers between the terminals and the ConRAC facility, plus the City's cost to demolish the previous temporary common use rental car facilities at the Airport, amortized over the initial ten-year term of the agreement. Facility rent will vary each year in relation to changes in any of these amounts.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

The next largest category is airline terminal rental which represents 31.1% of the total operating revenues. Revenues from terminal buildings/concessions, which came in at 12.3% of total operating revenues, include food and beverage, news and gift shops, advertising, and telephony fees. Fees for the use of the Federal Inspection Services (FIS) facility and rental of space, other than airline space, are also included in this category.

Landing fees from passenger and cargo carriers represent 10.5% of the total operating revenues. General aviation/other revenues (3.9%) are comprised of rents for aircraft hangars, aircraft parking spaces, building and land rentals, fingerprinting fees, and fees for tenant plan reviews, which are calculated on a cost recovery basis. The remaining categories, airfield and fuel handling fees represent 2.5% and 1.9%, of the total operating revenues, respectively. The airfield area category is comprised of air carrier parking fees, fees from the in-flight kitchen services, and fees from ground service providers. Fuel handling fees include sales of diesel, unleaded, propane, and compressed natural gases (CNG), as well as jet flowage fees, a fee charged to operators for engaging in the activity of retail sales of aviation fuel petroleum products.

A summary of revenues (in thousands) for the fiscal years ended June 30, 2013, 2012, and 2011 is as follows:

	<u>2013</u>	<u>2012</u>	<u>2011</u>
<b>Operating revenues:</b>			
Landing fees	\$ 12,888	\$ 11,414	\$ 13,370
Terminal rental	38,256	39,864	34,446
Terminal buildings/concessions	15,102	15,770	16,877
Airfield	3,038	2,783	2,925
Parking and roadway	46,700	51,023	47,320
Fuel handling fees	2,361	1,690	1,504
General aviation/other	4,770	4,431	4,521
<b>Total operating revenues</b>	<b><u>123,115</u></b>	<b><u>126,975</u></b>	<b><u>120,963</u></b>
<b>Nonoperating revenues:</b>			
Passenger facility charges	17,294	16,787	17,311
Customer facility charges	13,385	10,137	6,840
Investment income (loss)	(257)	2,217	1,614
Operating grants	565	670	701
Other, net	451	698	1,438
<b>Total nonoperating revenues</b>	<b><u>31,438</u></b>	<b><u>30,509</u></b>	<b><u>27,904</u></b>
<b>Capital contributions</b>	<b><u>6,954</u></b>	<b><u>7,399</u></b>	<b><u>10,862</u></b>
<b>Total revenues</b>	<b><u>\$ 161,507</u></b>	<b><u>\$ 164,883</u></b>	<b><u>\$ 159,729</u></b>

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

### 2013 versus 2012

Total operating revenues decreased by 3.0% from \$127.0 million in 2012 to \$123.1 million in 2013. Growth trends of various revenue categories showed mixed results when compared to the prior year. Terminal rental, terminal building/concessions, and parking and roadway revenues trended lower compared to prior year's performance. The decreases were offset by the increases in landing fees, airfield, fuel handling fees, and general aviation/other revenues.

Terminal rental decreased from \$39.9 million in 2012 to \$38.3 million in 2013. The decrease can be attributed to the lower terminal rental requirement as a result of higher surplus and debt service coverage carried over from the prior fiscal year. Terminal buildings/concessions declined by 4.2% or \$668,000 primarily due to the elimination of the Orange Alert surcharge effective July 1, 2012.

Parking and roadway revenues posted a decrease of 8.5% or \$4.3 million principally due to the significantly lower facility rents from rental car companies for the use of the ConRAC facility which decreased from \$6.7 million in 2012 to \$4.9 million in 2013. Lower facility rents were required from the rental car companies as a result of the higher CFC revenues generated. The decrease can also be attributed to the one-time revenue of \$3.4 million recorded in 2012 relating to the purchase/buyout agreement of 14 compressed natural gas (CNG) powered buses. The Airport had an operating lease contract covering the 14 CNG powered buses that was scheduled to expire on July 31, 2015. In May 2012, the contract was amended to allow the early termination of the lease with the Airport's payment of approximately \$4.4 million. Simultaneously, the Airport entered into an agreement relinquishing the use of the 14 CNG powered buses to a third party for a total price of \$3.4 million to relieve the Airport of its lease commitment. The Airport used the proceeds together with the difference of \$1.0 million to make the early termination payment of \$4.4 million.

Lower parking and roadway revenues can also be attributed to the lower ground transportation revenues, which declined from \$2.9 million in 2012 to \$1.9 in 2013. This was primarily due to the new agreement with the contractor providing on-demand ground transportation dispatch services at the Airport. Under the new agreement, which took effect in January 2013, the contractor is responsible for collecting fees and performing administrative functions directly. The decreases in parking and roadway revenues were partially offset by the \$1.9 million increase in public parking revenues over the prior fiscal year.

Landing fees posted a gain of 12.9% or \$1.5 million principally due to the increase in rate from \$2.14 in 2012 to \$2.38 per thousand pounds of the maximum gross landing weight. Higher ground support and in-flight kitchen concession fees accounted for the increase in airfield revenues by 9.2% or \$255,000. Fuel handling fees went up by 39.7% or \$671,000 boosted by the increases in CNG fuel sales and the jet flowage fees as a result of the increase in flowage fee rate from \$0.10 per gallon to \$0.20 per gallon that took effect in November 2012.

General aviation/other revenues tracked higher by 7.7% or \$339,000 due to the land rental rate adjustments based on increases in appraised values and consumer price index and additional land rental revenues derived from the temporary Westside parking lot leases.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

PFC revenues grew by 3.0% or \$507,000 reflective of the growth in passenger activity. Investment income in 2013 fell substantially lower compared to 2012. Investments posted a decrease in fair value of \$1.0 million as opposed to an increase in fair value of \$1.2 million in 2012. Interest earnings decreased from \$1.1 million 2012 to \$700,000 in 2013 due to lower interest rates.

CFCs are the charges to customers of rental car companies at the Airport in accordance with California Civil Code §1936 to help pay for capital costs and related debt service associated with the ConRAC and certain operating expenses related to the transportation of rental car customers between Terminal A and the ConRAC.

CFC revenues trended 32.0% or \$3.2 million higher than the prior year revenues. The increases were mainly attributed to the 6.9% increase in the number of rental car contracts compared to the prior year and the move to a new fee structure from \$10 per contract to a \$6.00 per day (up to a maximum of five days per rental car contract) which went into effect on December 1, 2011.

The operating grants pertained to grant funds awarded by the Transportation Security Administration (TSA) for the costs associated with the law enforcement officers at security checkpoints (\$252,200), canine security grant from TSA (\$241,500), and a grant from the Bay Area Air Quality Management District for the incremental costs of leasing compressed natural gas buses (\$71,300).

Other nonoperating revenues posted a decrease of 35.4% or \$247,000. The major contributor to this decline was the reversal of the \$296,000 revenue accrued in prior fiscal year related to an audit finding regarding the failure of the advertising concession contractor to expend the minimum capital improvement requirements in certain advertising categories. In October 2012, the City approved an amendment to the agreement which combined the minimum capital investment requirements of the various advertising categories. As a result, the advertising concession contractor is no longer liable for meeting the capital investment threshold for each category.

Capital contributions received during the fiscal year pertained to reimbursement from the FAA of \$7.0 million for the reconstruction of the Taxiway W project.

### 2012 versus 2011

Despite the decline in major airport traffic activities, operating revenues generated in 2012 increased by approximately \$9.3 million or 7.3% over that in 2011. Growth trends were mixed. While revenues grew in the terminal rental, parking and roadway, CFCs, and fuel handling fees, declines were experienced in the landing fees, terminal buildings/concessions, airfield, and general aviation/other revenues.

Terminal rental increased from \$34.4 million to \$39.9 million or an increase of approximately \$5.5 million due to higher terminal rental requirement as a result of the increase in debt service, largely offset by the reduced police service cost.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

Parking and roadway revenues posted a substantial increase of approximately \$3.7 million principally due to a receipt of \$3.4 million relating to the purchase/buyout of 14 compressed natural gas (CNG) powered buses. The increase in parking and roadway revenues was attributed to increases in public parking and rental car activities and the collection of additional revenues of approximately \$354,000 from Fox Rent A Car relating to prior years' concession fee audit adjustments. Ground transportation revenues also increased due to the change in the fee structure for off-airport parking courtesy van operators eliminating the percentage gross revenue fees and increasing the trip fees from \$1.50 per trip (\$1.00 per trip for clean fuel vehicles) to \$7.00 per trip (\$6.00 per trip for clean fuel vehicles). The increases were largely offset by lower facility rents charged to the rental car companies mainly due to the higher CFC revenues collected.

Higher compressed natural gas fuel sales in 2012 accounted for the increase in fuel handling fees by 12.4% or approximately \$186,000.

Landing fees decreased by \$2.0 million or 14.6% due to a variety of factors, including (1) the decrease in rate from \$2.47 to \$2.14 per thousand pounds of the maximum gross landing weight, (2) the termination of two daily flights to Reno by Southwest Airlines, (3) the reduction in American Airlines' flight schedule after its bankruptcy filing, (4) the reduction in routes by United Airlines when its merger with Continental airlines became official in March 2011, and (5) the termination of operations by Air Transportation International in September 2011.

Terminal buildings/concession revenues declined by \$1.1 million or 6.6% due to lower Orange Alert surcharge fees and the reduction of the minimum annual guarantee associated with the closure of the food and retail concessions in Terminal A+.

General aviation/other revenues in 2011 were higher by \$90,000 compared to 2012 due to a one-time billing to San Jose Jet Center in 2011 representing a rent adjustment covering the period November 2008 through March 2011.

PFC revenues declined by approximately \$524,000 or 3% compared to 2011 reflective of the decline in passenger activity.

CFC revenues posted a substantial increase of approximately \$3.3 million or 48.2% over that in 2011 primarily due to the approval of the alternative CFC. In November 2011, the City Council modified the CFC from \$10 per contract to \$6 per day, up to a maximum of five days per rental contract effective December 1, 2011.

Investment income in 2012 increased by approximately \$603,000 or 37.4% compared to 2011. Investments posted an increase in fair value of \$1.2 million in 2012 as opposed to a decline in fair value of \$1.0 million in 2011. The increase is largely offset by the \$1.6 million decrease in interest earnings as a result of lower interest rates.

The operating grants pertained to grant funds awarded by the Transportation Security Administration (TSA) for the costs associated with the law enforcement officers at security checkpoints (\$329,500), canine security grant from TSA (\$242,500), and a grant from the Bay Area Air Quality Management District for the incremental costs of leasing compressed natural gas buses (\$97,600).

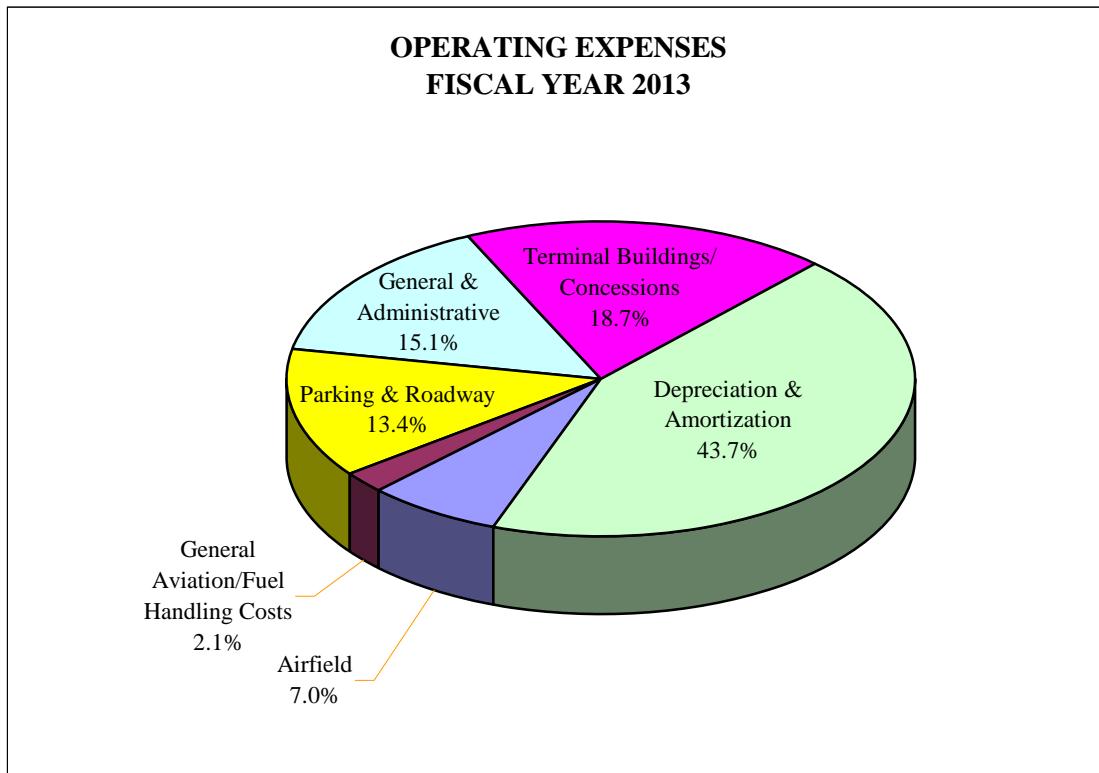
## **MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)**

Other net nonoperating revenues in 2012 were lower than the prior year revenues by \$740,000 or 51.5%. As provided in the operating sublease with City of San José Financing Authority, the Airport received reimbursements in 2011 amounting to \$429,000 representing costs incurred in the development of the Airport West property. Also, in 2011 the General Fund transferred back an amount of \$214,000 representing retiree healthcare contributions initially funded by the Airport. In 2012, the Airport transferred \$115,000 to the General Fund intended for the acquisition of a new payroll system.

Capital contributions received during the fiscal year pertained to reimbursement from the FAA of \$7.3 million for the reconstruction of Taxiway W and for use in the South Apron replacement project. The Airport also received \$81,000 from FAA's Voluntary Low Emissions program for use in retrofitting the gates at the terminals with preconditioned air and 400 Hz ground power to reduce airline engine use while parked at the gate, thereby reducing emissions.

### **EXPENSES**

The following chart reflects the major cost centers as a percentage of operating expenses for the fiscal year ended June 30, 2013:



## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

A summary of expenses (in thousands) for the fiscal years ended June 30, 2013, 2012, and 2011 is as follows:

	<b>2013</b>	<b>2012</b>	<b>2011</b>
<b>Operating expenses:</b>			
Terminal buildings/concessions	\$ 23,303	\$ 23,659	\$ 33,019
Airfield area	8,707	9,069	9,749
Parking and roadway	16,631	25,514	25,344
Fuel handling costs	1,065	556	288
General aviation	1,605	1,676	2,409
General and administrative	18,763	18,328	19,095
Depreciation and amortization	54,353	51,520	51,532
<b>Total operating expenses</b>	<b><u>124,427</u></b>	<b><u>130,322</u></b>	<b><u>141,436</u></b>
<b>Nonoperating expenses:</b>			
Interest expense	75,058	70,009	54,431
Bond issuance costs	196	4,141	-
Loss on capital assets disposal	-	9	-
<b>Total nonoperating expenses</b>	<b><u>75,254</u></b>	<b><u>74,159</u></b>	<b><u>54,431</u></b>
<b>Total expenses</b>	<b><u>\$ 199,681</u></b>	<b><u>\$ 204,481</u></b>	<b><u>\$ 195,867</u></b>

### 2013 versus 2012

Operating expenses in 2013 tracked 4.5% or \$5.9 million lower than the prior fiscal year. Decreases were experienced in nonpersonnel, overhead, and fees charged by the City for police and firefighting services. These were partially offset by increases in expensed capital costs, depreciation and amortization and workers' compensation.

Personnel expenses remained relatively flat compared to the prior fiscal year while overhead reflected a decrease of 4.9% or \$217,000 due to the rate change from 21.97% in 2012 to 21.1% in 2013.

Nonpersonnel expenses in 2013 posted a significant decline of \$8.1 million or 21.2%. The decrease can be attributed to a variety of factors. Nonpersonnel expenses in 2012 included the \$4.4 million buyout payment for the early termination of the lease agreement for the 14 CNG shuttle buses. Due to the early termination of the lease agreement for the 14 CNG buses and the reduced hours for the shuttle bus operator, the Airport saved an additional amount of \$1.1 million. The Airport also issued revenue bonds in December 2011 to refund \$224.7 million of commercial paper (CP) notes thus, resulting in \$2.7 million decline in the letter of credit fees associated with the CP program.

The fees charged by the City for airport rescue and firefighting services (ARFF) were reduced by \$1.4 million as a result of the negotiated matching of costs with outsourced service costs for the full fiscal year versus five months of the prior fiscal year and the capping of overhead at

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

approximately 25% with the balance covered with the Staffing for Adequate Fire and Emergency Response grant.

Workers' compensation costs in 2013 posted an increase of \$551,000 when compared to the prior fiscal year. Workers' compensation costs reflect a combination of the actual claim payments during the fiscal year and the adjustment of liability as of the end of the fiscal year. Actual claim payments amounted to \$383,000 in 2013 and \$554,000 in 2012 while adjustment of the liability amounted to an increase of \$48,000 in 2013 and a decrease of \$674,000 in 2012.

Operating expenses included certain costs for capital projects that did not meet the criteria for capitalization into capital assets. These costs increased from \$2.6 million in 2012 to \$3.4 million in 2013. A major portion of these costs in 2013 pertained to the clean-up of the old fuel tank farms and miscellaneous pavement improvements.

Depreciation and amortization increased by \$2.8 mainly due to assets placed in service, particularly the taxiway project, the taxi staging building, and the lounge. The increase can also be attributed to the cost segregation of systems installed in the terminals totaling \$9.3 million from building to equipment, thus accelerating the depreciation life from 40 to 15 years.

Interest expense in 2013 grew by \$5.0 million due to the fact that the Airport issued airport revenue bonds in the prior fiscal year to refund the \$224.7 million CP notes. The fixed rate bonds have higher interest rates compared to the variable rate CP notes. The CP notes were an interim financing vehicle used during the construction period of the Airport Master Plan. Refunding of CP notes allowed the Airport to mitigate the variable rate exposure and substantially reduce the size of the CP program at a time when market conditions had made it increasingly difficult to obtain credit facilities required to support the CP program.

Bond issuance costs of \$196,000 were paid in 2013 for the issuance of the Series 2012A Airport Revenue Bonds of \$49.1 million. In 2012, the Airport paid \$4.1 million bond issuance costs for the issuance of Series 2011A-1, Series 2011A-2, and Series 2011B Airport Revenue Bonds totaling \$508.6 million.

### 2012 versus 2011

Operating expenses declined by \$11.1 million from \$141.4 million in 2011 to \$130.3 million in 2012. Decreases were experienced in personnel and nonpersonnel expenses, fees charged by the City for police and firefighting services, workers' compensation costs, and expensed capital costs. These were partially offset by the increases in other postemployment benefits (OPEB) costs and overhead.

Personnel expenses in 2012 decreased by approximately \$297,000 due to the wage reductions implemented for all staff and the elimination of seven positions. The decreases were largely offset by higher retirement contributions (excluding OPEB costs), which increased from approximately 25.75% of salary in 2011 to approximately 28.34% in 2012. Overhead expenses increased by \$427,000 due to the rate change from 17.26% in 2011 to 21.97% in 2012.

Nonpersonnel expenses decreased by approximately \$239,000 principally due to the termination of leased space for the off-Airport administrative offices. Staffing levels were reduced to a level

## **MANAGEMENT'S DISCUSSION AND ANALYSIS (Unaudited)**

that made it possible to consolidate all staff on the Airport property. Additionally, lower nonpersonnel expenses were due to decreases in both parking and shuttle bus operator costs. A one-time reimbursement of parking operator costs was paid in 2011 to cover for the delay in the implementation of the new parking control system resulting in the reduction of the year-to-year costs. Also, the new agreement with the parking operator for parking management and in-lot shuttle services took effect on April 1, 2012. The new contract changed the compensation model from paying a percentage of revenues to management fee plus reimbursement of costs, which provides the Airport better control over costs. Shuttle bus costs declined due to several factors including the closure of the long-term lot resulting in shorter routes and the need for fewer buses. Also, an amendment to the shuttle bus service contract took effect on March 1, 2012 changing the compensation structure from a cost per hour of operation to a fixed monthly rate plus a cost per hour of operation allowing the Airport to reduce service hours without impacting the costs. The decreases were largely offset by the \$4.4 million buyout payment for the early termination of the lease agreement for the 14 CNG shuttle buses.

The fees charged by the City for police services were significantly reduced by \$5.3 million as a result of the new staffing model of 11 full-time positions, capping overhead at approximately 25% (versus approximately 45% in the prior year) with the staffing equivalent of 16 police officers funded with overtime which eliminates retirement, fringe, and overhead costs associated with the positions. This revised model was implemented in February 2012. The fees charged by the City for ARFF were also reduced by \$444,000 as a result of the negotiated matching of costs with outsourced service costs for five months of the fiscal year and the capping of overhead at approximately 25% (versus 45% in the prior year).

Expensed capital items decreased from \$8.2 million in 2011 to \$2.6 million. A major portion of these expensed capital items in 2011 pertained to the Terminal C demolition costs of \$6.5 million. Depreciation and amortization remained relatively flat compared to the prior year.

OPEB costs recorded in 2012, based on the latest actuarial study, posted an increase of \$644,000. Workers' compensation costs in 2012 posted a decline of \$321,000 when compared to the prior fiscal year. Workers' compensation costs reflect a combination of the actual claim payments during the fiscal year and the adjustment of liability as of the end of the fiscal year. Actual claim payments amounted to \$554,000 and \$858,000 while reductions of the liability amounted to \$674,000 and \$657,000 in 2012 and 2011, respectively.

### **CAPITAL ACQUISITIONS AND CONSTRUCTION ACTIVITIES**

The Airport expended \$17.5 million and \$20.2 million on both capitalized and noncapitalizable capital activities in fiscal years 2013 and 2012, respectively. Major capital projects in 2013 included the reconstruction of Taxiway W, the construction of the common lounge area, and the taxi staging building. Major capital projects in 2012 included the reconstruction of Taxiway W, public parking improvements, and several TAIP projects, including the parking revenue control system, Terminal A/A+ refurbishment, and terminal equity improvements.

As of June 30, 2013, the Airport was obligated for purchase commitments relating to capital projects of approximately \$4.2 million primarily for the costs of the pavement maintenance, parking revenue control system, and terminal building modifications.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

Detailed information about capital assets can be found in Note 3 to the financial statements.

### **LONG-TERM DEBT**

#### Commercial Paper (CP) Program

The CP debt is a form of variable rate debt with a maturity between 1 to 270 days. As of June 30, 2013 and 2012, the total amount of CP outstanding totaled \$45.4 million and \$47.9 million, respectively. The Airport issued Airport Revenue Bonds in fiscal year 2012 to refund CP notes totaling approximately \$354.2 million. During the fiscal years ended June 30, 2013 and 2012, the Airport paid principal of \$2.6 million and \$7.9 million, respectively. As of June 30, 2013, the CP notes were supported by the \$75 million letter of credit and reimbursement agreement with Wells Fargo Bank, N.A. (WFB).

Additional information about the Airport's commercial paper program can be found in Note 4 to the financial statements.

#### Revenue Bonds

As of June 30, 2013 and 2012, the Airport had total outstanding revenue bonds of \$1,407.0 million and \$1,420.4 million, respectively. During fiscal year 2013, the Airport refunded the Series 2002A Bonds in the amount of \$49,140,000 with the Series 2012A. During fiscal year 2012, the Airport issued a total of \$508.6 million revenue bonds (i) to refund certain variable rate commercial paper notes totaling \$354.2 million, (ii) to refund existing revenue bonds totaling \$92.2 million, (iii) to pay a portion of the cost of issuance of the bonds, and (iv) to make a cash deposit to the General Account of the Bond Reserve Fund. During the fiscal years ended June 30, 2013 and 2012, the Airport paid principal of \$13.4 million and \$21.9 million, respectively.

Additional information about the Airport's long-term debt can be found in Note 5 to the financial statements.

#### Credit Ratings

The underlying ratings of the outstanding Airport Revenue Bonds are "A-", "A2" and "BBB+" by Standard & Poor's (S&P), Moody's Investors Service (Moody's) and Fitch Ratings (Fitch), respectively. The rating outlook of all three rating agencies with respect to the outstanding Airport Revenue Bonds is stable. See Note 5 to the financial statements for a list of outstanding Airport Revenue Bonds.

Additional information about the Airport's credit ratings can be found in the Reporting of Significant Events section of the Bond Disclosure Report.

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

### **AIRLINE RATES AND CHARGES**

The Airport entered into an Airline-Airport Lease and Operating Agreement that took effect on December 1, 2007 with an expiration date of June 30, 2012. In August 2011, the City Council authorized the Director of Aviation to extend the term for five years through June 30, 2017, which allows the airlines to continue to conduct operations and occupy leased space through the extended term. The terminal rate methodology contained in the agreement is based on a compensatory rate-making approach. The average rental rate is calculated annually by dividing the Terminal Revenue Requirement sum by the total amount of rentable terminal space and multiplying the resulting quotient by the total square feet of airline premises at the Airport, yielding the Airline Terminal Revenue Requirement. The airlines' share of any net remaining revenues is credited against the Airline Terminal Revenue Requirement, yielding the Net Airline Terminal Revenue Requirement. The Terminal Revenue Requirement is the sum of expenses allocable to the Terminal for each fiscal year, which include (a) annual debt service funded from bonds or subordinated indebtedness net of any PFC revenues used to pay such debt service, plus (b) debt service coverage, plus (c) annual operating expenses, plus (d) amount needed to replenish the bond reserve fund to required levels, plus (e) the share of annual costs for renewal and replacement, less (f) any grant amounts used to pay debt service, less (g) the debt service coverage for the immediately preceding fiscal year.

The landing fee rate methodology in the agreement is based on a cost center residual rate-making approach. The landing fee is calculated by dividing the Airfield Revenue Requirement by the projected aggregate maximum gross landed weight for all aircraft carrying passengers or cargo in commercial service at the Airport during the fiscal year. The landing fee is expressed in dollars and cents per one thousand pounds in landed weight. The Airfield Revenue Requirement is the sum of expenses allocable to the Airfield for each fiscal year, which include (a) annual debt service funded from bonds or subordinated indebtedness net of any PFC revenues used to pay such debt service, plus (b) debt service coverage, plus (c) annual operating expenses, plus (d) amount needed to replenish the bond reserve fund to required levels, plus (e) the share of annual costs for renewal and replacement, less (f) revenues, other than landing fees, that are accrued for the use of the Airfield, including revenue accrued from landing fee premiums paid by non-signatory airlines, and revenues accrued from charges paid for parking aircraft at common use gates, less (g) any grant amounts used to pay debt service, less (h) the debt service coverage for the immediately preceding fiscal year.

The rates and charges for the signatory (passenger and cargo) airlines for fiscal years 2013 and 2012 were as follows:

	<u>2013</u>	<u>2012</u>
Landing fee (per 1,000 lbs MGLW):	\$2.38	\$2.14
Terminal average rental rate (per square foot)	\$154.65	\$153.20
Airline cost per enplanement (budgeted)	\$11.95	\$11.67

## **MANAGEMENT'S DISCUSSION AND ANALYSIS** **(Unaudited)**

Terminal rental rates and airline landing fees for fiscal year 2014 have been developed as part of the annual budget process. The rates and charges for the signatory airlines for fiscal year 2014, which became effective July 1, 2013, are as follows:

Landing fees (per 1,000 lbs MGLW):	\$2.22
Terminal average rental rates (per square foot)	\$159.72
Airline cost per enplanement (budgeted)	\$11.76

After completion of the year-end closing and annual audit, the Airport achieved savings of approximately \$5.9 million greater than what was anticipated in the preparation of the adopted 2013-14 Airline Rates and Charges. The surplus for 2013 will be allocated in accordance with the revenue sharing provisions of the lease agreement and to meet a cost per enplaned passenger of under \$12 as directed by the City Council.

### **FORWARD-LOOKING STATEMENTS**

When used in this CAFR, the words or phrases "will likely result," "are expected to," "will continue," "is "anticipated, "estimate," "project," "forecast," "expect," "intend" and similar expressions identify "forward-looking statements", but are not the exclusive means of identifying forward-looking statements in the CAFR. Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements. Any forecast is subject to such uncertainties. Inevitably, some assumptions used to develop the forecasts will not be realized and unanticipated events and circumstances may occur. Therefore, there are likely to be differences between forecasts and actual results, and those differences may be material.

Readers are urged not to place undue reliance on these forward-looking statements, which speak only as of the date of this CAFR. The City undertakes no obligation to revise or update any forward-looking statements in order to reflect any event or circumstance that may arise after the date of the CAFR.

### **REQUEST FOR INFORMATION**

This financial report is designed to provide readers with a general overview of the Airport's finances for all those interested. All summaries of documents contained in this CAFR are made subject to the provisions of such documents and do not purport to be complete statements of any or all such provisions. Each reference in this CAFR to a document is qualified in its entirety by reference to such document, which is on file with the Airport or with the City.

Questions concerning any of the information provided in this report or request for additional information should be addressed in writing to the Norman Y. Mineta San José International Airport, 1701 Airport Blvd., Suite B1130, San José, CA 95110 or to the Director of Finance, 200 East Santa Clara Street, San José, California 95113.

**Exhibit I**  
**(Continued)**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**Statements of Net Position**  
**June 30, 2013 and 2012**

	<b>2013</b>	<b>2012</b>
<b>Assets</b>		
Current assets:		
Unrestricted assets:		
Equity in pooled cash and investments held in City Treasury (Note 2)	\$ 91,952,901	86,109,304
Receivables:		
Accounts, net of allowance for uncollectible accounts of \$328,993 in 2013 and \$327,000 in 2012	6,710,286	6,120,618
Accrued interest	140,169	123,146
Grants	995,121	2,303,439
Prepaid expenses, advances, and deposits	177,834	185,509
Total unrestricted assets	<u>99,976,311</u>	<u>94,842,016</u>
Restricted assets:		
Equity in pooled cash and investments held in City Treasury (Note 2)	157,114,165	63,086,628
Investments held by fiscal agent (Note 2)	112,530,817	224,917,435
Receivables:		
Accounts, net of allowance for uncollectible accounts of \$15,000 in 2013 and \$9,000 in 2012	3,368,772	3,497,393
Accrued interest	167,584	174,439
Prepaid expenses, advances, and deposits	844	4,873
Current portion of prepaid bond insurance	56,262	201,420
Total restricted assets	<u>273,238,444</u>	<u>291,882,188</u>
Total current assets	<u>373,214,755</u>	<u>386,724,204</u>
Noncurrent assets:		
Capital assets (Note 3):		
Nondepreciable	99,504,789	117,749,117
Depreciable assets, net of accumulated depreciation	1,343,856,912	1,365,496,169
Total capital assets	<u>1,443,361,701</u>	<u>1,483,245,286</u>
Loan receivable	-	250,000
Advances and deposits	4,980,079	5,331,286
Prepaid bond insurance, less current portion	8,036,016	8,249,210
Total noncurrent assets	<u>1,456,377,796</u>	<u>1,497,075,782</u>
Total assets	<u>1,829,592,551</u>	<u>1,883,799,986</u>
Deferred outflows of resources:		
Loss on refundings of debt	\$ 697,758	1,758,089

See accompanying notes to financial statements.

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**Statements of Net Position**  
**June 30, 2013 and 2012**

	<b>2013</b>	<b>2012</b>
<b>Liabilities</b>		
Current liabilities:		
Payable from unrestricted assets:		
Accounts payable	\$ 3,286,622	3,570,373
Accrued salaries, wages and payroll taxes	423,087	476,599
Accrued vacation, sick leave and compensatory time, current (Note 5)	1,620,000	1,536,000
Advances and deposits payable	1,462,890	1,082,778
Unearned revenue	2,531,852	3,884,992
Estimated liability for self-insurance, current (Note 9)	560,000	560,000
Pollution remediation liability (Note 10 (c))	330,000	330,000
Accrued interest payable	5,229	7,635
Commercial paper notes payable (Note 4)	45,380,000	47,937,000
	<hr/>	<hr/>
Total payable from unrestricted assets	55,599,680	59,385,377
	<hr/>	<hr/>
Payable from restricted assets:		
Accounts payable	1,313,807	401,492
Accrued salaries, wages and payroll taxes	2,800	13,341
Unearned revenue	-	1,585,146
Pollution remediation liability (Note 10 (c))	1,428,657	384,000
Accrued interest payable	24,883,919	25,615,357
Current portion of bonds payable (Note 5)	22,294,734	13,806,084
	<hr/>	<hr/>
Total payable from restricted assets	49,923,917	41,805,420
	<hr/>	<hr/>
Total current liabilities	105,523,597	101,190,797
Noncurrent liabilities:		
Bonds payable, less current portion and net of unamortized discount/premium (Note 5)	1,376,037,499	1,401,745,620
Estimated liability for self-insurance, noncurrent (Note 9)	1,118,773	1,071,245
Other postemployment benefits liability (Note 7)	12,076,469	9,964,282
Accrued vacation, sick leave and compensatory time, noncurrent (Note 5)	526,791	509,695
	<hr/>	<hr/>
Total noncurrent liabilities	1,389,759,532	1,413,290,842
	<hr/>	<hr/>
Total liabilities	1,495,283,129	1,514,481,639
Deferred inflows of resources:		
Gain on refundings of debt	2,103,905	-
	<hr/>	<hr/>
<b>Net Position</b>		
Net investment in capital assets	209,380,615	242,915,928
Restricted:		
Per Airline Lease Agreement for:		
Airline revenue sharing	11,941,879	13,602,840
Per Master Trust Agreement for:		
Rolling debt service coverage	16,547,214	16,175,989
Per Rental Car Agreement	1,000,000	1,000,000
California Civil Code Section 1936 for Customer Facility Charges	2,293,260	-
Future debt service (Note 1 (i))	33,625,852	38,570,899
	<hr/>	<hr/>
Unrestricted	58,114,455	58,810,780
	<hr/>	<hr/>
Total net position	\$ 332,903,275	371,076,436
	<hr/>	<hr/>

See accompanying notes to financial statements.

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**For the Fiscal Years Ended June 30, 2013 and 2012**

	<b>2013</b>	<b>2012</b>
Operating revenues:		
Airline rates and charges:		
Landing fees	\$ 12,888,370	11,413,628
Terminal rental	<u>38,255,624</u>	<u>39,864,277</u>
Total airline rates and charges	51,143,994	51,277,905
Terminal buildings/concessions	15,101,644	15,770,190
Airfield area	3,038,241	2,783,446
Parking and roadway	46,700,448	51,023,465
Fuel handling fees	2,360,463	1,690,326
General aviation/other	<u>4,770,213</u>	<u>4,430,460</u>
Total operating revenues	<u>123,115,003</u>	<u>126,975,792</u>
Operating expenses:		
Terminal buildings/concessions	23,303,388	23,659,488
Airfield area	8,706,904	9,068,812
Parking and roadway	16,631,149	25,513,719
Fuel handling costs	1,064,804	556,312
General aviation	1,605,119	1,676,382
General and administrative	18,763,230	18,327,715
Depreciation and amortization	<u>54,352,406</u>	<u>51,519,769</u>
Total operating expenses	<u>124,427,000</u>	<u>130,322,197</u>
Operating loss	<u>(1,311,997)</u>	<u>(3,346,405)</u>
Nonoperating revenues (expenses):		
Passenger facility charges	17,294,383	16,786,978
Customer facility charges	13,384,764	10,137,053
Investment income (loss)	(257,014)	2,216,540
Interest expense	(75,058,424)	(70,009,305)
Bond issuance costs	(195,581)	(4,140,434)
Operating grants	565,035	669,566
Loss on capital assets disposal	-	(9,452)
Other, net	<u>451,375</u>	<u>698,166</u>
Total nonoperating revenues (expenses), net	<u>(43,815,462)</u>	<u>(43,650,888)</u>
Loss before capital contributions	<u>(45,127,459)</u>	<u>(46,997,293)</u>
Capital contributions		
Change in net position	<u>6,954,298</u>	<u>7,399,056</u>
Net position - beginning, as previously reported	<u>(38,173,161)</u>	<u>(39,598,237)</u>
Change in accounting principle	<u>-</u>	<u>(5,951,453)</u>
Net position - beginning, as restated	<u>371,076,436</u>	<u>416,626,126</u>
Net position - ending	<u>\$ 332,903,275</u>	<u>371,076,436</u>

See accompanying notes to financial statements.

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San Jose)**  
**Statements of Cash Flows**  
**For the Fiscal Years Ended June 30, 2013 and 2012**

	<b>2013</b>	<b>2012</b>
Cash flows from operating activities:		
Receipts from customers and users	\$ 120,162,846	127,868,434
Payments to suppliers	(27,848,807)	(41,752,735)
Payments to employees	(23,995,913)	(25,912,117)
Payments for City services	(13,934,913)	(12,873,615)
Claims paid	(351,214)	(606,059)
Other receipts	<u>451,375</u>	<u>1,207,718</u>
Net cash provided by operating activities	<u>54,483,374</u>	<u>47,931,626</u>
Cash flows from noncapital financing activities:		
Transfers to the City's General Fund	-	(115,010)
Operating grants	<u>887,753</u>	<u>740,443</u>
Net cash provided by noncapital financing activities	<u>887,753</u>	<u>625,433</u>
Cash flows from capital and related financing activities:		
Purchases of capital assets	(14,162,715)	(18,717,036)
Principal payments on bonds payable	(13,440,000)	(21,915,000)
Interest paid	(76,363,006)	(61,775,744)
Capital grants	7,939,898	6,196,466
Passenger facility charges received	17,271,541	16,735,241
Customer facility charges received	13,536,227	9,242,785
Proceeds from bond issuance	49,140,000	504,400,801
Payment for redemption of bonds	(49,140,000)	(92,165,000)
Bond issuance costs paid	(195,581)	(6,775,276)
Principal payments on commercial paper	(2,557,000)	(7,892,000)
Refunded commercial paper	-	(354,250,000)
Advances and deposits received	<u>351,207</u>	<u>594,350</u>
Net cash used in capital and related financing activities	<u>(67,619,429)</u>	<u>(26,320,413)</u>
Cash flows from investing activities:		
Proceeds from sale and maturities of investments	16,443,775	285,216,790
Purchases of investments	(17,435,969)	(300,469,581)
Investment income received	<u>688,259</u>	<u>1,057,481</u>
Net cash used in investing activities	<u>(303,935)</u>	<u>(14,195,310)</u>
Net change in cash and cash equivalents	<u>(12,552,237)</u>	<u>8,041,336</u>
Cash and cash equivalents - beginning	<u>336,257,434</u>	<u>328,216,098</u>
Cash and cash equivalents - ending	<u>\$ 323,705,197</u>	<u>336,257,434</u>

See accompanying notes to financial statements.

**Exhibit III**  
**(Concluded)**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**Statements of Cash Flows**  
**For the Fiscal Years Ended June 30, 2013 and 2012**

	<b>2013</b>	<b>2012</b>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income (loss)	\$ (1,311,997)	(3,346,405)
Adjustment to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	54,352,406	51,519,769
Other revenues	451,375	813,176
Decrease (increase) in:		
Accounts receivable	(589,668)	299,610
Loan receivable	250,000	-
Prepaid expenses, advances, and deposits	172	3,176
Increase (decrease) in:		
Accounts payable and accrued liabilities	3,841,732	(1,610,222)
Advances and deposits payable	380,112	14,789
Unearned revenue	(2,938,286)	912,127
Estimated liability for self-insurance	47,528	(674,394)
Net cash provided by operating activities	<hr/> \$ 54,483,374	<hr/> 47,931,626
Noncash noncapital financing activities:		
Change in operating grants receivable	<hr/> \$ 322,718	<hr/> 70,877
Noncash capital and related financing activities:		
Change in accounts payable related to acquisition of capital assets	19,281	1,132,550
Change in capital grants receivables	985,600	1,202,590
Unrealized gain on investments held by fiscal agent	36,754	961,329
Loss on capital assets disposal	-	(9,452)
Amortization of bond discount/premium	325,387	98,538
Amortization of deferred outflows/inflows of resources	582,270	571,200
Reconciliation of cash and cash equivalents to the statements of net assets		
Equity in pooled cash and investments held in City Treasury		
Unrestricted	\$ 91,952,901	86,109,304
Restricted	157,114,165	63,086,628
Investments held by fiscal agent classified as cash equivalents	<hr/> 74,638,131	<hr/> 187,061,502
Total cash and cash equivalents	<hr/> \$ 323,705,197	<hr/> 336,257,434

See accompanying notes to financial statements.

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
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**Notes to Financial Statements**  
**June 30, 2013 and 2012**

**(1) Summary of Significant Accounting Policies**

***(a) Description of Reporting Entity***

The Norman Y. Mineta San José International Airport had its beginning in 1945 with the lease of approximately 16 acres of farmland to Mr. James Nissen. Mr. Nissen and his associates formed an operating company, which undertook the construction of a 1,900-foot runway, a hangar and an office building. Flight operations were initiated in 1946. In the fall of 1948, the City of San José (the City) assumed responsibility for the operation of San José Municipal Airport, which was renamed San José International Airport in 1984 with the addition of airline service to Canada. In 2001, the San José International Airport was renamed the Norman Y. Mineta San José International Airport (the Airport).

The Airport is operated as a department of the City and is accounted for as a self-supporting enterprise fund in the basic financial statements of the City. The eleven members of the City Council serve as the governing body that oversees the operation of the Airport.

A variety of federal, state and local laws, agreements and regulations govern the operations at the Airport. The Federal Aviation Administration (FAA) has general jurisdiction over flying operations, including personnel, aircraft, ground facilities and other technical matters, as well as certain environmental matters. Pursuant to the Airport and Airway Improvement Act of 1982 and other statutes, the City is constrained from transferring Airport revenues to its General Fund. This restriction is embodied in the federal grant agreements entered into by the City. Additionally, federal laws govern the reasonableness of fees that may be charged for the use of Airport facilities, Airport noise limits, and impose certain other restrictions on the City and Airport operations.

***(b) Basis of Presentation – Fund Accounting***

The accounts of the Airport are organized on the basis of a proprietary fund type, specifically an enterprise fund. The activities of this fund are accounted for with a set of self-balancing accounts that comprise the Airport's assets, deferred outflows of resources, liabilities, deferred inflows of resources, net position, revenues and expenses. Enterprise funds account for activities (i) that are financed with debt that is secured solely by a pledge of the net revenues from fees and charges of the activity; or (ii) that are required by laws or regulations that the activity's cost of providing services, including capital costs (such as depreciation or debt service), be recovered with fees and charges, rather than with taxes or similar revenues; or (iii) where the pricing policies of the activity establish fees and charges designed to recover its costs, including capital costs (such as depreciation or debt service).

***(c) Basis of Accounting and Estimates***

- i. The Airport prepares its financial statements on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America (GAAP), which provide that revenues are recorded when earned and expenses are recorded when incurred. Grants are recorded as revenues when all eligibility

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**June 30, 2013 and 2012**

requirements have been met. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

- ii. Enterprise funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with an enterprise fund's principal ongoing operations. The principal operating revenues of the Airport's enterprise fund are charges to customers for use of property and for services provided. Operating expenses include the cost of services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.
- iii. Under the terms of grant agreements, the Airport funds certain programs with specific cost-reimbursement grants. Thus, when program expenses are incurred, there are both restricted and unrestricted net position available to finance the program. It is the Airport's policy to first apply restricted cost-reimbursement grant resources, if available, to such programs.
- iv. Governmental Accounting Standards Board (GASB) Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, incorporates into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in Financial Accounting Standards Board (FASB) Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the AICPA Committee on Accounting Procedures, which does not conflict with or contradict other GASB pronouncements. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2011. GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*, provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources and renames the resulting measure as net position rather than net assets. The provisions of this statement are effective for financial statements for periods beginning after December 15, 2011. As of July 1, 2011, the Airport adopted the above GASB statements, which did not have a significant impact on its financial statements.
- v. GASB Statement No. 65, *Items Previously Reported as Assets and Liabilities*, clarifies the appropriate reporting of deferred outflows of resources and deferred inflows of resources to ensure consistency in financial reporting. The statement also recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. As of July 1, 2011, the Airport adopted the provisions of GASB Statement No. 65 and restated the beginning net position in the amount of \$5,951,453 to write off unamortized bond issuance costs previously reported as an asset. During fiscal year ended June 30, 2012, the Airport has also written off bond issuance costs included in

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the deferred amounts related to the refunded bonds in the amount of \$1,338,755. In addition, the remaining unamortized loss on refunding in the amount of \$1,758,089 was reclassified from a contra liability to deferred outflows of resources.

**(d) *Cash and Investments***

Cash balances of the Airport, as well as other related entities, are pooled and invested by the City. The Airport's portion of this pool is displayed on the statement of net position as "equity in pooled cash and investments held in City Treasury." Income earned or losses arising from pooled investments are allocated on a monthly basis by the City Treasury to the Airport based on the average weekly cash balances.

The Airport reports its investments in investment agreements at cost and all other investments are reported at fair value in the accompanying financial statements and the corresponding change in fair value of investments is reported in the year in which the change occurred. The Airport has reported its investments at fair value based on quoted market information obtained from fiscal agents or other sources.

Pooled cash and investments in the City Treasury are considered to be cash and cash equivalents for purposes of the accompanying statements of cash flows. Pooled cash and investments represent deposits and investments held in the City's cash management pool. This cash management pool possesses the characteristics of a demand deposit account, therefore, investments in this pool are considered to be cash equivalents. The Airport also considers all highly liquid restricted investments with a maturity of three months or less when purchased to be cash equivalents.

**(e) *Capital Assets***

Capital assets include land, buildings and improvements, equipment, and intangible assets. Capital assets are defined as assets with an initial cost of more than \$5,000 and an estimated useful life in excess of one year. Capital assets are carried at cost. Certain property acquisition costs incurred in accordance with the California Noise Reduction Act have been capitalized in the land account in prior years. The purchase of land included movable structures that had to be removed for the land to be usable for the Airport's purposes.

Intangible assets, which are identifiable, are recorded as capital assets. The Airport has identified certain habitational rights and aviation/relocation easements acquired in connection with the California Noise Reduction Act as intangible assets with indefinite useful lives. Intangible assets not having indefinite useful lives will be amortized over the estimated service capacity of the asset.

Maintenance, repairs, and minor replacements are expended as incurred. Major replacements that extend the useful life of the related assets are capitalized. No depreciation is provided on construction in progress until construction is substantially complete and the asset is placed in service.

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Depreciation of capital assets is computed using the straight-line method at various rates considered adequate to allocate costs over the estimated useful lives of such assets. The estimated lives by general classification are as follows:

	<u>Years</u>
Buildings and improvements	5 – 40
Equipment	4 – 15

***(f) Capitalization of Interest***

Interest costs related to the acquisition of buildings and improvements acquired with tax-exempt debt are capitalized. The amount of interest to be capitalized is calculated by offsetting interest expense incurred from the date of the borrowing until completion of the project, with interest earned on invested debt proceeds over the same period. Capitalized interest cost is prorated to completed projects based on the completion date of each project. The Airport did not capitalize interest during fiscal years ended June 30, 2013 and 2012.

***(g) Bond Issuance Costs, Bond Discounts/Premiums, and Deferred Outflows/Inflows of Resources on Refunding***

Bond issuance costs related to prepaid insurance costs are capitalized and amortized using the effective interest method. Other bond issuance costs are expensed when incurred. Original issue bond discount or premium are offset against the related debt and are also amortized using the effective interest method. Deferred outflows/inflows of resources from refunding of debt are recognized as a component of interest expense using the effective interest method over the remaining life of the old debt or the life of the new debt, whichever is shorter.

***(h) Operating Grants and Capital Contributions***

Certain expenditures for airport capital improvements, airport safety and security operations, are significantly funded through the Airport Improvement Program (AIP) of the FAA and Transportation Security Administration (TSA), with certain matching funds provided by the Airport. Funding provided under government grants is considered earned as the related allowable expenditures are incurred.

Grants awarded by TSA to finance Airport safety and security are reported in the statement of revenues, expenses and changes in net position as nonoperating revenues. Grants for capital asset acquisition, facility development and rehabilitation are reported as capital contributions, after nonoperating revenues and expenses.

***(i) Passenger Facility Charges***

Passenger facility charges (PFCs) are recorded as nonoperating revenue in the year they are collected by the air carriers from the sale of air travel tickets and remitted to the Airport in accordance with Airport regulations. At June 30, 2013 and 2012, accumulated PFC revenues

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amounted to \$33,625,852 and \$38,570,899, respectively, and are reported as restricted for future debt service in the restricted net position category of the Airport's statements of net position.

Under the Airport's Master Trust Agreement, the Airport may for any period elect to designate any PFC revenues as "Available PFC Revenues" by filing with the Fiscal Agent a written statement designating the amount of such Available PFC Revenues and containing a statement that the Available PFC Revenues are legally available to be applied to pay bond debt service during such period. Amounts of \$22,099,631 and \$21,336,421 from accumulated PFC revenues had been designated as Available PFC Revenues for payment of eligible bond debt service in fiscal years ended June 30, 2013 and 2012, respectively.

***(j) Customer Facility Charges***

Customer facility charges (CFCs) are recorded as nonoperating revenues. CFCs are the charges to customers of rental car companies at the Airport in accordance with California Civil Code §1936 to help pay for capital costs and related debt service associated with the ConRAC and certain operating expenses related to the transportation of rental car customers between Terminal A and the ConRAC.

Under the Airport's Master Trust Agreement, the Airport may for any period elect to designate CFC revenues as "Other Available Funds" by filing with the Fiscal Agent a written statement designating the amount of such "Other Available Funds" and containing a statement that the "Other Available Funds" are legally available to be applied to pay debt service on the Series 2011B bonds during such period. CFC revenues of \$13,384,764 and \$10,137,053 had been designated as "Other Available Funds" for payment of eligible bond debt service in fiscal years ended June 30, 2013 and 2012, respectively.

***(k) Accrued Vacation, Sick Leave, and Compensatory Time***

Vested vacation, sick leave, compensatory time, and related benefits are accrued when incurred for all Airport employees.

***(l) Net Position***

The financial statements utilize a net position presentation. Net position is categorized as net investment in capital assets, restricted and unrestricted.

- Net Investment in Capital Assets - This category groups all capital assets, including infrastructure, into one component of net position. Accumulated depreciation and the outstanding balances of debt that are attributable to the acquisition, construction or improvement of these assets reduce the balance in this category.
- Restricted Net Position – This category presents external restrictions imposed by creditors, grantors, contributors or laws or regulations of other governments and restrictions imposed by law through constitutional provisions or enabling legislation.

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At June 30, 2013 and 2012, the Airport's statement of net position reports restricted net position of \$65,408,205 and \$69,349,728, respectively, of which \$35,919,112 and \$38,570,899, respectively, is restricted by enabling legislation.

- Unrestricted Net Position – This category represents the net amount that do not meet the criteria for “restricted” or “net investment in capital assets.”

***(m) New Pronouncements***

The Airport is analyzing its accounting practices and is evaluating the potential impacts on the financial statements of the following GASB Statements.

In March 2012, GASB issued Statement No. 66, *Technical Corrections – 2012 – an amendment of GASB Statements No. 10 and No. 62*. The objective of this statement is to improve accounting and financial reporting by resolving conflicting guidance that resulted from the issuance of GASB Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The requirements of this statement are effective for the Airport's fiscal year ending June 30, 2014.

In June 2012, GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions – an amendment of GASB Statement No. 27*. This statement replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* and Statement No. 50, *Pension Disclosures*, as they relate to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. Statement 68 requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. The Statement also enhances accountability and transparency through revised and new note disclosures and required supplementary information. The requirements of this statement are effective for the Airport's fiscal year ending June 30, 2015.

**(2) Cash and Investments**

The City Council adopted an investment policy (the “Investment Policy”) on April 2, 1985, as amended on August 28, 2012, related to the City’s cash and investment pool, which is subject to annual review. The Investment Policy specifically prohibits trading securities for the sole purpose of speculating or taking an un-hedged position on the future direction of interest rates. Per the Investment Policy the investments conform to Sections 53600 et seq. of the California Government Code and the applicable limitations contained within the Investment Policy.

The Airport invests funds subject to the Investment Policy and provisions of the Airport’s Master Trust Agreement for its various bond issues. According to the City’s Investment Policy and the Airport’s Master Trust Agreement, the Airport is permitted to invest in the City’s cash and investment pool, the State of California Local Agency Investment Fund (LAIF), obligations of the

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U.S. Treasury or U.S. Government Agencies, time deposits, investment agreements, money market mutual funds invested in U.S. Government securities, along with various other permitted investments.

The Airport maintains a portion of its investments in the City's cash and investment pool. As of June 30, 2013 and 2012, the Airport's share of the City's cash and investment pool totaled \$249,067,066 and \$149,195,932, respectively. It is not possible to disclose relevant information about the Airport's separate portion of the cash and investment pool, as there are no specific investments belonging to the Airport itself. Information regarding the characteristics of the entire investment pool can be found in the City's June 30, 2013 Comprehensive Annual Financial Report (CAFR). A copy of that report may be obtained by contacting the City's Finance Department, 200 East Santa Clara Street, 13<sup>th</sup> Floor, San José, CA, 95113 or can be found at the City's Finance Department website at <http://www.csjfinance.org/>.

The Master Trust Agreement authorizes long-term debt (discussed in Note 5) and requires certain amounts of investments to be held in trust by the Airport's trustee (Fiscal Agent) for the bondholders and to be used for repayment of principal and interest on outstanding debt, or to be spent only on authorized capital projects. As of June 30, 2013 and 2012, restricted investments held by the fiscal agent totaled \$112,530,817 and \$224,917,435, respectively. The Master Trust Agreement addresses any limitations in Airport investment of moneys. The investments are subject to certain types of risk, including interest rate risk, credit quality risk, and concentration credit risk. However, the Master Trust Agreement does not specifically address policies for each risk.

Provisions of the Airport's Master Trust Agreement limit the Airport's investment of moneys in Bond Reserve funds to time or demand deposits or permitted investments, which mature not more than five years from the date of investment, except for permitted investments, which, by their terms, permit withdrawal of the entire principal amount of such investment at par without penalty and at such times as required by the Master Trust Agreement. The Master Trust Agreement also limits the investments of moneys held by the City to time or demand deposits in any bank or trust authorized to accept public funds, and shall be secured at all times by such obligations, and to the fullest extent, as is required by law, and may at the written direction of the City be invested in permitted investments, maturing not later than the date on which such moneys are required for payment by the Director of Finance or the Fiscal Agent.

The Airport is a voluntary participant in the California Local Agency Investment Fund ("LAIF") that is governed by the California Government Code under the oversight of the Local Investment Advisory Board ("Board"). The Board consists of five members as designated by state statute. The fair value of the Airport's investment in the LAIF pool is reported in the accompanying financial statements at amounts based upon the Airport's pro rata share of the fair value provided by LAIF, for the entire LAIF portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis, which is different from the fair value of the Airport's position in the LAIF pool. LAIF is part of the State's Pooled Money investment Account (PMIA).

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As of June 30, 2013, the Airport's investments in LAIF held by the Fiscal Agent was \$74,607,188. The weighted average maturity of LAIF at June 30, 2013 was 278 days. The total amount recorded by all public agencies in the LAIF pool at June 30, 2013 was approximately \$21.2 billion. The total amount recorded by all public agencies in PMIA at June 30, 2013 was approximately \$58.8 billion and of that amount, 98.04% was invested in non-derivative financial products and 1.96% in structured notes and asset backed securities.

As of June 30, 2012, the Airport's investments in LAIF held by the Fiscal Agent was \$77,955,313. The weighted average maturity of LAIF at June 30, 2012 was 268 days. The total amount recorded by all public agencies in the LAIF pool at June 30, 2012 was approximately \$21.9 billion. The total amount recorded by all public agencies in PMIA at June 30, 2012 was approximately \$60.5 billion and of that amount, 96.53% was invested in non-derivative financial products and 3.47% in structured notes and asset backed securities.

**Interest Rate Risk** – Interest rate risk is the risk that changes in market rates will adversely affect the fair value of an investment. Generally, the longer the time of maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. Additionally, the fair values of the investments may be highly sensitive to interest rate fluctuations. One of the ways that the City manages its exposure to interest rate risk is by purchasing a combination of shorter-term and longer-term investments and by timing the cash flows from the maturities so that a portion is maturing or coming close to maturing evenly over time, as necessary to provide the cash flow and liquidity needs for operations.

The City has the ability and generally has the intention to hold all investments until their respective maturity dates. The weighted average maturity of the City's pooled cash and investments as of June 30, 2013, was approximately 560 days. The Investment Policy does not prohibit the sale of securities prior to maturity. However, any portfolio restructuring requires prior conceptual approval in writing from the Director of Finance. Section 17.2 of the Investment Policy further defines the parameters with respect to restructuring the portfolio.

**Credit Quality Risk** – Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This risk is measured by the assignment of a rating by the nationally recognized statistical rating organizations. The City's Investment Policy has mitigated credit risk by limiting investments to the safest types of securities, by prequalifying financial institutions, by diversifying the portfolio, and by establishing monitoring procedures.

**Concentration of Credit Risk** – It is not possible to disclose relevant information about the Airport's separate portion of the cash and investment pool, as there are no specific investments in the City's cash and investment pool belonging to the Airport itself. The City's investment policy sets forth the policies regarding concentration of credit risk.

The Investment Policy specifically prohibits trading securities for the sole purpose of speculating or taking an unhedged position on the future direction of interest rates. Per the Investment Policy the investments conform to Sections 53600 et seq. of the California Government Code and the

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applicable limitations contained within the Investment Policy.

The following schedule indicates the interest rate risk and credit risk of the investments held by the Fiscal Agent, by category and maturity, as of June 30, 2013 and 2012. The credit ratings listed are for Moody's Investors Service (Moody's) and Standard & Poor's (S&P), respectively. Certain investments, such as obligations, which are backed by the full faith and credit of the United States government, are not subject to credit ratings.

**As of June 30, 2013**

<u>Type of investments:</u>	Credit <u>Rating</u>	Maturities				Carrying <u>Value</u>
		Under 30 <u>Days</u>	31-180 <u>Days</u>	181-365 <u>Days</u>	1-5 <u>Years</u>	
Investments held by the Fiscal Agent						
Federated treasury obligations fund	Aaa-mf /AAAm	\$ 30,943	-	-	-	\$ 30,943
Federal Farm Credit Bank <sup>(1)</sup>	Aaa/AA+	-	37,892,686	-	-	37,892,686
Local agency investment fund	Not rated	-	-	74,607,188	-	74,607,188
		<u>\$ 30,943</u>	<u>37,892,686</u>	<u>74,607,188</u>	<u>-</u>	<u>\$ 112,530,817</u>

**As of June 30, 2012**

<u>Type of investments:</u>	Credit <u>Rating</u>	Maturities				Carrying <u>Value</u>
		Under 30 <u>Days</u>	181-365 <u>Days</u>	1-5 <u>Years</u>		
Investments held by the Fiscal Agent						
Federated treasury obligations fund	Aaa-mf /AAAm	\$ 109,106,189	-	-	-	\$ 109,106,189
Federal Farm Credit Bank <sup>(1)</sup>	Aaa/AA+	-	-	-	37,855,933	37,855,933
Local agency investment fund	Not rated	-	-	77,955,313	-	77,955,313
		<u>\$ 109,106,189</u>	<u>77,955,313</u>	<u>37,855,933</u>	<u>-</u>	<u>\$ 224,917,435</u>

(1) Investments with these issuers represent more than 5% of the Airport's investments held by the fiscal agent.

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**(3) Capital Assets**

Capital asset activities for the fiscal years ended June 30, 2013 and 2012, were as follows:

	Balance at July 1, 2012	Additions	Retirements	Transfers	Balance at June 30, 2013
Capital assets not depreciated:					
Land	\$ 75,781,265	-	-	-	75,781,265
Intangible assets	12,881,547	-	-	-	12,881,547
Construction in progress	29,086,305	13,157,460	-	(31,401,788)	10,841,977
Total capital assets, not depreciated	<u>117,749,117</u>	<u>13,157,460</u>	<u>-</u>	<u>(31,401,788)</u>	<u>99,504,789</u>
Capital assets, depreciated:					
Buildings	1,148,507,775	133,361	-	(6,295,783)	1,142,345,353
Other improvements	550,469,657	8,851	-	28,182,822	578,661,330
Equipment	44,579,134	843,763	(215,512)	9,514,749	54,722,134
Total capital assets, depreciated	<u>1,743,556,566</u>	<u>985,975</u>	<u>(215,512)</u>	<u>31,401,788</u>	<u>1,775,728,817</u>
Less accumulated depreciation					
Buildings	163,759,703	29,293,272	-	-	193,052,975
Other improvements	182,265,510	18,496,513	-	-	200,762,023
Equipment	32,035,184	6,237,235	(215,512)	-	38,056,907
Total accumulated depreciation	<u>378,060,397</u>	<u>54,027,020</u>	<u>(215,512)</u>	<u>-</u>	<u>431,871,905</u>
Total capital assets, depreciated, net	<u>1,365,496,169</u>	<u>(53,041,045)</u>	<u>-</u>	<u>31,401,788</u>	<u>1,343,856,912</u>
Total capital assets, net	<u>\$ 1,483,245,286</u>	<u>(39,883,585)</u>	<u>-</u>	<u>-</u>	<u>1,443,361,701</u>

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	Balance at June 30, 2011	Additions	Retirements	Transfers	Balance at June 30, 2012
Capital assets not depreciated:					
Land	\$ 75,781,265	-	-	-	75,781,265
Intangible assets	12,881,547	-	-	-	12,881,547
Construction in progress	19,770,461	16,590,236	-	(7,274,392)	29,086,305
Total capital assets, not depreciated	<u>108,433,273</u>	<u>16,590,236</u>	<u>-</u>	<u>(7,274,392)</u>	<u>117,749,117</u>
Capital assets, depreciated:					
Buildings	1,143,670,119	889,728	-	3,947,928	1,148,507,775
Other improvements	547,143,193	-	-	3,326,464	550,469,657
Equipment	45,514,525	104,521	(1,039,912)	-	44,579,134
Total capital assets, depreciated	<u>1,736,327,837</u>	<u>994,249</u>	<u>(1,039,912)</u>	<u>7,274,392</u>	<u>1,743,556,566</u>
Less accumulated depreciation					
Buildings	133,675,422	30,084,281	-	-	163,759,703
Other improvements	164,687,631	17,577,879	-	-	182,265,510
Equipment	29,070,832	3,994,812	(1,030,460)	-	32,035,184
Total accumulated depreciation	<u>327,433,885</u>	<u>51,656,972</u>	<u>(1,030,460)</u>	<u>-</u>	<u>378,060,397</u>
Total capital assets, depreciated, net	<u>1,408,893,952</u>	<u>(50,662,723)</u>	<u>(9,452)</u>	<u>7,274,392</u>	<u>1,365,496,169</u>
Total capital assets, net	<u>\$ 1,517,327,225</u>	<u>(34,072,487)</u>	<u>(9,452)</u>	<u>-</u>	<u>1,483,245,286</u>

The Airport's depreciation expense on capital assets was \$54,027,020 and \$51,656,972 for fiscal years ended June 30, 2013 and 2012, respectively.

#### (4) Commercial Paper Notes Payable

In November 1999, the City Council authorized the issuance of the City of San José, Norman Y. Mineta San José International Airport subordinated commercial paper. In March 2008, the City Council further authorized the subordinated commercial paper notes to be issued in an aggregate principal amount of up to \$600 million outstanding at any one time.

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

As of June 30, 2013, the commercial paper notes program is secured by a \$75 million letter of credit (LOC) provided by Wells Fargo Bank, N.A. (WFB). The LOC will expire on March 13, 2014. The terms of the credit facility are specified in the LOC and Reimbursement Agreement (the "Reimbursement Agreement"). In general, WFB agrees to advance funds to the issuing and paying agent in an amount sufficient to pay the principal and interest due on maturing commercial paper notes in an amount not to exceed the stated amount of the related LOC. In the event that the commercial paper dealer is unable to find investors to purchase commercial paper notes to repay the advance from the bank, the City must pay interest to the bank based on a formula specified in

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the Reimbursement Agreement and repay principal in accordance with the schedule and terms set forth in the Reimbursement Agreement and Term Loan. Additionally, WFB has a separate fee letter to specify the commitment fee payable by the City and the other fees and charges imposed by the bank related to the issuance of its LOC. The initial facility rate was established based on the underlying credit rating on the Airport's bonds. The facility fee rate can increase at any time when a rating is withdrawn, suspended or otherwise unavailable and upon occurrence of an event of default or rating downgrade. In July 2012, Fitch Ratings (Fitch) downgraded its rating with respect to the outstanding Airport Revenue Bonds from "A-" with negative outlook to "BBB+" with stable outlook. As a result, the facility rate charged by WFB increased to 1.65% effective July 20, 2012. The facility fee rates are 1.65% and 1.40% as of June 30, 2013 and 2012, respectively.

In July 2011, the Airport issued general airport revenue bonds to refund \$129,578,000 subordinated commercial paper notes that were originally issued to refund the Series 2004A and Series 2004B Airport Revenue Bonds (see note 5). In December 2011, the Airport issued general airport revenue bonds to refund \$224,672,000 subordinated commercial paper notes that were originally issued to fund the costs of the ConRAC (see note 5).

Commercial paper activities for the fiscal years ended June 30, 2013 and 2012 were as follows:

	<b>2013</b>	<b>2012</b>
Beginning balance	\$ 47,937,000	410,079,000
Refunded	-	(354,250,000)
Paid	(2,557,000)	(7,892,000)
Ending balance	<u>\$ 45,380,000</u>	<u>47,937,000</u>

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Balances of commercial paper notes payable as of June 30, 2013 and 2012 were as follows:

As of June 30, 2013

Series A-2 commercial paper notes maturing on December 4, 2013 were issued with an interest rate of 0.17%	\$ 11,992,000
Series B commercial paper notes maturing on December 4, 2013 were issued with an interest rate of 0.18%	13,045,000
Series C commercial paper notes maturing on September 17, 2013 were issued with an interest rate of 0.25%	<u>20,343,000</u>
Total commercial paper notes payable	<u>\$ 45,380,000</u>

As of June 30, 2012

Series A-2 commercial paper notes maturing on September 11, 2012 were issued with an interest rate of 0.19%	\$ 12,683,000
Series B commercial paper notes maturing on September 11, 2012 were issued with an interest rate of 0.19%	13,937,000
Series C commercial paper notes maturing on September 12, 2012 were issued with an interest rate of 0.47%	<u>21,317,000</u>
Total commercial paper notes payable	<u>\$ 47,937,000</u>

Although the commercial paper notes have short-term maturities, the Airport's intent is to pay the remaining balance on a long-term basis based on the assumption that the outstanding commercial paper notes will be paid on a 30-year amortization period with the first principal payments paid in fiscal year 2011.

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**(5) Long-Term Obligations**

Airport Revenue Bonds are issued primarily to finance the construction of capital improvements at the Airport. Pursuant to the Master Trust Agreement, the City has irrevocably pledged the general airport revenues and certain other funds held or made available under the Master Trust Agreement, first to the payment of maintenance and operation costs of the Airport, and second to the payment of principal of and premium, if any, and interest on the bonds. General airport revenues generally include all revenues, income, receipts and moneys derived by the City from the operation of the Airport with the exception of certain expressly excluded revenues.

The net revenues available to pay debt service in fiscal year ended June 30, 2013 totaled \$126,031,022, which is composed of \$60,025,263 of net general airport revenues and \$66,005,759 of other available funds. Other available funds include surplus carryover of \$30,642,898, rolling debt service coverage of \$16,175,989, CFC revenues of \$13,384,764, and unspent Series 2004 and Series 2007B bond proceeds of \$1,383,389 and \$4,418,719, respectively. The bond debt service paid from the general airport revenues and other available funds amounted to \$64,225,173, which is net of \$22,099,631 of bond debt service paid from the accumulated PFC revenues.

The net revenues available to pay debt service in fiscal year ended June 30, 2012 totaled \$120,565,994, which is composed of \$61,649,128 of net general airport revenues and \$58,916,866 of other available funds. Other available funds include surplus carryover of \$33,987,539, rolling debt service coverage of \$12,579,218, CFC revenues of \$10,137,053, grants of \$500,000, and unspent Series 2004 bond proceeds of \$1,713,056. The bond debt service paid from the general airport revenues and other available funds amounted to \$59,389,209, which is net of \$21,336,421 of bond debt service paid from the accumulated PFC revenues.

The City has covenanted in the Master Trust Agreement that net revenues available to pay debt service for each fiscal year plus any other available funds (as defined in the Master Trust Agreement) will be at least 125% of annual debt service for such fiscal year. Under the Master Trust Agreement, "debt service" means for any specified period the sum of (a) the interest falling due on any then outstanding current interest bonds, assuming that all principal installments are paid when due, but excluding any interest funded from the proceeds of any series of bonds and applied toward payment of interest on such bonds, and (b) the principal installments payable on any then outstanding bonds. Under the Master Trust Agreement, annual debt service excludes Available PFC Revenues, as defined in the Master Trust Agreement, for such fiscal year. Total principal and interest remaining on the bonds is \$2.8 billion, with the final payment due on March 1, 2047.

The reserve requirement in the general account is currently satisfied, in part, by approximately (a) \$4.25 million surety bond from Ambac Assurance Corporation (Ambac Assurance), a subsidiary of Ambac Financial Group, Inc. (Ambac Financial) and formerly known as Ambac Imdemnity Corporation that expires on March 1, 2018, and (b) approximately \$6.56 million surety bond from National Public Finance Guaranty Corporation ("NPFG"), as successor to MBIA Insurance Corporation, that expires on March 1, 2016. The ratings of Ambac Financial and NPFG were reduced or withdrawn subsequent to the deposit of the respective surety bonds to the general

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account. The Master Trust Agreement does not require that the rating of any surety bond held in the general account be maintained after the date of deposit.

Until March 1, 2016, when the NPFG surety bond expires, no additional deposits to the general account of the bond reserve fund are expected to be required to satisfy the general account required reserve (unless the general account is drawn upon to pay principal of or interest on bonds or is made available to any additional bonds in the future). If no additional bonds are issued and no additional amounts were to be deposited in or paid from the general account of the bond reserve fund prior to March 1, 2016, the City expects that, upon expiration of the NPFG surety bond, amounts on deposit in the general account would not be sufficient to satisfy the general account required reserve at that time. Therefore, the City expects that it will be required to deposit approximately \$6.56 million to the general account from accumulated airport surplus funds or a qualified reserve facility in the same amount. If no additional bonds are issued and no additional amounts were to be deposited in or paid from the general account of the bond reserve fund prior to the expiration of the surety bond provided by Ambac Assurance on March 1, 2018, the City expects that it will be required to deposit approximately \$4.25 million (in addition to the approximate \$6.56 million deposit following the expiration of the NPFG surety bond described above) to the general account from accumulated Airport surplus funds or provide a qualified reserve facility in the same amount.

**Qualified reserve facility** means (i) a surety bond or similar instrument issued by a municipal bond insurer, obligations insured by which have a rating of “AAA” (or the equivalent) by at least two rating agencies (one of which must be Moody’s) on the date the qualified reserve facility is issued, or (ii) a LOC issued by a qualified bank which has a rating of “AA” (or the equivalent) by at least two rating agencies (one of which must be Moody’s) on the date the qualified reserve facility is issued.

The City may also be required to make a deposit of cash or another qualified reserve facility in order to maintain the required reserve in the general account in the case of non-payment under, or cancellation of, either surety bond, including as a result of the liquidation of Ambac Assurance or NPFG.

On May 1, 2013, Ambac Financial emerged from bankruptcy protection which had been filed under Chapter 11 of the Bankruptcy Code in November 2010. Ambac Assurance remains subject to rehabilitation proceedings undertaken by the Wisconsin Office of the Commissioner of Insurance. No assurance can be made regarding the claims paying ability of Ambac Assurance on the surety bonds described above.

In July 2011, the City issued Airport Revenue Bonds Series 2011A-1 and Series 2011A-2 in the amount of \$150,405,000 and \$86,380,000, respectively. The Series 2011A-1 Bonds were issued (i) to refund certain variable rate subordinated commercial paper notes originally issued to refund the Airport Revenue Bond Series 2004A and Series 2004B, (ii) to refund all of the outstanding Airport Revenue Refunding Bonds, Series 1998A, (iii) to make a cash deposit to the General Account of the Bond Reserve Fund, and (iv) to pay a portion of the costs of issuing Series 2011A Bonds. The bonds were issued with interest rates ranging from 2.00% to 6.25% and will mature in March 2034.

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A portion of the Series 2011A-1 proceeds and the remaining balances in the 1998A principal and interest accounts totaling approximately \$6.7 million were used to pay the redemption price of the refunded Series 1998A Bonds. The refunding achieved approximately \$362,742 in aggregate debt service savings or \$302,861 on a present value basis.

The Series 2011A-2 Bonds were issued (i) to refund \$85,625,000 aggregate principal amount of the outstanding Series 2001A, and (ii) to pay a portion of the costs of issuing the Series 2011A Bonds. The bonds were issued with interest rates ranging from 2.00% to 5.25% and will mature in March 2034. The refunding achieved approximately \$7,861,163 in aggregate debt service savings or \$5,425,018 on a present value basis.

On December 2, 2011, the City issued Airport Revenue Bonds Series 2011B in the amount of \$271,820,000. The Series 2011B Bonds were issued (i) to refund certain subordinated commercial paper notes payable that were originally issued to finance and/or refinance the costs of designing and constructing certain improvements to the Airport (ii) to pay a portion of interest to accrue on the Series 2011B Bonds through March 1, 2014, (iii) to make a cash deposit to the 2011B account of the bond reserve fund, (iv) to fund an increase of the rolling coverage amount, and to pay the costs of issuing the Series 2011B Bonds. The bonds were issued with interest rates ranging from 1.00% to 6.75% and will mature in March 2041.

On November 8, 2012, the City issued Airport Revenue Bonds Series 2012A in the amount of \$49,140,000. The Series 2012A bonds were issued to refund the City of San José Airport Revenue Bonds, Series 2002A in the amount of \$49,140,000. The Series 2012A bonds were purchased as fixed rate direct placement with Bank of America Public Capital Corp with an interest rate of 1.53%. The refunding provides approximately \$6,152,462 in aggregate debt service savings or \$5,905,688 on a present value basis.

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Balances of bonds payable as of June 30, 2013 and 2012 were as follows:

	<b>2013</b>	<b>2012</b>
2012A Series Airport Revenue Bonds of \$49,140,000 at rate of 1.53%; payable in annual installments ranging from \$8,105,000 to \$8,585,000 with the final installment due in March 2018	\$ 41,710,000	-
2011B Series Airport Revenue Bonds of \$271,820,000 at rates of 3.32% to 6.75%; payable in annual installments ranging from \$495,000 to \$27,330,000 with the final installment due in March 2041	264,085,000	264,085,000
2011A-2 Series Airport Revenue Bonds of \$86,380,000 at rates of 2.5% to 5.25%, payable in annual installments ranging from \$1,865,000 to \$12,220,000 with the final installment due in March 2034	82,255,000	84,075,000
2011A-1 Series Airport Revenue Bonds of \$150,405,000 at rates of 3% to 6.25%; payable in annual installments ranging from \$3,280,000 to \$4,730,000 with the final installment due in March 2034	143,180,000	146,370,000
2007B Series Airport Revenue Bonds of \$179,260,000 at rates 4.25% to 5%; payable in annual installments ranging from \$2,245,000 to \$28,800,000 with the final installment due in March 2037	179,260,000	179,260,000
2007A Series Airport Revenue Bonds of \$545,755,000 at rates of 5% to 6%; payable in annual installments ranging from \$5,690,000 to \$73,500,000 with the final installment due in March 2047	545,755,000	545,755,000
2004D Series Airport Revenue Bonds of \$34,270,000 at a rate of 5%; payable in three annual installments of \$9,955,000, \$11,755,000 and \$12,560,000 in March 2026, March 2027 and March 2028, respectively	34,270,000	34,270,000

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	<b>2013</b>	<b>2012</b>
2004C Series Airport Revenue Bonds of \$75,730,000 at rates of 4.625% to 5.25%, payable in annual installments ranging from \$1,000,000 to \$10,590,000 with the final installment due in March 2026	70,730,000	71,730,000
2002A Series Airport Revenue Bonds of \$53,600,000; the remaining balance of \$49,140,000 was refunded in November 2012	-	49,140,000
2001A Series Airport Revenue Bonds of \$158,455,000 was partially refunded in July 2011; the remaining balance of \$45,710,000 with interest rate of 5% is payable in annual installments ranging from \$8,275,000 to \$10,055,000 with the first installment due in March 2031	45,710,000	45,710,000
Total bonds payable	<hr/> <hr/> \$ 1,406,955,000	<hr/> <hr/> 1,420,395,000

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Bonds outstanding and related activities for the fiscal years ended June 30, 2013 and 2012, were as follows:

	<b>Balance at July 1, 2012</b>	<b>Additions</b>	<b>Retirements</b>	<b>Balance at June 30, 2013</b>	<b>Amounts Due Within One Year</b>
2012A Series	\$ -	49,140,000	7,430,000	41,710,000	8,105,000
2011B Series	264,085,000	-	-	264,085,000	-
2011A-2 Series	84,075,000	-	1,820,000	82,255,000	1,865,000
2011A-1 Series	146,370,000	-	3,190,000	143,180,000	3,280,000
2007B Series	179,260,000	-	-	179,260,000	2,245,000
2007A Series	545,755,000	-	-	545,755,000	5,780,000
2004D Series	34,270,000	-	-	34,270,000	-
2004C Series	71,730,000	-	1,000,000	70,730,000	1,000,000
2002A Series	49,140,000	-	49,140,000	-	-
2001A Series	45,710,000	-	-	45,710,000	-
Total long-term debt	1,420,395,000	49,140,000	62,580,000	1,406,955,000	22,275,000
Add unamortized:					
Premium	6,730,592	-	3,803,747	2,926,845	62,907
Less unamortized:					
Discount	11,573,888	-	24,276	11,549,612	43,173
Total long-term debt, net	<u>\$ 1,415,551,704</u>	<u>49,140,000</u>	<u>66,359,471</u>	<u>1,398,332,233</u>	<u>22,294,734</u>
	<b>Balance at July 1, 2011, as restated</b>	<b>Additions</b>	<b>Retirements</b>	<b>Balance at June 30, 2012</b>	<b>Amounts Due Within One Year</b>
2011B Series	\$ -	271,820,000	7,735,000	264,085,000	-
2011A-2 Series	-	86,380,000	2,305,000	84,075,000	1,820,000
2011A-1 Series	-	150,405,000	4,035,000	146,370,000	3,190,000
2007B Series	179,260,000	-	-	179,260,000	-
2007A Series	545,755,000	-	-	545,755,000	-
2004D Series	34,270,000	-	-	34,270,000	-
2004C Series	72,730,000	-	1,000,000	71,730,000	1,000,000
2002B Series	2,380,000	-	2,380,000	-	-
2002A Series	53,600,000	-	4,460,000	49,140,000	7,170,000
2001A Series	131,335,000	-	85,625,000	45,710,000	-
1998A Series	6,540,000	-	6,540,000	-	-
Total long-term debt	1,025,870,000	508,605,000	114,080,000	1,420,395,000	13,180,000
Add unamortized:					
Premium	4,728,564	2,594,430	592,402	6,730,592	641,990
Less unamortized:					
Discount	5,709,168	6,798,627	933,907	11,573,888	15,906
Total long-term debt, net	<u>\$ 1,024,889,396</u>	<u>504,400,803</u>	<u>113,738,495</u>	<u>1,415,551,704</u>	<u>13,806,084</u>

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Scheduled maturities of outstanding bonds are as follows:

<b>Fiscal year ending June 30,</b>	<b>Principal</b>	<b>Interest</b>
2014	\$ 22,275,000	74,651,757
2015	23,450,000	73,922,588
2016	24,520,000	73,103,538
2017	25,605,000	72,283,976
2018	26,860,000	71,323,024
2019-2023	143,620,000	337,580,303
2024-2028	197,575,000	295,122,296
2029-2033	323,210,000	232,374,884
2034-2038	475,360,000	114,863,872
2039-2043	109,170,000	27,194,843
2044-2047	35,310,000	5,451,000
Total	<u>\$ 1,406,955,000</u>	<u>1,377,872,081</u>

A number of limitations and restrictions are imposed upon the Airport by covenants relating to certain outstanding revenue bonds. The Airport believes it is in compliance with all such limitations and restrictions as of June 30, 2013 and 2012.

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Other long-term liability activities for the fiscal years ended June 30, 2013 and 2012 were as follows:

	Balance at July 1, 2012	Adjustments/ Additions	Adjustments/ Retirements	Balance at June 30, 2013	Amounts Due Within One Year
Self-insurance	\$ 1,631,245	430,971	383,443	1,678,773	560,000
Accrued vacation, sick leave and compensatory time	2,045,695	1,684,575	1,583,479	2,146,791	1,620,000
Other postemployment benefits	9,964,282	3,677,300	1,565,113	12,076,469	-
Pollution remediation liability	<u>714,000</u>	<u>1,044,657</u>	<u>-</u>	<u>1,758,657</u>	<u>1,758,657</u>
<b>Total</b>	<b>\$ 14,355,222</b>	<b>6,837,503</b>	<b>3,532,035</b>	<b>17,660,690</b>	<b>3,938,657</b>
	Balance at July 1, 2011	Adjustments/ Additions	Adjustments/ Retirements	Balance at June 30, 2012	Amounts Due Within One Year
Self-insurance	\$ 2,305,639	(119,932)	554,462	1,631,245	560,000
Accrued vacation, sick leave and compensatory time	2,314,251	1,237,999	1,506,555	2,045,695	1,536,000
Other postemployment benefits	7,529,822	4,412,508	1,978,048	9,964,282	-
Pollution remediation liability	<u>714,000</u>	<u>108,686</u>	<u>108,686</u>	<u>714,000</u>	<u>714,000</u>
<b>Total</b>	<b>\$ 12,863,712</b>	<b>5,639,261</b>	<b>4,147,751</b>	<b>14,355,222</b>	<b>2,810,000</b>

## **(6) Leases and Agreements**

The City has entered into an Airline-Airport Lease and Operating Agreement with the various passenger and cargo airlines serving the Airport. The airline lease agreement, which took effect on December 1, 2007, was originally set to expire on June 30, 2012. In August 2011, the City Council authorized the Director of Aviation to extend the term for five years through June 30, 2017, which allows the airlines to continue to conduct operations and occupy leased space through the extended term. The existing rates and charges structure, as well as all other terms and conditions, remained unchanged.

The airline lease agreement provides that any passenger airline that (a) signs an agreement substantially similar to the airline lease agreement, (b) provides passenger service at the Airport, (c) leases from the City an amount of exclusive use premises (not including gates) in the terminal deemed sufficient by the Director of Aviation to support the airline's operation and (d) at the time the airline executes its agreement with the City, operates at least one scheduled flight, scheduled

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year-round, at least three days per week shall be a Signatory Airline. The airline lease agreement also provides that any air cargo carrier will also be a Signatory Airline if the air cargo carrier (a) signs an agreement with the City substantially similar to the airline lease agreement (other than in connection with terminal facilities), (b) leases from the City cargo support space at the Airport for a term at least equal to the term of the airline lease agreement, (c) guarantees a minimum of 142,000 pounds of maximum gross certificated landed weight per scheduled flight and (d) at the time it executes its agreement with the City, operates at least five scheduled flights per week.

Any passenger or air cargo carrier that does not meet the minimum requirements to be a Signatory Airline is given the opportunity to become a “Non-Signatory Airline” by executing a non-signatory agreement in a form similar to that of the airline lease agreement. Non-Signatory Airlines are charged a premium of 25% over the rates and charges applicable to Signatory Airlines and do not participate in the review by a “Majority of Interest” of capital projects proposed for the Airport.

Any passenger or air cargo carrier operating at the Airport that is neither a Signatory Airline nor a Non-Signatory Airline will be subject to the Airline Rates and Charges Ordinance, which requires such air carriers to comply with all applicable rules and regulations as established by the Director of Aviation regarding the proper use and occupancy of the Airport or any portion thereof. In addition, the Airline Rates and Charges Ordinance establishes all rates and charges applicable to such airline’s operations at and use of the Airport or any portion thereof, including airfield and terminal rates and charges, at a 30% premium over the rates and charges as determined pursuant to the terms of the City’s then current airline lease and operating agreement.

The key provisions in the airline lease agreement include compensatory rate making for the terminal cost center and residual rate making for the airfield cost center. The airline lease agreement also includes a revenue sharing provision to evenly divide net unobligated Airport revenues between the Airport and the airlines currently operating at the Airport after each fiscal year. In any fiscal year in which there are net unobligated Airport revenues and all requirements of the City’s Airport financing documents have been satisfied, the remaining net unobligated Airport revenues are to be evenly divided between the City and the airlines. If net revenues exceed the projected levels outlined in the Airport Forecast identified in the airline lease agreement, then the airlines share of the difference will be deposited into the Rate Stabilization Fund up to a cap of \$9 million. Once the Rate Stabilization Fund has been fully funded or in the event that the actual net revenues do not exceed the projected net revenues, the airlines share of net revenues shall be applied as a credit to the airline terminal revenue requirement for the following fiscal year, thus reducing terminal rental rates for the following fiscal year. The first \$1 million of City’s share of any net revenues shall be retained by the Airport in a discretionary fund to be used for any lawful Airport purpose.

For the fiscal years ended June 30, 2013 and 2012, the Airport’s revenues as defined in its lease agreements exceeded its expenditures and reserve requirements by \$29,740,661 and \$30,642,898, respectively. The surplus for fiscal year ended June 30, 2013 will be distributed in accordance with the revenue sharing provisions of the lease agreement as described above and/or used in the budget

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balancing actions for fiscal year 2015. Of the surplus for the year ended June 30, 2012, \$3,437,220 was used to balance the fiscal year 2014 budget and the remainder was distributed in accordance with the revenue sharing provisions.

The Airport also enters into leases with concessionaires, cargo carriers, and other business entities for building space and/or the privilege of operating a concession at the Airport. The remaining terms of these operating leases range from one month to 25 years. The leases with concessionaires are generally based on the greater of a percentage of their sales or a minimum annual guaranteed amount.

Rental revenues from the aforementioned operating leases were \$74,629,917 and \$78,227,057 for the fiscal years ended June 30, 2013 and 2012, respectively.

The future minimum rentals to be received from the existing operating leases are as follows:

Fiscal year ending June 30,

2014	\$ 88,234,243
2015	93,069,570
2016	93,655,275
2017	94,432,109
2018	30,615,587
2019-2023	77,899,777
2024-2028	117,031,331
2029-2033	114,412,665
2034-2038	112,792,122
2039-2041	<u>76,699,711</u>
Total minimum lease rentals	<u>\$ 898,842,390</u>

These future minimum rentals are based upon annual rates and charges currently agreed to by the airlines and other tenants.

As of June 30, 2013 and 2012, leased assets had total historical costs of \$1,028,621,495 and \$1,031,260,042 and accumulated depreciation of \$126,869,054 and \$101,478,416, respectively.

Pursuant to the terms of individual agreements entered into with the City, every airline, operator, tenant or any other entity or person, which is party to an agreement with the City authorizing them to conduct business at the Airport, is required to maintain a security deposit on file with the City. The deposit shall be in a form and amount acceptable to the Director of Aviation (Director), often in the form of irrevocable letter of credit, surety bond, cashier's check or other form acceptable to the Director. The Director has the authority to revise the amount of security deposit at any time to

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protect the interests of the City. Each deposit must be maintained in full force and effect during the entire term of the agreement to ensure faithful performance by the other party of all the covenants, terms and conditions of the agreement. Security deposits in the form of cashier's checks are recorded as advances and deposits payable on the accompanying statement of net position. The Airport maintains on file copies of all security deposits, in the form of letter of credit or surety bond, which are not recorded in the financial statements. The amount on file as of June 30, 2013 and 2012 totaled \$23,692,207 and \$23,788,567, respectively.

**(7) Employees' Retirement System**

All full-time and certain part-time employees of the Airport participate in the City of San José Federated City Employees' Retirement System (Federated Plan), which is a single employer defined benefit retirement system that covers substantially all City employees, except for employees who are members of the City's Police and Fire Department Retirement Plan, by providing retirement and certain other postemployment benefits. These benefits include pension, death, and disability, which are under the Defined Benefit Pension Plan, as well as medical and dental benefits, which are under the Postemployment Healthcare Plan. A stand-alone report is issued for the Federated Plan and is available from the City of San José Office of Retirement Services, 1737 North First Street, Suite 580, San José, California 95112. As a department of the City, the Airport shares in the risks, rewards and costs including benefit costs with the City. The Airport presents the related defined benefit disclosures as a participant in a cost-sharing plan arrangement with the City.

On June 5, 2012, San José voters adopted Measure B which enacted the Sustainable Retirement Benefits and Compensation Act (the Pension Act). The Pension Act amended the City Charter to, among other changes, (1) increase pension contribution requirements for current employees effective June 23, 2013; (2) require the City to establish an alternative voluntary plan with reduced benefits for current employees (the "Voluntary Election Plan" or "VEP") subject to Internal Revenue Service (IRS) approval; (3) place limitations on disability retirements, (4) authorize the City Council to temporarily suspend the cost of living adjustments if the City Council adopts a resolution declaring a fiscal and service level emergency; (5) require the elimination of the Supplemental Retirement Reserve within the Federated Plan; (6) codify in the City Charter contribution requirements for current employees for the retiree health and dental benefits and provide for a reservation of rights for the City Council to terminate or modify any retiree healthcare plan; (7) require the establishment of Tier 2 plans for new employees within the Federated Plan; and (8) reserve to the voters the right to approve future changes to retirement benefits.

Significant portions of Measure B are currently subject to legal challenge by bargaining units representing current employees and retirees in the Santa Clara County Superior Court. Additionally, various bargaining units representing current employees have filed unfair labor practice charges with the California Public Employment Relations Board related to Measure B. In connection with the litigation related to Measure B, the City entered into a stipulation to delay implementation of the increased pension contributions from current employees to a date no sooner than January 1, 2014. As of June 30, 2013, the IRS has not approved the VEP. A complete copy of

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Measure B is available from the San José City Clerk, 200 East Santa Clara Street, San José, California 95113.

On August 28, 2012, the City Council adopted ordinance No. 29120 amending the Federated Plan to provide for different retirement benefits for individuals hired or rehired by the City on or after September 30, 2012. Members subject to these new benefit provisions are referred to as Tier 2 members. On December 18, 2012, the City Council adopted ordinance No. 29184 that provides unclassified executive management and professional employees in Unit 99 who are first hired on or after January 20, 2013, with a one-time irrevocable election to either participate in a newly created Defined Contribution Plan or become a Tier 2 member in the Federated Plan.

The new tier includes significant benefit changes from the existing Tier 1 plan. In addition, the contribution rate for Tier 2 members includes a change in the cost sharing between the City and active Tier 2 members which is a 50/50 split of all costs. Currently, Tier 1 members split normal costs with 8/11 paid by the City and 3/11 paid by Tier 1 members. The prepayment made by the City on July 2, 2012, was not adjusted when Tier 2 became effective.

On August 27, 2013, the City Council adopted ordinance No. 29283 eliminating retiree medical and dental benefits for Federated Plan Tier 2 members hired on or after September 27, 2013. The ordinance also provides that the City shall bear and pay an amount equal to the additional costs incurred by the Federated Plan for that portion of the unfunded liability as determined by the actuary of the Federated Plan that the City and the new members hired on or after September 27, 2013, would have otherwise paid as contributions had those members been eligible for retiree healthcare. The additional payment by the City shall be for a period of time and under the terms and conditions set forth by the City Council. At their September 19, 2013 meeting, the Board of Administration for the Federated Plan approved the additional contribution rate to be paid by the City in compliance with the ordinance. The rate was based on the Tier 2 contribution rates from the June 30, 2012 actuarial valuation approved by the Board of Administration for the Federated Plan.

The payroll for Airport employees covered by the Federated Plan for the fiscal years ended June 30, 2013 and 2012 \$12,931,622 was \$13,530,731, respectively. The Airport's total payroll for the fiscal years ended June 30, 2013 and 2012 was \$15,092,920 and \$15,948,673, respectively. The Defined Benefit Pension Plan provides general retirement benefits including pension, death, and disability benefits to members. Benefits are based on average final compensation, years of service, and limited required cost-of-living increases. The contribution and benefit provisions and all other requirements are established by the City Charter and City ordinances.

Contributions to the Defined Benefit Pension Plan are based upon an actuarially determined percentage of each employee's base salary sufficient to provide adequate assets to pay benefits when due. As discussed below, contributions to the Postemployment Healthcare Plan are not currently sufficient to provide adequate assets to pay benefits when due.

Contribution rates for the Airport and the participating employees for the periods June 26, 2011 through June 23, 2012, June 24, 2012 through June 22, 2013 and June 23, 2013 through June 30, 2013 were established in accordance with actuarially determined requirements computed through

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actuarial valuations performed as of June 30, 2010, June 30, 2011, and June 30, 2012, respectively, for the Defined Benefit Pension Plan and the Postemployment Healthcare Plan.

The required contributions rates determined by the Federated Plan's actuary anticipate that the City will make contributions on a bi-weekly basis throughout the fiscal year. The City has elected since fiscal year 2008-09 to "prefund" all or part of its total Annual Required Contribution (ARC) to the Federated Plan at the beginning of each fiscal year and the Federated Plan's actuary applies an interest discount to the required contributions to account for the fact that contributions are made at the beginning of the year instead of throughout the year. The "prefunded" annual contributions are made on the basis of estimated bi-weekly pay for the fiscal year and are trued up at the end of the fiscal year based on actual bi-weekly payroll.

In fiscal year ended June 30, 2011, the Board of Administration for the Federated Plan approved an establishment of a "floor funding method" for payment of annual required contributions ("ARC") for pension and postemployment healthcare benefits to address unexpected shortfalls in contributions that may result when payroll does not grow at the rate assumed by the actuaries. The "floor funding method" interprets the ARC as the greater of the annual dollar contribution amount established in the valuation, or the ARC that would result from applying the employer contribution rate determined from that same valuation to the actual emerging payroll of Retirement Systems members throughout the fiscal year. Therefore, the resolutions adopted by the Board of Administration for the Federated Plan setting the contribution rates for the fiscal year ended June 30, 2013 provide that the employer's contribution rates may be adjusted in order to achieve a minimum dollar contribution for that fiscal year.

Pay Period	Airport's Contribution <sup>(1)</sup>		Employees' Contribution	
	Defined Benefit Pension	Post-employment Healthcare Plan	Defined Benefit Pension	Post-employment Healthcare Plan
06/26/2011 through 06/23/2012	28.34%	7.16%	4.68%	6.52%
06/24/2012 through 06/22/2013	44.45%	7.91%	5.74%	7.26%
09/30/2012 through 06/22/2013				
Tier 2	6.68%		6.68%	
06/23/2013 thorugh 06/30/2013				
Tier 1	50.85%	8.66%	5.97%	8.01%
Tier 2	6.68%		6.68%	

<sup>(1)</sup> Airport's contribution rates do not reflect contribution prefunding described above.

Contributions to the Postemployment Healthcare Plans are made by both the City and the participating members. Effective June 28, 2009, the bargaining units representing the Federated Plan members entered into Memorandums of Agreement (MOAs) with the City to increase the

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contribution rates for retiree health and dental in order to phase-in to full funding the GASB Statement No. 43 annual required contribution over the next 5 years; fiscal year 2013 was the fourth year of the phase-in. The funding specified in these agreements is also being applied to unrepresented employees. The Memorandums of Agreement between the City and the bargaining units representing the members of the Federated Plan provided that the five year phase-in of the ARC will not have an incremental increase of more than 0.75% of pensionable pay in each fiscal year for the Federated Plan members or the City. Notwithstanding these limitations on incremental increases, the agreements with members of the Federated Plan further provide that by the end of the five year phase-in, the City and the members “shall be contributing the full ARC in the ratio currently provided” in the relevant sections of the San Jose Municipal Code.

Effective June 18, 2013, bargaining units representing the Federated members and the City have agreed to extend the incremental increase limitation of not more than 0.75% of pension pay for the fiscal year ending June 30, 2014. In addition, the 0.75% limitation is extended to December 20, 2014. Beginning on December 21, 2014, the contribution rates will be based on the full ARC for the remainder of the fiscal year ending June 30, 2015 and all subsequent fiscal years. These terms related to payment of the ARC also apply to unrepresented members of the Federated Plan. The contributions are not currently sufficient to provide adequate assets to pay benefits when due in accordance with the requirements of GASB Statement No. 43.

Actuarially required contributions were equal to the contributions made for the Defined Benefit Pension Plan. The following is the three-year trend information for the Airport's ARC, Annual OPEB Cost (AOC), and contributions made:

Fiscal Year	Defined Benefit Pension					Postemployment Healthcare Plan				
			% of Unfunded		Liability			% of Unfunded		Liability
	ARC	Contributions	Contributions	Liability		ARC	AOC	Contributions	Contributions	
6/30/2011	\$ 4,455,031	\$ 4,455,031	100%	-		\$ 3,164,961	\$ 3,227,182	\$ 1,436,944	45%	\$ 7,529,822
6/30/2012	3,834,609	3,834,609	100%	-		4,385,496	4,412,508	1,978,048	45%	9,964,282
6/30/2013	5,748,106	5,748,106	100%	-		3,691,308	3,677,300	1,565,113	43%	12,076,469

The City has determined a Citywide ARC and OPEB cost based upon an actuarial valuation performed in accordance with GASB Statement No. 45 by the Federated Plan's actuary. The City allocated to the Airport its proportionate share of the Citywide ARC and OPEB cost for Federated Plan employee members. The difference between the cumulative OPEB cost allocated and the costs contributed by the Airport was \$12,076,469 and \$9,964,282 at June 30, 2013 and 2012, respectively, which is recorded as the Airport's net OPEB obligation. The Airport has earmarked funds from the unrestricted net position to pay the full amount of the net OPEB obligation.

The City issues a publicly available CAFR that includes the complete note disclosures and required supplementary information related to the City's other postemployment benefit obligations. A copy

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of that report may be obtained by contacting the City's Finance Department, 200 East Santa Clara Street, 13<sup>th</sup> Floor, San José, CA, 95113.

**(8) Related Party Transactions**

The City provides certain general support services to the Airport and charges a pro rata fee. The fees charged to the Airport for these services for the fiscal years ended June 30, 2013 and 2012, were \$3,128,883 and \$3,499,460, respectively. The City also charged the Airport fees of \$7,018,607 and \$8,446,291 for the fiscal years ended June 30, 2013 and 2012, respectively, for airport rescue and fire fighting and police services coverage. Additionally, various City departments charge the Airport for services they rendered on its behalf. These fees and service charges, which totaled \$1,090,265 and \$936,980 for the fiscal years ended June 30, 2013 and 2012, respectively, are included in operating expenses in the accompanying statements of revenues, expenses, and changes in net position.

The FAA auditors reviewed the City's allocation of its costs to the Airport for services provided by the City to the Airport in fiscal year 2011. The City uses both direct and indirect methodologies to allocate costs to the Airport. The FAA auditors found the direct cost allocations to be acceptable. The FAA contends that the City's indirect methodology does not correlate to the cost of services actually provided by the City to the Airport. Consequently, the auditors have recommended that the City re-allocate its costs charged to the Airport for fiscal years 2005 through 2010 using an allocation methodology that reflects services actually provided to the Airport and repay any overcharges to the Airport, with interest.

The City had proposed capping the indirect cost allocations for fiscal years 2003 through 2009 at 10% and crediting the Airport \$5.6 million including interest over the next seven years starting with fiscal year 2013. In addition, effective with fiscal year 2015, the City will cease utilizing the relative expenditure metric that includes the capital expenditures and debt service. The City will revise the cost allocation to the Airport for fiscal years 2011 through 2014 by excluding capital expenditures and debt service from the relative expenditure metric. A potential credit resulting from the revised calculation will be applied by the City in fiscal year 2015, or evenly spread over a four-year period starting with fiscal year 2015 at the City's discretion. Also, in preparing the fiscal year 2015 calculation, the City will consider utilizing a transaction based allocation for debt service, such as the number of transactions (payments) related to debt service. The City' proposal is yet to be accepted by the FAA and as such, the Airport has not recorded this contingency.

**(9) Risk Management**

**(a) Insurance Policies**

The Airport is covered under the City's annual all-risk property insurance policy with coverage for City property, including coverage for boiler and machinery exposures. The policy also provides coverage for loss due to business interruption and flood. The City does not carry earthquake insurance as it is not reasonably available. A summary of these coverages is provided below for the policy period of October 1, 2012 to October 1, 2013.

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<u>Coverage</u>	<u>Limit per Occurrence</u>	<u>Deductible per Occurrence</u>
Property, including Business Interruption	\$1 billion	\$100,000
Flood Zone, Special Flood Hazard Area	\$15 million per occurrence and annual aggregate	5% of values at risk (\$1 million minimum deductible)
Flood Zone B	\$25 million per occurrence and annual aggregate	2% of values at risk (\$100,000 minimum deductible)
Flood, Other Locations	\$100 million per occurrence and annual aggregate	\$100,000

The City has airport liability policies covering the Airport for the policy periods of October 1, 2012 to October 1, 2013 and October 1, 2011 to October 1, 2012 including operation of vehicles on premises, which provide a \$200 million combined single limit for bodily injury and property damage subject to a deductible of \$0 each occurrence and annual aggregate, with a sublimit of \$50 million each occurrence and in the annual aggregate for personal injury, and a sublimit of \$100 million each occurrence and in the annual aggregate for war liability. During the past three years, there have not been any instances that the amount of claim settlements exceeded the insurance coverage.

A separate automobile policy provides coverage for the off-premises operation of Airport vehicles including shuttle bus fleets with a limit of \$1 million per occurrence, combined single limit for bodily injury and property damage, and no deductible. Physical damage coverage is available for the Airport Shuttle Bus Fleet and is subject to a \$10,000 comprehensive and \$25,000 collision deductible. Settled claims have not exceeded the commercial coverage in any of the past three fiscal years.

As part of general support services, the City charges the Airport for the cost of general liability and property insurance coverage. The charges are expensed in the year incurred.

***(b) Workers' Compensation***

The Airport participates in the City's self-insurance program for workers' compensation. Workers' compensation liabilities are accounted for on a separate contribution basis under which workers' compensation liabilities are recorded in the respective funds (enterprise or governmental) to which they relate.

Estimated workers' compensation liabilities at year-end are determined using actuarial methods or other estimating techniques. The claims payments and liability include an estimate of allocated loss adjustment expenses and claims that have been incurred but not yet reported.

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The Airport recorded the following with respect to its self-insured workers' compensation liability:

	<b>2013</b>	<b>2012</b>
Accrued liability, beginning of fiscal year	\$ 1,631,245	2,305,639
Claims payments and adjustments	(383,443)	(554,462)
Provision for current year claims and changes in prior year estimates	<u>430,971</u>	<u>(119,932)</u>
Accrued liability, end of fiscal year	<u>\$ 1,678,773</u>	<u>1,631,245</u>

As of June 30, 2012, the Airport had established a reserve for self-insurance, in addition to the reserve established by the City. The reserve for self-insurance of \$803,000 was included in the unrestricted net position as of June 30, 2012. No such reserve was established as of June 30, 2013.

**(c) *Airport Owner Controlled Insurance Program***

On March 31, 2004, the City bound certain liability insurance coverage (see chart below) for major components of the “2004 Security Projects” (currently referred to as the North Concourse Project) through an Owner Controlled Insurance Program (OCIP) from Chartis, formerly American International Group, AIU Holdings, Inc. and AIU LLC (AIU). The OCIP is a single insurance program that provides commercial general liability, excess liability and workers’ compensation insurance coverage for construction job site risks of the project owner, general contractors and all subcontractors associated with construction at the designated project site.

<u>Coverage</u>	<u>Limits</u>	<u>Deductible Per Occurrence</u>
General Liability	\$2 million per occurrence/ \$4 million aggregate	\$250,000
Workers' Compensation	Statutory	\$250,000
Employers' Liability	\$2 million per accident	\$250,000
Excess Liability	\$150,000,000	None

The North Concourse OCIP required the City to fund a claims loss reserve fund with Chartis in the amount of \$3.9 million. The full amount of the claims loss reserve had been deposited with Chartis and was recorded as advances and deposits in the accompanying statement of net position. The claims loss reserve fund is available to Chartis to pay claims within the City’s

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deductible, subject to an aggregate maximum loss exposure within coverage limits to the City of \$3.9 million. Interest earned by the claims reserve fund is remitted to the Airport.

The North Concourse Project was completed in the fall of 2008. Chartis is currently in the process of closing out the North Concourse OCIP and is auditing the project payroll and cost factors associated with the premium. The closing out process for OCIP includes an actuarial review, which examines outstanding claims. The City was able to negotiate the return of a large portion of the unused claims reserve in advance of the 10-year coverage term and in March 2010, the amount of \$2,516,719 was returned to the Airport. Chartis will continue to hold the remaining funds in the claims loss reserve fund until such time as the exposure to risk of claims ceases or the City opts to cash out the remaining funds in exchange for accepting responsibility for potential future claims.

Activities relating to the North Concourse OCIP claims reserve fund for the fiscal years ended June 30, 2013 and 2012 were as follows:

	<u>2013</u>	<u>2012</u>
Beginning balance	\$ 1,028,172	1,065,664
Losses paid	<u>(80,485)</u>	<u>(37,492)</u>
Ending balance	<u>\$ 947,687</u>	<u>1,028,172</u>

On March 15, 2007, the City bought additional insurance coverages through Chartis for major components of the Terminal Area Improvement Program (TAIP) through another OCIP (the TAIP OCIP). The coverages for this program are as follows:

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

The liability under the TAIP OCIP is based upon an estimated payroll of \$92.5 million for the covered projects and a construction period of 45 months, commencing on March 15, 2007 through December 31, 2010. The terms of the TAIP OCIP require the City to fund a claims loss reserve fund with Chartis in the amount of \$8.9 million. The claims loss reserve fund is available to Chartis to pay claims within the City's deductible subject to an aggregate maximum loss exposure within coverage limits to the City of \$8.9 million. The City was able to negotiate to fund 74% of the claims loss reserve and interest generated remains in the fund.

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The full amount of \$6.5 million was deposited with Chartis in fiscal year 2009 and was recorded as advances and deposits in the accompanying statement of net position. In August 2013, as part of the annual loss reserve analysis by Chartis, an amount of \$1,397,838 has been returned to the Airport.

Activities relating to the TAIP OCIP claims reserve fund for the fiscal years ended June 30, 2013 and 2012 were as follows:

	<u>2013</u>	<u>2012</u>
Beginning balance	\$ 4,303,114	4,859,972
Interest earned	3,167	3,830
Losses paid	(273,889)	(560,688)
Ending balance	<u>\$ 4,032,392</u>	<u>4,303,114</u>

The City was obligated to maintain the TAIP OCIP through final acceptance of the Terminal Area Improvement Program, pursuant to the terms of its design-build contract with Hensel Phelps (HP). The term of the TAIP OCIP expired on June 30, 2011. All work covered under the contract with HP has been completed and accepted. Chartis will continue to hold the remaining funds in the claims loss reserve fund until such time as the exposure to risk of claims ceases or the City opts to cash out the remaining funds in exchange for accepting responsibility for potential future claims.

**(10) Commitments and Contingencies**

**(a) Lease Commitments**

In December 2007, the Airport entered into an operating lease and maintenance agreement of 14 compressed natural gas (CNG) powered buses. The lease and maintenance term of the agreement is from August 1, 2008 to July 31, 2015. In September 2009, the agreement was restated to add 10 CNG powered buses for the period June 30, 2010 to May 31, 2017. In May 2012, the restated lease was amended to allow the early termination of the lease term pertaining to the first 14 CNG powered buses with Airport's payment of \$4,407,508. Simultaneously, the Airport entered into an agreement relinquishing the use of the 14 CNG powered buses to a third party for a total price of \$3,400,000 to relieve the Airport of its lease commitment. The Airport used the proceeds together with the difference of \$1,007,508 to make the early termination payment of \$4,407,508. Rental and maintenance expenses were \$1,263,991 and \$2,499,217 for fiscal years ended June 30, 2013 and 2012, respectively.

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**(A Department of the City of San José)**

**Notes to Financial Statements**  
**June 30, 2013 and 2012**

The future minimum lease and maintenance payments required under the existing agreement for the 10 remaining CNG powered buses are as follows:

<b>Fiscal Year Ending June 30,</b>	<b>Amount</b>
2014	\$ 949,497
2015	952,376
2016	955,324
2017	878,459
Total minimum lease payments	<u>\$ 3,735,656</u>

***(b) Purchase Commitments and Capital Outlay Projections***

As of June 30, 2013, the Airport was obligated for purchase commitments of approximately \$7.1 million primarily for pavement maintenance, parking revenue control system, terminal building modifications, and various operating and maintenance agreements. The Airport has projected that it will expend or encumber \$87,433,000 on proposed capital projects during the next five fiscal years. It is anticipated that funding for such capital projects will be provided primarily by proceeds from federal grants, bond proceeds, and other Airport revenues.

***(c) Fuel Tank Farms***

Until December 22, 1998, the City and Chevron U.S.A., Inc. (“Chevron”), operated adjacent fuel storage facilities at the Airport. The City’s facilities have not been in operation since December 22, 1998, when the facilities were closed in response to the federal deadline for upgrade or closure of underground storage tanks. Since the discovery in fiscal year 1985-86 that petroleum products had been released into the soil and groundwater from either or both the City and Chevron fuel storage facilities, the City and Chevron have operated a groundwater extraction system to control migration (spread) of the contamination and to remediate (clean up) contaminated groundwater. This interim remediation system consists of an extraction and treatment system to remove floating jet fuel product from groundwater and to prevent its offsite migration. Chevron operates and maintains the system. Through June 1998, the City and Chevron shared in the cost of operating this system. The agreement expired but Chevron continued the work.

A new joint agreement was entered into by the City and Chevron in November 2009. Chevron was designated as the lead in the remediation efforts. The agreement provides for a 50%-50% cost sharing responsibility for actual future costs until successful closure of the site. As of June 30, 2013, the Airport has accrued its 50% of the remediation costs totaling \$1,044,657 while an amount of \$108,686 was paid during fiscal year ended June 30, 2012. The agreement also required the City to pay its 50% share of the past costs that Chevron has incurred during the period after expiration of the prior agreement and before the new agreement was in place. During the fiscal year ended June 30, 2010, the Airport paid its share of the past costs amounting to \$660,434.

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Chevron is responsible for administering the new agreement, including retaining a corrective action contractor. The agreement is also structured to facilitate potential reimbursement from the State Water Resources Control Board Underground Storage Tank Commingled Plume Fund (the “Fund”). Due to the proximity of the closed City jet fuel farm to the adjacent Chevron jet fuel farm that was still active, and the apparently stable contaminant plume, the regulators approved a waiver to allow the City tanks to be left in place until such time as a completely new fuel farm could be built, thereby allowing the Chevron site to be closed, and investigation/remediation to be done on both sites at once. The new jet fuel farm was constructed off-Airport across Highway 101 and was placed in service in December 2009. The Chevron fuel farm was subsequently closed upon commencement of the operation of the new fuel farm.

Chevron demolished its fuel farm during fiscal year 2010 and removed its USTs. The City removed its USTs in September 2011. Chevron completed the site’s interim remedial action in November 2012 pursuant to the plan, which was approved by the County of Santa Clara in February 2012. The approved plan is a fixed area remedial excavation to remove the secondary source materials beneath and adjacent to the former USTs. In March 2013, four groundwater monitoring wells were installed within the area of excavation to monitor and evaluate the effectiveness of the remedial excavation on water quality. As of July 29, 2013, the Airport has completed two consecutive quarters of groundwater monitoring and sampling. Analytical results continue to show a decrease in concentrations. Quarterly monitoring and sampling is recommended through the fourth quarter of 2013. Following four quarters of monitoring and sampling, the site conditions should be evaluated for closure using the framework of the State Water Resources Control Board Low-Threat Underground Storage Tank Closure Policy, which became effective August 17, 2012.

The Airport accrued \$1,758,657 and \$714,000 as of June 30, 2013 and 2012, respectively, to cover the costs of its portion of the interim remediation system. Latest estimates of costs to further investigate and cleanup this site is between \$1.4-2 million, depending upon method of accomplishment and actual remediation requirements.

***(d) Master Plan***

The Airport Master Plan consists of a program of facility improvements designed to fully accommodate commercial aviation demand (passengers and cargo) projected for the future, with development phased as demand warrants and is determined to be financially feasible. The Master Plan was originally adopted by the City of San José in June 1997 and approved by the FAA in December 1999. In June 2006, the City Council approved revisions to the Airport Master Plan regarding implementation of the TAIP. Most of the program elements of Phase 1 were completed as of June 30, 2013 with the completion of a common use lounge, a taxi staging building, Terminal A/A+ space refurbishment, and building system upgrades occurring in FY 2013. Ongoing projects include Terminal A baggage system ceiling protection, relocation of northeast electrical services, and completion of the northeast area (formerly the rental car fueling and wash site). Construction of the northeast area began

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**Notes to Financial Statements**  
**June 30, 2013 and 2012**

in August 2013 and will provide for a fuel truck maintenance facility, shuttle bus staging and storage, and adjacent employee parking. Construction of the Phase 2 projects is contingent upon satisfying specified activity-based triggers. Funding for Master Plan projects is from several sources, including grants, PFCs, airline rates and charges, airport revenue bonds, and subordinated commercial paper proceeds.

In June 2010, the City Council approved an additional amendment to the Master Plan that updated projected aviation demand and facility requirements, and modified specific components of the Airport Development Program. Pursuant to the amended Master Plan, the former interim long-term public parking and employee parking lots on the northwest side of the Airport (which have been relocated to the east side terminal area) will be gradually converted to new general aviation leasehold facilities. In April 2013, the Airport completed a request for proposals process to provide for new general aviation aeronautical services facilities and began negotiating with the successful proposer, Signature Flight Support. It is anticipated that negotiation with Signature will be completed in the fall of 2013 with issuance of a site development permit allowing for the start of construction to follow in early 2014. Signature will be funding the costs related to this project. Lawsuits were filed by Atlantic Aviation against the City challenging the environmental clearance for the facilities and the selection process in which the City Council awarded the lease to Signature.

**(e) FAA Audit of Use of Revenue**

Federal law requires all airport owners that receive federal assistance, such as the City, to use airport revenues for the capital or operating costs of the Airport. As a general rule, any use of airport revenues by an airport owner for costs that cannot properly be considered airport capital or operating costs is deemed to be improper revenue diversion. On June 2, 2010, auditors from the FAA provided the City with a draft of its audit findings alleging improper use of Airport revenues by the City in three areas of expenditure as described below.

Airport Lease Obligation - In 2005, the City purchased certain real property (referred to as the Airport West Property). The purchase was financed with lease revenue bonds issued by the City of José Financing Authority (Authority). Upon acquisition, the City leased the property from the Authority and used a portion for construction laydown needs to support the Terminal Airport Improvement Program (TAIP). The City agreed to make lease payments from Airport operating revenues. At the time of the acquisition, the City contemplated other potential Airport uses for the property, such as rental car storage, public or employee parking, flight kitchen operations, airport/airline warehouses and compatible non-aviation leaseholds. The City subsequently determined not to use the property for these other potential Airport uses. The City's use of the property for construction laydown needs ceased with the completion of the TAIP on June 30, 2010. The FAA determined that the City could use Airport operating revenues to pay rent only for those portions that the City actually used for Airport construction laydown but not for the remainder of the property not actually used for Airport purposes. The City believes there is no basis under applicable

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**Notes to Financial Statements**  
**June 30, 2013 and 2012**

federal law for the distinction made by the FAA auditors between rent payments for actual as opposed to planned Airport uses.

Guadalupe Gardens – In 2002, the City Council approved a Master Plan for Guadalupe Gardens, consisting of approximately 120 acres of mostly vacant, City-owned property located south of the Airport, much of which falls within an FAA-established safety zone. The City acquired the Guadalupe Gardens properties using FAA grants for airport approach protection and noise compatibility. The FAA grant agreements required FAA approval of any planned City-use of the properties acquired with grant proceeds. By letter dated August 9, 2002, addressed to the City’s Director of Aviation, the FAA San Francisco Airport District Office (“ADO”) approved the City’s Master Plan for reuse of Guadalupe Gardens for runway and approach protection, and the City finalized the Master Plan in reliance upon the FAA approval. Citing provisions of federal law that require recipients of FAA grants for acquisition of land for noise compatibility purposes to dispose of any such acquired land when no longer needed by the airport owner for noise compatibility purposes, the FAA auditors determined that the FAA ADO erred in its 2002 approval of the Guadalupe Gardens Master Plan and that the City is obligated to prepare an inventory of the Guadalupe Gardens to identify those parcels that were acquired by the City with noise compatibility grant proceeds. This inventory would then be used to prepare for FAA review and approval of a disposition plan for those parcels no longer needed by the City for noise compatibility. Proceeds of the sale of the parcels proportionate to the FAA grant share of the original purchase price would be required to be used for other approved noise compatibility projects at the Airport or returned to the FAA. Having received official FAA approval of its reuse of the parcels, the City believes it is under no obligation to take any further action to secure further FAA approval of its continuing use of the Guadalupe Gardens.

Cost Allocations - The City uses both direct and indirect methodologies to allocate costs to the Airport. The FAA auditors found the direct cost allocations to be acceptable. The FAA contends that the City’s indirect methodology does not correlate to the cost of services actually provided by the City to the Airport. Consequently, the auditors have recommended that the City re-allocate its costs charged to the Airport for fiscal years 2005 through 2010 using an allocation methodology that reflects services actually provided to the Airport and repay any overcharges to the Airport, with interest. The City believes the allocation methodology used to allocate costs to the Airport is in compliance with both the standards and regulations of the FAA Policy and Procedures Concerning the Use of Airport Revenue and OMB A-87. In an effort to resolve the issue, the City proposed to cap the indirect cost allocations for certain City departments at 10%, which was the approximate rate charged to the Airport in pre-capital intensive years. This resulted in a total credit of \$5.6 million that would be applied equally to the Airport cost allocation plan over a seven year period beginning in fiscal year 2012-13.

The City continues discussions with the FAA, but cannot predict the final outcome of the audit.

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***(f) Litigation***

The City is potentially liable to private citizens for property damage and personal injuries caused by noise from the Airport's operations or for other damages if a property owner can prove that the City's operations of the Airport has deprived them of the benefits of property ownership. There are several pending lawsuits in which the Airport is involved in the normal course of its operation. The Airport's and the City's management believe that any potential exposure will not have a material effect on the Airport's financial position or changes in financial position.



# STATISTICAL



The Club at SJC, a common use VIP lounge, is conveniently located between Terminals A and B and provides a unique mix of amenities and world-class customer service.



NORMAN Y. MINETA  
**SAN JOSE**  
INTERNATIONAL  
AIRPORT  
SILICON VALLEY'S AIRPORT

CITY OF  
**SAN JOSE**  
CAPITAL OF SILICON VALLEY

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**

**Statistical Section**  
**June 30, 2013**

This part of the comprehensive annual financial report for Norman Y. Mineta San José International Airport (Airport) presents detailed information as a context for understanding what the information in the financial statements, note disclosures, and required supplementary information says about the Airport's overall financial health.

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Schedule A

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
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**ANNUAL REVENUES, EXPENSES, CHANGES IN NET POSITION AND NET POSITION**  
**LAST TEN FISCAL YEARS**  
**(in \$ 000's)<sup>(2)(4)</sup>**

	2004	2005	2006	2007	2008	2009	2010	2011 <sup>(1)</sup>	2012	2013
Operating revenues										
Airline rates and charges:										
Landing fees	\$11,122	\$9,751	\$10,768	\$13,504	\$13,084	\$14,504	\$13,190	\$13,370	\$11,414	\$12,888
Terminal rental	16,408	16,979	16,575	11,308	26,539	29,716	33,459	34,446	39,864	38,256
Total airline rates and charges	27,530	26,730	27,343	24,812	39,623	44,220	46,649	47,816	51,278	51,144
Terminal buildings/concessions	6,912	8,005	8,672	9,201	11,470	11,947	11,157	16,877	15,770	15,102
Airfield area	3,071	2,976	3,074	2,519	2,833	3,171	2,791	2,925	2,783	3,038
Parking and roadway	43,913	43,858	46,484	48,226	48,369	44,227	38,934	47,320	51,023	46,700
Fuel handling fees	1,333	1,375	1,492	1,592	1,806	1,474	1,310	1,504	1,690	2,361
Customer facility charges <sup>(3)</sup>	4,183	4,297	4,491	4,451	6,351	6,713	6,021	-	-	-
General aviation/other	2,883	3,028	3,858	4,528	4,789	5,826	5,909	4,521	4,431	4,770
Total operating revenues	89,825	90,269	95,414	95,329	115,241	117,578	112,771	120,963	126,975	123,115
Operating expenses:										
Terminal buildings/concessions	21,630	24,130	24,685	26,929	31,790	28,813	31,701	33,019	23,659	23,303
Airfield area	22,660	20,980	21,765	19,860	22,692	16,170	10,911	9,749	9,069	8,707
Parking and roadway	24,382	26,486	28,518	28,559	27,936	26,853	24,032	25,344	25,514	16,631
Fuel handling costs	51	96	325	171	311	557	885	288	556	1,065
General aviation	2,826	2,838	3,152	3,679	3,428	4,072	3,052	2,409	1,676	1,605
General and administrative	21,963	21,741	24,665	28,787	32,879	28,268	23,624	19,095	18,328	18,763
Depreciation and amortization	17,696	19,118	19,153	19,323	22,834	20,647	55,288	51,532	51,520	54,353
Total operating expenses	111,208	115,389	122,263	127,308	141,870	125,380	149,493	141,436	130,322	124,427
Operating income (loss)	(21,383)	(25,120)	(26,849)	(31,979)	(26,629)	(7,802)	(36,722)	(20,473)	(3,347)	(1,312)
Nonoperating revenues (expenses):										
Passenger facility charges	21,842	21,768	22,271	22,169	21,224	17,416	17,043	17,311	16,787	17,294
Customer facility charges <sup>(3)</sup>	-	-	-	-	-	-	-	6,840	10,137	13,385
Investment income	1,060	4,584	5,376	9,294	15,446	8,138	311	1,613	2,217	(257)
Interest expense	(5,594)	(7,173)	(3,184)	(11,995)	(11,737)	(11,404)	(10,750)	(54,430)	(70,009)	(75,058)
Bond issuance costs	-	-	-	-	-	-	-	-	(4,141)	(196)
Operating grants	5,724	5,570	8398	8,284	8,444	4,625	1,150	701	670	565
Loss on disposal of capital assets	-	-	(3)	-	-	(3,537)	(11,733)	-	(9)	-
Other, net	2,091	747	2,332	2,541	2,767	4,227	200	1,438	698	451
Total nonoperating revenues (expenses), net	25,123	25,496	35,190	30,293	36,144	19,465	(3,779)	(26,527)	(43,650)	(43,816)
Income before capital contributions	3,740	376	8,341	(1,686)	9,515	11,663	(40,501)	(47,000)	(46,997)	(45,127)
Capital contributions	11,725	13,791	10,508	9,694	4,970	12,868	34,722	10,862	7,399	6,954
Change in Net Position	\$15,465	\$14,167	\$18,849	\$8,008	\$14,485	\$24,531	(\$5,779)	(\$36,138)	(\$39,598)	(\$38,173)
Net Position at Year-End										
Net investment in capital assets	\$250,955	\$251,370	\$219,510	\$239,960	\$267,321	\$316,935	\$314,664	\$272,598	\$242,916	\$209,381
Restricted	121,548	133,413	113,182	118,334	84,491	45,260	61,349	64,128	69,350	65,408
Unrestricted	6,000	7,887	78,827	61,233	82,200	96,348	76,751	79,900	58,811	58,114
Net Position at Year-End	\$378,503	\$392,670	\$411,519	\$419,527	\$434,012	\$458,543	\$452,764	\$416,626	\$371,077	\$332,903

(1) As of July 1, 2011, the Airport adopted the provisions of GASB Statement No. 65 and restated the beginning net position in the amount of \$5,951,453 to write off unamortized bond issuance costs previously reported as an asset. During fiscal year ended June 30, 2012, the Airport has also written off bond issuance costs included in the deferred amounts related to the refunded bonds in the amount of \$1,338,755. In addition, the remaining unamortized loss on refunding as of June 30, 2012 in the amount of \$1,758,089 was reclassified from a contra liability to deferred outflows of resources. Fiscal years 2004 through 2011 have not been restated for GASB 65.

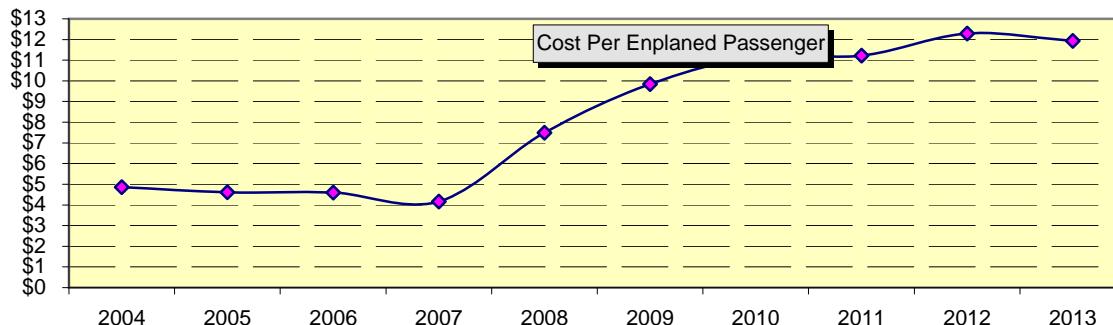
(2) Fiscal years 2004 through 2011 net assets have been renamed net position.

(3) Customer facility charges (CFCs) are used to pay for capital costs and related debt service associated with the consolidated rental car facility (ConRAC) and certain operating expenses related to the transportation of rental car customers. CFCs were reclassified from operating to nonoperating revenues in fiscal years 2011 through 2013 because the Airport started using CFCs mostly for the debt service associated with the ConRAC.

(4) Totals may not add due to rounding.

Source: Finance and Administration, Norman Y. Mineta San José International Airport, City of San José

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**AIRLINE COST PER ENPLANED PASSENGER**  
**LAST TEN FISCAL YEARS**  
**(\$ and Passengers in 000's)**



	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>
Airline revenues:										
Terminal rental	\$ 16,294 <sup>(1)</sup>	16,390 <sup>(1)</sup>	15,886 <sup>(1)</sup>	10,748 <sup>(1)</sup>	26,539	29,716	33,459	34,446	39,864	38,256
Landing fees (Passenger Carriers)	9,384	8,262	9,036	11,390	12,252	13,560	12,443	12,582	10,838	12,298
Total	25,678	24,652	24,922	22,138	38,791	43,276	45,902	47,028	50,702	50,554
Enplaned passengers	5,292	5,346	5,415	5,319	5,179	4,400	4,107	4,189	4,125	4,235
Airline cost per enplaned passenger (not in 000's)	\$ 4.85	4.61	4.60	4.16	7.49 <sup>(2)</sup>	9.84 <sup>(2)</sup>	11.18 <sup>(2)</sup>	11.23 <sup>(2)</sup>	12.29 <sup>(2)</sup>	11.94 <sup>(2)</sup>

<sup>(1)</sup> Terminal Rental for fiscal years 2004 through 2007 do not agree with Schedule A where revenue categories have been presented in accordance with the provisions of the current Airline-Airport Lease and Operating Agreement. Secondary and shared holdroom revenues, previously included in the Terminal Buildings/Concessions category, were reclassified to Terminal Rental in Schedule A.

<sup>(2)</sup> Increases in airline cost per enplaned passenger during fiscal years 2008 through 2013 were principally due to the decreases in enplaned passengers and the increases in debt service.

Source: Norman Y. Mineta San José International Airport audited financial statements and activity reports

Schedule C

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**GROSS CONCESSION REVENUE PER ENPLANED PASSENGER**  
**LAST TEN FISCAL YEARS**  
**(\$ and passengers in \$ 000's)**

	2004	2005	2006	2007	2008	2009	2010	2011	2012 <sup>(3)</sup>	2013
<b>Gross Concession Revenue:<sup>(1)</sup></b>										
Parking <sup>(2)</sup>	\$ 29,693	29,225	29,744	29,702	28,625	23,632	21,260	22,081	22,943	24,814
Rental Cars	110,385	110,111	125,371	142,115	156,227	127,661	114,614	125,730	126,333	129,643
Food and Beverage	16,763	17,841	18,251	20,156	20,041	16,753	16,493	21,141	22,280	24,216
Advertising	2,878	3,705	4,627	3,451	1,892	1,923	1,736	1,903	1,873	2,355
Gift Shop & Retail	8,325	8,325	8,534	8,007	7,957	7,380	8,868	11,290	11,983	12,668
In-Flight Kitchen	12,697	9,883	7,731	7,277	5,819	6,173	8,580	9,823	8,920	10,680
Total Gross Concession Revenue	<u>\$ 180,741</u>	<u>179,090</u>	<u>194,258</u>	<u>210,708</u>	<u>220,561</u>	<u>183,522</u>	<u>171,551</u>	<u>191,968</u>	<u>194,332</u>	<u>204,376</u>
Enplaned Passengers:	5,292	5,346	5,415	5,319	5,179	4,400	4,107	4,189	4,125	4,235
Gross Concession Revenue Per Enplaned Passenger (not in 000's)	<u>\$ 34.15</u>	<u>33.50</u>	<u>35.87</u>	<u>39.61</u>	<u>42.59</u>	<u>41.71</u>	<u>41.77</u>	<u>45.83</u>	<u>47.11</u>	<u>48.26</u>

<sup>(1)</sup> Gross revenues of major concessionaires only.

<sup>(2)</sup> Gross public parking revenues only.

<sup>(3)</sup> Amounts reported previously were revised to reflect the correct information.

Source: Norman Y. Mineta San José International Airport activity reports and concession records

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**

**Schedule D**

(A Department of the City of San José)

**SCHEDULED AIRLINE RATES AND CHARGES**

**FISCAL YEARS 2004 THROUGH 2007 AND THE PERIOD JULY 1 TO NOVEMBER 30, 2007**

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007<sup>(2)</sup></u>	<u>2008<sup>(3)</sup></u>
Landing Fees (per 1,000 lbs. MGLW) <sup>(1)</sup>	\$ 1.34	\$ 1.28	\$ 1.43	\$ 1.80	\$ 1.44
Terminal Rental Rates (per square foot)					
Terminal A :					
Ticket counter	232	240	224	133	
Operations	174	180	168	100	
Holdroom	208	216	202	120	
Baggage claim	116	120	112	67	
Baggage makeup/storage	81	84	79	47	
Terminal C :					
Ticket counter	100	103	111	110	
Operations	75	77	84	83	
Holdroom	90	93	100	99	
Baggage Claim <sup>(4)</sup>	50	52	56	55	
Baggage makeup/storage	35	36	39	39	
Blended:					
Ticket counter			351		
Operations			316		
Holdroom			263		
Baggage Claim <sup>(4)</sup>			175		
Baggage makeup/storage			123		

(1) MGLW - Maximum Gross Landing Weight

(2) The Airport was able to reduce the terminal rental rates in fiscal year 2006-07 by utilizing \$4.0 million of the Safety Net Reserve Account. The account was established in 1993 to reserve funds for unusual or exceptional circumstances such as a significant imbalance of rates and charges for various facilities, projected extraordinary vacancy rates, and unusual discrepancies in activity levels.

(3) These rates and charges were only for the period July 1 to November 30, 2007. A new Airline-Airport Lease and Operating Agreement took effect on December 1, 2007. The rates for the period December 1, 2007 to June 30, 2008 (shown on the next page) were calculated in accordance with the provisions of the current agreement. Blended rental rates for Terminals A and C were calculated with the concurrence of the airlines.

(4) The baggage claim requirement is allocated among the airlines using the 20/80 formula. The revenue requirement applicable to the baggage claim areas is calculated by multiplying the square footage of all baggage claim areas by the square foot rate for those areas. 20% of the revenue requirement is divided equally among all airlines. The remaining 80% is distributed among all airlines based on the number of enplaned passengers.

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
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**Schedule D**  
 (Concluded)

**SCHEDULED AIRLINE RATES AND CHARGES <sup>(1)</sup>**

**PERIOD DECEMBER 1, 2007 to JUNE 30, 2008 THROUGH FISCAL YEAR 2013**

	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>Unit</u>
Landing Fees	\$ 2.00	\$ 2.24	\$ 2.32	\$ 2.47	\$ 2.14	\$ 2.38	per 1,000 lbs. MGLW <sup>(4)</sup>
Terminal Rental Rates							
Group A:							
Ticket counter and queuing, Skycap/Curbside Check-in							
- Preferential	73,729	81,192	145,136	241,041	319,205	296,954	per counter
- Common	35	63	57	73	97	90	per hour
Airline ticket office, Club/VIP	166.07	237.81	204.57	157.18	184.19	186.55	per sq. ft.
Holdroom (Gate)							
- Preferential	418,598	481,687	726,212	742,245	872,527	886,424	per gate
- Common	228	330	497	496	598	607	per turn
Group B:							
Baggage Claim <sup>(2)</sup>	132.86	190.25	163.66	125.74	147.35	149.24	per sq. ft.
Other Office	132.86	190.25	163.66	125.74	147.35	149.24	per sq. ft.
Group C:							
Baggage Make-up <sup>(3)</sup>	83.04	118.91	102.29	78.59	92.09	93.28	per sq. ft.
Operations Space	83.04	118.91	102.29	78.59	92.09	93.28	per sq. ft.

(1) These rates and charges were for the period December 1, 2007 to June 30, 2013 and were calculated based on the provisions of the current Airline-Airport Lease and Operating Agreement which took effect on December 1, 2007.

(2) The baggage claim requirement is allocated among the airlines using the 20/80 formula. The revenue requirements applicable to the baggage claim areas is calculated by multiplying the square footage of all baggage claim areas by the per-square foot rate for those areas. 20% of the revenue requirement is divided equally among all airlines. The remaining 80% of the revenue requirement is distributed among all airlines based on the number of deplaned passengers.

(3) The baggage make-up requirement is allocated among the airlines using the 20/80 formula. The revenue requirements applicable to the baggage make-up areas is calculated by multiplying the square footage of all baggage make-up areas by the per-square foot rate for those areas. 20% of the revenue requirement is divided equally among the airlines. The remaining 80% of the revenue requirement is distributed among the airlines based on the number of enplaned passengers.

(4) MGLW - Maximum Gross Landing Weight

Source: Norman Y. Mineta San José International Airport annual rates and charges analysis.

Schedule E

NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT

(A Department of the City of San José)

RATIOS OF OUTSTANDING DEBT AND DEBT SERVICE

LAST TEN FISCAL YEARS

(\$ and Passengers in 000's)

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
<b>Outstanding Debt per Enplaned Passenger</b>										
Outstanding debt by type:										
Revenue bonds	\$ 509,247	501,378	493,100	484,347	1,057,386	1,046,606	1,035,266	1,023,304	1,415,552	1,398,332
Commercial paper notes	5,786	7,755	8,089	41,424	186,190	323,561	417,348	410,079	47,937	45,380
Total outstanding debt	\$ 515,033	509,133	501,189	525,771	1,243,576	1,370,167	1,452,614	1,433,383	1,463,489	1,443,712
Enplaned Passengers	5,292	5,346	5,415	5,319	5,179	4,400	4,107	4,189	4,125	4,235
Total outstanding debt per enplaned passenger (not in 000's)	\$ 97	95	93	99	240	311	354	342	355	341
<b>Debt Service</b>										
Revenue bonds (2) (3)	\$ 17,454	17,932	21,423	20,837	21,567	23,037	31,367	53,890	80,725	86,325
Commercial paper notes (4) (5)	561	679	737	3,391	710	292	734	16,605	6,818	4,043
Total debt service	18,015	18,611	22,160	24,228	22,277	23,329	32,101	70,495	87,543	90,368
Less: Funds available for debt service										
Passenger facility charges	-	-	-	-	-	-	4,588	21,388	21,336	22,100
Customer facility charges <sup>(6)</sup>	-	-	-	-	-	-	-	6,840	10,137	13,385
Unspent bond proceeds <sup>(6)</sup>	-	-	-	-	-	-	-	-	1,713	5,802
Net debt service	\$ 18,015	18,611	22,160	24,228	22,277	23,329	27,513	42,267	54,357	49,081
Net debt service per enplaned passenger (not in 000's)	\$ 3.40	3.48	4.09	4.55	4.30	5.30	6.70	10.09	13.18	11.59

(1) Debt Limit information is not shown because the City does not establish or impose a debt limit.

(2) Under the Master Trust Agreement dated July 1, 2001, and as amended and supplemented to date (Master Trust), "Bond Debt Service" means for any specified period the sum of (a) the interest falling due on any then outstanding current interest bonds, assuming that all principal installments are paid when due, but excluding any interest funded from the proceeds of any series of bonds and applied toward payment of interest on such bonds, and (b) the principal installments payable on any then outstanding bonds. Also, under the Master Trust, the City may designate Passenger Facility Charges as "Available Passenger Facility Charges" for payment of eligible debt service. The amount of Debt Service is reduced by the amount Available Passenger Facility Charges designated by the City and deposited with the Trustee to pay Bond Debt Service.

(3) Per the Master Trust, rates used to calculate the interest payable on variable rate bonds, Series 2004A&B Airport Revenue Bonds, which were outstanding during fiscal years 2005 through 2008, were the actual interest rates that were in effect for the relevant period of calculation.

(4) As required by the Letter of Credit and Reimbursement Agreements related to the Airport's Commercial Paper (CP) Program, the principal amount of the CP is assumed to be amortized on a substantially level debt service for a period of 25 years commencing on the estimated completion date of the respective project to which such obligations relate or the date of issuance if the CP proceeds were not used for a project. As also required, the interest rate on the CP is assumed to be equal to an interest rate calculated by multiplying the average interest rate during the 90-day period prior to the end of the fiscal year by 1.15, as certified by a certificate of a financial advisor. As permitted by the Letter of Credit and Reimbursement Agreements, the outstanding CP as of June 30, 2011 was adjusted to reflect the repayment of certain CP from the proceeds of the Airport Revenue Bond Series 2011A. Under the previous Letter of Credit and Reimbursement Agreements, the calculation of debt service did not include the CP, which funded capitalizable projects during the fiscal years 2008 through 2010.

(5) Includes letter of credit fees associated with subordinated commercial paper.

(6) Fiscal years 2010 through 2012 were revised to reflect "Other Available Funds for Debt Service." Under the MTA, the Airport may for any period elect to designate Customer Facility Charges and Unspent Bond Proceeds as "Other Available Funds" eligible for payment of debt service.

## NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT

(A Department of the City of San José)

## DEBT SERVICE COVERAGE

## LAST TEN FISCAL YEARS

(in \$ 000's)

Year	Adjusted			Other	Net Revenues	Total	Available Passenger	Net Bond Debt Service	Estimated Commercial Paper (CP)	Coverage Ratio- Bonds & CP
	General Airport Revenues <sup>(1)</sup>	Operating Expenses <sup>(2) &amp; (3)</sup>	Net Revenues		Available Funds	Available for Debt Service	Bond Debt Service <sup>(4)</sup>	Facility Charges <sup>(4)</sup>		
2004	\$ 88,214	\$ 71,020	\$ 17,194	\$ 37,565	\$ 54,759	\$ 17,454		\$ 17,454	3.14	\$ 561 3.04
2005	89,806	73,422	16,384	37,666	54,050	17,932 <sup>(5)</sup>		17,932	3.01	679 2.90
2006	100,531	78,156	22,375	37,022	59,397	21,423 <sup>(5)</sup>		21,423	2.77	737 2.68
2007	96,661	86,120	10,541	44,250	54,791	20,837 <sup>(5)</sup>		20,837	2.63	3,391 2.26
2008	115,184	95,615	19,569	44,175	63,744	21,567 <sup>(5)</sup>		21,567	2.96	710 2.86
2009	115,115	90,783	24,332	49,053	73,385	23,037		23,037	3.19	292 3.15
2010	106,503	82,606	23,897	51,610	75,507	31,367	\$ 4,588	26,779	2.82	734 2.74
2011	123,447	76,850	46,597	52,447	99,044	53,890	21,388	32,502	3.05	16,605 2.02
2012	129,524	67,875	61,649	58,917	120,566	80,725	21,336	59,389	2.03	6,818 1.82
2013	124,803	64,778	60,025	66,006	126,031	86,325	22,100	64,225	1.96	4,043 1.85

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(1) Does not include Passenger Facility Charges (PFCs) or AIP grant proceeds. PFC revenues and AIP grant proceeds are included in the Statements of Revenues, Expenses, and Changes in Net Position as nonoperating revenues.

(2) Includes operating expenses less depreciation and expenses paid from sources other than General Airport Revenues.

(3) Excludes letter of credit fees associated with subordinated commercial paper. Letter of credit fees, net of capitalized fees, are reflected as part of operating expenses for accounting purposes. However, fees imposed pursuant to the reimbursement agreements relating to such letters of credit are Subordinate Obligations and are not incorporated in operating expenses for purposes of calculating debt service coverage.

(4) Under the Master Trust Agreement dated July 1, 2001, and as amended and supplemented to date (Master Trust), "Bond Debt Service" means for any specified period the sum of (a) the interest falling due on any then outstanding current interest bonds, assuming that all principal installments are paid when due, but excluding any interest funded from the proceeds of any series of bonds and applied toward payment of interest on such bonds, and (b) the principal installments payable on any then outstanding bonds. Also, under the Master Trust, the City may designate Passenger Facility Charges as "Available Passenger Facility Charges" for payment of eligible debt service. The amount of Debt Service is reduced by the amount Available Passenger Facility Charges designated by the City and deposited with the Trustee to pay Bond Debt Service.

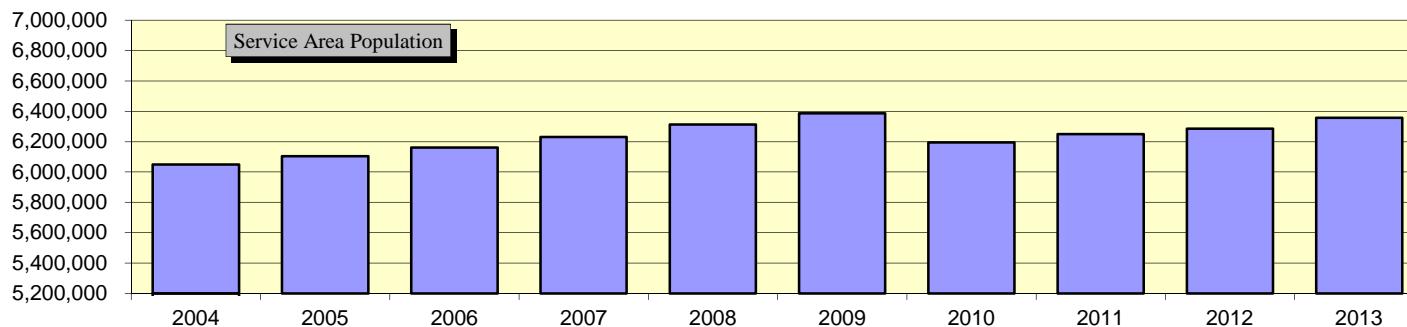
(5) Per the Master Trust, rates used to calculate the interest payable on variable rate bonds, Series 2004A&B Airport Revenue Bonds, which were outstanding during fiscal years 2005 through 2008, were the actual interest rates that were in effect for the relevant period of calculation.

(6) As required by the Letter of Credit and Reimbursement Agreements related to the Airport's Commercial Paper (CP) Program, the principal amount of the CP is assumed to be amortized on a substantially level debt service for a period of 25 years commencing on the estimated completion date of the respective project to which such obligations relate or the date of issuance if the CP proceeds were not used for a project. As also required, the interest rate on the CP is assumed to be equal to an interest rate calculated by multiplying the average interest rate during the 90-day period prior to the end of the fiscal year by 1.15, as certified by a certificate of a financial advisor. As permitted by the Letter of Credit and Reimbursement Agreements, the outstanding CP as of June 30, 2011 was adjusted to reflect the repayment of certain CP from the proceeds of the Airport Revenue Bond Series 2011A. Under the previous Letter of Credit and Reimbursement Agreements, the calculation of debt service did not include the CP which funded capitalizable projects during the fiscal years 2008 through 2010.

(7) Includes letter of credit fees associated with subordinated commercial paper.

**Schedule G**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**SERVICE AREA POPULATION IN THE AIR TRADE AREA**  
**LAST TEN CALENDAR YEARS**



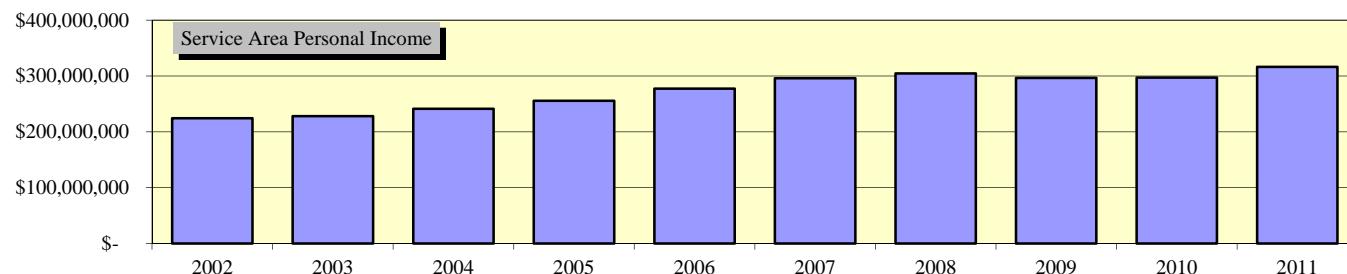
5

Years	Primary Service Area						Secondary Service Area				Total
	Alameda	Monterey	San Benito	San Mateo	Santa Clara	Santa Cruz	Merced	San Joaquin	Stanislaus		
2004	1,494,675	420,612	56,736	717,653	1,738,654	259,020	233,404	635,252	493,646	6,049,652	
2005	1,498,967	421,235	56,946	720,042	1,753,041	259,960	239,659	652,248	503,157	6,105,255	
2006	1,506,176	420,967	57,014	722,994	1,771,610	261,183	245,436	664,889	511,617	6,161,886	
2007	1,519,326	422,586	57,162	728,314	1,798,242	263,105	250,022	674,331	517,837	6,230,925	
2008	1,537,719	426,670	57,517	736,951	1,829,480	265,782	253,471	682,316	522,313	6,312,219	
2009	1,557,749	431,041	57,920	745,654	1,857,516	268,795	255,591	687,854	525,090	6,387,210	
2010	1,509,240	415,108	55,272	718,614	1,781,427	262,552	255,399	684,057	514,003	6,195,672	
2011	1,521,157	419,038	55,619	724,702	1,797,375	264,430	257,984	690,899	517,685	6,248,889	
2012	1,530,176	419,586	56,137	727,795	1,813,696	265,350	260,029	692,997	519,339	6,285,105	
2013	1,548,681	421,494	56,669	735,678	1,842,254	266,662	262,478	698,414	524,124	6,356,454	

Source: California Department of Finance

Schedule H

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**SERVICE AREA PERSONAL INCOME IN THE AIR TRADE AREA**  
**LAST TEN AVAILABLE CALENDAR YEARS (1)**  
(in \$ 000's)



01-S

Years	Primary Service Area						Secondary Service Area				Total
	<u>Alameda</u>	<u>Monterey</u>	<u>San Benito</u>	<u>San Mateo</u>	<u>Santa Clara</u>	<u>Santa Cruz</u>	<u>Merced</u>	<u>San Joaquin</u>	<u>Stanislaus</u>		
2002	\$ 55,316,772	12,676,027	1,575,049	36,736,603	77,548,912	9,495,857	4,644,678	14,788,895	11,460,836	224,243,629	
2003	56,424,129	13,380,948	1,623,818	36,466,977	78,152,243	9,498,586	4,989,214	15,576,802	11,959,040	228,071,757	
2004	59,339,211	14,096,150	1,681,863	39,408,618	81,920,659	10,194,797	5,359,381	16,555,526	12,868,305	241,424,510	
2005	62,015,782	14,653,598	1,704,973	42,846,390	87,909,716	10,462,655	5,409,165	17,189,529	13,472,415	255,664,223	
2006	66,998,496	15,774,227	1,809,212	46,881,900	96,443,117	11,464,854	5,613,205	18,292,157	14,076,261	277,353,429	
2007	70,761,435	16,694,108	1,897,021	50,347,246	104,102,421	12,116,023	6,108,301	19,194,503	14,755,527	295,976,585	
2008	73,819,703	17,243,092	1,954,831	51,062,495	103,697,458	12,962,445	6,842,821	21,121,955	16,072,573	304,777,373	
2009	71,596,468	17,126,664	1,945,249	50,014,142	99,549,995	12,591,938	6,750,415	20,968,710	15,948,738	296,492,319	
2010	72,024,822	16,677,674	1,882,370	47,946,507	102,589,854	12,246,607	6,956,076	20,802,181	15,980,924	297,107,015	
2011	75,908,145	17,355,940	1,964,156	50,596,839	111,880,131	12,919,550	7,406,375	21,591,743	16,652,338	316,275,217	

(1) Information for calendar years 2012 and 2013 is not available.

Source: U.S. Department of Commerce, Bureau of Economic Analysis

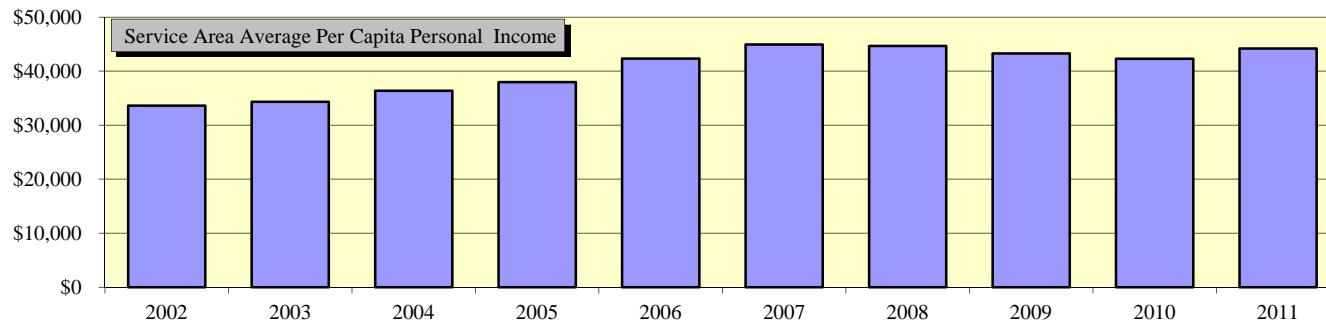
Schedule I

NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT

(A Department of the City of San José)

SERVICE AREA PER CAPITA PERSONAL INCOME IN THE AIR TRADE AREA

LAST TEN AVAILABLE CALENDAR YEARS <sup>(1)</sup>



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Years	Primary Service Area						Secondary Service Area			
	Alameda	Monterey	San Benito	San Mateo	Santa Clara	Santa Cruz	Merced	San Joaquin	Stanislaus	Average PCPI
2002	\$ 37,839	30,931	28,531	52,480	46,292	37,397	20,801	24,290	24,000	33,618
2003	38,835	32,527	29,327	52,405	46,769	37,708	21,810	24,883	24,551	34,313
2004	41,083	34,362	30,534	56,788	48,958	40,632	22,955	25,785	26,132	36,359
2005	43,074	36,014	31,041	61,678	52,081	41,917	22,724	26,209	26,954	37,966
2006	47,781	40,908	34,139	68,843	56,521	48,206	25,205	29,513	29,654	42,308
2007	49,915	42,322	36,173	74,343	60,098	51,669	27,981	31,018	30,816	44,926
2008	50,206	42,506	35,674	72,112	59,058	51,249	28,003	31,584	31,673	44,674
2009	48,004	41,735	35,331	69,562	55,781	49,145	27,517	31,071	31,248	43,266
2010	47,603	40,055	33,904	66,629	57,433	46,586	27,092	30,251	31,006	42,284
2011	49,617	41,138	35,029	69,577	61,833	48,883	28,497	31,013	32,115	44,189

<sup>(1)</sup> Information for calendar years 2012 and 2013 is not available.

Source: U.S. Department of Commerce, Bureau of Economic Analysis

**Schedule J**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**

(A Department of the City of San José)

**PRINCIPAL EMPLOYERS IN THE CITY OF SAN JOSE  
CURRENT YEAR AND SEVEN YEARS AGO**

Company or Organization	2013			2006		
	Number of Employees	Rank	Percent of Total Employment	Number of Employees	Rank	Percent of Total Employment
County of Santa Clara	14,950	1	3.33%	14,860	2	3.66%
Cisco Systems	13,600	2	3.03%	16,500	1	4.06%
City of San Jose*	5,651	3	1.26%	6,670	3	1.64%
eBay Inc.	4,700	4	1.05%	2,200	8	0.54%
IBM	4,200	5	0.93%	5,800	4	1.43%
U.S. Postal Service	3,920	6	0.87%	na (**)	na (**)	na (**)
San Jose State University	3,119	7	0.69%	3,100	5	0.76%
San Jose Unified School District	2,330	8	0.52%	1,820	13	0.45%
Hitatchi	2,070	9	0.46%	2,880	6	0.71%
Adobe Systems, Inc.	2,000	10	0.45%	2,000	10	0.49%
Good Samaritan Hospital	1,950	11	0.43%	1,850	12	0.46%
Kaiser Permanente	1,940	12	0.43%	na (**)	na (**)	na (**)
Cadence Design Systems	1,800	13	0.40%	1,750	14	0.43%
Sanmina-SCI	1,770	14	0.39%	2,100	9	0.52%
Maxim Integrated	1,650	15	0.37%	na (**)	na (**)	na (**)

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Note: Data pertaining to principal employers for nine years ago is not readily available. As such, we used 2006 information which was the earliest available.

(\*) Full-time employees

(\*\*) Companies or organizations not included in top 15 principal employers in 2006

Sources: Office of Economic Development, City of San Jose  
California Employment Development Department, Labor Market Information Division

**Schedule K**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**AIRPORT EMPLOYEES**  
**LAST TEN FISCAL YEARS**

<b>Functional Area</b>	<b>Budgeted Full-time-Equivalent <sup>(1)</sup> Employees as of Fiscal Year-End</b>									
	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>	<b>2011</b>	<b>2012</b>	<b>2013</b>
Acoustical Treatment Program (ACT)	16.25	10.00	9.00	7.00	7.00	4.00	0.00	0.00	0.00	0.00
Administration	39.35	35.55	34.55	37.75	39.75	34.65	31.00	26.70	27.00	27.00
Air Service Development	3.00	3.25	4.50	4.60	4.60	2.00	2.00	1.00	1.00	1.00
Airport Technology Services	8.00	8.00	17.00	21.00	21.00	19.00	16.00	13.00	13.00	13.00
Airside Operations	58.00	49.20	46.00	46.50	46.55	47.25	38.45	35.15	39.53	41.97
Customer Service and Outreach	9.00	8.75	7.60	11.40	10.40	8.00	6.00	5.00	6.00	7.00
Capital and Airport Development	45.75	52.05	46.05	38.05	28.25	27.25	25.50	18.00	14.00	15.00
Environmental	4.25	3.20	4.20	3.20	3.00	3.50	3.00	1.00	1.00	1.00
Facilities (Building Services, Trades and Maintenance)	161.00	148.00	143.00	143.00	155.00	134.50	127.50	64.00	66.00	64.00
Landside Operations and Services	64.50	66.30	64.50	61.50	62.45	55.75	46.55	34.15	29.47	9.03
Property Management	10.40	12.20	12.10	12.00	13.00	12.10	9.00	8.00	8.00	8.00
	<b><u>419.50</u></b>	<b><u>396.50</u></b>	<b><u>388.50</u></b>	<b><u>386.00</u></b>	<b><u>391.00</u></b>	<b><u>348.00</u></b>	<b><u>305.00</u></b>	<b><u>206.00</u></b>	<b><u>205.00</u></b>	<b><u>187.00</u></b>

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<sup>(1)</sup> A full-time employee is scheduled to work 2,088 hours per year (including vacation and sick leave).

Full-time-equivalent employment is calculated by dividing total labor hours by 2,088.

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**AIRPORT INFORMATION**  
**JUNE 30, 2013**

<b>Location:</b>	Two miles north of downtown San José, "Capital of Silicon Valley"																
<b>Area:</b>	1,050 acres																
<b>Elevation:</b>	56 ft.																
<b>Airport Code:</b>	SJC																
<b>Runways:</b>	11/29 (temporarily closed)	North/South	4,599 × 100 ft.														
	12R/30L	North/South	11,000 × 150 ft. ILS/ VOR / GPS														
	12L/30R	North/South	11,000 × 150 ft. GPS (VOR 30R only)														
<b>Terminal:</b>	<table border="0"> <tr> <td>Airlines</td> <td>242,435 sq. ft.</td> </tr> <tr> <td>Concessions and Other Rentables</td> <td>63,276 sq. ft.</td> </tr> <tr> <td>Public/common</td> <td>167,006 sq. ft.</td> </tr> <tr> <td>Airport</td> <td>367,779 sq. ft.</td> </tr> <tr> <td>Vacant</td> <td>44,107 sq. ft.</td> </tr> <tr> <td>Other</td> <td>106,962 sq. ft.</td> </tr> <tr> <td>Total</td> <td>991,565 sq. ft.</td> </tr> </table>			Airlines	242,435 sq. ft.	Concessions and Other Rentables	63,276 sq. ft.	Public/common	167,006 sq. ft.	Airport	367,779 sq. ft.	Vacant	44,107 sq. ft.	Other	106,962 sq. ft.	Total	991,565 sq. ft.
Airlines	242,435 sq. ft.																
Concessions and Other Rentables	63,276 sq. ft.																
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Vacant	44,107 sq. ft.																
Other	106,962 sq. ft.																
Total	991,565 sq. ft.																
	<table border="0"> <tr> <td>Number of passenger gates - Terminal A and FIS</td> <td>16</td> </tr> <tr> <td>Number of passenger gates - Terminal B</td> <td>12</td> </tr> <tr> <td>Number of loading bridges</td> <td>28</td> </tr> <tr> <td>Number of concessionaires in terminal</td> <td>43</td> </tr> <tr> <td>Number of rental car agencies</td> <td>12</td> </tr> </table>			Number of passenger gates - Terminal A and FIS	16	Number of passenger gates - Terminal B	12	Number of loading bridges	28	Number of concessionaires in terminal	43	Number of rental car agencies	12				
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Number of concessionaires in terminal	43																
Number of rental car agencies	12																
<b>Apron:</b>	<table border="0"> <tr> <td>Commercial Airlines</td> <td>1,130,408 sq. ft.</td> </tr> <tr> <td>Cargo Airlines</td> <td>596,436 sq. ft.</td> </tr> <tr> <td>Fixed Base Operator (FBO)</td> <td>426,071 sq. ft.</td> </tr> <tr> <td>General Aviation West</td> <td>436,659 sq. ft.</td> </tr> </table>			Commercial Airlines	1,130,408 sq. ft.	Cargo Airlines	596,436 sq. ft.	Fixed Base Operator (FBO)	426,071 sq. ft.	General Aviation West	436,659 sq. ft.						
Commercial Airlines	1,130,408 sq. ft.																
Cargo Airlines	596,436 sq. ft.																
Fixed Base Operator (FBO)	426,071 sq. ft.																
General Aviation West	436,659 sq. ft.																
<b>Parking:</b>	Spaces assigned:	Hourly - Terminal A Garage Hourly - Terminal B Garage & Surface Daily lots Economy lots Rental cars Employees	1,315 1,203 1,358 1,676 3,000 <hr/> 800														
		Total	<hr/> 9,352														
<b>Cargo:</b>	Air Freight Building																
	19,200 sq. ft.																
<b>International:</b>	Customs / Federal Inspection Service Facility																
<b>Tower:</b>	Operational hours 0600 - 0000, after hours CTAF 124.0/TRACON 24/7																
<b>FBOs:</b>	Atlantic San Jose AvBase																

Source: Norman Y. Mineta San José International Airport, City of San José

Schedule M

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**ENPLANED COMMERCIAL PASSENGERS BY AIRLINE<sup>(1)</sup>**  
**LAST TEN FISCAL YEARS**  
**(Ranked by Fiscal Year 2013 Results)**

Airline	2004		2005		2006		2007		2008	
	Enplanements	% of Total								
Southwest Airlines	2,003,802	37.9%	2,140,938	40.1%	2,198,806	40.6%	2,266,766	42.6%	2,333,432	45.1%
Alaska Airlines	490,392	9.3%	492,357	9.2%	489,022	9.0%	467,324	8.8%	445,689	8.6%
American Airlines	1,316,502	24.9%	1,221,431	22.8%	1,029,154	19.0%	923,052	17.4%	771,429	14.9%
US Airways	281,303	5.3%	309,692	5.8%	308,204	5.7%	308,522	5.8%	298,193	5.8%
Continental Airlines <sup>(2)</sup>	138,500	2.6%	147,045	2.8%	155,324	2.9%	169,220	3.2%	171,189	3.3%
United Airlines <sup>(2)(3)</sup>	398,245	7.5%	386,361	7.2%	392,199	7.2%	380,109	7.1%	349,962	6.8%
Skywest <sup>(4)</sup>	116,235	2.2%	133,875	2.5%	124,565	2.3%	139,956	2.6%	115,184	2.2%
Delta Airlines <sup>(5)</sup>	181,008	3.4%	183,957	3.4%	215,062	4.0%	182,524	3.4%	156,339	3.0%
Hawaiian Airlines					62,261	1.1%	82,561	1.6%	84,259	1.6%
JetBlue Airways	2,934	0.1%	64,003	1.2%	136,666	2.5%	109,351	2.1%	116,776	2.3%
Concesionaria Vuela Compania de Aviacion S.A. DE CV <sup>(6)</sup>										
All Other Airlines <sup>(7)</sup>	362,928	6.9%	265,974	5.0%	303,568	5.6%	289,474	5.4%	336,151	6.5%
Total <sup>(8)</sup>	<b>5,291,849</b>	<b>100%</b>	<b>5,345,633</b>	<b>100%</b>	<b>5,414,831</b>	<b>100%</b>	<b>5,318,859</b>	<b>100%</b>	<b>5,178,603</b>	<b>100%</b>

<sup>(1)</sup> Except as noted, mainline carriers and their regional/commuter affiliates are grouped to show relative market share by carrier.

<sup>(2)</sup> Continental and United merged in October 2010. The combined airlines (named United Airlines) received FAA approval to operate under a single certificate in December 2011 but continued to operate as separate airlines until June 30, 2012.

<sup>(3)</sup> Excludes enplaned passengers on flights operated by Skywest as United Express.

<sup>(4)</sup> Operates as United Express, Delta Connection, and American Eagle.

<sup>(5)</sup> Excludes enplaned passengers on flights operated by Skywest as Delta Connection.

<sup>(6)</sup> Concesionaria Vuela Compania de Aviacion S.A DE CV (aka Volaris) started operations in April 2010.

<sup>(7)</sup> Consists of airlines no longer serving the Airport and charter airlines.

<sup>(8)</sup> Percentage totals may not add due to rounding.

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**ENPLANED COMMERCIAL PASSENGERS BY AIRLINE <sup>(1)</sup>**  
**LAST TEN FISCAL YEARS**  
**(Ranked by Fiscal Year 2013 Results)**

Airline	2009		2010		2011		2012		2013	
	Enplanements	% of Total								
Southwest Airlines	2,082,271	47.3%	2,121,917	51.7%	2,187,033	52.2%	2,192,234	53.1%	2,169,956	51.2%
Alaska Airlines	345,419	7.9%	393,982	9.6%	561,400	13.4%	609,315	14.8%	727,616	17.2%
American Airlines <sup>(2)</sup>	632,723	14.4%	480,402	11.7%	435,815	10.4%	386,997	9.4%	355,024	8.4%
US Airways	250,458	5.7%	208,809	5.1%	184,380	4.4%	183,955	4.5%	187,583	4.4%
Continental Airlines <sup>(3)</sup>	136,153	3.1%	132,942	3.2%	134,449	3.2%	121,933	3.0%		
United Airlines <sup>(3)(4)</sup>	208,184	4.7%	138,836	3.4%	133,794	3.2%	117,292	2.8%	186,890	4.4%
Skywest <sup>(5)</sup>	139,478	3.2%	180,337	4.4%	149,912	3.6%	131,412	3.2%	182,113	4.3%
Delta Airlines <sup>(6)</sup>	94,241	2.1%	100,539	2.4%	155,885	3.7%	146,661	3.6%	158,880	3.8%
Hawaiian Airlines	81,397	1.9%	72,266	1.8%	85,571	2.0%	103,483	2.5%	116,928	2.8%
JetBlue Airways	148,643	3.4%	95,118	2.3%	80,797	1.9%	76,063	1.8%	71,506	1.7%
Concesionaria Vuela Compania de Aviacion S.A. DE CV <sup>(7)</sup>			8,072	0.2%	48,325	1.2%	49,709	1.2%	49,700	1.2%
Virgin America <sup>(8)</sup>									18,265	0.4%
All Nippon Airways Co., LTD <sup>(9)</sup>									3,273	0.1%
All Other Airlines <sup>(10)</sup>	280,595	6.4%	174,174	4.2%	31,862	0.8%	5,831	0.1%	7,019	0.2%
Total <sup>(11)</sup>	4,399,562	100%	4,107,394	100%	4,189,223	100%	4,124,885	100%	4,234,753	100%

<sup>(1)</sup> Except as noted, mainline carriers and their regional/commuter affiliates are grouped to show relative market share by carrier.

<sup>(2)</sup> Excludes enplaned passengers on flights operated by Skywest as American Eagle, which started in November 2012.

<sup>(3)</sup> Continental and United merged in October 2010. The combined airlines (named United Airlines) received FAA approval to operate under a single certificate in December 2011 but continued to operate as separate airlines until June 30, 2012. Continental Airlines passengers are grouped with United Airlines starting July 1, 2012.

<sup>(4)</sup> Excludes enplaned passengers on flights operated by Skywest as United Express.

<sup>(5)</sup> Operates as United Express, Delta Connection, and American Eagle.

<sup>(6)</sup> Excludes enplaned passengers on flights operated by Skywest as Delta Connection.

<sup>(7)</sup> Concesionaria Vuela Compania de Aviacion S.A DE CV (aka Volaris) started operations in April 2010.

<sup>(8)</sup> Virgin America started operations in May 2013.

<sup>(9)</sup> All Nippon Airways Co., LTD started operations in January 2013.

<sup>(10)</sup> Consists of airlines no longer serving the Airport and charter airlines.

<sup>(11)</sup> Percentage totals may not add due to rounding.

## Schedule N

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**AIRLINE LANDED WEIGHTS (1,000's lb)**  
**LAST TEN FISCAL YEARS**

<u>Airline<sup>(1)</sup></u>	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Air Canada				1,612	2,207	1,469	284	3,159	2,654	2,381
Alaska Airlines	600,898	508,275	490,114	472,515	441,300	337,540	363,017	503,725	505,340	606,086
All Nippon Airways Co., LTD										9,880
Atlantic Southeast Airlines		8,643	17,554	5,025						
American Airlines	1,563,878	1,279,122	850,139	733,523	572,925	480,870	366,797	359,335	305,694	315,986
American Eagle	380,940	351,441	391,471	346,514	305,779	254,983	131,181	87,935	86,967	50,923
ATA	105,132	396	224	550	566					
Concesionaria Vuela compania De Aviacion S.A										
DE CV (aka Volaris)							8,320	54,663	59,451	52,014
Continental Airlines	159,142	164,344	164,858	178,500	181,657	142,465	133,055	135,858	128,219	93,682
Delta Airlines	244,109	226,950	259,322	233,734	194,892	119,454	116,624	165,760	155,622	175,260
Expressjet Airlines Inc. dba Delta Airlines				44	58,816	8,047	41			
Frontier Airlines	92,045	97,781	128,282	143,487	153,166	158,644	78,484	672		672
Hawaiian Airlines			87,360	128,960	115,545	109,970	94,075	110,895	133,520	161,560
Horizon Air	114,176	130,792	104,759	98,525	115,790	111,530	144,240	189,443	175,246	200,317
Independence Airlines		8,405	9,231							
JetBlue Airways	2,986	68,682	155,706	124,565	147,688	188,439	115,710	91,292	82,903	79,348
Mesa Airlines	26,273	5,338	12,640	21,664	22,399	4,168		168		167
Mexicana Airlines	83,270	78,780	116,903	113,125	100,668	86,527	76,916	10,890		
Northwest Airlines	172,244	118,242	107,918	100,756	101,591	101,284	51,691			
Skywest	155,754	164,480	151,419	166,716	146,500	174,983	217,883	163,478	143,527	202,560
Southwest Airlines	2,867,763	3,009,958	3,065,960	3,197,472	3,366,428	3,236,828	3,033,408	2,877,878	2,917,030	2,838,160
United Airlines	535,528	499,892	515,943	490,735	474,724	277,027	182,268	178,965	161,273	126,942
US Airways	351,611	401,640	377,223	415,366	387,348	316,454	262,199	245,557	250,324	245,444
Virgin America										32,515
All Other Airlines	16,985	6,046	13,670	16,145	22,137	19,387	34,324	41,329	17,454	19,466
<b>Subtotal</b>	<b>7,472,734</b>	<b>7,129,207</b>	<b>7,020,696</b>	<b>6,989,533</b>	<b>6,912,126</b>	<b>6,130,069</b>	<b>5,410,517</b>	<b>5,221,002</b>	<b>5,125,391</b>	<b>5,213,194</b>
<b>Cargo Carriers</b>										
Air Transport Int'l.	55,798	61,414	55,733	57,941	59,379	56,042	57,159	71,055	12,015	250
Airborne Express	71,094	70,720	68,816	70,176	57,392	1,088				
Emery Worldwide Express										
Fedex	289,284	268,055	223,154	252,539	241,953	231,594	168,403	164,642	163,213	158,845
Kitty Hawk	638			155						
United Parcel Service	127,399	128,470	126,660	129,090	133,653	132,055	96,505	83,136	93,250	88,940
All Other Cargo Airlines	2,844	3,184	4,013	1,862	247	309	200	352	270	33
<b>Subtotal</b>	<b>547,057</b>	<b>531,843</b>	<b>478,376</b>	<b>511,763</b>	<b>492,624</b>	<b>421,088</b>	<b>322,267</b>	<b>319,185</b>	<b>268,748</b>	<b>248,067</b>
<b>Total</b>	<b>8,019,791</b>	<b>7,661,050</b>	<b>7,499,072</b>	<b>7,501,296</b>	<b>7,404,750</b>	<b>6,551,157</b>	<b>5,732,784</b>	<b>5,540,187</b>	<b>5,394,139</b>	<b>5,461,261</b>

(1) See Notes on Schedule M.

Source: Norman Y. Mineta San José International Airport activity reports

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**AIRLINE FLIGHT OPERATIONS BY AIRLINE AND CARGO CARRIER**  
**LAST TEN FISCAL YEARS**

<u>Airline<sup>(1)</sup></u>	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Air Canada	18			2	4	22		46	38	36
Alaska Airlines	9,464	7,926	7,592	7,264	6,760	5,176	5,444	7,308	7,272	8,684
All Nippon Airways Co., LTD										52
Atlantic Southeast Airlines		258	524	150						
American Airlines	19,136	16,214	11,678	10,734	9,012	7,704	5,800	5,552	4,728	4,878
American Eagle	18,554	17,094	19,018	16,816	14,838	12,370	6,364	4,266	4,098	2,018
ATA	1,160	4	2	4	6	378				
Concessionaria Vuela Compania De Aviacion S.A DE CV							124	812	886	770
Continental Airlines	2,342	2,404	2,490	2,730	2,770	2,060	1,898	1,862	1,750	1,284
Delta Airlines	3,326	3,122	3,524	2,852	2,526	1,504	1,570	2,264	2,094	2,358
ExpressJet Airlines Inc dba Delta Airlines					2,738		2			
Frontier Airlines	1,388	1,476	1,942	2,190	2,360	2,426	1,202	10		10
Hawaiian Airlines			546	806	732	732	620	732	882	1,036
Horizon Air	3,424	3,960	3,200	3,086	3,602	3,428	4,484	6,062	5,676	6,488
Independence Airlines			122	134						
JetBlue Airways	42	966	2,190	1,752	2,102	2,986	1,876	1,284	1,166	1,116
Mesa Airlines	1,118	226	434	592	614	126		14	6	6
Mexicana Airlines	1,090	1,044	1,588	1,600	1,430	1,250	1,126	160		
Northwest Airlines	2,474	1,670	1,540	1,434	1,446	1,410	746			
Skywest	7,742	8,134	7,580	8,158	7,518	7,526	8,636	5,838	5,026	7,404
Southwest Airlines	49,254	50,402	50,936	52,872	54,974	52,414	48,942	46,584	47,002	45,486
United Airlines	8,222	7,386	7,076	6,932	6,420	3,572	2,224	2,124	1,988	1,586
US Airways	5,342	6,076	5,748	6,168	6,070	5,110	4,130	3,624	3,618	3,554
Virgin America										458
All Other Airlines	268	80	212	260	442	304	598	732	248	290
<b>Subtotal</b>	<b>134,364</b>	<b>128,564</b>	<b>127,954</b>	<b>126,402</b>	<b>126,364</b>	<b>110,498</b>	<b>95,800</b>	<b>89,266</b>	<b>86,478</b>	<b>87,508</b>
<b>Cargo Carriers</b>										
Air Transport Int'l.	422	468	424	442	452	426	434	538	88	2
Airborne Express	524	520	506	516	422	8				
Emery Worldwide Express										
FedEx	1,430	1,400	1,270	1,326	1,324	1,264	958	926	928	918
Kitty Hawk	8			2						
United Parcel Service	910	924	908	926	916	854	672	566	652	610
All Other Cargo Airlines	292	282	356	176	26	6	12	16	10	6
<b>Subtotal</b>	<b>3,586</b>	<b>3,594</b>	<b>3,464</b>	<b>3,388</b>	<b>3,140</b>	<b>2,558</b>	<b>2,076</b>	<b>2,046</b>	<b>1,678</b>	<b>1,536</b>
<b>Total</b>	<b>137,950</b>	<b>132,158</b>	<b>131,418</b>	<b>129,790</b>	<b>129,504</b>	<b>113,056</b>	<b>97,876</b>	<b>91,312</b>	<b>88,156</b>	<b>89,044</b>

<sup>(1)</sup> See notes on Schedule M.

Source: Norman Y. Mineta San José International Airport activity reports

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**SCHEDULED/COMMUTER/ALL-CARGO AIRLINE SERVICE**

**Schedule P**

**CARRIER**

**NONSTOP SERVICE**

**SCHEDULED DOMESTIC AIRLINE SERVICE**

Alaska Airlines

Honolulu, Oahu (HNL)  
 Kahului, Maui (OGG)  
 Kona, Hawaii (KOA)  
 Lihue, Kauai (LIH)  
 Portland (PDX)  
 Seattle (SEA)

American Airlines

Chicago/O'Hare (ORD)  
 Dallas/Ft. Worth (DFW)

Delta Airlines

Atlanta (ATL)  
 Minneapolis/St. Paul (MSP)  
 Salt Lake City (SLC)

Hawaiian Airlines

Honolulu, Oahu (HNL)  
 Kahului, Maui (OGG)

JetBlue Airlines

Boston (BOS)  
 New York (JFK)

Southwest Airlines

Austin (AUS)  
 Burbank (BUR)  
 Chicago/Midway (MDW)  
 Denver (DEN)  
 Las Vegas (LAS)  
 Los Angeles (LAX)  
 Ontario (ONT)  
 Orange County (SNA)  
 Phoenix (PHX)  
 Portland (PDX)  
 San Diego (SAN)  
 Seattle (SEA)

United Airlines

Denver (DEN)  
 Houston (IAH)

US Airways

Phoenix (PHX)

Virgin America

Los Angeles (LAX)

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**SCHEDULED/COMMUTER/ALL-CARGO AIRLINE SERVICE**

**Schedule P  
(Concluded)**

**CARRIER**

**NONSTOP SERVICE**

**COMMUTER AIRLINE SERVICE**

American Eagle (regional carrier for American Airlines)	Los Angeles (LAX)
Horizon Air (regional carrier for Alaska Airlines)	Boise (BOI) Los Angeles (LAX) Portland (PDX) Reno (RNO)
Mesa Airlines (on behalf of US Airways)	Phoenix (PHX)
Skywest (on behalf of Delta and United)	Denver (DEN) Los Angeles (LAX) Salt Lake City (SLC)

**SCHEDULED FOREIGN AIRLINE SERVICE**

Alaska Airlines	Cabo San Lucas (SJD) Guadalajara (GDL)
ANA	Tokyo-Narita (NRT)
Volaris	Guadalajara (GDL)

**ALL-CARGO AIRLINES**

Federal Express Corporation
United Parcel Service

Source: Norman Y. Mineta San José International Airport activity reports

## Schedule Q

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**PASSENGERS, MAIL, FREIGHT, AND CARGO STATISTICS**  
**LAST TEN FISCAL YEARS**

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
<b>Passengers (1,000's):</b>										
Enplanements	5,292	5,346	5,415	5,319	5,179	4,400	4,107	4,189	4,125	4,235
Deplanements	5,276	5,382	5,437	5,335	5,202	4,422	4,125	4,200	4,131	4,254
Total Passengers	<b>10,568</b>	<b>10,728</b>	<b>10,852</b>	<b>10,654</b>	<b>10,381</b>	<b>8,822</b>	<b>8,232</b>	<b>8,389</b>	<b>8,256</b>	<b>8,489</b>
<b>Mail/Freight/Cargo (1,000 lbs):</b>										
Mail	8,988	9,213	7,593	4,342	3,044	1,987	3,357	2,264	1,160	1,431
Freight/Express	26,462	25,449	22,577	12,228	7,101	5,995	5,432	5,060	5,303	6,172
Cargo	<b>203,444</b>	<b>190,871</b>	<b>179,612</b>	<b>171,754</b>	<b>166,509</b>	<b>129,809</b>	<b>97,578</b>	<b>87,329</b>	<b>77,303</b>	<b>78,766</b>
Total mail/freight/cargo	<b>238,894</b>	<b>225,533</b>	<b>209,782</b>	<b>188,324</b>	<b>176,654</b>	<b>137,791</b>	<b>106,367</b>	<b>94,653</b>	<b>83,766</b>	<b>86,369</b>

S-21

Source: Norman Y. Mineta San José International Airport activity reports

Schedule R

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**HISTORICAL AIRCRAFT OPERATIONS <sup>(1)</sup>**  
**LAST TEN FISCAL YEARS**

Fiscal Year	Air Carrier <u>Operations</u> <sup>(2)</sup>	Commuter <u>Operations</u>	Cargo <u>Operations</u>	Total Commercial <u>Operations</u> <sup>(3)</sup>	Percent Commercial <u>Operations</u>	General Aviation <u>Operations</u>	Military <u>Operations</u>	Total <u>Operations</u>
2004	103,526	30,838	3,586	137,950	69.8%	59,521	113	197,584
2005	98,892	29,672	3,594	132,158	67.4%	63,708	99	195,965
2006	97,198	30,756	3,464	131,418	67.9%	61,907	83	193,408
2007	97,596	28,806	3,388	129,790	70.2%	55,021	103	184,914
2008	96,860	29,504	3,140	129,504	70.1%	55,146	64	184,714
2009	86,668	23,830	2,558	113,056	70.7%	46,674	242	159,972
2010	76,024	19,776	2,076	97,876	74.4%	33,439	275	131,590
2011	73,094	16,172	2,046	91,312	74.8%	30,503	276	122,091
2012	71,672	14,806	1,678	88,156	73.4%	31,664	285	120,105
2013	71,598	15,910	1,536	89,044	73.8%	31,321	210	120,575

**Annual Compound**

**Growth Rate**

FY 2004  
through  
FY 2013

-3.6%            -6.4%            -8.1%            -4.3%            0.6%            -6.2%            6.4%            -4.8%

<sup>(1)</sup> An aircraft operation is defined as the takeoff or landing of an aircraft.

<sup>(2)</sup> Includes domestic and international airlines.

<sup>(3)</sup> Represents the sum of Mainline Air Carrier Operations, Regional Commuter Operations and All-Cargo Operations.

Source: Norman Y. Mineta San José International Airport activity reports



# BOND DISCLOSURE



All Nippon Airways, Japan's largest airline and a pioneer in the commercial aviation industry, now operates daily flights to Narita International Airport in Tokyo on the Boeing 787 Dreamliner.

Virgin America, a favorite of tech savvy travelers and recently recognized as the nation's best performing airline by the annual Airline Quality Rating, now operates nonstop service to Los Angeles International Airport with four daily flights.



NORMAN Y. MINETA  
**SAN JOSE**  
INTERNATIONAL  
AIRPORT  
SILICON VALLEY'S AIRPORT

CITY OF  
**SAN JOSE**  
CAPITAL OF SILICON VALLEY

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT  
(A Department of the City of San José)**

**Bond Disclosure Report**

**June 30, 2013**

In accordance with the requirements of the Continuing Disclosure Agreements (Disclosure Agreements) for the City of San José Airport Revenue Bonds Series 2001A, 2004C, 2004D, 2007A, 2007B, 2011A-1, 2011A-2, 2011B, and Airport Revenue Refunding Bonds Series 2012A, the Airport is including this section to meet the requirements of Securities and Exchange Commission Rule 15c2-12(b)(5) (the Rule).

Section 4 of the Disclosure Agreements requires the City to provide an Annual Report, which is consistent with the requirements of Section 4 of the Disclosure Agreements, no later than six months after the end of the City's fiscal year. The Annual Report may be submitted to the Municipal Securities Rulemaking Board's EMMA system as a single document or as separate documents comprising a package, and may include by reference other information as provided in Section 4 of the Disclosure Agreements. The Bond Disclosure Report included in this CAFR meets the requirements of Section 4 of the Disclosure Agreements.

**Annual Report**

The following items are required by the Disclosure Agreements to be included in the Annual Report:

- ◆ Audited financial statements of the Airport, updated to incorporate information for the most recent fiscal year, prepared in accordance with generally accepted accounting principles as promulgated to apply to governmental entities from time to time by the Governmental Accounting Standards Board and further modified according to applicable State law.

**Refer to the Financial Section, pages 1-61 of this report.**

- ◆ A schedule showing the debt service requirements (required only to the extent there are changes).

**Refer to Table 1, page B-3 of the Bond Disclosure Section of this report.**

- ◆ A schedule showing, for the Airport's most recently completed fiscal year, historical passenger enplanements.

**Refer to Table 2, page B-4 of the Bond Disclosure Section of this report.**

- ◆ A table showing, for the Airport's most recently completed fiscal year, historical connecting enplaned passenger traffic.

**Refer to Table 3, page B-5 of the Bond Disclosure Section of this report.**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT  
(A Department of the City of San José)**

**Bond Disclosure Report**

**June 30, 2013**

- ◆ A schedule showing, for the Airport's most recently completed fiscal year, historical aircraft operations.

**Refer to Schedule R, page S-22 of the Statistical Section of this report.**

- ◆ A schedule showing, for the Airport's most recently completed fiscal year, historical landing weight.

**Refer to Table 4, page B-6 of the Bond Disclosure Section of this report.**

- ◆ A list showing, for the Airport's most recently completed fiscal year, air carriers serving the Airport.

**Refer to Schedule P, pages S-19 and S-20 of the Statistical Section of this report.**

- ◆ A schedule showing, for the Airport's most recently completed fiscal year, airline activity shares of enplaned commercial passengers.

**Refer to Schedule M, pages S-15 and S-16 of the Statistical Section of this report.**

- ◆ A table showing, for the Airport's most recently completed fiscal year, summary of revenues and maintenance and operation expenses.

**Refer to Financial Section, Exhibit II, page 22 of this report.**

- ◆ A table showing, for the Airport's most recently completed fiscal year, historical debt service coverage.

**Refer to Schedule F, page S-8 of the Statistical Section of this report.**

- ◆ A list showing, for the Airport's most recently completed fiscal year, ten largest sources of revenue.

**Refer to Table 5, page B-7 of the Bond Disclosure Section of this report.**

**REPORTING OF SIGNIFICANT EVENTS**

On July 26, 2012, the City filed a material event notice relating to the Fitch's Rating Services downgrade of the Airport's financial strength rating from "A-" to "BBB+." On January 25, 2013, the City submitted a notice of rating change related to a bond insurer downgrade and the corresponding impact on the City's Airport Revenue Bonds, Series 2011B. On July 1, 2013, the City submitted a rating change notification related to a bond insurer upgrade and the corresponding impact on the City's Airport Revenue Bonds, Series 2001A, Series 2004C and Series 2004D.

Table 1

**SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**BOND DEBT SERVICE REQUIREMENTS**

Year Ending June 30	Total Debt Service Requirements on Outstanding Bonds <sup>(1)</sup>	Principal Requirements on Series 2012 A Bonds	Interest Requirements on Series 2012 A Bonds	Total Debt Service Requirements on Series 2012 Bonds	Total Debt Service Requirements on All Bonds
2014	\$88,502,675	\$8,105,000	\$319,082	\$8,424,082	\$96,926,757
2015	88,895,510	8,220,000	257,078	8,477,078	97,372,588
2016	89,089,343	8,340,000	194,195	8,534,195	97,623,538
2017	89,298,582	8,460,000	130,394	8,590,394	97,888,976
2018	89,532,349	8,585,000	65,675	8,650,675	98,183,024
2019	95,551,435				95,551,435
2020	95,700,095				95,700,095
2021	96,347,070				96,347,070
2022	96,452,104				96,452,104
2023	97,149,599				97,149,599
2024	97,574,429				97,574,429
2025	97,769,766				97,769,766
2026	98,471,929				98,471,929
2027	99,119,448				99,119,448
2028	99,761,725				99,761,725
2029	103,378,580				103,378,580
2030	104,129,878				104,129,878
2031	104,527,725				104,527,725
2032	104,925,440				104,925,440
2033	138,623,263				138,623,263
2034	138,686,875				138,686,875
2035	137,505,185				137,505,185
2036	138,031,715				138,031,715
2037	138,572,335				138,572,335
2038	37,427,763				37,427,763
2039	37,935,095				37,935,095
2040	38,722,033				38,722,033
2041	39,325,615				39,325,615
2042	10,191,600				10,191,600
2043	10,190,500				10,190,500
2044	10,188,600				10,188,600
2045	10,189,400				10,189,400
2046	10,191,100				10,191,100
2047	10,191,900				10,191,900
Totals <sup>(2)</sup>	<b>\$2,742,150,657</b>	<b>\$41,710,000</b>	<b>\$966,424</b>	<b>\$42,676,424</b>	<b>\$2,784,827,081</b>

<sup>(1)</sup>These amounts pertain to total debt service requirements on outstanding Airport Revenue Bonds Series 2001A, 2004C, 2004D, 2007A, 2007B, 2011A, and 2011B.

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

**Table 2**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**HISTORICAL PASSENGER ENPLANEMENTS**  
**LAST TEN FISCAL YEARS**

Fiscal <u>Year</u>	Air Carrier Domestic <u>Enplanements</u>	Air Carrier International <u>Enplanements</u>	Total Air Carrier <u>Enplanements</u>	Commuter <u>Enplanements</u>	Total <u>Enplanements</u>	Total Percent <u>Change %</u>
2004	4,651,137	134,176	4,785,313	506,536	5,291,849	
2005	4,660,730	138,142	4,798,872	546,761	5,345,633	1.02%
2006	4,706,038	137,054	4,843,092	571,739	5,414,831	1.29%
2007	4,686,496	102,368	4,788,864	529,995	5,318,859	-1.77%
2008	4,584,448	67,459	4,651,907	526,696	5,178,603	-2.64%
2009	3,907,376	60,381	3,967,757	431,805	4,399,562	-15.04%
2010	3,636,146	62,437	3,698,583	408,811	4,107,394	-6.64%
2011	3,728,493	77,963	3,806,456	382,767	4,189,223	1.99%
2012	3,672,704	83,261	3,755,965	368,920	4,124,885	-1.54%
2013	3,720,640	110,289	3,830,929	403,824	4,234,753	2.66%

**Annual Compound  
Growth Rate**

FY 2004 through

FY 2013

-2.4%

-2.2%

-2.4%

-2.5%

-2.4%

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**Table 3**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**A Department of the City of San José)**  
**HISTORICAL CONNECTING/ENPLANED PASSENGER TRAFFIC**  
**LAST TEN FISCAL YEARS**

Fiscal <u>Year</u>	Total <u>Enplanements</u>	Total Origin and Destination <u>Enplanements</u>	Total Connecting <u>Enplanements</u>	Connecting Enplanements as a Percentage of Total <u>Enplanements</u>
2004	5,291,849	5,018,790	273,059	5.2%
2005	5,345,633	5,075,122	270,511	5.1%
2006	5,414,831	5,192,594	222,237	4.1%
2007	5,318,859	5,145,726	173,133	3.3%
2008	5,178,603	5,044,473	134,130	2.6%
2009	4,399,562	4,281,747	117,815	2.7%
2010	4,107,394	3,997,764	109,630	2.7%
2011	4,189,223	4,083,459	105,764	2.5%
2012	4,124,885	4,013,758	111,127	2.7%
2013	4,234,753	4,146,393	88,360	2.1%
<b>Annual Compound Growth Rate</b>				
FY 2004 through				
FY 2013		-2.4%	-2.1%	-11.8%

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Source: Norman Y. Mineta San José International Airport activity reports

**Table 4**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**HISTORICAL MAXIMUM GROSS LANDING WEIGHT**  
**LAST TEN FISCAL YEARS**  
**(In thousand pounds)**

Fiscal <u>Year</u>	<u>Air Carrier</u> <sup>(1)</sup>	<u>Commuter</u>	<u>Cargo</u> <sup>(2)</sup>	<u>Total</u>
2004	6,795,591	677,143	547,057	8,019,791
2005	6,468,513	660,694	531,843	7,661,050
2006	6,342,853	677,843	478,376	7,499,072
2007	6,351,084	638,449	511,763	7,501,296
2008	6,255,828	656,298	492,624	7,404,750
2009	5,576,343	553,726	421,088	6,551,157
2010	4,903,780	506,737	322,267	5,732,784
2011	4,779,979	441,023	319,185	5,540,187
2012	4,719,484	405,907	268,748	5,394,139
2013	4,759,393	453,801	248,067	5,461,261

**Annual Compound  
Growth Rate**

FY 2004 through FY 2013	-4%	-4%	-8%	-4%
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<sup>(1)</sup> Includes domestic and international air carriers.

<sup>(2)</sup> Includes all-cargo airlines.

**Table 5**

**NORMAN Y. MINETA SAN JOSE INTERNATIONAL AIRPORT**  
**(A Department of the City of San José)**  
**TEN LARGEST SOURCES OF REVENUES**  
**Fiscal Year Ended June 30, 2013**

<b><u>Category</u></b>	<b><u>Amount</u></b>
Airline Terminal Rentals	\$ 38,255,624
Public Parking Fees	24,813,754
Rental Cars	13,584,308
Landing Fees (Passenger and Cargo)	12,888,370
Food and Beverage	4,713,878
Land and Building Rentals	4,355,637
Advertising	4,222,320
Gift Shop & Retail	3,459,624
Fuel Handling Fees	2,360,463
Ground Transportation	1,924,284

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Source: Norman Y. Mineta San José International Airport management records.

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**APPENDIX E**  
**PROPOSED FORM OF BOND COUNSEL OPINION**

October 7, 2014

City Council  
City of San José  
San José, California

City of San José  
Airport Revenue Refunding Bonds  
Series 2014A (AMT), Series 2014B (Non-AMT), and Series 2014C (Non-AMT)  
(Final Opinion)

Ladies and Gentlemen:

We have acted as bond counsel to the City of San José (the “Issuer”), in connection with the issuance by the Issuer of \$57,350,000 aggregate principal amount of City of San José Airport Revenue Refunding Bonds, Series 2014A (AMT) (the “Series 2014A Bonds”), \$28,010,000 aggregate principal amount of City of San José Airport Revenue Refunding Bonds, Series 2014B (Non-AMT) (the “Series 2014B Bonds”), and \$40,285,000 aggregate principal amount of City of San José Airport Revenue Refunding Bonds, Series 2014C (Non-AMT) (the “Series 2014C Bonds” and, collectively with the Series 2014A Bonds and the Series 2014B Bonds, the “Bonds”), issued pursuant to Sections 200 and 1220 of the Charter and Chapter 4.38 of the San José Municipal Code (collectively, the “Law”), the Nineteenth Supplemental Resolution No. 77158 adopted by the Council on September 16, 2014 (the “Resolution”), and a Master Trust Agreement, dated as of July 1, 2001, between the Issuer and The Bank of New York Mellon Trust Company, N.A., formerly known as BNY Western Trust Company (the “Trustee”), as previously supplemented and amended, and as supplemented by the Tenth Supplemental Trust Agreement, dated as of October 1, 2014 (the “Tenth Supplemental Trust Agreement”), between the Issuer and the Trustee (collectively, the “Trust Agreement”). Capitalized terms not otherwise defined herein shall have the meanings set forth in the Trust Agreement.

In such connection, we have reviewed the Law, the Resolution, the Trust Agreement, the Tax Certificate, dated the date hereof (the “Tax Certificate”), opinions of counsel to the Issuer, the Trustee and the purchasers of the Bonds (the “Underwriters”), certificates of the Issuer, the Trustee, the Underwriters and others, and such other documents, opinions and matters to the extent we deemed necessary to render the opinions set forth herein.

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof. Accordingly, this opinion speaks only as of its date and is not intended to, and may not, be relied upon or otherwise used in connection with any such actions, events or matters. We disclaim any obligation to update this opinion. We have assumed the genuineness of all documents and signatures presented to us (whether as originals or as copies) and the

due and legal execution and delivery thereof by, and validity against, any parties other than the Issuer. We have assumed, without undertaking to verify, the accuracy of the factual matters represented, warranted or certified in the documents, and of the legal conclusions contained in the opinions, referred to in the second paragraph hereof. Furthermore, we have assumed compliance with all covenants and agreements contained in the Trust Agreement and the Tax Certificate, including without limitation covenants and agreements compliance with which is necessary to assure that future actions, omissions or events will not cause interest on the Bonds to be included in gross income for federal income tax purposes. We call attention to the fact that the rights and obligations under the Bonds, the Trust Agreement and the Tax Certificate and their enforceability may be subject to bankruptcy, insolvency, receivership, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases and to the limitations on legal remedies against cities in the State of California. We express no opinion with respect to any indemnification, contribution, liquidated damages, penalty (including any remedy deemed to constitute a penalty), right of set-off, arbitration, judicial reference, choice of law, choice of forum, choice of venue, non-exclusivity of remedies, waiver or severability provisions contained in the foregoing documents, nor do we express any opinion with respect to the state or quality of title to or interest in any of the real or personal property described in or as subject to the lien of the Trust Agreement or the accuracy or sufficiency of the description contained therein of, or the remedies available to enforce liens on, any such property. Our services did not include financial or other non-legal advice. Finally, we undertake no responsibility for the accuracy, completeness or fairness of the Official Statement or other offering material relating to the Bonds and express no opinion with respect thereto.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The Bonds constitute the valid and binding limited obligations of the Issuer.

2. The Trust Agreement has been duly executed and delivered by, and constitutes the valid and binding obligation of, the Issuer. The Trust Agreement creates a valid pledge, to secure the payment of the principal of and interest on the Bonds, of the General Airport Revenues and certain other amounts held by the Trustee in any fund or account established pursuant to the Trust Agreement, except the Rebate Fund, subject to the provisions of the Trust Agreement permitting the application thereof for the purposes and on the terms and conditions set forth in the Trust Agreement.

3. The Bonds are not a lien or charge upon the funds or property of the Issuer except to the extent of the aforementioned pledge. Neither the faith and credit nor the taxing power of the Issuer or the State of California or of any political subdivision thereof is pledged to the payment of the principal of or interest on the Bonds. The Bonds are not a debt of the State of California, and said State is not liable for the payment thereof.

4. Interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 (the "1986 Code") and is exempt from State of California personal income taxes, except that no opinion is expressed as to the status of interest on any Series 2014A Bond for any period that such Series 2014A Bond is held by a "substantial user" of the facilities refinanced by the proceeds of the Series 2014A Bonds, or by a "related person" within the meaning of Section 147(a) of the Code. We observe, however, that interest on the Series 2014A Bonds is a specific preference item for purposes of the federal individual and corporate alternative minimum taxes. We are further of the opinion that interest on the Series 2014B Bonds and Series 2014C Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although we observe that it is included in adjusted current earnings in calculating corporate alternative

minimum taxable income. We express no opinion regarding other tax consequences relating to the ownership or disposition of, or the amount, accrual or receipt of interest on, the Bonds.

Faithfully yours,

ORRICK, HERRINGTON & SUTCLIFFE LLP  
per

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## APPENDIX F

### FORM OF CONTINUING DISCLOSURE CERTIFICATE

This Continuing Disclosure Certificate (the "Disclosure Certificate") is executed and delivered by the City of San José, California (the "City") in connection with the issuance of \$57,350,000 City of San José Airport Revenue Refunding Bonds, Series 2014A (the "Series 2014A Bonds"), \$28,010,000 City of San José Airport Revenue Refunding Bonds, Series 2014B (the "Series 2014B Bonds") and \$40,285,000 City of San José Airport Revenue Refunding Bonds, Series 2014C (the "Series 2014C Bonds" and, together with the Series 2014A Bonds and the Series 2014B Bonds, the "Series 2014 Bonds"). The Series 2014 Bonds are being issued pursuant to a Master Trust Agreement, dated as of July 1, 2001, between the City and The Bank of New York Mellon Trust Company, N.A., as successor to BNY Western Trust Company, as trustee (the "Trustee"), as supplemented by a First Supplemental Trust Agreement, dated as of July 1, 2001, by a Second Supplemental Trust Agreement, dated as of December 1, 2002, by a Third Supplemental Trust Agreement, dated as of June 1, 2004, by a Fourth Supplemental Trust Agreement, dated as of June 1, 2004, by a Fifth Supplemental Trust Agreement, dated as of September 1, 2007, by a Sixth Supplemental Trust Agreement, dated as of May 1, 2009, by a Seventh Supplemental Trust Agreement, dated as of July 1, 2011, by an Eighth Supplemental Trust Agreement, dated as of December 1, 2011, by a Ninth Supplemental Trust Agreement, dated as of November 1, 2012 and by a Tenth Supplemental Trust Agreement, dated as of October 1, 2014 (the "Tenth Supplemental Trust Agreement" and, collectively, the "Master Trust Agreement"), each by and between the City and the Trustee. The City covenants and agrees as follows:

Section 1. ***Purpose of the Disclosure Certificate.*** This Disclosure Certificate is being executed and delivered by the City for the benefit of the holders and Beneficial Owners of the Series 2014 Bonds and in order to assist the Participating Underwriters in complying with Securities and Exchange Commission (the "SEC") Rule 15c2-12(b)(5).

Section 2. ***Definitions.*** In addition to the definitions set forth in the Master Trust Agreement, which apply to any capitalized term used in this Disclosure Certificate unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

"*Annual Report*" means any Annual Report provided by the City pursuant to, and as described in, Sections 3 and 4 of this Disclosure Certificate.

"*Beneficial Owner*" means any person which has or shares the power, directly or indirectly, to make investment decisions concerning ownership of any Series 2014 Bonds (including persons holding Series 2014 Bonds through nominees, depositories or other intermediaries).

"*Dissemination Agent*" means the City of San José, California, or any successor Dissemination Agent designated in writing by the City and which has filed with the City a written acceptance of such designation.

"*Holder*" shall mean the person in whose name any Series 2014 Bonds shall be registered.

"*Listed Events*" means any of the events listed in Section 5(a) or (b) of this Disclosure Certificate.

"*MSRB*" means the Municipal Securities Rulemaking Board or any other entity designated or authorized by the SEC to receive reports pursuant to the Rule. Until otherwise designated by the MSRB

or the Securities and Exchange Commission, filings with the MSRB are to be made through the Electronic Municipal Market Access (EMMA) website of the MSRB, currently located at <http://emma.msrb.org>.

"*Participating Underwriters*" means any of the original underwriters of the Series 2014 Bonds required to comply with the Rule in connection with the offering of the Series 2014 Bonds.

"*Rule*" means Rule 15c2-12(b)(5) adopted by the SEC under the Securities Exchange Act of 1934, as the same may be amended from time to time.

"*State*" means the State of California.

**Section 3. *Provision of Annual Reports.***

(a) The City shall, or shall cause the Dissemination Agent to, not later than nine months after the end of the City's fiscal year (which shall be March 1 of each year, so long as the City's fiscal year ends on June 30), commencing with the report for the 2013-14 fiscal year (which is due not later than March 1, 2015), provide to the MSRB an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Certificate. The Annual Report may cross-reference other information as provided in Section 4 of this Disclosure Certificate; provided ,that the audited financial statements of the City may be submitted separately from the balance of the Annual Report and later than the date required above for the filing of the Annual Report if they are not available by that date. If the City's fiscal year changes, it shall give notice of such change in a filing with the MSRB. The Annual Report shall be submitted on a standard form in use by industry participants or other appropriate form and shall identify the Series 2014 Bonds by name and CUSIP number.

(b) Not later than 15 Business Days prior to said date, the City shall provide the Annual Report to the Dissemination Agent (if other than the City). If the City is unable to provide to the MSRB an Annual Report by the date required in subsection (a), the City shall, in a timely manner, send or cause to be sent to the MSRB a notice in substantially the form attached as Exhibit A.

(c) The Dissemination Agent shall (if the Dissemination Agent is other than the City) file a report with the City certifying that the Annual Report has been provided pursuant to this Disclosure Certificate, stating the date it was provided to the MSRB.

**Section 4. *Content of Annual Reports.*** The Annual Report shall contain or include by reference the following:

(a) Audited financial statements of the Airport for the prior fiscal year, prepared in accordance with generally accepted accounting principles as promulgated to apply to governmental entities from time to time by the Governmental Accounting Standards Board, and as further modified according to applicable State law. If the Airport's audited financial statements are not available by the time the Annual Report is required to be provided to the MSRB pursuant to Section 3(a), the Annual Report shall contain unaudited financial statements in a format similar to the usual format utilized by the City for the Airport, and the audited financial statements shall be provided to the MSRB in the same manner as the Annual Report when they become available;

(b) To the extent not included in the audited financial statement of the Airport, the Annual Report shall also include the following:

(i) Historical financial information of the type shown in Table 4 of the Official

Statement, entitled “Airport Revenue Bonds Debt Service Requirements” (required only to the extent there are changes);

(ii) Historical operating information of the type shown in Table 5 of Appendix A of the Official Statement, entitled “Norman Y. Mineta San José International Airport Airlines Serving the Airport as of June 30, 2014”;

(iii) Historical operating information of the type shown in Table 6 of Appendix A of the Official Statement, entitled “Norman Y. Mineta San José International Airport Historical Passenger Enplanements Fiscal Years ended June 30”;

(iv) Historical operating information of the type shown in Table 8 of Appendix A of the Official Statement, entitled “Norman Y. Mineta San José International Airport Enplaned Commercial Passengers by Airline Fiscal Years Ended June 30”;

(v) Historical operating information of the type shown in Table 9 of Appendix A of the Official Statement, entitled “Norman Y. Mineta San José International Airport Historical Gross Landed Weight (in thousand pounds) Fiscal Years Ended June 30”;

(vi) Historical operating information of the type shown in Table 10 of Appendix A of the Official Statement, entitled “Norman Y. Mineta San José International Airport Historical Aircraft Operations Fiscal Years Ended June 30”;

(vii) Historical financial information of the type shown in Table 11 of Appendix A of the Official Statement, entitled “Norman Y. Mineta San José International Airport Summary of Operating Revenues and Maintenance and Operation Expenses Fiscal Years Ended June 30”; and

(viii) Historical financial information of the type shown in Table 12b of Appendix A of the Official Statement, entitled “Norman Y. Mineta San José International Airport Historical Bond Debt Service Coverage Fiscal Years Ended June 30”.

Any or all of the items listed above may be set forth in one or a set of documents or may be included by specific reference to other documents, including official statements of debt issues of the City or related public entities, which have been made available to the public on the MSRB's website. The City shall clearly identify each such other document so included by reference.

(c) Information contained in an Annual Report for any fiscal year containing any modified operating data or financial information for such fiscal year shall explain, in narrative form, the reasons for such modification and the effect of such modification on the Annual Report being provided for such fiscal year. If a change in accounting principles is included in any such modification, such Annual Report shall present a comparison between the financial statements or information prepared on the basis of modified accounting principles and those prepared on the basis of former accounting principles.

## Section 5. *Reporting of Significant Events.*

(a) The City shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Series 2014 Bonds in a timely manner not later than ten business days after the occurrence of the event:

(i) Principal and interest payment delinquencies;

- (ii) Unscheduled draws on debt service reserves reflecting financial difficulties;
- (iii) Unscheduled draws on credit enhancements reflecting financial difficulties;
- (iv) Substitution of credit or liquidity providers, or their failure to perform;
- (v) Adverse tax opinions with respect to tax status of the Series 2014 Bonds or the issuance by the Internal Revenue Service of proposed or final determination of taxability or of a Notice of Proposed Issue (IRS Form 5701 TEB);
- (vi) Tender offers;
- (vii) Defeasances;
- (viii) Rating changes; or
- (ix) Bankruptcy, insolvency, receivership or similar event of the obligated person.

For the purposes of the event identified in subparagraph (ix), the event is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent or similar officer for an obligated person in a proceeding under the U.S. Bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the obligated person, or if such jurisdiction has been assumed by leaving the existing governmental body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the obligated person.

(b) The City shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Series 2014 Bonds, if material, in a timely manner not later than ten business days after the occurrence of the event:

- (i) Unless described in paragraph 5(a)(v), adverse tax opinions or other material notices or determinations by the Internal Revenue Service with respect to the tax status of the Series 2014 Bonds or other material events affecting the tax status of the Series 2014 Bonds;
- (ii) Modifications to rights of Holders;
- (iii) Optional, unscheduled or contingent Bond calls;
- (iv) Release, substitution, or sale of property securing repayment of the Series 2014 Bonds;
- (v) Non-payment related defaults;
- (vi) The consummation of a merger, consolidation, or acquisition involving an obligated person or the sale of all or substantially all of the assets of the obligated person, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms; or
- (vii) Appointment of a successor or additional trustee or the change of name of a

trustee.

(c) Whenever the City obtains knowledge of the occurrence of a Listed Event described in Section 5(b), the City shall determine if such event would be material under applicable federal securities laws.

(d) If the City learns of the occurrence of a Listed Event described in Section 5(a), or determines that knowledge of a Listed Event described in Section 5(b) would be material under applicable federal securities laws, the City shall within ten business days of such occurrence file a notice of such occurrence with the MSRB. Notwithstanding the foregoing, notice of the Listed Event described in subsections (a)(vii) or (b)(iii) need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to Holders of affected Series 2014 Bonds pursuant to the Master Trust Agreement.

Section 6. ***Format for Filings with MSRB.*** Any report or filing with the MSRB pursuant to this Disclosure Certificate must be submitted in electronic format, accompanied by such identifying information as is prescribed by the MSRB.

Section 7. ***Termination of Reporting Obligation.*** The City's obligations under this Disclosure Certificate shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Series 2014 Bonds, or upon delivery to the City or the Dissemination Agent (if other than the City) of an opinion of nationally recognized bond counsel to the effect that continuing disclosure is no longer required. If such termination occurs prior to the final maturity of the Series 2014 Bonds, the City shall give notice of such termination in a filing with the MSRB.

Section 8. ***Dissemination Agent.*** From time to time, the City may appoint or engage a Dissemination Agent to assist it in carrying out its obligations under this Disclosure Certificate, and may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent. If at any time there is not any other designated Dissemination Agent, the City shall be the Dissemination Agent. The initial Dissemination Agent shall be the City. The sole remedy of any party against the Dissemination Agent shall be nonmonetary and specific performance. The Dissemination Agent shall not be responsible in any manner for the form or content of any notice, report or other document prepared by the City pursuant to this Disclosure Certificate. The Dissemination Agent shall receive reasonable compensation for its services provided hereunder. The Dissemination Agent may resign at any time by providing at least 60 days' notice to the City.

Section 9. ***Amendment Waiver.*** Notwithstanding any other provision of this Disclosure Certificate, the City may amend this Disclosure Certificate, and any provision of this Disclosure Certificate may be waived, provided that all of the following conditions are satisfied:

(a) If the amendment or waiver relates to the provisions of Sections 3(a), 4, or 5(a) of (b), it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of an obligated person with respect to the Series 2014 Bonds, or the type of business conducted;

(b) The undertaking, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Series 2014 Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Holders of the Series 2014 Bonds in the same manner as provided in the Master Trust Agreement for amendments to the Master Trust Agreement with the consent of Holders, or (ii) does not, in the opinion of nationally recognized bond counsel, materially impair the interests of the Holders or Beneficial Owners of the Series 2014 Bonds.

In the event of any amendment or waiver of a provision of this Disclosure Certificate, the City shall describe such amendment in the next Annual Report, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or in the case of a change of accounting principles, on the presentation) of financial information or operating data being presented by the City. In addition, if the amendment relates to the accounting principles to be followed in preparing financial statements, (i) notice of such change shall be given in a filing with the MSRB, and (ii) the Annual Report for the year in which the change is made should present a comparison (in narrative form and also, if feasible, in quantitative form) between the financial statements as prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles.

Section 10. ***Additional Information.*** Nothing in this Disclosure Certificate shall be deemed to prevent the City from disseminating any other information, using the means of dissemination set forth in this Disclosure Certificate or any other means of communication, or including any other information in any Annual Report or notice in addition to that which is required by this Disclosure Certificate. If the City chooses to include any information in any Annual Report or notice of occurrence of a Listed Event in addition to that which is specifically required by this Disclosure Certificate, the City shall have no obligation under this Disclosure Certificate to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event or any other event required to be reported.

Section 11. ***Default.*** In the event of a failure of the City to comply with any provision of this Disclosure Certificate, any Holder or Beneficial Owner of the Series 2014 Bonds may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the City or the Dissemination Agent (if other than the City), as the case may be, to comply with its obligations under this Disclosure Certificate; provided, that any such action may be instituted only in the Superior Court of the State of California in and for the County of Santa Clara or in the U.S. District Court in or nearest to such County. A default under this Disclosure Certificate shall not be deemed an Event of Default under the Master Trust Agreement, and the sole remedy under this Disclosure Certificate in the event of any failure of the City or the Dissemination Agent to comply with this Disclosure Certificate shall be an action to compel performance.

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Section 12. ***Beneficiaries.*** This Disclosure Certificate shall inure solely to the benefit of the City, the Dissemination Agent, the Participating Underwriters and Holders and Beneficial Owners from time to time of the Series 2014 Bonds, and shall create no rights in any other person or entity.

Date: October 7, 2014

CITY OF SAN JOSE, CALIFORNIA

By: \_\_\_\_\_  
Authorized Representative

APPROVED AS TO FORM:

RICHARD DOYLE, CITY ATTORNEY

By: \_\_\_\_\_  
Authorized Representative

## **EXHIBIT A**

### **NOTICE OF FAILURE TO FILE ANNUAL REPORT**

Name of Issuer: City of San José

Name of Bond Issue: \$57,350,000 City of San José Airport Revenue Refunding Bonds, Series 2014A; \$28,010,000 City of San José Airport Revenue Refunding Bonds, Series 2014B and \$40,285,000 City of San José Airport Revenue Refunding Bonds, Series 2014C

Date of Issuance: October 7, 2014

Name of Obligated Person: City of San José

NOTICE IS HEREBY GIVEN that the City of San José (the "City") has not provided an Annual Report with respect to the above-named Series 2014A Bonds, Series 2014B Bonds and Series 2014C Bonds as required by Section 3 of the Continuing Disclosure Certificate dated October 7, 2014. The City anticipates that the Annual Report will be filed by \_\_\_\_\_.

Dated:

CITY OF SAN JOSE

By: [to be signed only if filed]  
Authorized Representative

cc: City of San José  
200 E. Santa Clara St., 13th Floor Tower  
San José, CA 95113-1905  
Attn: Debt Management

## **APPENDIX G**

### **SUMMARY OF CERTAIN PROVISIONS OF THE AIRLINE LEASE AGREEMENT**

The following is a summary of certain provisions of the Airline-Airport Lease and Operating Agreement (the “Airline Lease Agreement”) for the Norman Y. Mineta San José International Airport (the “Airport”). The following summary is qualified in its entirety by reference to the Airline Lease Agreement, a copy of which can be obtained from the City of San José.

#### **Term of Lease**

The Airline Lease Agreement became effective on December 1, 2007 and will terminate on June 30, 2017.

Any airline that holds over beyond the specified expiration date of the Airline Lease Agreement is deemed a month to month tenant, and each holdover airline is to be required to pay a 25% premium on all rates and charges established by the Airline Lease Agreement.

#### **Signatory Airlines, Non-Signatory Airlines and Affiliates**

Any passenger airline that (a) signs an agreement with the City substantially similar to the Airline Lease Agreement, (b) provides passenger service at the Airport, (c) leases from the City an amount of Exclusive Use Premises in the terminal deemed sufficient by the Director of Aviation of the City (the “Director”) to support its operation, and (d) at the time it executes its agreement with the City, operates at least one scheduled flight, scheduled year round, at least three days per week is defined as a “Signatory Airline” under the Airline Lease Agreement.

In addition, any all-cargo airline that (a) signs an agreement with the City substantially similar to the Airline Lease Agreement, (b) leases from the City cargo support space at the Airport for a term at least equal to the term of the Airline Lease Agreement, (c) guarantees a minimum of 142,000 pounds of maximum gross certificated landing weight per scheduled flight, and (d) at the time it executes its agreement with the City, operates at least five scheduled flights per week is also considered a “Signatory Airline” under the Airline Lease Agreement.

Any airline that does not qualify as a Signatory Airline but does execute an agreement with the City pertaining to the Non-Signatory Airline’s operations and use of certain facilities at the Airport (a “Non-Signatory Operating Agreement”) is defined as a “Non-Signatory Airline” under the Airline Lease Agreement. Non-Signatory Airlines are required to pay a 25% premium on all rates and charges established by the Airline Lease Agreement.

A Signatory Airline may designate another airline as an “Affiliate” provided that each such designated airline is a wholly-owned subsidiary or code-share partner of the Signatory Airline and each such designated airline is a party to a Non-Signatory Operating Agreement. For so long as the designating airline is a Signatory Airline and for so long as the conditions of the Airline Lease Agreement are satisfied, an Affiliate will be treated as if it were the Signatory Airline for the purposes of the assignment and use of gates and ticket counters, the assessment of rates and charges and the approval of Capital Expenditures (as defined below) by the City.

Each Signatory Airline is to be responsible for the actions and obligations of each of its Affiliates. Each Signatory Airline also is to be responsible for ensuring that each of its Affiliates complies with all terms and conditions of the Airline Lease Agreement to the same extent that the Signatory Airline is responsible for compliance, and the Signatory Airline is to be the financial guarantor of all amounts owed to the City by each of the Signatory Airline's Affiliates.

The designation of an Affiliate is to be effective for so long as the conditions for designating the Affiliate continue to be satisfied or until a Signatory Airline withdraws its designation of the Affiliate by submitting a withdrawal of designation form to the City.

### **Lease of Premises**

The City leases terminal space under the Airline Lease Agreement on various bases, including on an exclusive use basis, a preferential use basis and a common use basis.

Each Signatory Airline is to have preferential use of certain Preferential Use Premises, including gates, ticket counters and skycap positions, during the term of the Airline Lease Agreement. Signatory Airlines also are to be entitled to the exclusive use of certain Exclusive Use Premises, such as office spaces, storage areas and VIP lounges. Finally, Signatory Airlines are to be entitled to use Common Use Premises, which consist of certain areas of the Airport (excluding public spaces) that are to be used in common by the airlines and that are not assigned on a preferential use basis or an exclusive use basis.

### ***Assignment and Use of Gates***

The Airline Lease Agreement provides that all Gates (defined in the Airline Lease Agreement to include a passenger loading bridge, if any, a hold room, and a gate ramp) within the Terminal shall be for either Common Use or Preferential Use and that no Gates will be for Exclusive Use.

Effective July 1 each year, the Director is to have sole discretion to determine the total number of gates to be reserved for use as Common Use Gates during a fiscal year (after taking into consideration any recommendations by the Resource Management Advisory Committee ("RMAC"), which committee is to consist of representatives designated by the City and representatives of the Signatory Airlines designated by the Airport-Airline Affairs Committee for the Airport). All remaining gates will be offered by the City to the Signatory Airlines for use as Preferential Use Gates.

The Airline Lease Agreement provides that, effective July 1 each year, the City is to apply the following methodology to determine the total number of gates that will be offered to each Signatory Airline for preferential use during a fiscal year:

(a) The City shall first divide the average daily number of outbound seats on the Signatory Airline's scheduled flights for the most recent month of August by the average daily number of outbound seats in August for all Signatory Airlines to determine the Signatory Airline's percentage share of all scheduled seats (the "Scheduled Seats Percentage").

(b) The City shall then calculate the number of Preferential Use Gates to be offered to the Signatory Airline by multiplying the Signatory Airline's Scheduled Seats Percentage by the total number of gates to be made available for preferential use, rounding the product to the nearest whole number; provided, however, that a product less than 0.5 shall not be eligible for rounding.

(c) If as a result of rounding, the total number of Preferential Use Gates to be offered to all Signatory Airlines is less than the total number of gates available for preferential use, the City shall offer

additional Preferential Use Gates to Signatory Airlines based on the unrounded results of the computations described above. The unallocated Preferential Use Gates shall be offered in priority order by first increasing by one the number of Preferential Use Gates to be offered to the Signatory Airline whose unrounded product is nearest to 0.5 without equaling or exceeding 0.5 and next proceeding to increase by one the number of Preferential Use Gates to be offered to the Signatory Airline whose unrounded product is second nearest to 0.5 without equaling or exceeding 0.5 and so on until the total number of Preferential Use Gates to be made available to all Signatory Airlines by the City is reached.

(d) If as a result of rounding, the total number of Preferential Use Gates to be offered to all Signatory Airlines exceeds the total number of gates available for preferential use, the City shall reduce the number of calculated Preferential Use Gates to be offered to Signatory Airlines based on the unrounded results of the computations described above. The number of over-allocated Preferential Use Gates shall be reduced in priority order by first reducing by one the number of allocated Preferential Use Gates to the Signatory Airline whose unrounded product is nearest to 0.5 without being less than 0.5 and next proceeding to reduce by one the number of Preferential Use Gates to be offered to the Signatory Airline whose unrounded product is second nearest 0.5 without being less than 0.5 and so on until the total number of Preferential Use Gates to be made available to all Signatory Airlines by the City is reached.

(e) If any Signatory Airline does not accept assignment of a Preferential Use Gate, that Preferential Use Gate shall be designated as a Common Use Gate. In such a situation, the City may elect to reassign the Preferential Use Gate to another Signatory Airline if the City determines the number of Common Use Gates is adequate to accommodate all airline operations at the Airport. The City may reallocate such Preferential Use Gates using the methodology described above until all gates available for assignment as Preferential Use Gates are allocated to Signatory Airlines or rejected for assignment as Preferential Use Gates. Any gate rejected for assignment as a Preferential Use Gate by all eligible Signatory Airlines will become a Common Use Gate.

(f) If a Preferential Use Gate is designated as a Common Use Gate and is not reassigned to a Signatory Airline for preferential use, the costs that would otherwise have been assigned to such gate for rate-setting purposes shall be evenly redistributed among all of the other rented Group A gate space (as defined below); provided, however, that any Common Use Gate charges paid to the City for the use of such a gate shall be credited against such redistributed costs.

(g) The City shall in its sole discretion determine the locations of any Preferential Use Gates to be offered to the Signatory Airlines, after taking into consideration the desirability of assigning contiguous gates for preferential use by any given Signatory Airline and minimizing the frequency of changes in the locations of Preferential Use Gates as well as any recommendations by the RMAC.

(h) No later than October 1<sup>st</sup> of each fiscal year during the term of the Airline Lease Agreement, the City shall provide written notice to all Signatory Airlines of its annual determination with respect to Preferential Use Gates and shall offer each Signatory Airline the opportunity to be assigned the number of Preferential Use Gates indicated by the calculations described above. Each Signatory Airline shall provide written notice to the City no later than 45 days after October 1<sup>st</sup> of each fiscal year during the term if it wishes to reject any or all of that number of gates offered by the City for preferential use.

(i) If the numbers or locations of Preferential Use Gates offered to the Signatory Airlines are changed during the term of the Airline Lease Agreement for any reason other than a year-to-year decrease in the number of a Signatory Airline's scheduled seats, the Signatory Airline may, upon 30 days' written notice to the City, terminate its rights to those portions of the Exclusive Use Premises that are no longer proximate to the Preferential Use Gates offered to the Signatory Airline. Upon the Signatory Airline's

request, the City shall use reasonable efforts to provide the Signatory Airline with substitute Exclusive Use Premises more proximate to newly assigned Preferential Use Gates assigned to the Signatory Airline for the remaining term. In such a situation, the reasonable costs of relocating the Preferential Use Gates assigned to any Signatory Airline plus the reasonable costs of any Signatory Airline's tenant improvements at the substitute Exclusive Use Premises when constructed with the City's consent shall be paid by the City and included in the rate base.

(j) If the number of Preferential Use Gates offered to the Signatory Airline is reduced during the term of the Airline Lease Agreement as the result of a year-to-year decrease in the Signatory Airline's Scheduled Seats Percentage, the City may, upon 30 days' written notice to the Signatory Airline, terminate the Signatory Airline's rights to use those portions of the Exclusive Use Premises that are no longer proximate to the Preferential Use Gates offered to the Signatory Airline and that are no longer necessary, in the Director's reasonable discretion, to support the Signatory Airline's operations at the Signatory Airline's remaining Preferential Use Gates.

#### ***Assignment and Use of Ticket Counters***

The Airline Lease Agreement provides that all ticket counters within the Terminal will be for either common use or preferential use and that no ticket counters will be for exclusive use. The Director shall have sole discretion to determine the total number of ticket counters to be reserved for use as Common Use Ticket Counters during a fiscal year (after taking into consideration any recommendations by the RMAC). All remaining ticket counters will be offered by the City to the Signatory Airlines for use as Preferential Use Ticket Counters.

The Airline Lease Agreement provides that, effective July 1 each year, the City will apply the following methodology to determine the total number of ticket counters that will be offered to each Signatory Airline for preferential use during a fiscal year:

(a) The City shall allocate two ticket counters for a Signatory Airline's first Preferential Use Gate, and the City shall allocate one additional ticket counter for each additional Preferential Use Gate granted to a Signatory Airline under the Airline Lease Agreement. This same method shall be applied to all Signatory Airlines.

(b) If additional Preferential Use Ticket Counters remain available after the allocation for all Signatory Airlines that is detailed above, a Signatory Airline shall be entitled to one additional Preferential Use Ticket Counter for each unallocated Preferential Use Gate that the Signatory Airline is entitled to accept, regardless of whether the Signatory Airline accepts the allocation of any such Preferential Use Gate under the Airline Lease Agreement.

(c) If the total number of Preferential Use Ticket Counters to be offered to all Signatory Airlines exceeds the total number of ticket counters available for preferential use, the City shall reduce the number of calculated Preferential Use Ticket Counters to match the available Preferential Use Ticket Counters. The allocation of the over-allocated Preferential Use Ticket Counters shall be reduced accordingly based on the over-allocation process for Preferential Use Gates until the total number of Preferential Use Ticket Counters offered to all Signatory Airlines by the City matches the total number of Preferential Use Ticket Counters that are available.

(d) If any Signatory Airline does not accept assignment of a Preferential Use Ticket Counter, such Preferential Use Ticket Counter shall be designated as a Common Use Ticket Counter. In such a situation, the City may elect to reassign a Preferential Use Ticket Counter not accepted by a Signatory Airline to another Signatory Airline if the City determines the number of Common Use Ticket Counters is

adequate to accommodate all airline operations at the Airport. The City may reallocate such ticket counters using the methodology described above until all ticket counters available for assignment as Preferential Use Ticket Counters are allocated to Signatory Airlines or rejected for assignment as a Preferential Use Ticket Counter. Any ticket counter rejected for assignment as a Preferential Use Ticket Counter by all eligible Signatory Airlines will become a Common Use Ticket Counter.

(e) If a Preferential Use Ticket Counter is designated as a Common Use Ticket Counter and is not reassigned to a Signatory Airline for preferential use, the costs that would otherwise have been assigned to such ticket counter for rate-setting purposes will be evenly redistributed among all of the other rented Group A ticket counter space; provided, however, that any Common Use Ticket Counter charges paid to the City for use of such ticket counter shall be credited against such redistributed costs.

(f) The City shall in its sole discretion determine the locations of any Preferential Use Ticket Counters to be offered to the Signatory Airlines, after taking into consideration the desirability of assigning contiguous ticket counters for preferential use by any given Signatory Airline and minimizing the frequency of changes in the locations of Preferential Use Ticket Counters as well as any recommendations by the RMAC.

(g) No later than October 1<sup>st</sup> of each fiscal year during the term of the Airline Lease Agreement, the City shall provide written notice to all Signatory Airlines of its annual determination with respect to Preferential Use Ticket Counters and shall offer each Signatory Airline the opportunity to be assigned the number of Preferential Use Ticket Counters indicated by the calculations described above. Airline shall provide written notice to the City no later than 45 days after October 1<sup>st</sup> of each fiscal year during the term if it wishes to reject any or all of that number of ticket counters offered by the City for preferential use.

#### ***Assignment and Use of Skycap Positions***

Each fiscal year during the term of the Airline Lease Agreement, the Director is to assign skycap positions (areas designated for curbside check in) to each Signatory Airline in approximately the same proportions as ticket counters have been assigned, and Preferential Use Skycap Positions and Common Use Skycap Positions shall be assigned by the Director in approximately the same proportions as Preferential Use and Common Use Ticket Counters have been assigned. Before assigning skycap positions, the Director is to ask the RMAC for a recommendation with respect to the assignments, but the final determination with respect to the assignment of skycap positions is to be made by the Director in the Director's sole discretion.

#### ***Use of Preferential Use Premises by Other Airlines***

The Airline Lease Agreement provides that the Director may authorize the use of Preferential Use Premises by airlines other than the Signatory Airlines to which they are assigned, and each Signatory Airline is required, in the event another scheduled airline is unable to obtain necessary facilities to operate at the Airport, to accommodate the scheduled airline at the Signatory Airline's Preferential Use Gate or Preferential Use Ticket Counter so long as the Preferential Use Gate or Preferential Use Ticket Counter is not being used by the Signatory Airline during the period of accommodation for a scheduled flight.

In the event of any such accommodation, the accommodated airline is to pay the City the same charges for the use of the gate or ticket counter that it would have paid for a Common Use Gate or Common Use Ticket Counter, and the City is to provide a credit to the accommodating Signatory Airline for one-half of the amount of any such payment. In addition, the accommodated airline is to pay all reasonable towing, Remain Overnight ("RON") fees and other charges related to the accommodation that

may be assessed to the accommodating Signatory Airline. If an arrival or departure of a Signatory Airline that would have utilized one of the Signatory Airline's Preferential Use Gates is early or late and the Signatory Airline is prevented from utilizing any of its Preferential Use Gates because they are already being utilized by Requesting Airlines, the City shall, whenever possible, accommodate the Signatory Airline's arrival or departure on a Common Use Gate at no additional charge to the Signatory Airline for its use of the Common Use Gate. In addition, the Signatory Airline shall continue to be entitled to the credit with regard to the accommodated operation at its Preferential Use Gate and Ticket Counter as described above.

As a condition of accommodation on a Signatory Airline's Preferential Use Gate or Preferential Use Ticket Counter, the Airline Lease Agreement provides that the accommodated airline must execute the Airline Lease Agreement or a Non-Signatory Operating Agreement through which the accommodated airline is bound by insurance and indemnification obligations that are substantially similar to the insurance and indemnification obligations in the Airline Lease Agreement. Those obligations shall inure to the benefit of the accommodating Signatory Airline as a third-party beneficiary during any period of accommodation.

### **Reallocation of Leased Premises**

From time to time, part or all of a Signatory Airline's premises may be required (a) for implementation of improvements at the Airport, (b) for accommodation of the traveling public, or (c) in order to maximize the use of the terminal and related facilities by airlines and other tenants, lessees, permittees and users thereof. In such an event, the City may reallocate the Signatory Airline's premises upon 30 days' advance written notice to the Signatory Airline, and the Signatory Airline is required to comply with any reallocation requirements. In any such reallocation, the actual, reasonable requirements of the Signatory Airline for terminal space to accommodate its operations at the Airport are to be given consideration.

All moving costs resulting from the relocation of a Signatory Airline in a City-imposed reallocation are to be funded by the City, subject to recovery in the rate base under the Airline Lease Agreement. Notwithstanding the foregoing, a Signatory Airline is not entitled to reimbursement for any relocation of or within the Common Use Premises at the Airport, and a Signatory Airline is not entitled to new trade fixtures or new movable property to the extent that the removal of those items from the existing premises and the reinstallation of those items at the Signatory Airline's new premises is possible and not unreasonable.

### **Rentals, Fees and Charges**

Under the Airline Lease Agreement, Signatory Airlines pay monthly landing fees ("Landing Fees") as well as rentals on the premises in the terminal ("Terminal Rents").

**Landing Fees.** Landing Fees are determined by calculating the Airfield Revenue Requirement for the Airport (as described below) and dividing this requirement by the projected maximum gross certificated landed weight for all aircraft carrying passengers or cargo in commercial service that are expected to land at the Airport during the year. This calculation yields a Landing Fee that will be expressed in dollars and cents per one thousand pounds of landed weight. Landing Fees will be levied upon airlines based on the aggregate gross landed weight of all chargeable landings during the year.

The Airfield Revenue Requirement that is used to determine Landing Fees is computed by taking the sum of the following budgetary items: (a) debt service allocable to airfield capital projects funded from bonds or subordinated indebtedness; (b) the coverage amount applicable to the debt service allocable

to airfield capital projects funded from bonds or subordinated indebtedness; (c) annual operating expenses allocable to the airfield; (d) the portion of the total deposits needed to replenish the bond reserve fund required by the Master Trust Agreement for the Airport to required levels allocable to the airfield; and (e) the share of annual costs for renewal and replacement allocable to the airfield. The following items are then subtracted from this sum to arrive at the Airfield Revenue Requirement: (a) the Revenues (as described below) that are accrued by the City for the use of the airfield (excluding Landing Fees charged to airlines at the Airport but including landing fee premiums payable by Non-Signatory Airlines and Revenues accrued from parking fees at common-use gates), and (b) the coverage amount applicable to the debt service allocable to airfield capital projects funded from bonds or subordinated indebtedness for the immediately preceding fiscal year.

Under the Airline Lease Agreement, “Revenues” are defined as income, revenues, receipts and moneys accrued by City in accordance with generally accepted accounting principles, including investment earnings, from or in connection with the ownership or operation of the Airport or any part thereof or the leasing or use thereof. This general definition is subject to certain specific exclusions as detailed in the Airline Lease Agreement.

**Terminal Rents.** Terminal Rents are calculated by determining the Airline Terminal Revenue Requirement (as described below), crediting any Net Remaining Revenues (as described below) pursuant to the Revenue-Sharing provision of the Airline Lease Agreement, and then distributing the resulting Net Airline Terminal Revenue Requirement into three cost assignment groups for (a) ticket counters, gates, skycap positions, VIP rooms and airline ticket offices (collectively, “Group A”), (b) baggage claim and other offices (collectively “Group B”), and (c) baggage make-up and operations (collectively, “Group C”) to determine the square foot costs for each of these areas. The Airline Lease Agreement provides that differential rates shall apply to these different types of space provided that the sums of the amounts applicable to the different cost centers equal the total Airline Terminal Revenue Requirement; the costs assigned to the rented space within each of these groups shall bear the following relativities to each other on a square foot basis: (a) 1.00 for Group A, (b) 0.80 for Group B and (c) 0.50 for Group C.

The Airline Terminal Revenue Requirement that is used to determine Terminal Rents is computed by taking the sum of the following budgetary items: (a) debt service allocable to terminal capital projects funded from bonds or subordinated Indebtedness; (b) the coverage amount applicable to the debt service amount allocable to terminal capital projects funded from bonds or subordinated indebtedness; (c) the annual operating expenses allocable to the terminal; (d) the portion of the total deposits needed to replenish the bond reserve fund required by the Master Trust Agreement for the Airport to required levels allocable to the terminal; and (e) the share of annual costs for renewal and replacement allocable to the terminal. The coverage amount applicable to the debt service allocable to terminal capital projects funded from bonds or subordinated indebtedness for the immediately preceding fiscal year is then subtracted from this sum. The City will then divide that sum by the total amount of rentable terminal space and multiply the resulting quotient by the total square feet of airline premises at the Airport, yielding the Airline Terminal Revenue Requirement to be met by all Airlines.

The Airline Lease Agreement defines “Net Remaining Revenues” used to calculate the Net Airline Terminal Revenue Requirement as, for each fiscal year, the amount equal to Revenues plus Other Available Funds (as described below) less Operating Expenses less Debt Service less the Coverage Amount (for the current Fiscal Year) less other required fund deposits or payments pursuant to the Master Trust Agreement (including required renewal and replacement expenditures and subordinated indebtedness, if any).

The Airline Lease Agreement defines “Other Available Funds” used to calculate Net Remaining Revenues as amounts (other than Revenues or passenger facility charge Revenues, otherwise known as

“PFC Revenues”) made available to pay debt service in any period pursuant to the Master Trust Agreement and restrictions contained therein. Other Available Funds includes, but is not limited to, rolling debt service coverage amounts, revenue sharing amounts credited to the terminal cost and revenue center, and grant funds used to pay debt service.

*Charges for Use of Gates.* The Airline Lease Agreement provides that the City will calculate the revenue requirement for each gate by multiplying the total square footage of all gates at the Airport by the per-square foot cost for gates that is calculated as provided above for Group A space and then dividing that product by the total number of gates. Charges for Preferential Use Gates will be levied on a per-gate basis based on the revenue requirement for each gate, and charges for Common Use Gates will be levied on a per-turn basis where the charge for each turn will be calculated by dividing the revenue requirement for all Common Use Gates by the number of turns expected on all Common Use Gates during a fiscal year. The Airline Lease Agreement also provides for the City to levy aircraft parking charges in an amount determined by City Council resolution for parking at a common use gate for longer than the minimum time established by the City Council.

*Charges for Use of Ticket Counters.* The Airline Lease Agreement provides that the City will calculate the revenue requirement for each ticket counter by multiplying the total square footage of all ticket counters at the Airport by the per-square foot cost for ticket counters that is calculated as provided above for Group A space and then dividing that product by the total number of active ticket counters. Charges for Preferential Use Ticket Counters will be levied on a per-ticket counter basis based on the revenue requirement for each active ticket counter, while charges for Common Use Ticket Counters will be levied on an hourly basis where the charges for each hour will be calculated by dividing the revenue requirement for all Common Use Ticket Counters by the number of hours that the City expects all Common Use Ticket Counters to be used during the fiscal year.

*Charges for Use of Baggage Areas.*

Baggage Make-up Charges. The Airline Lease Agreement provides that the City will calculate the revenue requirement applicable to baggage make-up areas by multiplying the total square footage of all baggage make-up areas by the per-square foot cost for the Group C space that is calculated as provided above. The City will allocate 20% of that revenue requirement equally among all of the airlines, and the City will divide the remaining 80% by the total number of passengers enplaned during the fiscal year to determine the baggage make-up charge per enplaned passenger. Each airline will pay for the use of baggage make-up areas by paying (a) its share of the 20% revenue requirement plus (b) the product of the total number of passengers it enplanes during the fiscal year times the per-passenger baggage make-up charge.

Domestic Baggage Claim Charges. The Airline Lease Agreement provides that the City will calculate the revenue requirement applicable to baggage claim areas serving domestic flights by multiplying the total square footage of these baggage claim areas by the per-square foot cost for the Group B space that is calculated as provided above. The City will allocate 20% of this revenue requirement equally among all of the airlines with scheduled domestic service at the Airport, and the City will divide the remaining 80% by the total number of passengers deplaning from domestic flights arriving during the fiscal year to determine the domestic baggage claim charge per deplaned passenger. Each airline will pay for the use of baggage claim areas serving domestic flights by paying (a) its share of the 20% revenue requirement plus (b) the product of the total number of passengers it deplanes from domestic flights times the per-passenger domestic baggage claim charge.

*Charges for Use of Exclusive Use Premises.* The City is to calculate the annual rental rate for the use of airline ticket offices, VIP lounges and other Exclusive Use Premises by multiplying the square

footage of all Exclusive Use Premises at the Airport by the per-square foot cost for the Group A, Group B or Group C space, as applicable. Charges for the use of such Exclusive Use Premises are to be levied upon each airline on a fee per square foot basis.

*Charges for Use of the FIS Facility and International Baggage Claim Area.* The City is to levy charges for the FIS Facility and the International Baggage Claim Area as determined by the City Council from time to time.

*Charges for Use of Storage Space.* The annual rental rate for the use of storage space is to equal the per-square foot cost for Group C space. Charges are to be levied on the basis of the total square footage of such space assigned to each airline.

*Adjustments.* The Airline Lease Agreement provides that the Terminal Rents and the Landing Fees identified above will be established and may be adjusted annually after consultation with the Signatory Airlines. The City has the right to make more frequent adjustments if it appears to the City, on the basis of information it is able to accumulate during the course of a fiscal year, that the budgeted airfield or terminal costs or projected landed aircraft weight or rented terminal space the City used in calculating the Landing Fees or Terminal Rents will likely vary by more than 10% from actual results or if changes in Landing Fees or Terminal Rents are required by the terms and conditions of the Master Trust Agreement or any subordinated financing agreement. Adjustments also may be made if necessary to satisfy coverage requirements as described below under "Extraordinary Coverage Protection."

*Non-Signatory Premium.* The Airline Lease Agreement requires the City to charge Non-Signatory Airlines a 25% premium on all rates and charges set forth in the Airline Lease Agreement. Pursuant to a City ordinance, airlines that do not sign either a Signatory or a Non-Signatory Agreement will pay a 30% premium on all rates and charges set forth in the Airline Lease Agreement.

*Handling Agreements.* In the event that a Signatory Airline agrees to ground handle any portion of the operations of another airline, the Airline Lease Agreement provides that the Signatory Airline shall provide advance written notice of such proposed activities to the City, and the Signatory Airline shall pay 10% of its gross revenue from any ground handling agreement (other than a ground handling agreement with an Affiliate of the Signatory Airline) to the City. Notwithstanding the foregoing, a Signatory Airline shall not ground handle any airline which does not have the consent of the City for the operation of its business at the Airport.

*Revenue-Sharing.* In any fiscal year in which there are Net Remaining Revenues generated at the Airport and all requirements (including the minimum rate covenant requirement) of the Master Trust Agreement and any subordinated financing agreement have been satisfied, the Airline Lease Agreement provides that the Net Remaining Revenues will be divided 50/50 between the City and the airlines. If the actual Net Remaining Revenues exceed the Net Remaining Revenues that were forecast at the time of the execution of the Airline Lease Agreement, the airlines' share of the Net Remaining Revenues will be deposited into a rate stabilization fund for the Airport up to a cap of \$9 million. Once the rate stabilization fund has been fully funded or in the event that the actual Net Remaining Revenues do not exceed the projected Net Remaining Revenues, the airlines' share of the balance will be applied as a credit to the Airline Terminal Revenue Requirement for the following year. The first \$1 million of the City's share of any Net Remaining Revenues shall be retained by the Airport in a discretionary fund to be used for any lawful Airport purpose. The remaining balance of the City's share (at least during the term of the Airline Lease Agreement) shall be applied to the capital costs of Phase 1 projects or Phase 2 projects (as those terms are defined in Appendix A).

**Rate Stabilization Fund.** The Airline Lease Agreement provides that the rate stabilization fund will be maintained by the City up to a cap of \$9 million. Once that cap is reached, the City shall not deposit any additional sums into this fund until the balance falls below \$9 million. Interest earned on the fund will be credited to the fund until the fund reaches the \$9 million cap. So long as the rate stabilization fund contains \$9 million, any additional interest earned on the rate stabilization fund is to be deposited into the “Revenue Fund” established pursuant to the Master Trust Agreement.

As part of City’s rate-setting process, the budgeted cost per enplaned passenger (“CPE”) for each fiscal year will be compared to the applicable CPE in the airport forecast. The Airline Lease Agreement provides that in any year in which the budgeted CPE is higher than the projected CPE, the amount needed to lower the budgeted CPE to the projected CPE will be deducted from the rate stabilization fund and credited against Landing Fees or Terminal Rents as part of the rate-setting process to the extent that funds are available in the rate stabilization fund for this purpose. In any year in which the budgeted CPE is lower than the projected CPE and the rate stabilization fund contains less than \$9 million, the City may increase the budgeted CPE up to the projected CPE to fully fund the rate stabilization fund by raising the otherwise-determined Airline Terminal Revenue Requirement or Airfield Revenue Requirement.

**Extraordinary Coverage Protection.** The airlines acknowledge in the Airline Lease Agreement that in order to satisfy the applicable coverage amount for debt service on bonds and subordinated indebtedness, each airline will be required to make extraordinary coverage protection payments in addition to Landing Fees and Terminal Rents otherwise established by the Airline Lease Agreement in any fiscal year in which the amount of Revenues (less any credits for Landing Fees and Terminal Rents as provided in the Airline Lease Agreement) less operating expenses is projected to be less than the sum of the debt service plus the coverage amount applicable thereto. Any amounts that must be collected for any such extraordinary coverage protection payments shall be allocated to the Airfield Revenue Requirement or the Airline Terminal Revenue Requirement.

## **Security for Performance**

Each airline must provide the City with an irrevocable letter of credit, or other security acceptable to the City in the City’s sole discretion, in an amount equal to the estimate of two months’ rentals, fees and charges payable by each airline (excluding PFCs) to guarantee the faithful performance of each airline’s obligations under the Airline Lease Agreement and the payment of all rentals, fees and charges due thereunder. The Director may adjust the amount of the security from time to time upon a determination that an additional amount is warranted to protect the City and the Airport. If the City adjusts the amount of the security or deducts any delinquent or unpaid fees, costs or charges (including late payments) from the security, the affected airline must promptly replenish the deposit to the full amount required by the Director within 10 business days of a written demand. The failure to replenish the security within 30 days after written notice to the airline shall constitute a default under the Airline Lease Agreement.

## **Municipally-Funded Air Service Incentive Program**

The Airline Lease Agreement provides that if in any year during the term of the Airline Lease Agreement the percentage growth in annual enplanements at the Airport exceeds the growth in annual enplanements nationwide, the City will reduce the amount of its indirect overhead expenses that would otherwise be allocated to the Airport’s operating budget for the next succeeding fiscal year by a corresponding percentage, thereby reducing the otherwise-indicated Landing Fees and Terminal Rents. For example, if in a given year the rate of growth in annual enplanements at the Airport (for purposes of illustration, 6%) exceeds the national growth rate (4%) by two percentage points, the City shall reduce the percentage share of the City’s indirect overhead expenses allocated to the Airport for the next year (for

purposes of illustration, 22%) by two percentage points (to 20%). Notwithstanding the foregoing, in no event will the indirect overhead expenses of the City allocated to the Airport's operating budget exceed twenty-five percent (25%) of those expenses or be less than fifteen percent (15%) of those expenses during the term of the Airline Lease Agreement. In addition, the City reserves the sole right to reassess, amend or terminate the incentive program that is described above after any increase in the number of gates at the Airport (including without limitation the completion of Phase II of the City's Master Plan Program (referred to as Phase 2 projects in Appendix A), which Master Plan Program is detailed in Exhibit K to the Airline Lease Agreement).

## **Capital Expenditures**

"Capital Expenditure" is defined in the Airline Lease Agreement as "an expenditure made to acquire, purchase or construct a single capital item or project for the purpose(s) of improving, maintaining or developing the Airport and shall include expenses incurred for acquisition, development, study, analysis, review, design, or capital planning efforts."

In general, the Airline Lease Agreement provides that the Capital Expenditures to be paid for or financed with Revenues are subject to review by the Signatory Airlines. Unless a Capital Expenditure is excluded from Signatory Airline review as provided below, the City shall notify each Signatory Airline in writing of its intent to undertake a Capital Expenditure. Within 20 days after the delivery of such notification, a Signatory Airline may request in writing a meeting with the City and all Signatory Airlines for the purpose of discussing the proposed Capital Expenditure(s). Should such a request be made, the City shall meet collectively with the Signatory Airlines within 60 days of the City's original notice, and the City will consider the comments and recommendations of the Signatory Airlines with respect to proposed Capital Expenditure(s). Unless Signatory Airlines that constitute a Majority in Interest or "MII" (as defined below) for the airfield cost and revenue center or the terminal cost and revenue center shall issue written disapprovals for a particular Capital Expenditure in the applicable cost and revenue center within 30 days of the date of the City's meeting with the Signatory Airlines, the City may proceed with that Capital Expenditure. If Signatory Airlines that constitute an MII disapprove of a proposed Capital Expenditure subject to MII consideration, the City shall defer the project for one year. The City will be entitled, however, to move forward with any disapproved Capital Expenditure after the one-year waiting period (or earlier if the disapproval is reversed by an MII at any time).

"MII" (or "Majority In Interest") is defined in the Airline Lease Agreement to mean: (a) for the airfield cost and revenue center, such group of Signatory Airlines representing at least 50% of the Signatory Airlines and who together have paid at least 50% of the total Landing Fees paid by Signatory Airlines during the immediately preceding fiscal year, and (b) for the terminal cost and revenue center, such group of Signatory Airlines representing at least 50% of the Signatory Airlines and who together have (i) paid at least 50% of the total Signatory Airline Terminal Rents for the immediately preceding fiscal year and (ii) carried at least 50% of the enplaned passengers in the immediately preceding fiscal year.

The City is entitled to proceed with certain Capital Expenditure that are to be paid for or financed with Revenues under the Airline Lease Agreement without consideration by the Signatory Airlines. These Capital Expenditures are:

- (a) New development, planning or expansion projects in the airfield or terminal cost and revenue centers, other than projects identified in the Airport Master Plan Program, that have a gross project cost of less than \$5 million (the City shall not unreasonably segment these development, planning or expansion projects for the purpose of avoiding the \$5 million threshold);

(b) Phase I of the Airport Master Plan Program (referred to as Phase 1 projects in Appendix A) as identified in the Airline Lease Agreement;

(c) Phase II of the Airport Master Plan Program (referred to as Phase 2 projects in Appendix A), so long as one of the following activity triggers is met: (i) 217 scheduled flights at the Airport on any one day or (ii) 12.2 million total enplaned passengers and deplaned passengers at the Airport in any given fiscal year. In the event that either of these triggers is met and, subsequently, the number of scheduled flights per day falls below 163 for a period of at least 180 days or the total number of enplaned and deplaned passengers at the Airport falls below 9.15 million for any fiscal year, Phase II will be subject to Signatory Airline consideration until either activity trigger is reattained; provided, however, that this reconsideration provision will not be applicable to a Phase II project, or portion thereof, for which the City has issued bonds, commercial paper or subordinated indebtedness or for which the City has awarded a construction contract after the attainment of either of the triggers identified above;

(d) Projects required by the FAA, U.S. Department of Transportation, Transportation Security Administration or a similar government authority, other than the City;

(e) Projects to repair casualty damage to Airport property that must be rebuilt or replaced in order for the City to meet its obligations under the Airline Lease Agreement or any other agreements with lessees at the Airport;

(f) Projects undertaken in cost and revenue centers other than the airfield cost and revenue center and the terminal cost and revenue center;

(g) Reasonable repairs, rebuilding, improvements or additions, including associated costs, necessary to comply with the Airline Lease Agreement or applicable law or to settle lawful claims, satisfy judgments or comply with judicial orders against the City by reason of its ownership, operation, maintenance or use of the Airport;

(h) Expenditures of an emergency nature which, if not made within 48 hours, would result in the closing of any portion of the Airport;

(i) Projects funded directly or indirectly by PFC Revenues, customer facility charges or grants;

(j) Projects that are undertaken to satisfy the increased requirements of any Signatory Airline so long as such Signatory Airline agrees to pay all increased rentals, fees, charges and operating and maintenance costs that are sufficient to cover the annual debt service or operating and maintenance costs associated with the projects; and

(k) Projects related to special purpose facilities for which the user agrees to pay or reimburse the Airport.

The Airline Lease Agreement provides that notwithstanding the foregoing, in the event that the CPE for a fiscal year is projected to exceed \$9 (in 2005 dollars) after the application of available funds from the rate stabilization fund, the City shall consult with the Signatory Airlines before commencing with design or construction for Phase II of the Airport Master Plan Program unless the City has already proceeded to issue applicable bonds, commercial paper or subordinated indebtedness or the City has awarded any applicable construction contract(s). The City shall not, however, be obligated to consult with the Signatory Airlines before commencing with design or construction for Phase II of the Airport Master Plan Program if the CPE for a fiscal year is projected to exceed \$9 (in 2005 dollars) after the

application of available funds from the rate stabilization fund, solely as the result of the inclusion of costs for certain additional approved improvement projects listed in the airport forecast that was prepared in conjunction with the execution of the Airline Lease Agreement in the calculation of the CPE.

### **Damage and Destruction and Force Majeure**

If an airline's premises are partially damaged by fire, flood, windstorm, earthquake, or other casualty, the Airline Lease Agreement provides for no abatement or reduction in the rates and charges otherwise payable by the airline, so long as debt service payments are required; and (1) the portion of the airline's premises so damaged are promptly repaired, rebuilt, or restored by the City with such changes, alterations, and modifications as may be agreed upon by the City and the airline; and (2) the City has applied any net proceeds received by City under insurance policies as necessary to cover such losses, after payment by the City of any expenses of obtaining or recovering such net proceeds. In the event that such net insurance proceeds are insufficient to pay in full the costs of such repair, rebuilding, or restoration, the City will endeavor to arrange financing through the issuance of financing or other means and complete such repair, rebuilding, or restoration.

If an airline's premises are substantially or completely damaged or destroyed by fire, flood, windstorm, earthquake, or other casualty, the Airline Lease Agreement provides that the City shall make an equitable and proportional abatement or reduction in the rates and charges payable by the airline, based on the degree to which the portion of the airline's premises rendered untenantable is related to the airline's total premises, until such time as the affected premises is restored for Airline's use; and (1) the portion of the airline's premises so damaged are promptly repaired, rebuilt, or restored by the City with such changes, alterations, and modifications as may be agreed upon by the City and the airline; and (2) the City has applied any net proceeds received by City under insurance policies as necessary to cover such losses, after payment by the City of any expenses of obtaining or recovering such net proceeds. In the event that such net insurance proceeds are insufficient to pay in full the costs of such repair, rebuilding, or restoration, the City will endeavor to arrange financing through the issuance of financing or other means and complete such repair, rebuilding, or restoration.

In the event that an airline's premises are damaged or destroyed as the result of the negligence or willful act or omission of an airline, its employees, its agents, or licensees, the Airline Lease Agreement provides that there shall be no abatement of rent during the repair or replacement of said airline's premises. To the extent that the costs of repairs exceed the amount of any insurance proceeds payable to the City by reason of such damage or destruction, the responsible airline shall pay the amount of such additional costs to the City.

The Airline Lease Agreement provides that, except as otherwise expressly provided in the Airline Lease Agreement, neither the City nor the airlines shall be deemed to be in default if either party is prevented from performing any of the obligations, other than the payment of rentals, fees, and charges, by reason of strikes, boycotts, labor disputes, epidemics, embargoes, shortages of energy or materials, acts of God, acts of the public enemy, weather conditions, riots, rebellion, or sabotage, or any other circumstances for which it is not responsible or which are not within its control.

### **Indemnification, Insurance and Public Liability**

The Airline Lease Agreement provides that the Signatory Airlines will indemnify the City for all claims and causes of action of every kind and character arising out of or incident to or in connection with the performance of the Signatory Airlines under the Airline Lease Agreement, a Signatory Airline's use and occupancy of the airline premises under the Airline Lease Agreement, a Signatory Airline's negligent acts, omissions or operations under the Airline Lease Agreement or the performance, non-performance or

purported performance of a Signatory Airline or any breach of the terms of the Airline Lease Agreement. The Airline Lease Agreement provides, however, that this indemnification will not apply when the applicable claim, liability, expense, loss, cost, fine, damage or cause of action is caused by the negligence of the agents, employees, contractors, officers or boards of the City (but only to the extent of the portion of the claim, liability, expense, loss, cost, fine, damage or cause of action caused by such negligence).

The Airline Lease Agreement requires each of the Signatory Airlines to maintain insurance in full force and effect as specified below: (a) aircraft liability insurance with coverage of \$100,000,000 combined single limit for bodily injury and property damage; (b) \$50,000,000 war and named perils coverage for bodily injury and property damage, each occurrence and annual aggregate (or the U.S. government equivalent); (c) worker's compensation and employers' liability insurance written in accordance with the laws of the State of California with \$1,000,000 in employer's liability coverage; (d) commercial business auto insurance with a minimum limit of not less than \$1,000,000 combined single limit for bodily injury and property damage; and (e) property insurance in an amount equal to "Value of Airline Improvements and Betterments" during the course of construction and after completion, which coverage shall include replacement value, covering airline improvements and betterments, for fire and extended coverage, including sprinkler leakage, vandalism and malicious mischief, and debris removal.

Each insurance policy shall state that coverage shall not be suspended, voided, canceled or reduced in limits except after 30 days' prior written notice has been given to the City; provided, however, that the notice period for war and named perils insurance may be seven days or such lesser period as may be customarily available.

The City has retained the right at any time to review the coverage, form and amount of the insurance required under the Airline Lease Agreement and to require each airline to obtain insurance sufficient in coverage, form and amount to provide adequate protection for the City and/or for members of the public.

Under the terms of the Airline Lease Agreement, the City and the airlines agree to have all property insurance carried with respect to the Airport endorsed with a clause that waives all rights of subrogation that the insurer of one party may have against the other party, and the City and the airlines will employ diligent efforts to cause their insurance companies to endorse the affected property insurance policies with a waiver of subrogation clause.

### **Relation to Master Trust Agreement**

The Airline Lease Agreement provides that it is expressly subject and subordinate to (a) the Master Trust Agreement (defined elsewhere in this Official Statement) and (b) any bond resolution, trust agreement, indenture or other financing agreement providing for or authorizing the issuance by the City of subordinated indebtedness, including an agreement related to the security or credit enhancement for the subordinated indebtedness, as each may be supplemented or amended from time to time (a "Subordinated Financing Agreement").

In the event that the City intends to amend or supplement the Master Trust Agreement or any Subordinated Financing Agreement in a manner that would materially alter the terms and provisions of the Airline Lease Agreement or materially impact the levels of rentals, fees and charges paid by a Signatory Airline, City shall notify each Signatory Airline in advance.

## **Default and Termination**

Upon the occurrence of any of the following events, subject to applicable notice and cure periods, the Airline Lease Agreement provides that the City may terminate the Airline Lease Agreement, may reenter the airline premises and remove all Signatory Airline persons and property and may relet the airline premises:

- (a) The conduct of any business or performance by the Signatory Airline of any acts at the Airport not specifically authorized under the Airline Lease Agreement or by any other agreements between the City and the Signatory Airline, and said business or acts do not cease within 30 days of receipt of the City's written notice to cease said business or acts.
- (b) The failure by the Signatory Airline to cure a default in the performance of any of the terms, covenants, and conditions required in the Airline Lease Agreement (except insurance requirements and payment of rentals, fees, and charges) within 30 days of receipt of written notice by the City to do so; or if by reason of the nature of such default, the same cannot be remedied within 30 days following receipt by a Signatory Airline of written demand from the City to do so, the Signatory Airline fails to commence the remedying of such default within said 30 days following such written notice, or having so commenced, shall fail thereafter to continue with diligence the curing thereof. The Airline Lease Agreement provides that the Signatory Airline shall have the burden of proof to demonstrate (i) that the default cannot be cured within 30 days, and (ii) that it is proceeding with diligence to cure said default and that such default will be cured within a reasonable period of time.
- (c) The failure by the Signatory Airline to pay any part of the rentals, fees, and charges due under the Airline Lease Agreement and the continued failure to pay said amounts in full within 30 days of the City's written notice of payments past due; provided, however, if a dispute arises between the City and the Signatory Airline with respect to any obligation or alleged obligation of the Signatory Airline to make payments to the City, payments under protest by the Signatory Airline of the amount due shall not waive any of the Signatory Airline's rights to contest the validity or amount of such payment.
- (d) The failure by the Signatory Airline to provide and keep in force insurance coverage in accordance with the Airline Lease Agreement.
- (e) The appointment of a trustee, custodian, or receiver of all or a substantial portion of a Signatory Airline's assets.
- (f) The divestiture of a Signatory Airline's estate in the Airline Lease Agreement by operation of law, by dissolution or by liquidation (not including a merger or sale of assets).
- (g) The abandonment by the Signatory Airline of the airline premises, or its conduct of business at the Airport; and, in this connection, suspension of operations for a period of 60 days will be considered abandonment in the absence of a labor dispute or other governmental action in which the Signatory Airline is directly involved.
- (h) The failure by the Signatory Airline to remit PFC Revenues in accordance with the Airline Lease Agreement.

In the event that the City relets the airline premises, rentals, fees, and charges received by the City from such reletting shall be applied: (i) to the payment of any indebtedness, other than rentals, fees, and charges due under the Airline Lease Agreement, from the Signatory Airline to City; (ii) to the payment of any cost of such reletting; and (iii) to the payment of rentals, fees, and charges due and unpaid under the

Airline Lease Agreement. The residue, if any, shall be held by the City and applied in payment of future rentals, fees, and charges as the same may become due and payable the Airline Lease Agreement. If that portion of such rentals, fees, and charges received from such reletting and applied to the payment of rentals, fees, and charges under the Airline Lease Agreement is less than the rentals, fees, and charges as would have been payable during applicable periods by the Signatory Airline under the Airline Lease Agreement, then the Signatory Airline shall pay such deficiency to the City whenever rentals, fees or charges are due to the City under the Airline Lease Agreement. The Signatory Airline shall also pay to the City, as soon as ascertained, any reasonable costs and expenses incurred by the City in such reletting not covered by the rentals, fees, and charges received from such reletting.

### **Remedies Following Bankruptcy**

Notwithstanding any other default provisions in the Airline Lease Agreement, upon the filing by or against a Signatory Airline of any proceeding under Federal bankruptcy laws, the Airline Lease Agreement provides that it shall automatically terminate (unless such termination is affirmatively waived at the time of the filing or subsequently by the City) in addition to other remedies provided under provisions of the Federal Bankruptcy Rules and Regulations and Federal Judgeship Act of 1984, as such may be subsequently amended, supplemented, or replaced. Notwithstanding the foregoing, the City shall be entitled to waive the automatic termination provision mentioned above in writing. In the event that the City waives the automatic termination requirement, the City shall not be obligated to perform under the terms of the Airline Lease Agreement so long as any proceeding under Federal bankruptcy laws remains outstanding. Any waiver by City of the automatic termination provision is not to be construed to be a waiver of any subsequent automatic termination.

### **Customer Service**

The Airline Lease Agreement provides that each Signatory Airline shall appoint a customer service representative who will work with representatives from the Airport's Customer Service and Operations Division and representatives from the other passenger airlines at the Airport to voluntarily and collectively set minimum performance standards to provide passengers at the Airport with the highest and best customer service possible. These standards are to be self-imposed and self-policed by the Airport and the passenger airlines. The Airport reserves the right to disclose the success of the passenger airlines in meeting these standards.

### **Assignment and Subletting by Signatory Airline**

No Signatory Airline may assign or transfer the Airline Lease Agreement or any interest therein nor sublet the whole or any portion of the Signatory Airline's premises without first obtaining the City's written consent. The Airline Lease Agreement also provides that neither the Airline Lease Agreement nor any interest thereunder shall be assignable or transferable by operation of law or by any process or proceeding of any court or otherwise without the consent of the City, which consent shall not be unreasonably withheld.

Notwithstanding the foregoing, a Signatory Airline shall have the right, without first obtaining the City's written consent, to assign or transfer the Airline Lease Agreement to an entity controlling, controlled by or under common control with the Signatory Airline or a successor by merger, consolidation or acquisition to all or substantially all of the assets of the Signatory Airline.

The City in its sole discretion may terminate the Airline Lease Agreement upon 30 days' written notice in the event the Signatory Airline, directly or indirectly, assigns, sells, hypothecates or otherwise

transfers the Airline Lease Agreement or any portion of the Signatory Airline's premises in contravention of the Agreement, without the prior written consent of the City.

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## APPENDIX H

### DTC AND THE BOOK-ENTRY SYSTEM

*The following information regarding DTC and DTC's book-entry system has been extracted from information provided by DTC. The City makes no representation as to the accuracy or the completeness of such information or as to the absence of material adverse changes in such information. Additionally, the City undertakes no responsibility for and makes no representations as to the accuracy or the completeness of the content of any material contained on DTC's website as described in this Appendix H including, but not limited to, updates of such information or links to other Internet sites accessed through such website.*

DTC will act as the securities depository for the Series 2014 Bonds. The Series 2014 Bonds will be issued as fully-registered bonds in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Series 2014 Bond certificate will be issued for each maturity of the Series 2014 Bonds in the principal amount of such maturity and will be deposited with DTC.

DTC, the world's largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has a Standard & Poor's rating of AA+. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at [www.dtcc.com](http://www.dtcc.com) and [www.dtc.org](http://www.dtc.org); nothing contained in such websites is incorporated into this Official Statement.

Purchases of the Series 2014 Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Series 2014 Bonds on DTC's records. The ownership interest of each actual purchaser of each Series 2014 Bond ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Series 2014 Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Series 2014 Bonds, except in the event that use of the book-entry system for the Series 2014 Bonds is discontinued.

To facilitate subsequent transfers, all Series 2014 Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of the Series 2014 Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Series 2014 Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such Series 2014 Bonds are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of the Series 2014 Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Series 2014 Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Security documents. For example, Beneficial Owners of the Series 2014 Bonds may wish to ascertain that the nominee holding the Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Series 2014 Bonds are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Series 2014 Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the Series 2014 Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Payments of principal of, premium, if any, and interest evidenced by the Series 2014 Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the City or the Trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC (nor its nominee), the Trustee, or the City, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal of, premium, if any, and interest evidenced by the 2014 Bonds to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the City or the Trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

THE CITY, THE UNDERWRITERS OR THE TRUSTEE WILL NOT HAVE ANY RESPONSIBILITY OR OBLIGATION TO DTC PARTICIPANTS, INDIRECT PARTICIPANTS OR BENEFICIAL OWNERS WITH RESPECT TO THE PAYMENTS OR THE PROVIDING OF NOTICE TO DTC PARTICIPANTS, INDIRECT PARTICIPANTS OR BENEFICIAL OWNERS OR THE SELECTION OF BONDS FOR REDEMPTION.

None of the City, the Airport, the Underwriters or the Trustee can give any assurances that DTC, DTC Participants, Indirect Participants or others will distribute payments of principal of, premium, if any, and interest on the Series 2014 Bonds paid to DTC or its nominee, as the registered Owner, or any redemption or other notice, to the Beneficial Owners or that they will do so on a timely basis or that DTC will serve and act in a manner described in this Official Statement.

DTC may discontinue providing its services as depository with respect to the Series 2014 Bonds at any time by giving reasonable notice to the City or the Trustee. Under such circumstances, in the event that a successor depository is not obtained, 2014 Bond certificates are required to be printed and delivered.

The City may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, Series 2014 Bond certificates will be printed and delivered to DTC.

According to DTC, the foregoing information with respect to DTC has been provided to the Industry for informational purposes only and is not intended to serve as a representation, warranty or contract modification of any kind.

Neither the City nor the Trustee will have any responsibility or obligation to Participants or the persons for whom they act as nominees with respect to the Series 2014 Bonds for the accuracy of any records maintained by DTC or any Participant, the payment by DTC or any Participant of any amount in respect of principal or interest on the Series 2014 Bonds, any notice that is permitted or required to be given to Registered Owners under the Master Trust Agreement (except such notices as shall be required to be given by the City to the Trustee or to DTC), the selection by DTC or any Participant of any person to receive payment in the event of a partial redemption of the Series 2014 Bonds, or any consent given or other action taken by DTC as the Registered Owner (through its partnership nominee). The City and the Trustee may treat and consider Cede & Co., in whose name each Series 2014 Bond is registered on the Bond Register, as the holder and absolute owner of such Series 2014 Bond for all purposes, except as provided in the Master Trust Agreement. For the purposes of this Official Statement, the term "Beneficial Owner" includes the person for whom the Participant acquires an interest in the Series 2014 Bonds.

If the City is unable to retain a qualified successor to DTC or the City has determined that DTC or its successor is no longer able to carry out its functions as a depository or that it is no longer desirable to use a depository, the City will be required to deliver a written request to the Trustee, together with a supply of definitive Series 2014 Bonds in certificated form, to issue Series 2014 Bonds in any authorized denomination. Thereafter, the principal of the Series 2014 Bonds shall be in lawful money of the United States upon due presentment and surrender thereof at the principal office of the Trustee, interest on the Series 2014 Bonds will be payable by check mailed to the persons in whose names such Series 2014 Bonds are registered, at the address appearing upon the registration books on the 15th day of the month next preceding an interest payment date, and the Series 2014 Bonds will be transferable as provided in the Master Trust Agreement.

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