



**CITY OF PALO ALTO, CA
2008-09**



**Comprehensive
Annual Financial Report**
Fiscal Year Ended June 30, 2009

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*City of Palo Alto
California*

**Comprehensive
Annual Financial
Report**

**For the fiscal year ended
June 30, 2009**



Prepared by: Administrative Services Department

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Table of Contents.....

INTRODUCTION

Letter of Transmittal v

City Officials ix

Organizational Structure x

Administrative Services Department Organization xi

GFOA Certificate of Achievement for Excellence in Financial Reporting xii

FINANCIAL SECTION

Independent Auditor’s Report on Basic Financial Statements xiii

M D & A

Management’s Discussion and Analysis..... 1

BASIC FINANCIAL STATEMENTS

Citywide Financial Statements:

Statement of Net Assets 25

Statement of Activities 26

Fund Financial Statements

Major Governmental Funds:

Balance Sheet 29

Reconciliation of Fund Balances to Governmental Activities Net Assets..... 30

Statement of Revenues, Expenditures, and Changes in Fund Balance 31

Reconciliation of the Statement of Revenues, Expenditures and Changes
in Fund Balances of Governmental Funds to the Statement of Activities..... 32

Statement of Revenues, Expenditures, and Changes in Fund Balances –
Budget and Actual – General Fund 33

BASIC FINANCIAL STATEMENTS (Continued)

Major Proprietary Funds:

Statement of Net Assets36

Statements of Revenues, Expenses and Changes in Net Assets38

Statement of Cash Flows.....40

Fiduciary Funds:

Statement of Fiduciary Net Assets45

Notes to Financial Statements

Index to the Notes to the Basic Financial Statements47

Notes to Basic Financial Statements49

SUPPLEMENTAL INFORMATION

Non-major Governmental Funds

Combining Balance Sheets 106

Combining Statements of Revenues, Expenditures
and Changes in Fund Balances..... 110

Combining Statements of Revenues, Expenditures and Changes
in Fund Balance–Budget and Actual..... 114

Internal Service Funds

Combining Statements of Net Assets 123

Combining Statements of Revenues, Expenses and Changes in Net Assets..... 124

Combining Statements of Cash Flows..... 125

Fiduciary Funds

Statement of Changes in Assets and Liabilities - All Agency Funds..... 128



STATISTICAL SECTION

Financial Trends

Net Assets by Component	131
Changes in Net Assets	132
Fund Balances of Governmental Funds	134
Changes in Fund Balance of Governmental Funds	136

Revenue Capacity

Electric Daily Loads and Top Customers by Usage.....	138
Electric Operating Revenue by Source	139
Assessed Value of Taxable Property.....	140
Property Tax Rates, All Overlapping Governments	141
Property Tax Levies and Collections	142
Principal Property Taxpayers	143

Debt Capacity

Ratio of Outstanding Debt by Type.....	144
Computation of Direct and Overlapping Debt.....	145
Computation of Legal Bonded Debt Margin	146
Revenue Bond Coverage.....	147

Demographic and Economic Information

Taxable Transactions by Type of Business.....	148
Demographic and Economic Statistics	149
Principal Employers	150

Operating Information

Full-Time Equivalent City Government Employees by Function	151
Operating Indicators by Function/Program.....	152
Capital Asset Statistics by Function/Program	154
Insurance Coverage.....	156



SINGLE AUDIT SECTION

Schedule of Current Year Findings and Questioned Costs 161

Section I – Summary of Auditor’s Results 161

Section II – Financial Statement Findings 162

Section III – Federal Award Findings and Questioned Costs..... 162

Section IV – Status of Prior Year Findings
and Questioned Costs 162

Schedule of Expenditures of Federal Awards..... 163

Notes to the Schedule of Expenditures of Federal Awards..... 165

Report on Internal Control over Financial Reporting and On Compliance
And Other Matters Based on an Audit of Financial Statements
Performed In Accordance with Government Auditing Standards 167

Report on Compliance with Requirements Applicable To
Each Major Program and on Internal Control Over Compliance
in Accordance with OMB Circular A-133..... 169

City of Palo Alto
Office of the City Manager

Transmittal Letter.....

December 15, 2009

THE HONORABLE CITY COUNCIL
Palo Alto, California

Attention: Finance Committee

COMPREHENSIVE ANNUAL FINANCIAL REPORT
YEAR ENDED JUNE 30, 2009

Members of the Council and Citizens of Palo Alto:

Transmittal: The Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2009, is submitted for Council review in accordance with Article III, Section 16 and Article IV, Section 13 of the City of Palo Alto Charter and is published as a matter of public record for interested citizens. This transmittal letter provides information regarding the economy and the governing structure in Palo Alto. An overview of the City's financial activities for the fiscal year is discussed in detail in the Management's Discussion and Analysis section of the CAFR. While the independent auditor has expressed an opinion on the financial statements contained in this report, management takes sole responsibility for the completeness and reliability of the information contained in this report, based upon a comprehensive framework of internal control that it has established for this purpose. The objective of internal controls is to provide reasonable, rather than absolute, assurance that the CAFR information is accurate in all material respects.

INDEPENDENT AUDIT

The City of Palo Alto's financial statements have been audited by Maze and Associates, a firm of licensed certified public accountants. The goal of the audit is to obtain reasonable assurance that the financial statements are free of material misstatement. Maze and Associates concluded, based on the audit, that there was a reasonable basis for rendering an unqualified opinion for the fiscal year ended June 30, 2009, and that the financial statements are fairly presented in conformity with generally accepted accounting principles (GAAP). The independent auditor's report is presented as the first component of the financial section of this report.

In addition, Maze and Associates also conducts the federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. The standards governing the Single Audit require the independent auditor to report on the fair presentation of the financial statements, government's internal controls and compliance with legal requirements. These reports are available in the Single Audit section of the CAFR.

THE PALO ALTO ECONOMY

Local Trends: The City of Palo Alto, population 64,484, is a largely “built-out” community in the heart of Silicon Valley and the greater San Francisco and San Jose areas. The adjacent Stanford University, one of the premier institutions of higher education in the nation, has produced much of the talent that founded many successful high-tech companies in Palo Alto and Silicon Valley. With varied and relatively stable employers such as Stanford University, the Stanford Medical Center, the Palo Alto Medical Foundation, the Palo Alto Unified School District, the Stanford Shopping Center and businesses such as, Hewlett-Packard Company, VMware, Facebook, Space Systems Loral, Palo Alto has enjoyed a diverse employment and revenue base.

Like other jurisdictions in Silicon Valley, the State and the nation, the City has been impacted by the “Great Recession.” In Fiscal Year (FY) 2009 the City’s unemployment rate has risen to 6.4 percent, local retail sales have decreased, and residential and commercial property transactions have dropped. The recession has acutely affected local revenues and the City’s budget. Economically sensitive revenue sources such as sales, transient occupancy, and documentary transfer taxes have decreased by 11.2 percent, 10.8 percent, and 42.5 percent over FY 2008 levels, respectively. Although property taxes rose by 10 percent over FY 2008, they are expected to have minimal growth in the next 2 years.

Preliminary data for FY 2010 presages another weak revenue performance. New automobile and department store sales are soft, hotel occupancy and daily rates remain low, and property transactions are below the level of activity in prior years. While there is some evidence that the recession has “bottomed out,” a recovery is expected to be lengthy and slow. As long as the economy is faced with high unemployment, stagnant income, and tight credit, spending is expected to be muted.

As with past economic downturns, the City is proactively taking steps to align expenses and revenues through service and program cuts, revenue enhancements, and employee compensation savings. Facing budget deficits for FY 2009 and FY 2010, the City has eliminated 20.3 full-time equivalent positions in the General Fund and reduced other expenses. Unlike prior recessions where mostly short-term solutions were used to balance the budget (e.g. furloughs), the City believes it now faces long-term structural budget problems such as a growing General Fund infrastructure liability and unsustainable retirement and retiree medical commitments. It is currently negotiating employee contributions to health care and retirement costs as well as possible changes in those plans.

On the revenue side, the City has been active in maintaining and attracting business that generate tax revenues. Examples include assisting Magnussen Toyota with their expansion on Middlefield Road and promoting Palo Alto retail properties through the International Council of Shopping Centers annual meeting. The City is proud to report that its citizens have approved of a \$76 million General Obligation bond issue to expand and rehabilitate its libraries and to build a new community center.

Employment Trends: Palo Alto is home to a strong mix of small, medium, and large firms. Employment opportunities within the City are much sought after and include; education at Stanford University, high technology at the Stanford Research Park, and health care at two medical facilities of national stature. Numerous institutions that have more than 1,000 employees include: the University, the Veterans Affairs Palo Alto Health Care facility, the Palo Alto Medical Foundation, Hewlett Packard, the Palo Alto Unified School District, and the City of Palo Alto. Palo Alto’s unemployment rate is 6.4 percent while the State’s is 12.2 percent and the nation’s 9.4 percent.

Real Estate Market: In its most recent annual report, the Santa Clara County Assessor’s Office noted that “for the first time in more than a decade both the commercial and residential sectors experienced declines”. In FY 2007 the countywide rate of growth was 8.3 percent; in FY 2008 it was 7.0 percent; in FY 2009 it was 0.2 percent; and in FY 2010 it is expected to be virtually flat. The Assessor went on to say, “The total net assessed value of all real and business property grew by a meager \$542 million for FY2010, an increase of only 0.18 percent over the prior year.”

There are, however, significant geographic differences within the county with growth ranging from 6.22 percent in Mountain View to negative 9.48 percent in Gilroy.

The City of Palo Alto’s assessed value increased by 11.4 percent in FY 2009 and 3.8 percent in FY 2010. In calendar year 2008 and the first two quarters of 2009, there were 6,214 and 2,324 foreclosures in the county but only 8 and 3 foreclosures in Palo Alto for the same periods. These figures show a stable, local real estate market where properties have maintained their value in spite of considerable real estate volatility. Nevertheless, residential and commercial transactions were low due to credit conditions and the reluctance of owners to sell into a buyer’s market. With its highly regarded school district, well-educated and high-income population, cultural amenities, and the presence of Stanford University, the City’s real estate values are typically shielded from major price swings. In discussing the impacts on property values recently, the County Assessor stated, “Local communities composed of ‘high-end’ housing and/or solid commercial, industrial property base, were impacted only marginally.”

Long Range Financial Forecast: The City of Palo Alto produces a 10 year Long Range Financial Forecast (LRFF) annually. This comprehensive report analyzes, for example, local, state, and federal economic conditions; short and long-term revenue and expense trends; expense challenges such as funding retiree medical benefits; revenue opportunities such as instituting an occupancy tax increase; and infrastructure needs. The forecast is designed to highlight finance issues which the City can address proactively. Moreover, it is a tool that allows policymakers an opportunity to prioritize funding needs over time.

Delivered to Council in December, this forecast sets the tone and themes for the annual budget process that begins in January. The forecast is one of the many tools and reports the City uses for financial planning. These include, for example: quarterly revenue and expense analyses, midyear budget adjustments, a five-year capital improvement plan, quarterly sales tax reports, and actuarial reports to ascertain long-term retiree liabilities. Basically, the City is conscientious and pro-active in financial planning. It is worthwhile to note that during the last two economic downturns, the City has balanced its annual budget via expenditure reductions or revenue enhancements and has not drawn down reserves, as a consequence of revenue shortfalls.

Cash and Investments: The City of Palo Alto invests its excess cash prudently and has adopted an investment policy as prescribed by State law. The policy states that investments are to be made in the following priority order: safety, liquidity, and yield. As of June 30, 2009, the City had \$327.2 million (par value) in its portfolio. Its principal investments were in agency securities, treasuries, and a State of California investment pool. The City’s investment practice is to buy securities and hold them to maturity to avoid principal loss. Staff provides a quarterly report of investments for Council review. During FY 2009, staff complied with all requirements of the City’s investment policy.

THE PALO ALTO GOVERNMENT

As a charter city delivering a full range of municipal services and public utilities under the council-manager form of government, Palo Alto offers an outstanding quality of life for its residents. The independent Palo Alto Unified School District (PAUSD) has achieved state and national recognition for the excellence of its programs. The City has dedicated 4,000 acres of open space to parks and wildlife preserves. Public facilities include five libraries, four community centers, a cultural arts center, an adult and children’s theater, a junior museum and zoo, and a golf course. The City provides a diversity of human services for seniors and youths, an extensive continuing education program, concerts, exhibits, team sports and special events.

City Council: The Council consists of nine members elected at-large for four-year, staggered terms. At the first meeting of each calendar year, the Council elects a Mayor and Vice-Mayor from its membership, with the Mayor having the duty of presiding over Council meetings. The Council is the

appointing authority for which the City Manager and three other officials, the City Attorney, City Clerk, and City Auditor, report directly to.

Finance Committee: While retaining the authority to approve all actions, the City Council has established a subcommittee to review financial matters. Staff provides the CAFR, the results of external and internal audits, periodic budget-versus-actual, and investment and performance measure reports to the Finance Committee and Council to assist in their evaluation of the City’s financial performance.

City Manager: The City Manager directs administrative services, human resources, libraries, public works, planning and community environment, public safety, community services departments and also the municipal electric, water, gas, fiber optics, wastewater collection, wastewater treatment, storm drainage, and refuse utilities (the utilities represent almost two-thirds of the City’s revenues).

SUMMARY

Awards: During the past year, the City received an award for the prior fiscal year CAFR from the Government Finance Officers Association (GFOA) for “excellence in financial reporting.” The 2008-09 CAFR has been submitted to the GFOA award program and management believes that, once again, it will meet the criteria for this distinguished financial reporting award.

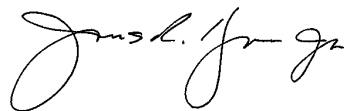
Acknowledgment: This CAFR reflects the hard work, talent and commitment of the staff members of the Administrative Services Department. This document could not have been accomplished without their efforts and each contributor deserves sincere appreciation. Management wishes to acknowledge the support of Trudy Eikenberry, Accounting Manager, and the Senior Accountants, Staff Accountants, Payroll Analysts and Accounting Specialists for the high level of professionalism and dedication they bring to the City of Palo Alto. Management would also like to express its appreciation to Maze & Associates, the City’s independent external auditors, who assisted and contributed to the preparation of this Comprehensive Annual Financial Report.

Special acknowledgment must be given to the City Council Finance Committee for its support and interest in directing the financial affairs of the City in a responsible, professional and progressive manner.

Respectfully submitted,



LALO PEREZ,
Administrative Services Director



JAMES KEENE,
City Manager



City of Palo Alto City Officials

City Council

Peter Drekmeier, *Mayor*

Jack Morton, *Vice-Mayor*

John Barton

Patrick Burt

Sid Espinosa

Yoriko Kishimoto

Larry Klein

Greg Schmid

Yiaway Yeh

Finance Committee

Pat Burt, *Chair*

Larry Klein

Jack Morton

*Greg Schmid

Policy and Services Committee

Sid Espinosa, *Chair*

John Barton

Yoriko Kishimoto

*Yiaway Yeh

Council-Appointed Officers

City Manager

James Keene

City Attorney

Gary Baum

City Clerk

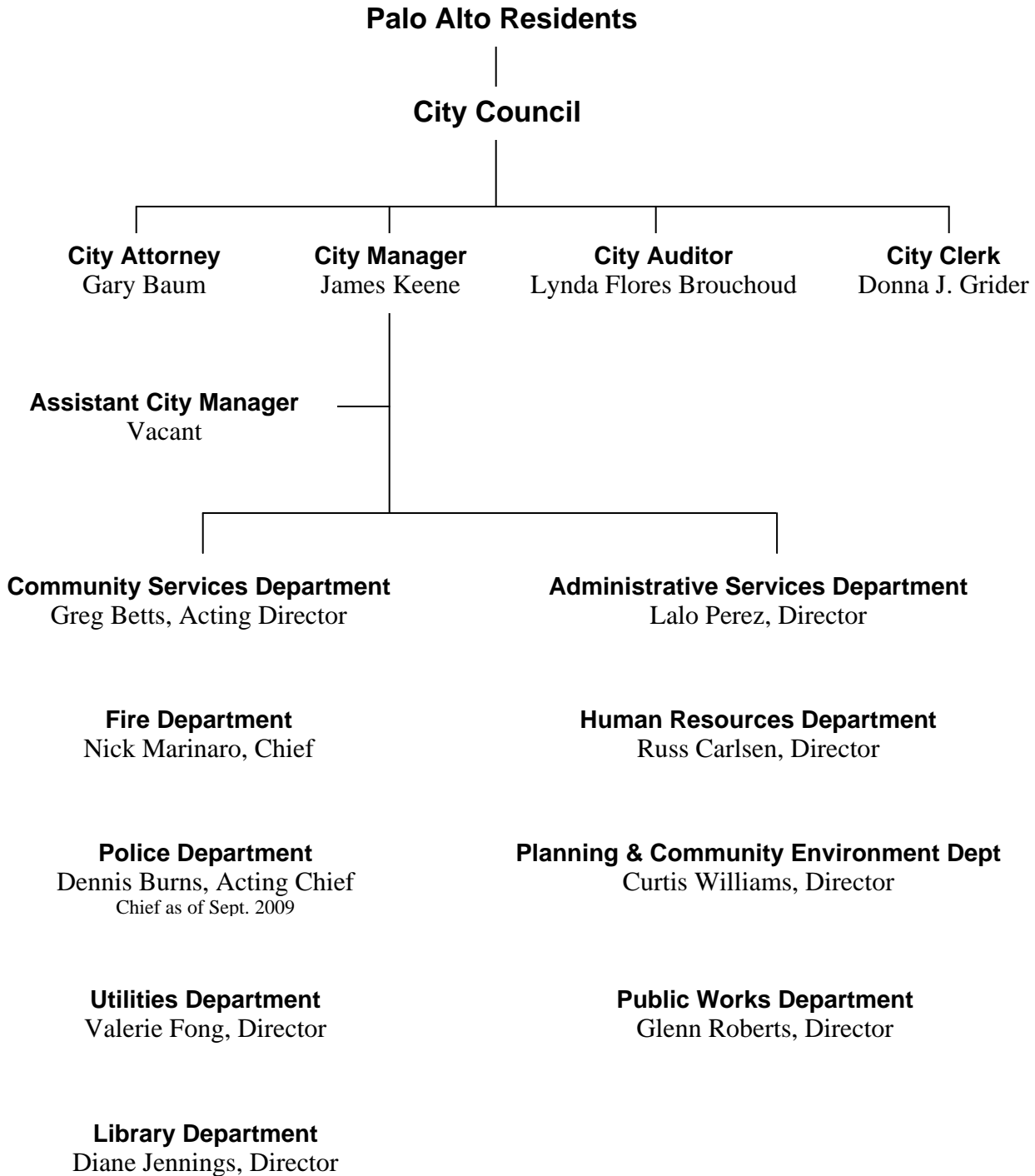
Donna Grider

City Auditor

Lynda Flores Brouchoud

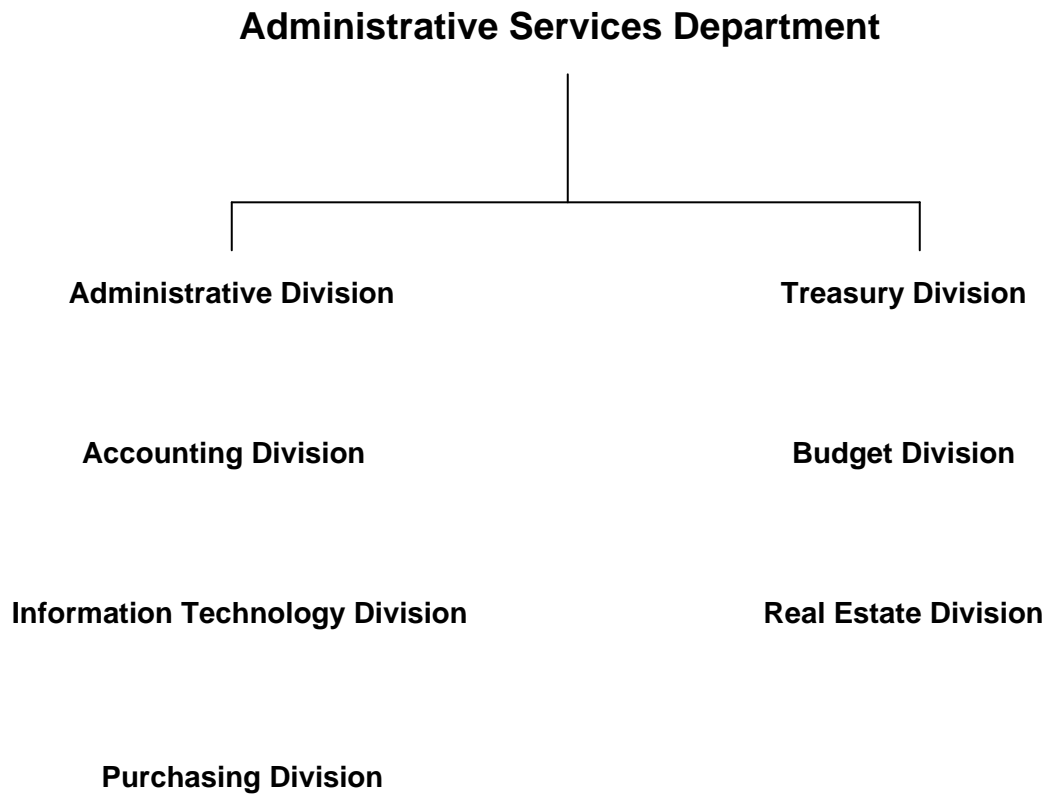
*As of Sept. 2009 Greg Schmid is on the Policy and Services Committee and Yiaway Yeh is on the Finance Committee

City of Palo Alto Organization





Administrative Services Organization



Mission Statement

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

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

Certificate of Achievement for Excellence in Financial Reporting

Presented to

City of Palo Alto
California

For its Comprehensive Annual
Financial Report
for the Fiscal Year Ended
June 30, 2008

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



President

Executive Director

Independent Auditor's Report.....

MAZE & ASSOCIATES

**INDEPENDENT AUDITOR'S REPORT
ON BASIC FINANCIAL STATEMENTS**

ACCOUNTANCY CORPORATION
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Pleasant Hill, California 94523
(925) 930-0902 • FAX (925) 930-0135
maze@mazeassociates.com
www.mazeassociates.com

Honorable Mayor and City Council
City of Palo Alto, California

We have audited the basic financial statements of the governmental activities, business-type activities, each major fund and the aggregate remaining fund information of the City of Palo Alto, California as of and for the year ended June 30, 2009, which collectively comprise the City's basic financial statements as listed in the Table of Contents. These financial statements are the responsibility of the City's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in the United States of America and the standards for financial audits contained in *Government Auditing Standard*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement. An audit includes examining on a test basis evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the City of Palo Alto, California as of June 30, 2009 and the respective changes in the financial position and cash flows, where applicable thereof and the respective budgetary comparisons listed as part of the basic financial statements for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Note 10 to the basic financial statements, the City restated Enterprise Fund Net Assets to recategorize the Fiber Optic Enterprise as a separate fund effective July 1, 2008.

In accordance with Government Auditing Standards, we have also issued our report dated October 23, 2009 on our consideration of the City of Palo Alto's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is 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 and should be considered in assessing the results of our audit.

Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit this information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the basic financial statements. The supplemental section listed in the Table of Contents is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information has been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

The Introductory and Statistical Sections have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly we express no opinion on them.

October 23, 2009

A Professional Corporation



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Management's Discussion and Analysis

Management's Discussion and Analysis (MD&A) provides an overview of the City of Palo Alto's financial performance for the fiscal year ended June 30, 2009. To obtain a complete understanding of the City's financial condition, this document should be read in conjunction with the accompanying Transmittal Letter and Basic Financial Statements.

OVERVIEW OF THE COMPREHENSIVE ANNUAL FINANCIAL REPORT

The CAFR is presented in six sections:

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

Basic Financial Statements

The Basic Financial Statements contain the Citywide Financial Statements and the Fund Financial Statements. These statements provide long and short-term views of the City's financial activities and financial position.

The Citywide Financial Statements provide a longer-term view of the City's activities as a whole. They include the Statement of Net Assets and the Statement of Activities. The Statement of Net Assets includes the City's capital assets and long-term liabilities on a full accrual basis of accounting similar to that used by private-sector companies. The Statement of Activities provides information about the City's revenues and expenses on a full accrual basis, with an emphasis on measuring net revenues or expenses for each of the City's programs. The Statement of Activities explains in detail the change in net assets for the year. The amounts in the Statement of Net Assets and the Statement of Activities are separated into Governmental and Business-type Activities in order to provide a summary of these activities for the City.

The Fund Financial Statements display the City's operations in more detail than the Citywide statements. Their focus is primarily on the short-term activities of the City's General Fund and



other major funds such as the Capital Projects Fund, Water Services Fund, Electric Services Fund, Fiber Optic Fund, Gas Services Fund, Wastewater Collection Fund, Wastewater Treatment Fund, Refuse Services Fund and Storm Drainage Services Fund.

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

Together, all these statements are called the Basic Financial Statements.

Citywide Financial Statements

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

The City's governmental activities also include the activities of the Palo Alto Public Improvement Corporation and the Redevelopment Agency which are separate legal entities financially accountable to the City.

Business-type Activities - All of the City's enterprise activities are reported as Business-type Activities, including Water, Electric, Fiber Optics, Gas, Wastewater Collection, Wastewater Treatment, Refuse and Storm Drainage. Unlike governmental services, these services are supported by charges paid by customers based on services used.

Citywide Financial Statements are prepared on the accrual basis of accounting, which means they measure the flow of all economic resources for the City as a whole.

Fund Financial Statements

The Fund Financial Statements provide detailed information about each of the City's most significant funds, called Major Funds. The concept of Major Funds, and the determination of which are Major Funds, was established by GASB 34 and replaces the concept of combining like funds and presenting them in total. Therefore, each Major Fund is presented individually, with all Non-major Funds combined in a single column on each fund statement. Subordinate schedules display these Non-major Funds in more detail. Major Funds present the major activities of the City for the year. The General Fund is always considered a Major Fund, but other funds may change from year to year as a result of changes in the pattern of City activities.

Fund Financial Statements include Governmental, Enterprise and Internal Service Funds.

Governmental Fund financial statements are prepared on the modified accrual basis of accounting, which means they measure only current financial resources and uses. Capital assets and other long-lived assets, along with long-term liabilities, are presented only in the Citywide Financial



Statements. In Fiscal Year (FY) 2009, the City had two Major Governmental Funds, the General Fund and the Capital Projects Fund.

Enterprise and Internal Service Fund financial statements are prepared on the full accrual basis of accounting, similar to that used by private-sector companies. These statements, as in the past include all their assets and liabilities, current and long-term.

Since the City’s Internal Service Funds provide goods and services exclusively to the City’s Governmental and Business-type Activities, their activities are only reported in total at the Fund level. Internal Service Funds, such as Printing and Mailing services, cannot be considered Major Funds because their revenues are derived from other City Funds. Revenues between Funds are eliminated in the Citywide Financial Statements and any related profits or losses in Internal Service Funds are returned to the activities in which they were created, along with any residual net assets of the Internal Service Funds.

Budget vs. Actual financial comparisons information is presented only for the General Fund and all Major Special Revenue Funds.

Fiduciary Statements

The City is the fiduciary agent for certain assessment districts, holding amounts collected from property owners which await transfer to these Districts’ bond trustees. The City’s fiduciary activities are reported in the separate Statements of Fiduciary Net Assets and the Agency Funds Statement of Changes in Assets and Liabilities. These activities are excluded from the City’s other financial statements because the City cannot utilize these assets to finance its own operations.

FINANCIAL HIGHLIGHTS

Economic Background

The local and State economies were under considerable stress in FY 2009 and continue to show duress in FY 2010. Unemployment rates currently register at 6.4 and 12.9 percent, respectively. The effects of high unemployment, burdensome consumer debt, declining household wealth, stagnant incomes, low consumer confidence, and tight credit market conditions have resulted in lower, economically sensitive revenues.

Sales, transient occupancy, and documentary transfer taxes dropped considerably in FY 2009 compared to the prior year. Cumulatively, they declined by 15.8 percent or \$5.7 million. While property taxes were strong in FY 2009, they are not expected to increase significantly in FY 2010. To solve its severe budget crisis, the State of California will take away \$2.4 million in local property taxes in FY 2010. These monies are expected to be repaid at the end of 3 years, but this “borrowing” will exert additional pressure on City finances.

Revenues are expected to remain weak through at least the first half of FY 2010. Although economists have tentatively declared that the national economy has “bottomed out,” they expect a lengthy and slow recovery and one that could be “jobless.” Such a projection hits local jurisdictions heavily since they are dependent on consumer spending for sales and other taxes. To date there is no evidence that the local economy is improving and that revenues have begun an upward trend.

As in the past, the City continues to face and address a number of expense and revenue challenges. These include funding existing and new infrastructure and operational needs; warding off strong competition from neighboring city retail outlets for sales tax dollars; preventing the potential exodus of key sales tax generators; and keeping pace with rising medical and retirement costs. The City has been and continues to be proactive in dealing with these challenges. In FY 2009, the budget was reduced to bring expenses into alignment with incoming revenues. For FY 2010, the City's budget strategy was to mix service reductions, employee salary and benefit concessions, expense deferrals, and one-time cuts to address an expected \$10.0 million deficit.

The City is proud to report that its underlying Triple A General Fund credit rating has been reaffirmed by Standard and Poor's (S & P) and that S & P has recently raised a number of Utility Revenue Bonds from AA- to AAA. Although the City does face a variety of financial challenges, the S & P findings show solid confidence in the City's financial position and stewardship.

Citywide

- The City's total net assets increased to \$1,105.5 million, a \$5.6 million increase. Governmental activities had an increase of \$10.0 million and are discussed on page 6. Business-type activities had a decrease of \$4.4 million and are discussed on page 11.
- The City's total capital assets, net of related debt, increased to \$741.0 million, a \$27.1 million increase. Governmental activities had an increase of \$13.1 million, primarily for roadway network and recreation and open space network. Business-type activities had an increase of \$14.0 million primarily from the storm drain pipeline network and utility transmission, distribution and treatment system.
- The City's total restricted net assets increased to \$38.4 million, a \$9.2 million increase. This increase is for \$4.6 million of governmental capital projects and \$2.3 million for governmental special revenue programs.
- The City's total unrestricted net assets decreased to \$326.2 million, a \$30.8 million decrease. Governmental activities had a decrease of \$12.3 million and business activities had a decrease of \$18.5 million.
- Citywide revenues totaled \$418.5 million, an increase of \$16.5 million from the prior year. This total consists of \$313.2 million in program revenues and \$105.3 million in general revenues. Program revenues increased by \$22.1 million and general revenues decreased by \$5.6 million.
- Total Citywide expenses were \$413.0 million, a \$49.3 million increase.
- Citywide total assets increased to \$1,229.9 million, a \$6.5 million increase.
- Citywide capital assets increased by \$21.9 million to \$790.4 million.
- Citywide other assets decreased \$15.4 million to \$439.5 million.
- Citywide total liabilities were \$124.4 million, an increase of \$1.0 million.
- Citywide long-term debt decreased \$0.5 million to \$54.2 million.
- Citywide other liabilities were \$70.2 million, an increase of \$1.5 million.



Fund Level – Governmental Funds

- Governmental Fund balances increased to \$104.6 million, a \$0.7 million increase.
- Governmental Fund revenues decreased to \$125.6 million, a \$1.4 million decrease.
- Governmental Fund expenditures were \$142.4 million, a \$2.8 million decrease.
- General Fund revenues came in at \$113.8 million, a decrease of \$1.2 million over the prior year.
- General Fund expenditures are \$114.8 million, a decrease of \$0.6 million.
- The General Fund balance of \$43.2 million at June 30, 2009, was an increase of \$0.8 million from the prior year (refer to Performance of Governmental Funds – General Fund, Page 14).

Fund Level – Enterprise Funds

- Enterprise Fund net assets increased to \$605.5 million, a \$5.4 million increase.
- Enterprise Fund operating revenues increased to \$275.1 million, a \$23.4 million increase from prior year revenues.
- Enterprise Fund operating expenses increased to \$229.0 million, a \$13.2 million increase.

FINANCIAL PERFORMANCE

Citywide Financial Statements – Governmental Activities

The following analysis focuses on the net assets and changes in net assets of the City’s Governmental Activities, presented in the Citywide Statement of Net Assets and Statement of Activities.

GOVERNMENTAL ACTIVITIES

Net Assets at June 30

(in Millions)

	2009	2008	Increase/ (Decrease) from 2008
Cash and investments	\$141.0	\$149.9	(\$8.9)
Other assets	59.9	53.0	6.9
Capital assets	364.3	351.9	12.4
Total Assets	565.2	554.8	10.4
Long-term debt outstanding	7.6	8.4	(0.8)
Other liabilities	46.2	45.0	1.2
Total Liabilities	53.8	53.4	0.4
Net Assets:			
Invested in capital assets, net of debt	356.7	343.5	13.2
Restricted	36.6	27.4	9.2
Unrestricted	118.1	130.5	(12.4)
Total Net Assets	\$511.4	\$501.4	\$10.0

The City’s governmental total net assets increased \$10.0 million to \$511.4 million in FY 2009. This change results from the following:

- Cash and investments decreased by \$8.9 million primarily from a decrease in the Internal Service Funds cash balance.
- Other assets increased by \$6.9 million due to allocation of Internal Service Fund costs to the Enterprise Funds.
- Capital assets increased \$12.4 million primarily due to infrastructure improvements to the City’s roadway network, curbs, gutters, and sidewalks.
- Net assets invested in capital assets, net of related debt, increased \$13.2 million as the City added General Fund infrastructure assets as discussed in the Capital Assets section.

- Unrestricted net assets decreased \$12.4 million for a total of \$118.1 million; this represents current net assets available to finance subsequent year operations and other expenditures approved by City Council.

GOVERNMENTAL ACTIVITIES

Revenues for the Year ended June 30

(in Millions)

Revenues by Source	2009	2008	Increase/ (Decrease) from 2008
Program Revenues:			
Charges for services	\$30.0	\$31.9	(\$1.9)
Operating contributions & grants	3.6	4.0	(0.4)
Capital contributions & grants	3.8	1.9	1.9
Total Program Revenues	37.4	37.8	(0.4)
General Revenues:			
Property Taxes	25.4	23.1	2.3
Sales Taxes	20.1	22.6	(2.5)
Utility User's Taxes	11.0	10.3	0.7
Transient Occupancy Tax	7.1	8.0	(0.9)
Other Taxes and Fines	3.4	6.3	(2.9)
Investment Earnings	8.5	12.3	(3.8)
Rents and Miscellaneous	15.7	11.9	3.8
Total General Revenues	91.2	94.5	(3.3)
Total Revenues	\$128.6	\$132.3	(\$3.7)

Governmental Activities – Revenues

The table above shows that governmental revenues totaled \$128.6 million in FY 2009, a decrease of \$3.7 million compared to prior year revenues of \$132.3 million.

Property taxes had an increase of \$2.3 million, sales taxes decreased by \$2.5 million, the utility user’s tax rose by \$0.7 million, and transient occupancy taxes decreased by \$0.9 million. Investment earnings decreased by \$3.8 million. This is a result of a decrease in investment earnings of \$1.8 and \$1.7 million for the year-end adjustment to carrying value for investments and reflects the year-to-year change in carrying value. This mark to market value is a requirement of GASB 31.

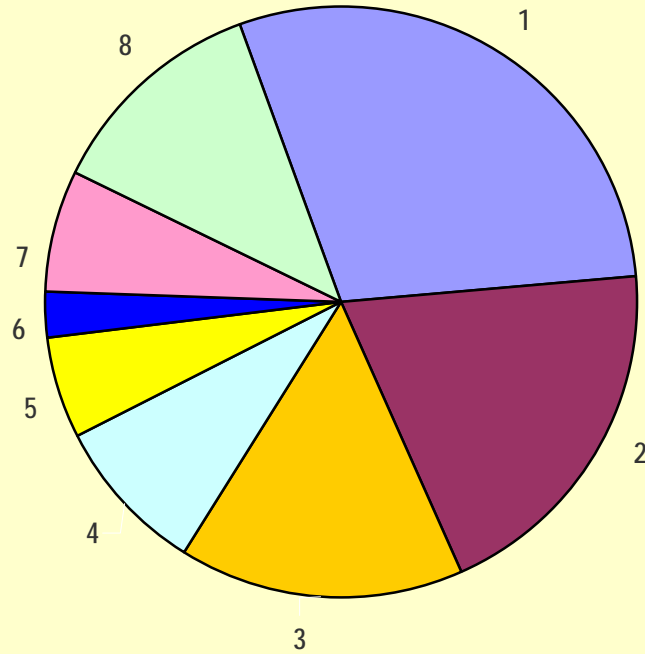
Miscellaneous revenues had an increase of \$3.8 million from the prior year. Miscellaneous revenues include the net of inter-department revenues and charges. General fund inter-department charges for transfers to the Technology Fund were \$3.5 million less than prior year.

Program revenues such as charges for services; operating grants and contributions; and capital grants and contributions are generated from or restricted to each activity. Program revenues

include contributions from the University Avenue Off-Street Parking Assessment District as well as other recurring resources.

Sources of Revenues

- 1- Program Revenues - 29%
- 2- Property Taxes - 20%
- 3- Sales Taxes - 16%
- 4- Utility User's Taxes - 8%
- 5- Transient Occupancy Tax - 5%
- 6- Other Taxes & Fines - 3%
- 7- Investment Earnings - 7%
- 8- Rents and Miscellaneous - 12%



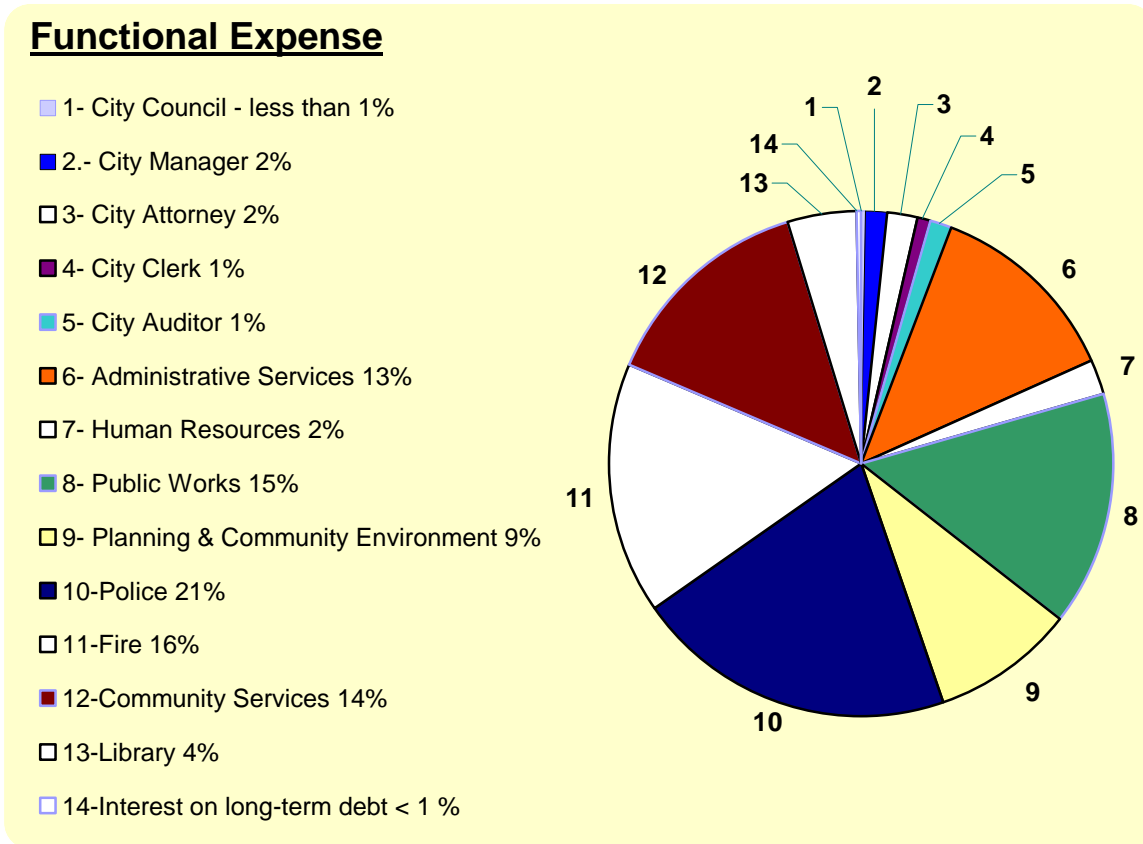
General revenues are composed of taxes and other revenues not specifically generated by or restricted to individual activities. All tax revenues, investment earnings, rents for governmental facilities, and fees for services are included in general revenues.

Governmental Activities – Expenses

The table below presents a comparison of FY 2009 and FY 2008 expenses (does not include encumbrances and reappropriations) by Governmental Activities and interest on long-term debt. Total Governmental Activities functional expense was \$142.6 million in FY 2009, an increase of \$6.9 million.

GOVERNMENTAL ACTIVITIES			
<i>Expenses for the Year ended June 30</i>			
(in Millions)			
Activities	2009	2008	Increase/ (Decrease) from 2008
City Council	\$0.4	\$0.3	\$0.1
City Manager	2.1	2.3	(0.2)
City Attorney	2.6	2.7	(0.1)
City Clerk	1.1	1.2	(0.1)
City Auditor	2.0	1.4	0.6
Administrative Services	17.8	15.5	2.3
Human Resources	3.4	2.8	0.6
Public Works	21.3	18.6	2.7
Planning and Community Environment	12.9	16.4	(3.5)
Police	29.3	27.7	1.6
Fire	23.2	22.4	0.8
Community Services	19.9	17.7	2.2
Library	6.2	6.3	(0.1)
Interest on long-term debt	0.4	0.4	0.0
Total Functional Expense	\$142.6	\$135.7	\$6.9
Increase/(Decrease) in Net Assets before Transfers	(14.0)	(3.5)	(10.5)
Transfers in	\$24.0	\$18.7	\$5.3
Change in Net Assets	\$10.0	\$15.2	(\$5.2)
Net Assets-Beginning	501.4	486.2	15.2
Net Assets-Ending	<u>\$511.4</u>	<u>\$501.4</u>	<u>\$10.0</u>

The Functional Expenses Chart below includes only current year expenses. It does not include capital outlays, which are now added to the City’s capital assets. In FY 2009, the City added \$12.4 million in capital assets. The composition of FY 2009 additions is shown in detail in the Capital Asset section of the Management’s Discussion and Analysis.



Citywide Financial Statements – Business-Type Activities

The following analysis focuses on the net assets and changes in net assets of the City’s Business-type Activities presented in the Citywide Statement of Net Assets and Statement of Activities.

BUSINESS-TYPE ACTIVITIES*Net Assets at June 30*

(in Millions)

	<u>2009</u>	<u>2008</u>	<u>Increase/ (Decrease) from 2008</u>
Cash and investments	\$205.2	\$218.6	(\$13.4)
Other assets	33.4	33.3	0.1
Capital assets	426.1	416.6	9.5
Total Assets	<u>664.7</u>	<u>668.5</u>	<u>(3.8)</u>
Long-term debt outstanding	46.6	46.4	0.2
Other liabilities	24.0	23.6	0.4
Total Liabilities	<u>70.6</u>	<u>70.0</u>	<u>0.6</u>
Net assets:			
Invested in capital assets, net of debt	384.4	370.3	14.1
Restricted	1.7	1.7	0.0
Unrestricted	208.0	226.5	(18.5)
Total Net Assets	<u>\$594.1</u>	<u>\$598.5</u>	<u>(\$4.4)</u>

The City's Business-type total net assets decreased \$4.4 million to \$594.1 million in FY 2009.

- Cash and investments decreased \$13.4 million as a result of \$8.7 million increase in the Electric Fund retail purchase of utilities and a \$2.5 million increase in Surplus Energy costs. (Further detail may be found in Note 16 to the financial statements.)
- Capital assets increased \$9.5 million to \$426.1 million in FY 2009. This increase is primarily a result of water, electric and gas infrastructure improvements totaling \$9.4 million.
- Net assets invested in capital assets net of related debt increased \$14.1 million to \$384.4 million. The increase was mostly due to \$4.5 million of improvements in the Gas Fund and \$4.8 million in Water Fund improvements.
- Unrestricted net assets of \$208.0 million, a decrease of \$18.5 million from the prior year, represent liquid assets available to finance day-to-day operations and other expenditures approved by the City Council. This amount includes Council designated reserves such as the rate stabilization reserves of \$59.3 million, the Calaveras reserve for stranded costs of \$64.5 million and the emergency plant replacement reserve of \$7.2 million.

BUSINESS-TYPE ACTIVITIES

Revenues for the Year ended June 30

(in Millions)

Revenues by Source	2009	2008	Increase/ (Decrease) from 2008
Program Revenues:			
Water	\$27.1	\$27.5	(\$0.4)
Electric	119.3	103.8	15.5
Fiber Optics *	3.3	0.0	3.3
Gas	47.8	49.0	(1.2)
Wastewater Collection	14.5	15.7	(1.2)
Wastewater Treatment	28.5	22.9	5.6
Refuse	29.1	28.8	0.3
Storm Drainage	5.5	5.5	0.0
External Services **	0.0	0.1	(0.1)
Total Program Revenues	275.1	253.3	21.8
General Revenues:			
Investment Earnings	14.1	16.4	(2.3)
Total General Revenues	14.1	16.4	(2.3)
Total Revenues	\$289.2	\$269.7	\$19.5

* Prior to FY 2009 this was reported in the Electric Fund

** Closed in FY 2009

The table above presents the revenues for each of the City's Business-type Activities or Enterprise Funds. The City operates the Water, Electric, Fiber Optics, Gas, Wastewater Collection, Wastewater Treatment, Refuse, and Storm Drainage Funds, which are Major Funds and are presented in the Basic Financial Statements.

Business-type Activity revenues totaled \$289.2 million, an increase of \$19.5 million from the prior year. Revenues were significantly affected by the following events:

- Program Revenue for the Electric Fund increased \$15.5 million primarily due a 14 percent rate increase effective July 1, 2008.
- Program Revenue for the Wastewater Treatment Fund increased \$5.6 million primarily due to \$1.8 million grant revenues and a \$3.8 million expenditure reimbursement from City of Mountain View for the Water Reclamation Project, which is a joint project between the two Cities.

- Investment earnings decreased \$2.3 million due to a decrease in interest earnings on investments for the Electric Fund of \$2.2 million.

BUSINESS-TYPE ACTIVITIES

Expenses for the Year ended June 30
(in Millions)

Activities	2009	2008	Increase/ (Decrease) from 2008
Water	\$20.3	\$18.9	\$1.4
Electric	122.3	108.0	14.3
Fiber Optics *	1.3	0.0	1.3
Gas	34.6	37.2	(2.6)
Wastewater Collection	14.9	12.0	2.9
Wastewater Treatment	36.9	18.9	18.0
Refuse	37.2	28.8	8.4
Storm Drainage	2.9	3.2	(0.3)
External Services **	0.0	1.0	(1.0)
Total Functional Expense	\$270.4	\$228.0	\$42.4
Increase in Net Assets before Transfers/Special Items	19.5	41.7	(22.2)
Transfers out	24.0	18.7	5.3
Total Transfers/Special Items	\$24.0	\$18.7	\$5.3
Change in Net Assets	(\$4.5)	\$23.0	(\$27.5)
Net Assets-Beginning	598.6	575.5	23.1
Net Assets-Ending	\$594.1	\$598.5	(\$4.4)

* Prior to FY 2009 this was reported in the Electric Fund

** Closed in FY 2009

The table above presents a comparison of the FY 2009 and FY 2008 expenses for the City's Business-type Activities. Encumbrances and reappropriations are not included.

Business-type Activity expenses, transfers and special items increased \$47.7 million for a total of \$294.4 million. Changes to expenses were significantly affected by the following events:

- Functional Expense for the Electric Fund increased \$14.3 million primarily due to an \$8.7 million increase in the retail purchase of utilities and a \$2.5 million increase in Surplus Energy costs. Both costs are associated with the City's need to purchase high-cost power during the year due to unfavorable weather conditions. (Further detail may be found in Note 16 to the financial statements.)



Management Discussion and Analysis

- Functional Expense for the Gas Fund decreased \$2.6 million, primarily due to a \$2.1 million decrease in retail purchase of utilities. (Further detail may be found in Note 16 to the financial statements.)
- Functional Expense for the Wastewater Treatment Fund increased \$17.9 million primarily due to an increase of non-operating charges to \$15.6 million. This is primarily the recognition of \$15.2 million for the City of Mountain View asset portion of the Water Reclamation Project. This expense is offset by receivables due from the City of Mountain View of \$3.8 million, annual loan payments due of \$250 thousand for twenty years and grant revenues received in prior year and current year. (Further detail may be found in Note 7 to the financial statements.)
- Functional Expense for the Refuse Fund increased \$8.4 million primarily due to a \$4.7 million increase for operations and maintenance charges (Further detail may be found in Note 9 to the financial statements.)

FUND FINANCIAL STATEMENTS

Performance of Governmental Funds

At June 30, 2009, the City's Governmental Funds reported combined fund balances of \$104.6 million, an increase of \$0.7 million or 0.7 percent compared with the prior year.

Governmental Fund revenues and other financing sources increased \$5.1 million for a total of \$165.5 million. Revenues and other financing sources in the General Fund decreased \$0.7 million; Capital Project Fund increased \$2.8 million and Non-major Fund revenues and other financing sources increased by \$3.0 million.

Governmental Fund expenditures and other uses increased \$2.7 million this year to \$164.8 million. General Fund expenditures and other uses increased \$1.5 million, Capital Projects Fund expenditures increased by \$2.3 million; and Non-major Fund expenditures and other uses decreased by \$1.1 million.

General Fund – The General Fund ended the year with a \$0.8 million increase for a total of \$43.2 million fund balance, compared to \$3.0 million increase in the prior year.

Palo Alto's General Fund revenues totaled \$113.8 million in FY 2009. This represents a decrease of \$1.2 million or 1.0 percent compared to the prior year.

Property Taxes increased by \$2.3 million or 10 percent from FY 2008 to FY 2009 for a total of \$25.4 million. The \$25.4 million is \$1.9 million greater than the adopted budget and \$0.3 million greater than the adjusted budget. Though Palo Alto assessed values remained healthy for FY 2009, the growth in the assessed values is expected to moderate.

Sales taxes declined by \$2.5 million or 11.2 percent over FY 2008 levels for a total of \$20.1 million, which is \$2.3 million less than the adopted budget and \$74 thousand greater than the adjusted



budget. Retrenchment in consumer spending is the principal reason for sales tax declines. New automobile, department store, and miscellaneous retails sales have been especially weak.

The City's Utility Users Tax (UUT), which is 5 percent, is levied on telephone, water, electricity, and gas usage. This revenue source rose by \$745 thousand or 7.3 percent over the prior year for a total of \$11.0 million, and is \$247 thousand greater than the adopted budget. This increase is primarily due to utility rate increases over the prior year to cover commodity costs and strengthen reserve levels.

Transient Occupancy Tax (TOT) receipts were \$7.1 million in FY 2009, an \$865 thousand or 10.8 percent decline over the prior year. The \$7.1 million is \$1.3 million less than the adopted budget and \$139 thousand less than the adjusted budget. Average occupancy and room rates decreased over the prior year from 75.5 percent to 65.2 percent and from \$149 to \$146, respectively. This economically sensitive revenue source is anticipated to further soften in FY 2010 due to the economic downturn.

Other Taxes, Fines & Penalties totaled \$5.4 million in FY 2009, a decrease of \$2.4 million from the prior year, and \$3.4 million less than the adopted budget and \$376 thousand less than the adjusted budget. After two years of solid results, the Documentary Transfer Tax came in at \$3.1 million, a decline of 42.5 percent from the prior year. Actual revenue results were slightly above the FY 2009 adjusted budget. This revenue source is highly dependent on sales volume and the mix of commercial and residential sales. Commercial transactions decreased due to low occupancy rates and residential transactions were minimal due to sellers holding onto their homes during a period of market softness. In addition, credit conditions were abysmal due to the collapsing credit markets for commercial and jumbo home loans. Further softening in the transfer tax is anticipated in the first half of FY 2010. Parking violations decreased by \$0.3 million compared to the prior year.

Charges for Services were \$19.8 million in FY 2009, an increase of \$0.5 million from the prior year and a decrease of \$1.1 million from the adopted budget

Permits and Licenses were \$4.3 million in FY 2009, a decrease of \$0.5 million from the prior year and a decrease of \$0.9 million from the adjusted budget and a decrease of \$1.5 million from the adopted budget. The decrease is mainly due to decreases in new construction building permits.

Other Revenues totaled \$6.0 million in FY 2009, a decrease of \$1.8 million from the prior year. This decrease is primarily due to a \$1.0 million decrease in the year-end adjustment to the carrying value of investments. Prior year included \$0.7 million due to the sale of the Eyerly condominium property. The \$6.0 million is an increase of \$1.8 million from the adjusted budget and a decrease of \$2.1 million from the adopted budget. The budget does not include the year-end adjustment to the carrying value of investments.

At June 30, 2009, the General Fund Balance totaled \$43.2 million. This represents 37.6 percent of direct General Fund expenditures providing a buffer against unexpected financial events. Of this, \$10.1 million is reserved and \$33.1 million is unreserved. Included in the reserved amount is \$1.8 million for the prepayment of Storm Drain rate increases over a three-year period. A substantial portion of the unreserved balance amount is designated by the Council for budget stabilization, \$24.7 million at year-end. The designation for equity transfer stabilization, established in FY 2002,



Management Discussion and Analysis

amounted to \$3.6 million at year-end. This reserve would be utilized in the event that the Electric or Gas Funds were not in a position to make their required equity transfer to the General Fund.

General Fund expenditures and other uses totaled \$130.6 million, an increase of \$1.5 million from the prior year. Transfers out had an increase of \$2.5 million to the adopted budget for a final budget of \$15.8 million and actual expenditures of \$15.8 million. Transfers out had an increase over prior year of \$2.2 million. These increases were primarily due to an increase of \$3.4 million for the Public Safety Building project, offset by \$1.0 million decrease for funds returned to infrastructure reserves.

Due to the effects of the current recession on key City revenues, expenditure reductions were made at mid-year and are reflected in the adjusted budget. Although the expenditure reductions include salary and non-salary expenditures, the majority relate to savings from open positions and a hiring freeze.

The Planning department had an increase in expenditures and encumbrances of \$0.3 million from the prior year for a total of \$10.5 million, which was \$138 thousand less than the adjusted budget.

The adopted budget for Administrative departments was increased by \$0.8 million for a final budget of \$18.3 million. Administrative departments had a decrease of \$1.4 million from prior year for a total of \$17.7 million.

Public Works department had an increase in expenditures and encumbrances from prior year of \$0.2 million, for a total of \$13.5 million. Expenditures and encumbrances for the Public Works department were \$370 thousand less than adopted budget and \$269 thousand less than adjusted budget.

Community Services department expenditures and encumbrances were \$0.2 million less than the prior year for a total of \$21.7 million. The \$21.7 million is \$77 thousand greater than adopted budget but \$241 thousand less than the adjusted budget.

The Police department had a decrease of \$0.8 million to the adopted budget for a final budget of \$29.1 million. The Police department expenditures and encumbrances totaled \$28.5 million, which is \$1.3 million less than prior year, and \$1.4 million less than the adopted budget and \$613 thousand less than final budget.

Fire department had a decrease of \$0.5 million from prior year for expenditures and encumbrances, for a total of \$23.8 million. The \$23.8 million is \$495 thousand less than the adopted budget and \$447 thousand less than the adjusted budget.

The Library department expenditures and encumbrances totaled \$6.5 million and were \$0.5 million less than prior year. The \$6.5 million is \$105 thousand less than the adjusted budget.

Capital Projects Fund – Capital Projects Fund expenditures and other uses were \$21.5 million in FY2009, which is a decrease of \$0.1 thousand from the prior year. This level of expenditure is consistent with the City's effort to rehabilitate and maintain its existing infrastructure.

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

Performance of Enterprise Funds

At June 30, 2009, the City's Enterprise Funds reported total net assets of \$605.5 million, an increase of \$5.4 million or 0.9 percent compared with the prior year. The Water and Gas Funds net assets increased \$4.9 million and \$10.5 million, respectively. The Electric Fund net assets decreased \$7.2 million (for comparison purposes FY 2008 net assets are reduced by Fiber Optics portion). These assets constitute 75.2 percent of the Enterprise Funds' total net assets. Unrestricted net assets for these three funds totaled \$182.4 million, a 3.4 percent decrease from FY 2008.

Water Fund - The Water Fund ended the year with net income of \$4.9 million, compared to \$7.5 million in the prior year, a \$2.6 million decrease. The decrease in net income is primarily due to an increase in operating expenses of \$1.0 million and an increase in other financing uses of \$1.5 million.

Electric Fund - Operating revenues increased to \$119.3 million, a \$15.5 million increase from the prior year. The Electric Fund ended the year with a net loss of \$7.2 million compared to a net loss of \$4.5 million in the prior year. The net loss is due to an \$8.7 million increase in the purchase of utilities and \$2.5 million increase in surplus energy costs caused by the unfavorable weather conditions.

Fiber Optics Fund - The Fiber Optics Fund ended the year with a net income of \$2.4 million. Prior to FY 2009, this activity was reported as part of the Electric Fund.

Gas Fund - The Gas Fund ended the year with a net income of \$10.5 million, compared to a \$9.3 million in prior year, an increase of \$1.2 million.

Wastewater Collection Fund - Operating revenues decreased to \$14.4 million, a \$0.6 million decrease from prior year. Operating expenses decreased to \$11.0 million, a \$0.7 million decrease from 2008. The Wastewater Collection Fund ended the year with a net loss of \$62 thousand compared to prior year net income of \$4.3 million. The loss is primarily due to a \$3.7 million loss on retirement of assets: 14 thousand 4" plastic polyethylene lateral pipes.

Wastewater Treatment Fund - Revenues increased in FY 2009 by \$5.6 million due to \$1.8 million in grant revenues and a \$3.8 million expenditure reimbursement from City of Mountain View for the Water Reclamation Project, which is a joint project between the two Cities. The Wastewater Treatment Fund ended the year with a net loss of \$3.2 million, compared to a net income of \$5.0 million in FY 2008.

Refuse Fund - Refuse Fund revenues increased to \$29.1 million in FY 2009, compared to \$28.8 million in prior year. Operating expenses increased \$5.0 million to \$33.5 million in FY 2009 due to \$3.1 million increase of the landfill's updated forecasted closure costs. The Refuse Fund ended the year with a net loss of \$5.4 million, compared to a \$0.2 million net income in FY 2008.

Storm Drainage Fund – The Storm Drainage Fund ended the year with a net income of \$3.4 million, compared to \$2.7 million in the prior year. Operating expenses decreased to \$1.6 million, a \$0.9 million decrease from FY 2008.

CAPITAL ASSETS

GASB 34 requires the City to record all its capital assets, including infrastructure. Infrastructure includes roads, bridges, signals and similar assets used by the entire population. Although GASB 34 allowed the City four years to record all its infrastructure assets in its financial statements, as of June 30, 2002, all assets were included in the financial statements. The table below shows capital assets and the amount of accumulated depreciation for these assets for Governmental and Business-type Activities (further detail may be found in Note 6 to the financial statements).

CAPITAL ASSETS AT JUNE 30			
(in Millions)			
	<u>2009</u>	<u>2008</u>	<u>Increase/ (Decrease) from 2008</u>
Governmental Activities			
<i>Capital Assets</i>			
Land and improvements	\$75.5	\$73.1	\$2.4
Street trees	15.1	15.1	0.0
Construction in progress	33.5	37.3	(3.8)
Buildings and improvements	103.2	99.7	3.5
Equipment	7.9	7.8	0.1
Roadway network	255.2	243.7	11.5
Recreation & open space network	16.2	13.9	2.3
Less accumulated depreciation	(165.0)	(156.5)	(8.5)
<i>Internal Service Fund Assets</i>			
Construction in progress	3.1	7.2	(4.1)
Equipment	45.9	35.3	10.6
Less accumulated depreciation	(26.3)	(24.7)	(1.6)
Total Governmental	\$364.3	\$351.9	\$12.4
Business-type Activities			
Land	\$2.0	\$2.0	\$0.0
Construction in progress	103.0	130.0	(27.0)
Buildings and improvements	30.7	19.6	11.1
Transmission, Distribution & Treatment Systems	511.5	481.4	30.1
Less accumulated depreciation	(221.1)	(216.4)	(4.7)
Total Business-type	\$426.1	\$416.6	\$9.5



Governmental Activities capital assets net of depreciation increased by \$12.4 million compared to FY 2008. This increase was primarily due to a \$3.5 million increase for buildings and improvements, \$11.5 million for roadway network, and \$2.4 million for land and improvements.

Work on the City's infrastructure is the continuation of a ten-year plan, totaling \$100 million, developed to address the needs of the City's aging infrastructure. The ten-year plan included an assessment and prioritization of work needed on buildings, facilities, streets, sidewalks, medians, bikeways, parks and open space. Current key infrastructure projects include improvements to streets and sidewalks, refurbishing of park playgrounds and irrigation systems, upgrading athletic fields, open space and trail improvements, and facility renovations.

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

DEBT ADMINISTRATION

Each of the City's debt issues is discussed in detail in Notes 7 and 8 to the financial statements. At June 30, 2009, the City's debt was comprised of the following:

LONG-TERM DEBT AT JUNE 30

(in Millions)

	2009	2008	Increase/ (Decrease) from 2008
Governmental Activity Debt:			
General Long Term Obligations:			
1998 Golf Course Certificates of Participation	\$4.4	\$4.8	(\$0.4)
2002A Civic Center Refinancing Certificates of Participation	1.2	1.5	(0.3)
2002B Downtown Parking Improvements Certificates of Participation	2.0	2.1	(0.1)
Total Governmental Activity Debt	\$7.6	\$8.4	(\$0.8)
Business-type Activity Debt:			
Enterprise Long Term Obligations:			
Utility Revenue Bonds			
1995 Series A	\$5.3	\$5.6	(\$0.3)
1999 Refunding	13.7	14.2	(0.5)
2002 Series A	19.7	20.5	(0.8)
Energy Tax Credit Bonds			
2007 Series A	1.3	1.4	(0.1)
State Water Resources Loan			
2007	9.0	5.6	3.4
Less: unamortized discount/issuance cost	(2.5)	(1.0)	(1.5)
Total Business-type Activity	\$46.5	\$46.3	\$0.2

The City did not issue any new debt in FY 2009. As stated in the Statistical Section of the CAFR, the combined direct debt ratio to assessed valuation for the General Fund is a low 0.04 percent compared to the allowable, legal debt margin of 15 percent.



SPECIAL ASSESSMENT DISTRICT DEBT

Special assessment districts throughout different parts of the City have also issued debt to finance infrastructure and facilities construction exclusively in their districts. At June 30, 2009, the City had no special assessment district debt with City commitment outstanding. The final payment of \$0.1 million for the California Avenue Parking Special Assessment District was made in September 2007.

ECONOMIC OUTLOOK

The economy of the City is discussed in the accompanying Transmittal Letter and in this Discussion and Analysis.

CONTACTING THE CITY'S FINANCIAL MANAGEMENT

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



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Citywide Statement of Net Assets and Statement of Activities.....

The Citywide Statement of Net Assets and the Statement of Activities summarize all of the City’s financial activities and financial position. They are prepared on the same basis as is used by most businesses, which means they include all the City’s assets and all its liabilities, as well as all its revenues and expenses. This is known as the full accrual basis – the effect of all the City’s transactions is taken into account, regardless of whether or when cash changes hands. All material internal transactions between City funds have been eliminated.

The Statement of Net Assets reports the difference between the City’s total assets and the City’s total liabilities, including all the City’s capital assets and all its long-term debt. The Statement of Net Assets focuses the reader on the composition of the City’s net assets, by subtracting total liabilities from total assets.

The Statement of Net Assets summarizes the financial position of all the City’s Governmental Activities in a single column, and the financial position of all the City’s Business-type Activities in a single column; these columns are followed by a Total column that presents the financial position of the entire City.

The City’s Governmental and Business-type Activities include the activities of its General Fund, along with all its Special Revenue, Capital Projects, Debt Service Funds, and Enterprise Funds. Since the City’s Internal Service Funds service these Funds, their activities are consolidated with Governmental and Business-type Activities, after eliminating inter-fund transactions and balances.

The Statement of Activities reports increases and decreases in the City’s net assets. It is also prepared on the full accrual basis, which means it includes all the City’s revenues and all its expenses, regardless of when cash changes hands. This differs from the “modified accrual” basis used in the Fund financial statements, which reflect only current assets, current liabilities, available revenues and measurable expenditures.

The format of the Statement of Activities presents the City’s expenses first, listed by program, and follows these with the expenses of its Business-type Activities. Program revenues – that is, revenues which are generated directly by these programs – are then deducted from program expenses to arrive at the net expense of each governmental and Business-type program. The City’s general revenues are then listed in the Governmental Activities or Business-type Activities column, as appropriate, and the Change in Net Assets is computed and reconciled with the Statement of Net Assets.

These Statements include the financial activities of the City Public Improvement Corporation and Redevelopment Agency, which are legally separate component units of the City because they are controlled by the City, which is financially accountable for its activities.

These financial statements along with the fund financial statements and footnotes are called *Basic Financial Statements*.



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City of Palo Alto - Statement of Net Assets

June 30, 2009

(In thousands of dollars)

	Governmental Activities	Business-type Activities	Totals
ASSETS			
Cash and investments (Note 3):			
Available for operations	\$139,057	\$203,264	\$342,321
Cash and investments with fiscal agent	1,955	1,972	3,927
Receivables:			
Accounts and intergovernmental	5,646	43,476	49,122
Interest receivable	1,512	2,375	3,887
Notes and loans receivable (Note 5)	8,479		8,479
Internal balances (Note 4)	12,497	(12,497)	
Assets in excess of OPEB obligation (Note 12)	26,352		26,352
Inventory of materials and supplies and prepaids	5,415		5,415
Capital assets (Note 6):			
Nondepreciable	127,099	105,042	232,141
Depreciable, net of depreciation	237,163	321,086	558,249
Total assets	<u>565,175</u>	<u>664,718</u>	<u>1,229,893</u>
LIABILITIES			
Accounts payable and accrued liabilities	9,231	12,342	21,573
Accrued salaries and benefits	2,052	750	2,802
Unearned revenue	759		759
Accrued compensated absences (Note 1):			
Due within one year	4,054		4,054
Due in more than one year	8,614		8,614
Claims payable (Note 14):			
Due within one year	5,855		5,855
Due in more than one year	15,583		15,583
Accrued landfill closure liability (Note 9):			
Due in more than one year		10,991	10,991
Long-term debt (Note 7):			
Due within one year	840	2,205	3,045
Due in more than one year	6,765	44,360	51,125
Total liabilities	<u>53,753</u>	<u>70,648</u>	<u>124,401</u>
NET ASSETS (Note 10)			
Invested in capital assets, net of related debt	<u>356,657</u>	<u>384,313</u>	<u>740,970</u>
Restricted for:			
Special revenue programs	23,973		23,973
Capital projects	11,247		11,247
Debt service	1,412	1,732	3,144
Total Restricted	<u>36,632</u>	<u>1,732</u>	<u>38,364</u>
Unrestricted net assets	<u>118,133</u>	<u>208,025</u>	<u>326,158</u>
Total net assets	<u>\$511,422</u>	<u>\$594,070</u>	<u>\$1,105,492</u>

See accompanying notes to financial statements

City of Palo Alto - Statement of Activities
For the Year Ended June 30, 2009
(In thousands of dollars)

Functions/Programs	Total Expenses	Program Revenues			Net (Expense) Revenue and Change in Net Assets		Total
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	Governmental Activities	Business-type Activities	
Governmental Activities:							
City Council	\$394				(\$394)		(\$394)
City Manager	2,085				(2,085)		(2,085)
City Attorney	2,575	\$12			(2,563)		(2,563)
City Clerk	1,098				(1,098)		(1,098)
City Auditor	2,053				(2,053)		(2,053)
Administrative Services	17,784	726			(17,058)		(17,058)
Human Resources	3,448				(3,448)		(3,448)
Public Works	21,270	1,169	\$1,222	\$3,730	(15,149)		(15,149)
Planning and Community Environment	12,940	4,704	2,037	80	(6,119)		(6,119)
Police	29,288	3,947	185		(25,156)		(25,156)
Fire	23,199	10,723			(12,476)		(12,476)
Community Services	19,862	8,522	49		(11,291)		(11,291)
Library	6,244	177	106		(5,961)		(5,961)
Interest on long-term debt	404				(404)		(404)
Total Governmental Activities	142,644	29,980	3,599	3,810	(105,255)		(105,255)
Business-type Activities:							
Water	20,271	27,120		523		\$7,372	7,372
Electric	122,268	119,320				(2,948)	(2,948)
Fiber Optics	1,284	3,336				2,052	2,052
Gas	34,603	47,838		1		13,236	13,236
Wastewater Collection	14,875	14,486		115		(274)	(274)
Wastewater Treatment	36,896	28,425				(8,471)	(8,471)
Refuse	37,217	29,101				(8,116)	(8,116)
Storm Drainage	2,943	5,505				2,562	2,562
Total Business-type Activities	270,357	275,131		639		5,413	5,413
Total	\$413,001	\$305,111	\$3,599	\$4,449	(105,255)	5,413	(99,842)
General revenues:							
Taxes:							
Property taxes					25,432		25,432
Sales taxes					20,089		20,089
Utility user's taxes					11,030		11,030
Transient occupancy tax					7,111		7,111
Transfer and other taxes					3,364		3,364
Investment earnings					8,525	14,103	22,628
Miscellaneous					15,682		15,682
Transfers (Note 4)					24,020	(24,020)	
Total general revenues and transfers					115,253	(9,917)	105,336
Change in Net Assets					9,998	(4,504)	5,494
Net Assets-Beginning					501,424	598,574	1,099,998
Net Assets-Ending					\$511,422	\$594,070	\$1,105,492

See accompanying notes to financial statements



Fund Financial Statements.....

Introduction

The Fund Financial Statements are presented by individual major funds, while non-major funds are combined in a single column. Major funds are defined generally as having significant activities or balances in the current year.

Major Governmental Funds

The funds described below were determined to be Major Funds by the City in fiscal year 2009. Individual non-major funds may be found in the Supplemental section.

General Fund

The General Fund is used for all the general revenues of the City not specifically levied or collected for other City funds, and related expenditures.

Capital Projects Fund

The Capital Projects Fund is utilized to account for resources used for the acquisition and construction of capital facilities by the City, with the exception of those assets financed by proprietary funds.



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City of Palo Alto - Governmental Funds

Balance Sheet - June 30, 2009

(In thousands of dollars)

	General	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
ASSETS				
Cash and investments (Note 3):				
Available for operations	\$37,645	\$36,262	\$15,818	\$89,725
Cash and investments with fiscal agent		591	1,364	1,955
Receivables:				
Accounts and intergovernmental	4,980	312	326	5,618
Interest receivable	736		186	922
Notes and loans receivable (Note 5)	428		8,051	8,479
Interfund receivables and advances (Note 4)	1,210			1,210
Prepaid items	1,775			1,775
Inventory of materials and supplies	3,173			3,173
Total Assets	<u>\$49,947</u>	<u>\$37,165</u>	<u>\$25,745</u>	<u>\$112,857</u>
LIABILITIES				
Accounts payable and accrued liabilities	\$4,427	\$1,119	\$250	\$5,796
Accrued salaries and benefits	1,537	39		1,576
Interfund payable and advances (Note 4)			110	110
Deferred revenue	759			759
Total Liabilities	<u>6,723</u>	<u>1,158</u>	<u>360</u>	<u>8,241</u>
FUND BALANCES				
Reserved for (Note 10):				
Encumbrances	3,659	11,247	81	14,987
Notes and loans	428		8,051	8,479
Interfund advances	1,100			1,100
Prepaid items	1,775			1,775
Inventory of materials and supplies	3,173			3,173
Debt service			1,412	1,412
Unreserved, designated for:				
General Fund				
Unrealized gain on investment	2,441			2,441
Equity transfer stabilization	3,636			3,636
Reappropriations	2,265			2,265
Budget stabilization	24,747			24,747
Capital Project Fund				
Reappropriations		17,744		17,744
Infrastructure		7,016		7,016
Special Revenue Funds				
Unrealized gain on investment			541	541
Unreserved, undesignated, reported in:				
Special Revenue Funds			13,992	13,992
Permanent Fund			1,308	1,308
Total Fund Balances	<u>43,224</u>	<u>36,007</u>	<u>25,385</u>	<u>104,616</u>
Total Liabilities and Fund Balances	<u>\$49,947</u>	<u>\$37,165</u>	<u>\$25,745</u>	<u>\$112,857</u>

See accompanying notes to financial statements



City of Palo Alto - Governmental Funds
Reconciliation of Fund Balances to Governmental Activities Net Assets
June 30, 2009

(In thousands of dollars)

Governmental Fund fund balances from prior page	\$104,616
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds (Note 6)	364,262
Internal service funds are used by management to charge the costs of certain activities, such as insurance and central services and maintenance, to individual funds. The assets and liabilities of the internal service funds are included in governmental activities in the statement of net assets. (Excludes capital assets reported above and debt reported below)	50,278
Some liabilities, including bonds payable, are not due and payable in the current period and therefore are not reported in the funds	
Interest payable	(129)
Long Term debt (Note 7)	<u>(7,605)</u>
Net assets of governmental activities	<u><u>\$511,422</u></u>

See accompanying notes to financial statements

City of Palo Alto - Governmental Funds

Statement of Revenues, Expenditures and

Changes in Fund Balance - For the Year Ended June 30, 2009

(In thousands of dollars)

	General	Capital Projects Fund	Other Governmental Funds	Total Governmental Funds
REVENUES				
Property taxes	\$25,432			\$25,432
Special assessments			\$96	96
Sales taxes	20,089			20,089
Utility users' tax	11,030			11,030
Transient occupancy tax	7,111			7,111
Other taxes and fines	5,453		1,153	6,606
Charges for services	19,769		68	19,837
From other agencies	277	\$2,987	2,720	5,984
Permits and licenses	3,825		208	4,033
Investment earnings	3,433	1,009	1,085	5,527
Rental income	13,646		10	13,656
Other revenue	3,782	94	2,347	6,223
Total Revenues	<u>113,847</u>	<u>4,090</u>	<u>7,687</u>	<u>125,624</u>
EXPENDITURES				
Current operations:				
City Council	278			278
City Manager	1,922			1,922
City Attorney	2,464			2,464
City Clerk	1,096			1,096
City Auditor	804			804
Administrative Services	6,848			6,848
Human Resources	2,590			2,590
Public Works	10,064			10,064
Planning and Community Environment	9,509		953	10,462
Police	26,988		65	27,053
Fire	21,904			21,904
Community Services	17,451			17,451
Library	5,985			5,985
Non-Departmental	6,923		3,842	10,765
Capital outlay		21,485		21,485
Debt service:				
Principal payments			800	800
Interest and fiscal fees			416	416
Total Expenditures	<u>114,826</u>	<u>21,485</u>	<u>6,076</u>	<u>142,387</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>(979)</u>	<u>(17,395)</u>	<u>1,611</u>	<u>(16,763)</u>
OTHER FINANCING SOURCES (USES)				
Transfers in (Note 4)	17,603	17,675	4,625	39,903
Transfers (out) (Note 4)	(15,815)	(2,551)	(4,033)	(22,399)
Total Other Financing Sources (Uses)	<u>1,788</u>	<u>15,124</u>	<u>592</u>	<u>17,504</u>
Net change in fund balances	809	(2,271)	2,203	741
Fund balances at beginning of year	<u>42,415</u>	<u>38,278</u>	<u>23,182</u>	<u>103,875</u>
Fund balances at end of year	<u>\$43,224</u>	<u>\$36,007</u>	<u>\$25,385</u>	<u>\$104,616</u>

See accompanying notes to financial statements

**City of Palo Alto - Reconciliation of the
Statement of Revenues, Expenditures and
Changes in Fund Balances of
Governmental Funds to the Statement of Activities.....
For the Year Ended June 30, 2009
(In thousands of dollars)**

Net change in fund balances-total governmental funds \$741

Amounts reported for Governmental Activities in the Statement of
Activities are different because:

Governmental Funds report capital outlays as expenditures.
However, in the Statement of Activities the cost of those assets is
allocated over their estimated useful lives and reported as
depreciation expense. The capital outlay expenditures are therefore
added back to fund balance.

The capital outlay, net of retirements, are therefore deducted from
fund balance. 15,804

Depreciation expense is deducted from fund balance
(Depreciation expense is net of Internal Service Fund depreciation
\$1,095 million which has already been allocated to serviced
funds.) (8,549)

Bond proceeds provide current financial resources to Governmental
Funds, but issuing debt increases long-term liabilities in the
Statement of Net Assets. Repayment of bond principal is an
expenditure in the Governmental Funds, but in the Statement of Net
Assets the repayment reduces long-term liabilities.

Fund balance is increased by the amount of debt repayment. 800

Some amounts reported in the Statement of Activities do not require
the use of current financial resources and therefore are not reported
as expenditures in Governmental Funds.

Interest payable 12

Internal Service Funds are used by management to charge the costs
of certain activities, such as equipment acquisition, maintenance,
and insurance to individual funds. The net revenue (expense) of all
Internal Service Funds is reported with Governmental Activities. 1,190

Change in net assets of Governmental Activities \$9,998

See accompanying notes to financial statements

City of Palo Alto - General Fund

Statement of Revenues, Expenditures and Changes in Fund Balance
Budget and Actual - For the Year Ended June 30, 2009

(In thousands of dollars)

	Budgeted Amount		Actual Amount Budgetary Basis	Variance from Final Budget
	Adopted	Adjusted		Positive (Negative)
REVENUES				
Property taxes	\$23,510	\$25,098	\$25,445	\$347
Sales taxes	22,402	20,015	20,089	74
Utility users' tax	10,783	11,024	11,030	6
Transient occupancy tax	8,424	7,250	7,111	(139)
Other taxes, fines & penalties	8,816	5,816	5,440	(376)
Charges for services	20,849	19,938	19,769	(169)
Permits and licenses	5,767	5,160	4,310	(850)
Charges to other funds	10,952	10,999	11,168	169
Rental income	13,426	13,121	13,646	525
Other revenues	3,965	4,251	6,044	1,793
Transfers in	17,677	17,677	17,602	(75)
Prior year encumbrance and reappropriations		4,460	4,460	
Total Revenues	146,571	144,809	146,114	1,305
EXPENDITURES				
Current operations:				
Administrative Departments	17,490	18,333	17,717	616
Community Services	21,600	21,918	21,677	241
Fire	24,260	24,212	23,765	447
Library	6,570	6,607	6,502	105
Planning and Community Environment	10,419	10,621	10,483	138
Police	29,831	29,077	28,464	613
Public Works	13,859	13,758	13,489	269
Non-Departmental	7,980	8,834	8,866	(32)
Transfers out	13,300	15,817	15,815	2
Total Use of Funds	145,309	149,177	146,778	2,399
EXCESS OF REVENUES OR EXPENDITURES BUDGETARY BASIS	\$1,262	(\$4,368)	(664)	\$3,704
Adjustments to Budgetary Basis:				
Current year encumbrance/reappropriations			5,920	
Prior year encumbrance/reappropriations			(4,460)	
Current year stores adjustment, net			(24)	
Prior year stores adjustment			37	
EXCESS OF REVENUES OVER EXPENDITURES - GAAP BASIS			809	
Fund balances at beginning of year			42,415	
Fund balances at end of year, GAAP basis			\$43,224	

See accompanying notes to financial statements



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Proprietary Funds.....

Introduction

Proprietary Funds account for City operations financed and operated in a manner similar to a private business enterprise. The intent of the City is that the cost of providing goods and services be financed primarily through user charges.

The City has elected to treat all of its Enterprise Funds as Major Funds in fiscal year 2009.

Proprietary Funds do not provide for the disclosure of budget versus actual comparisons.

Water Services Fund

This fund accounts for all financial transactions relating to the City's Water service. Services are on a user charge basis to residents and business owners located in Palo Alto.

Electric Services Fund

This fund accounts for all financial transactions relating to the City's Electric service. Services are on a user charge basis to residents and business owners located in Palo Alto.

Fiber Optics Fund

This fund accounts for all financial transactions relating to the City's Fiber Optics service. Services are on a user charge basis to licensees located in Palo Alto.

Gas Services Fund

This fund accounts for all financial transactions relating to the City's Gas service. Services are on a user charge basis to residents and business owners located in Palo Alto.

Wastewater Collection Fund

This fund accounts for all financial transactions relating to the City's Wastewater Collection service. Collections are on a user charge basis to residents and business owners located in Palo Alto.

Wastewater Treatment Fund

This fund accounts for all financial transactions relating to the City's Wastewater Treatment. Services are on a user charge basis to residents and business owners located in Palo Alto.

Refuse Services Fund

This fund accounts for all financial transactions relating to the City's Refuse service. Services are on a user charge basis to residents and business owners located in Palo Alto.

Storm Drainage Services Fund

This fund accounts for all financial transactions relating to the City's Storm Drain service. Services are on a user charge basis to residents and business owners located in Palo Alto.

City of Palo Alto - Proprietary Funds

Statement of Net Assets - June 30, 2009

(In thousands of dollars)

	Business-type Activities-Enterprise Funds				
	Water	Electric	Fiber Optics	Gas	Wastewater Collection
ASSETS					
Current Assets:					
Cash and investments (Note 3):					
Available for operations	\$23,958	\$112,526	\$7,646	\$24,024	\$12,706
Cash and investments with fiscal agent	888			1,084	
Accounts receivable, net	3,886	18,024	389	3,894	1,956
Interest receivable	272	1,328	76	260	130
Due from other government agencies					
Inventory of materials and supplies					
Prepaid items					
Total Current Assets	29,004	131,878	8,111	29,262	14,792
Noncurrent Assets:					
Due from other government agencies					
Capital assets, nondepreciable (Note 6)	12,075	39,854	1,014	20,435	18,995
Capital assets, depreciable (Note 6)	51,846	113,818	5,617	54,603	43,693
Total Noncurrent Assets	63,921	153,672	6,631	75,038	62,688
Total Assets	92,925	285,550	14,742	104,300	77,480
LIABILITIES					
Current Liabilities:					
Accounts payable and accrued liabilities	1,508	2,264	53	1,828	610
Accrued salaries and benefits	97	246	15	104	59
Accrued compensated absences (Note 1)					
Current portion of revenue bonds (Note 7)	412	100		443	61
Accrued claims payable (Note 14)					
Total Current Liabilities	2,017	2,610	68	2,375	730
Noncurrent liabilities:					
Accrued compensated absences (Note 1)					
Accrued claims payable (Note 14)					
Interfund payable (Note 4)					
Landfill closure and postclosure care (Note 9)					
Utility revenue bonds, net of unamortized issuance costs and discounts (Note 7)	9,154	1,067		10,214	1,228
Total Noncurrent Liabilities	9,154	1,067		10,214	1,228
Total Liabilities	11,171	3,677	68	12,589	1,958
NET ASSETS					
Invested in capital assets, net of related debt	54,355	152,505	6,631	64,381	61,399
Restricted for debt service	780			952	
Unrestricted	26,619	129,368	8,043	26,378	14,123
Total Net Assets	\$81,754	\$281,873	\$14,674	\$91,711	\$75,522

(b)

Some amounts reported for *Business-type Activities* in the Statement of Net Assets are different because certain Internal Service Fund assets and liabilities are included with Business-type Activities

Net Business-type Activities

(a) External Service Fund closed in FY 2008, activity on Statement of Cash Flows for FY 2009 only

(b) Electric Fund Net Assets restated to recategorize Fiber Optics as a separate fund effective FY 2009 (See Note 10)

See accompanying notes to financial statements



Business-type Activities-Enterprise funds					Governmental
Wastewater	Refuse	Storm	External	TOTALS	Activities -
Treatment		Drainage	Service		Internal Service
					Funds
\$9,133	\$9,499	\$3,772		\$203,264	\$49,332
				1,972	
5,033	3,000	641		36,823	28
127	122	60		2,375	590
1,903				1,903	
					467
					26,352
16,196	12,621	4,473		246,337	76,769
4,750				4,750	
9,075	2,703	891		105,042	3,122
25,863	1,272	24,374		321,086	19,644
39,688	3,975	25,265		430,878	22,766
55,884	16,596	29,738		677,215	99,535
3,193	741	2,145		12,342	3,306
147	62	20		750	476
					4,054
784		405		2,205	
					5,855
4,124	803	2,570		15,297	13,691
					8,614
					15,583
		1,100		1,100	
	10,991			10,991	
14,018		8,679		44,360	
14,018	10,991	9,779		56,451	24,197
18,142	11,794	12,349		71,748	37,888
24,886	3,975	16,181		384,313	22,766
				1,732	
12,856	827	1,208		219,422	38,881
\$37,742	\$4,802	\$17,389		605,467	\$61,647
			(a)		
				(11,397)	
				\$594,070	

City of Palo Alto - Proprietary Funds
Statements of Revenues, Expenses and Changes in Net Assets
For the Year Ended June 30, 2009
(In thousands of dollars)

	Business-type Activities - Enterprise Funds				
	Water	Electric	Fiber Optics	Gas	Wastewater Collection
OPERATING REVENUES					
Sales of utilities:					
Customers	\$25,086	\$101,975	\$22	\$46,059	\$13,513
City departments	1,468	2,834		1,194	242
Surplus energy		3,312			
Wastewater treatment					
Service connection charges and miscellaneous	325	1,053		461	486
Charges for services					
Other operating revenues	241	10,146	3,314	124	245
Total Operating Revenues	27,120	119,320	3,336	47,838	14,486
OPERATING EXPENSES					
Purchase of utilities:					
Retail	8,444	79,043		25,091	6,131
Surplus energy		3,305			
Administration and general	3,065	5,234	389	1,830	879
Engineering (operating)	333	1,055		310	283
Resource management and energy efficiency programs	394	5,396		1,037	
Operations and maintenance	4,040	8,977	735	3,234	2,157
Rent	1,919	3,253	13	205	109
Depreciation and amortization	1,171	6,140	236	1,674	1,452
Claims payments and changes in estimated self-insurance liability					
Compensated absences and other benefits					
Total Operating Expenses	19,366	112,403	1,373	33,381	11,011
Operating Income	7,754	6,917	1,963	14,457	3,475
NONOPERATING REVENUES (EXPENSES)					
Return on investment	1,788	7,712	460	1,615	805
Interest (expense)	(426)			(521)	(70)
Joint venture debt service (Note 15)		(8,089)			
Gain (loss) on disposal of capital assets	(199)	(1,069)		(329)	(3,717)
Capacity fees	523			1	115
Other					
Net Nonoperating Revenues (Expenses)	1,686	(1,446)	460	766	(2,867)
Income (Loss) Before Transfers	9,440	5,471	2,423	15,223	608
Transfers in (Note 4)	44	33		39	64
Transfers (out) (Note 4)	(4,555)	(12,686)	(14)	(4,784)	(734)
Change in Net Assets	4,929	(7,182)	2,409	10,478	(62)
Total net assets at beginning of year	76,825	289,055	12,265	81,233	75,584
Total net assets at end of year	\$81,754	\$281,873	\$14,674	\$91,711	\$75,522

(b)

Some amounts reported for *Business-type Activities* in the Statement of Net Assets are different because certain Internal Service Fund assets and liabilities are included with Business-type Activities

Change in Net Assets of Business-type Activities

(a) External Service Fund closed in FY 2008, activity on Statement of Cash Flows for FY 2009 only

(b) Electric Fund Net Assets restated to recategorize Fiber Optics as a separate fund effective FY 2009 (See Note 10)

See accompanying notes to financial statements



Business-type Activities - Enterprise Funds					Governmental
Wastewater Treatment	Refuse	Storm Drainage	External Service	TOTALS	Activities - Internal Service Funds
\$34	\$24,384	\$5,161		\$216,234	
6,178	1,173	302		13,391	
				3,312	
18,804				18,804	
				2,325	
					\$55,909
3,409	3,544	42		21,065	
28,425	29,101	5,505		275,131	55,909
	9,504			128,213	
				3,305	
	1,520			12,917	16,237
1,645	421	365		4,412	
		252		7,079	
12,489	17,166	406		49,204	7,793
	4,289			9,788	
2,226	636	573		14,108	2,316
					2,168
					45,682
16,360	33,536	1,596		229,026	74,196
12,065	(4,435)	3,909		46,105	(18,287)
664	741	318		14,103	2,998
(499)	(603)	(564)		(2,683)	
				(8,089)	
		(114)		(5,428)	29
				639	
(15,261)				(15,261)	63
(15,096)	138	(360)		(16,719)	3,090
(3,031)	(4,297)	3,549		29,386	(15,197)
30	179			389	6,720
(182)	(1,291)	(163)		(24,409)	(204)
(3,183)	(5,409)	3,386		5,366	(8,681)
40,925	10,211	14,003			70,328
\$37,742	\$4,802	\$17,389			\$61,647
			(a)		
				(9,870)	
				(\$4,504)	

City of Palo Alto - Proprietary Funds
Statement of Cash Flows -
For the Year Ended June 30, 2009
(In thousands of dollars)

	Business-type Activities - Enterprise Funds				
	Water	Electric	Fiber Optics	Gas	Wastewater Collection
CASH FLOWS FROM OPERATING ACTIVITIES:					
Receipts from customers	\$25,758	\$109,734	\$2,947	\$46,340	\$14,119
Payments to suppliers	(15,244)	(96,530)	(695)	(30,665)	(8,188)
Payments to employees	(3,049)	(5,198)	(374)	(1,805)	(868)
Internal activity - receipts from other funds	1,468	2,834		1,194	242
Claims paid					
Interfund receipts					
Interfund payment					
Other receipts	241			124	245
Net Cash From Operating Activities	9,174	10,840	1,878	15,188	5,550
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:					
Transfers in	44	33		39	64
Transfers (out)	(4,555)	(12,686)	(14)	(4,784)	(734)
Net Cash From Noncapital Financing Activities	(4,511)	(12,653)	(14)	(4,745)	(670)
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES:					
Acquisition and construction of capital assets	(5,865)	(3,613)	(6,867)	(7,516)	(4,681)
Proceeds from sale of capital assets					
Proceeds from debt issuance	750	1,500	1,500		
Cost of issuance paid		(143)	(143)		
Capacity fees	523			1	115
Principal paid on long-term debt	(1,011)	(1,447)	(1,357)	(419)	(56)
Interest paid on long-term debt	(426)	(8,089)		(521)	(70)
Cash Flows From Capital Financing Activities	(6,029)	(11,792)	(6,867)	(8,455)	(4,692)
CASH FLOWS FROM INVESTING ACTIVITIES:					
Interest on investments	1,788	8,120	384	1,586	814
Net Cash Flows	422	(5,485)	(4,619)	3,574	1,002
Cash and cash equivalents at beginning of year	24,424	118,011	12,265	21,534	11,704
Cash and cash equivalents at end of year	<u>\$24,846</u>	<u>\$112,526</u>	<u>\$7,646</u>	<u>\$25,108</u>	<u>\$12,706</u>
FINANCIAL STATEMENT PRESENTATION:					
Cash and investments available for operations	\$23,958	\$112,526	\$7,646	\$24,024	\$12,706
Cash and investments with fiscal agent	888			1,084	
Cash and cash equivalents at end of year	<u>\$24,846</u>	<u>\$112,526</u>	<u>\$7,646</u>	<u>\$25,108</u>	<u>\$12,706</u>
Reconciliation of operating income (loss) to Cash Flows from Operating income (loss)					
Operating income (loss)	\$7,754	\$6,917	\$1,963	\$14,457	\$3,475
Adjustments to reconcile operating income (loss) to cash					
Depreciation and amortization	1,171	6,140	236	1,674	1,452
Other					
Changes in assets and liabilities:					
Accounts receivable	347	(3,440)	(389)	(180)	120
Inventory of materials and supplies					
Prepaid items					
Accounts and other payables	(98)	1,223	68	(763)	503
Interfund receipts					
Interfund payable					
Accrued compensated absences					
Accrued claims payable and other liabilities					
Net Cash From Operating Activities	<u>\$9,174</u>	<u>\$10,840</u>	<u>\$1,878</u>	<u>\$15,188</u>	<u>\$5,550</u>

(a) External Service Fund closed in FY 2008, activity on Statement of Cash Flows for FY 2009 only

See accompanying notes to financial statements

Business-type Activities - Enterprise Funds					Governmental Activities - Internal Service Funds
Wastewater Treatment	Refuse	Storm Drainage	External Service	TOTALS	
\$19,031	\$24,050	\$5,222		\$247,201	\$56,213
(9,260)	(30,971)	(573)	(\$9)	(192,135)	(6,607)
(8,102)	(1,512)	(1,276)		(22,184)	(57,440)
6,178	1,173	302		13,391	(4,256)
<u>3,409</u>	<u>6,628</u>	<u>42</u>		<u>10,689</u>	<u>63</u>
<u>11,256</u>	<u>(632)</u>	<u>3,717</u>	<u>(9)</u>	<u>56,962</u>	<u>(12,027)</u>
30	179			389	6,720
(182)	(1,291)	(163)		(24,409)	(204)
<u>(152)</u>	<u>(1,112)</u>	<u>(163)</u>		<u>(24,020)</u>	<u>6,516</u>
(15,869)	(741)	(5,814)		(50,966)	(7,381)
				3,750	29
				(286)	
1,435		(354)		(3,209)	
(499)	(603)	(564)		(10,772)	
<u>(14,933)</u>	<u>(1,344)</u>	<u>(6,732)</u>		<u>(60,844)</u>	<u>(7,352)</u>
713	762	334		14,501	3,257
(3,116)	(2,326)	(2,844)	(9)	(13,401)	(9,606)
12,249	11,825	6,616	9	218,637	58,938
<u>\$9,133</u>	<u>\$9,499</u>	<u>\$3,772</u>		<u>\$205,236</u>	<u>\$49,332</u>
\$9,133	\$9,499	\$3,772		\$203,264	\$49,332
				1,972	
<u>\$9,133</u>	<u>\$9,499</u>	<u>\$3,772</u>		<u>\$205,236</u>	<u>\$49,332</u>
\$12,065	(\$4,435)	\$3,909		\$46,105	(\$18,287)
2,226	636	573		14,108	2,316
					63
193	(334)	61		(3,622)	304
					65
(3,228)	417	(826)	(\$9)	(2,713)	2,825
					2,791
					(16)
	3,084			3,084	(2,088)
<u>\$11,256</u>	<u>(\$632)</u>	<u>\$3,717</u>	<u>(\$9)</u>	<u>\$56,962</u>	<u>(\$12,027)</u>

(a)



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Fiduciary Funds.....

Introduction

These funds account for assets held by the City in trust or as an agent for various assessment and community facilities districts. The financial activities of these funds are excluded from the Citywide financial statements, but are presented in separate Fiduciary Fund financial statements.



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City of Palo Alto - Fiduciary Funds

Statement of Fiduciary Net Assets - June 30, 2009 (In thousands of dollars)

	<u>Agency Funds</u>
ASSETS	
Cash and investments available for operations (Note 3)	\$1,106
Cash and investments with fiscal agents (Note 3)	6,062
Interest receivable	<u>42</u>
Total Assets	<u><u>\$7,210</u></u>
LIABILITIES	
Due to bondholders	\$6,333
Due to other governments	<u>877</u>
Total Liabilities	<u><u>\$7,210</u></u>

See accompanying notes to financial statements



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Index.....

	Page
1. Summary of Significant Accounting Policies	49
2. Budgets and Budgetary Accounting	55
3. Cash and Investments	56
4. Interfund Transactions	61
5. Notes and Loans Receivable	64
6. Capital Assets	70
7. General Long-Term Obligations	76
8. Special Assessment Debt	82
9. Landfill Closure and Post-closure Care	83
10. Net Assets and Fund Balances	84
11. Pension Plans	87
12. Retiree Health Benefits	89
13. Deferred Compensation Plan	92
14. Risk Management	92
15. Joint Ventures	94
16. Commitments and Contingencies	97

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



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Note 1.....

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

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

Reporting Entity

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

The Palo Alto Public Improvement Corporation provides financing of public capital improvements for the City through the issuance of Certificates of Participation (COPs), a form of debt, which allows investors to participate in a stream of future lease payments. Proceeds from the COPs are used to construct projects which are leased to the City. The lease payments are sufficient in timing and amount to meet the debt service requirements of the COPs. The Corporation is controlled by the City, which performs all accounting and administrative functions for the Corporation. The financial activities of the Corporation are included in the Golf Course and Civic Center Debt Service Funds and the Capital Projects Fund.

The Palo Alto Redevelopment Agency is a separate government entity whose purpose is to prepare and implement plans for improvement, rehabilitation, and development of certain areas within the City. The City Council and the Redevelopment Agency Board are composed of the same individuals. Certain administrative and accounting functions are performed by City staff. The financial activities of the Agency have been included in these financial statements in the Redevelopment Agency Special Revenue Fund.

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

Basis of Presentation

The City's Basic Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America. The Government Accounting Standards Board is the acknowledged standard setting body for establishing accounting and financial reporting standards followed by governmental entities in the United States.

These Standards require that the financial statements described below be presented.

Citywide Statements: The Statement of Net Assets and the Statement of Activities display information about the primary government (the City) and its component units. These statements include the financial activities of the overall City government, except for fiduciary activities. Eliminations have been made to minimize the double counting of internal activities. However, interfund goods and services transactions have not been eliminated in the consolidation process. These statements distinguish between the *Governmental* and *Business-type Activities* of the City. Governmental Activities generally are financed through taxes, intergovernmental revenues, and other non-exchange transactions. Business-type Activities are financed in whole or in part by fees charged to external parties.

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

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

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

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

Major Funds

The City's Major Governmental and Business-type Funds need to be identified and presented separately in the Fund financial statements. All other funds, called Non-major Funds, are combined and reported in a single column, regardless of their fund-type.

Major Funds are defined as funds that have either assets, liabilities, revenues or expenditures/expenses equal to 10 percent of their fund-type total and five percent of the grand total. The General Fund is always a Major Fund. The City may also select other funds it believes should be presented as Major Funds.

The City reported the following Major Governmental Funds in the accompanying financial statements:

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

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

The City reported all its Enterprise Funds as Major Funds in the accompanying financial statements:

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

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

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

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

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

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

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

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

The City also reports the following fund types:

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

Vehicle Replacement and Maintenance – This fund accounts for the maintenance and replacement of vehicles and equipment used by all City departments. The source of revenue is an accumulation of resources.

Technology – This fund accounts for replacement and upgrade of technology, and covers four primary areas used by all City departments: desktop, infrastructure, applications, and technology research and development. The source of revenue is an accumulation of resources.

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

General Benefits and Insurance – This fund accounts for the administration of compensated absences and health benefits, and the City’s self-insured workers’ compensation and general liability programs.

Retiree Health Benefit – This fund accounts for the retiree health benefits.

Fiduciary Funds – These funds account for assets held by the City in trust or as an agent for various assessment and community facilities districts. The financial activities of these funds are excluded from the Citywide financial statements, but are presented in separate Fiduciary Fund financial statements.

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

California Avenue Parking Assessment District – This fund accounts for receipts and disbursements associated with the 1993 Parking District No. 92-13 Assessment Bonds.

Cable Joint Powers Authority – This fund was established to account for the activities of the cable television system on behalf of the members.

University Avenue Area Parking Assessment District – This fund accounts for the receipts and disbursements associated with the Series 2001-A University Avenue Area Off-Street Parking Assessments Bonds.

Basis of Accounting

The Citywide and Proprietary fund financial statements are reported using the *economic resources measurement focus* and the full *accrual basis* of accounting. Revenues are recorded when *earned* and expenses are recorded at the time liabilities are *incurred*, regardless of when the related cash flows take place.

Governmental Funds are reported using the *current financial resources* measurement focus and the *modified accrual* basis of accounting. Under this method, revenues are recognized when *measurable and available*. The City considers revenues susceptible to accrual reported in the Governmental Funds to be available if the revenues are collected within ninety days after year-end, except for property taxes. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, and compensated absences, which are recognized as expenditures to the extent they have matured. General capital asset acquisitions are reported as *expenditures* in Governmental Funds. Proceeds of general long-term debt and acquisitions under capital leases are reported as *other financing sources*.

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

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

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

The City follows those Financial Accounting Standard Board Statements issued before November 30, 1989, which do not conflict with Governmental Accounting Standards Board Statements.

Inventory of Materials and Supplies

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

Compensated Absences

The liability for compensated absences includes the vested portions of vacation, sick leave, and overtime compensation pay. The City’s liability for accrued compensated absences is recorded in the General Benefits and Insurance Internal Service Fund. Amounts expected to be “permanently liquidated”, such as what is due to be paid because of a realized employment action, are recorded as fund liabilities in the General Benefits and Insurance Internal Service Fund. The Fund is reimbursed through payroll charges to all other funds. Earned but unpaid vacation and overtime compensation pay is recognized as an expense or expenditure in the Proprietary and Governmental Fund types when earned because the City has provided financial resources for the full amount through its budgetary process. Vested accumulated sick pay is paid in the event of termination due to disability and under certain conditions specified in employment agreements.

During fiscal year ended June 30, 2009, changes to the compensated absences were as follows:

Beginning Balance	\$10,423
Additions	7,146
Payments	<u>(4,901)</u>
Ending Balance	<u><u>\$12,668</u></u>
Current Portion	<u><u>\$4,054</u></u>

Property Tax

Santa Clara County assesses properties and bills, collects, and distributes property taxes to the City. The County remits the entire amount levied and handles all delinquencies, retaining interest and penalties. Secured and unsecured property taxes are levied on January 1 of the preceding fiscal year.

Secured property tax is due in two installments, on November 1 and February 1, and becomes a lien on those dates. It becomes delinquent on December 10 and April 10, respectively. Unsecured property tax is due on July 1, and becomes delinquent on August 31. Collection of delinquent accounts is the responsibility of the County, which retains all penalties.

The term “unsecured” refers to taxes on personal property other than real estate, land and buildings. These taxes are secured by liens on the property being taxed. Property tax revenues are recognized by the City in the fiscal year they are assessed, provided they become available as defined above within 60 days after year end.

Rounding

All amounts included on the basic financial statements, combining statements, fiduciary statements, footnotes and schedules are presented to the nearest thousands in accordance with the City’s policy.

Estimates

The accompanying basic financial statements have been prepared on the modified accrual and/or accrual basis of accounting in accordance with generally accepted accounting principles. This requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amounts of revenues and expenditures/expenses during the reporting period. Actual results could differ from those estimates.

Note 2.....

BUDGETS AND BUDGETARY ACCOUNTING

1. The City Manager submits to the City Council a proposed operating budget for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and the means of financing them.
2. Public hearings are conducted to obtain public comments.
3. The Adopted budget is legally enacted through passage of a budget ordinance for all funds except for Agency Funds.
4. The City Manager is authorized to reallocate funds from a contingent account maintained in the General Fund in conformance with the adopted policies set by the City Council. Additional appropriations to departments in the General Fund, or to total appropriations for all other budgeted funds, or transfers of appropriations between funds, require approval by the City Council. These amendments are added to the Adopted budget and the resulting totals are reflected as Adjusted budget amounts.
5. Expenditures may not legally exceed budgeted appropriations at the department level for the General Fund, and at the fund level for Special Revenue and Debt Service Funds.
6. Formal budgetary integration is employed as a management control device during the year in all funds except Agency Funds and the Civic Center Refinancing and Downtown Parking Improvement Debt Service Funds.
7. Budgets for governmental funds are adopted on a basis consistent with generally accepted accounting principles (GAAP) for all funds, except that General Fund encumbrances are treated as budgetary expenditures when incurred and stores (materials, parts and supplies) transactions included in the General Fund are not budgeted.
8. Expenditures for the Capital Projects Fund are budgeted and managed on a project length basis. Budget to actual comparisons for these expenditures have been excluded from the accompanying financial statements.



Note 3.....

CASH AND INVESTMENTS

The City pools cash from all sources and all funds except Restricted Cash and Investments with Fiscal Agents so that it can be invested at the maximum yield, consistent with safety and liquidity, while individual funds can make expenditures at any time.

Policies

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

The City’s investments are carried at fair value, as required by generally accepted accounting principles. The City adjusts the carrying value of its investments to reflect their fair value at each fiscal year end, and it includes the effects of these adjustments in income for that fiscal year.

Classification

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

Cash and investments available for operations	\$342,321
Cash and investments with fiscal agents	<u>3,927</u>
City cash and investments	346,248
Cash and investments available for operations in	
Fiduciary Funds (separate Statement)	1,106
Cash and investments with fiscal agents	
Fiduciary Funds (separate Statement)	<u>6,062</u>
Total cash and investments	<u><u>\$353,416</u></u>



Investments Authorized by the City's Investment Policy & Debt Agreements

The table below identifies the investment types that are authorized by the City's Investment Policy. The table also identifies certain provisions of the City's Investment Policy that address interest rate risk, credit risk and concentration of credit risk. The table addresses investments of debt proceeds held by bond trustee that are governed by the provisions of debt agreements of the City, rather than the general provisions of the City's investment policy.

Authorized Investment Type	Maximum Maturity	Credit Minimum Quality	Maximum Percentage of Portfolio	Maximum Investment In One Issuer
U.S. Government Securities	10 years	N/A	No Limit	No Limit
U.S. Government Agency Securities (C)	10 years	N/A	No Limit (A)	No Limit
Certificates of Deposit	10 years	N/A	20%	10% of the par value of portfolio
Bankers Acceptances	180 days (D)	N/A (D)	30%	\$5 million
Commercial Paper	270 days	AAA	15%	\$3 million (B)
Local Agency Investment Fund	N/A	N/A	No Limit	\$40 million per account
Short-Term Repurchase Agreements	1 year	N/A	No Limit	No Limit
City of Palo Alto Bonds	N/A	N/A	No Limit	No Limit
Money Market Deposit Accounts	N/A	N/A (E)	No Limit	10%
Mutual Funds (F)	N/A	N/A	20%	10%
Negotiable Certificates of Deposit	10 years	N/A	10%	\$5 million
Medium Term Corporate Notes	5 years	AA	10%	\$5 million

(A) Callable and multi-step securities are limited to no more than twenty percent of the par value of the portfolio, provided that:

- 1) the potential call dates are known at the time of purchase.
- 2) the interest rates at which they "step-up" are known at the time of purchase.
- 3) the entire face value of the security is redeemed at the call date.

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

Debt Agreements:

(C) Utility Revenue Bonds 2002 Series A and 1999 Series A allow General Obligations of states with a Minimum Credit Quality Rating of A2/A by Moody's and S&P.

(D) Utility Revenue Bonds 2002 Series A and 1999 Series A require a Minimum Credit Quality Rating of A-1/P-1 by Moody's and S&P and maturing after no more than 360 days.

Utility Revenue Bonds 1995 limit the maximum maturity to 365 days.

(E) Utility Revenue Bonds 2002 Series A and 1999 Series A require a Minimum Credit Quality Rating of AAAM or AAAM-G by S&P.

(F) Utility Revenue Bonds 2002 Series A, Golf PIC COP 1998, University Avenue Parking Bond 2001 and University Avenue Parking Bond 2002 are allowed to invest in the California Asset Management Program.

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

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates and may adversely affect the fair value of an investment. Normally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates.

Information about the sensitivity of the fair values of the City’s investments (including investments held by bond trustees) to market interest rate fluctuations is provided by the following table that shows the distribution of the City’s investments by maturity or earliest call date (in thousands):

Type of Investments	Less Than One Year	One to Three Years	Three to Five Years	Over Five Years	Total
U.S. Federal Agency Securities	\$65,088	\$80,371	\$102,337	\$78,378	\$326,174
U.S. Treasury Notes			2,106		2,106
Money Market Mutual Funds (government securities)	747				747
Certificates of Deposit	181	341			522
California Asset Management Program	3,849				3,849
Local Agency Investment Fund	16,427				16,427
Total Investments	<u>\$86,292</u>	<u>\$80,712</u>	<u>\$104,443</u>	<u>\$78,378</u>	349,825
Cash in banks and on hand					3,591
Total Cash and Investments					<u>\$353,416</u>

Local Agency Investment Fund

The City is a participant in the Local Agency Investment Fund (LAIF) that is regulated by California Government Code Section 16429 under the oversight of the Treasurer of the State of California. LAIF management calculates the fair value and cost of the entire LAIF pool. The City adjusts its cost basis invested in LAIF to fair value based on this ratio. The balance available for withdrawal on demand is based on the accounting records maintained by LAIF, which are recorded on an amortized cost basis. Included in LAIF’s investment portfolio are collateralized mortgage obligation, mortgage-backed securities, other asset-backed securities, loans to certain state funds, and floating rate securities issued by Federal agencies, government-sponsored enterprises, and corporations. At June 30, 2009, these investments matured in an average of 235 days.

California Asset Management Program

The City is a voluntary participant in the California Asset Management Program (CAMP). CAMP is an investment pool offered by the California Asset Management Trust (the Trust). The Trust is a joint powers authority and public agency created by the Declaration of Trust and established under the provisions of the California Joint Exercise of Powers Act (California Government Code Sections 6500 et seq., or the “Act”) for the purpose of exercising the common power of its Participants to invest certain proceeds of debt issues and surplus funds. The Pool’s investments are limited to investments permitted by subdivisions (a) to (n), inclusive, of Section 53601 of the California Government Code. The City reports its investments in CAMP at the fair value amounts provided by CAMP, which is the same as the value of the pool share. At June 30, 2009 the fair value approximated is the City’s cost. At June 30, 2009, these investments have an average maturity of 56 days.

Money Market Mutual Funds are available for withdrawal on demand and at June 30, 2009 matured in an average of 55 days.



Investments with Fair Values Highly Sensitive to Interest Rate Fluctuations

The City's investments (including investments held by bond trustees) include the following investments that are highly sensitive to interest rate fluctuations (to a greater degree than already indicated in the information provided above):

Highly Sensitive Investments

Fair Value at Year End
(in thousands)

US Federal Agency Callable Securities. These securities are subject to early redemption in a period of declining interest rates. The resultant reduction in expected total cash flows affects the fair value of these securities and makes the values of these securities highly sensitive to changes in interest rates.

\$65,354

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization. Presented below is the actual rating as provided by Standard & Poor's investment rating system as of June 30, 2009 for each investment type (in thousands):

Investment Type	AAA	Total
U.S. Federal Agency Securities	\$326,174	\$326,174
U.S. Treasury Notes	2,106	2,106
Money Market Mutual Funds (government securities)	747	747
California Asset Management Program	3,849	3,849
Total	\$332,876	332,876
Not Rated:		
Certificates of Deposit		522
Local Agency Investment Fund		16,427
<i>Cash in banks and on hand</i>		3,591
Total Cash and Investments		\$353,416



Concentration of Credit Risk

Investments in any one issuer, other than U.S. Treasury securities, mutual funds, and external investment pools, that represent 5 percent or more of total City portfolio Entity-wide investments, are as follows at June 30, 2009 (in thousands):

<u>Investments</u>	<u>Reporting Type</u>	<u>Investment Amount</u>
Federal Agriculture Mortgage Corp.	U.S. Federal Agency Securities	\$20,736
Federal Farm Credit Bank	U.S. Federal Agency Securities	112,712
Federal Home Loan Bank	U.S. Federal Agency Securities	109,754
Federal Home Loan Mortgage Corp.	U.S. Federal Agency Securities	27,304
Federal National Mortgage Assoc.	U.S. Federal Agency Securities	40,063

Custodial Risk

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

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

Note 4

INTERFUND TRANSACTIONS

Transfers Between Funds

With Council approval, resources may be transferred from one City fund to another. The purpose of the majority of transfers is to subsidize a fund. Less often, a transfer may be made to open or close a fund. Transfers between City funds during fiscal year 2009 were as follows (in thousands):

Fund Receiving Transfer	Fund Making Transfer	Amount Transferred		
General Fund	Street Improvement Special Revenue Fund	\$292		
	Special Districts Special Revenue Fund	888		
	Redevelopment Agency Special Revenue Fund	6		
	Capital Projects Fund	9		
	Water Enterprise Fund	2,772	A	
	Electric Enterprise Fund	9,715	A	
	Gas Enterprise Fund	3,308	A	
	Wastewater Collection Enterprise Fund	68	A	
	Refuse Enterprise Fund	271	A	
	Wastewater Treatment Enterprise Fund	134	A	
	Storm Drainage Enterprise Fund	27	A	
	Fiber Optics Enterprise Fund	3	A	
	Vehicle Replacement and Maintenance Internal Service Fund	27		
	Technology Fund Internal Service Fund	75		
	Printing and Mailing Services Internal Service Fund	8		
	Special Revenue Funds:	Street Improvement Capital Projects Fund	1,800	C
Special District		31	C	
Transportation Mitigation Street Improvement Special Revenue Fund		994		
Developer's Impact Fee Capital Projects Fund		596	C	
Redevelopment Agency General Fund		35	C	
Debt Service Funds:	Golf Course Improvements General Fund	526		
	Civic Center Refinancing General Fund	332		
		Special Districts Special Revenue Fund	80	
	Downtown Parking Improvement General Fund	225		
Capital Projects Fund:	General Fund	14,648	B	
	Street Improvement Special Revenue Fund	485		
	Developer's Impact Fee Special Revenue Fund	1,090		
	Transportation Mitigation Special Revenue Fund	82		
	Electric Enterprise Fund	234	B	
	Gas Enterprise Fund	83		
	Water Enterprise Fund	971		
	Wastewater Collection Enterprise Fund	71		
Fiber Optics Enterprise Fund	11			



Notes to Basic Financial Statements – Note 4

Fund Receiving Transfer	Fund Making Transfer	Amount Transferred	
Enterprise Funds:			
Water	Gas Enterprise Fund	\$22	
	Wastewater Collection Enterprise Fund	22	
Electric	General Fund	33	
	Water Enterprise Fund	13	
Gas	Electric Enterprise Fund	13	
	Wastewater Collection Enterprise Fund	13	
	Special Districts Special Revenue Fund	116	
Refuse	Wastewater Collection Enterprise Fund	63	
	Retiree Health Benefit Internal Service Fund	64	
Wastewater Collection	Technology Fund Internal Service Fund	30	
Wastewater Treatment			
Internal Service Funds:			
Vehicle Replacement and Maintenance	General Fund	45	
	Capital Projects Fund	80	
	Gas Enterprise Fund	10	
	Wastewater Collection Enterprise Fund	20	
	Refuse Enterprise Fund	200	
	Technology	Water Enterprise Fund	799
		Electric Enterprise Fund	2,724
		Gas Enterprise Fund	1,361
		Wastewater Collection Enterprise Fund	477
		Wastewater Treatment Enterprise Fund	48
		Refuse Enterprise Fund	820
		Storm Drainage Enterprise Fund	136
			<u>136</u>
		<u>\$47,012</u>	

The reasons for these transfers are set forth below:

- (A) Transfer to reimburse the General Fund for costs incurred for the benefit of funds making the transfer.
- (B) Allocation of funds to construct capital assets.
- (C) Transfer to return unspent construction funds

Current Interfund Balance

Current interfund balances arise in the normal course of business and are expected to be repaid shortly after the end of the fiscal year. At June 30, 2009, the Federal Revenue Special Revenue Fund and the Local Law Enforcement Special Revenue Fund owed the General Fund \$105 thousand and \$5 thousand respectively.



Interfund Commitment

During fiscal year 2002, the City established the Palo Alto Redevelopment Agency. The Agency and the City have an agreement whereby the City will advance funds to the Agency in support of start up and formation costs. However, the interfund advances have no specific repayment date. Generally accepted accounting principals require that such amounts be treated as transfers in the year made. Advances without specified repayment terms total \$373 thousand as of June 30, 2009.

Long-Term Interfund Advances

On August 6, 2007, the City authorized a loan in the amount up to \$1.7 million from the General Fund Budget Stabilization Reserve to the Storm Drainage Fund for Capital Improvement Program project San Francisquito Creek Storm Water Pump Station. The General Fund Budget Stabilization Reserve will be paid back in three years after receipt of the last payment, together with interest at an interest rate commensurate with the Reserve's annual rate of return during the time period of the loan. The Storm Drain Fund will be charged interest on the principal borrowed (loan) from the General Fund. The interest rate will be equal to the average yield on the City's portfolio from the time the loan is issued through the time of repayment. The loan will be repaid over a three year period. There shall be no prepayment penalty. At June 30, 2009, the balance of the advance including principal and accrued interest, was \$1.1 million.

Internal Balances

Internal balances represent the net interfund receivables and payables remaining after the elimination of all such balances within Governmental and Business-type Activities.



Note 5.....

NOTES AND LOANS RECEIVABLE

At June 30, 2009, the City's notes and loans receivable totaled (in thousands):

Palo Alto Housing Corporation:	
Oak Manor Townhouse	\$935
Tree House Apartments	2,838
Emerson Street Project	375
Alma Single Room Occupancy Development	2,222
Barker Hotel	2,111
Sheridan Apartments	2,247
Oak Court Apartments, L.P.	7,835
Mid-Peninsula Housing Coalition:	
Palo Alto Gardens Apartments	498
Community Working Group, Inc	1,280
Opportunity Center Associates, L.P.	750
Home Rehabilitation Loans	83
Executive Relocation Assistance Loans	428
Below Market Rate Assessment Loans	74
Stevenson Housing:	
Hot Water	81
Fire Alarm	48
Oak Manor Townhouse Water System	114
Palo Alto Senior Housing Project	28
Clara-Mateo Alliance	11
Lytton Gardens Assisted Living	101
Emergency Housing Consortium	75
Alma Gardens Apartment	<u>1,150</u>
Total Loans and Notes	<u>23,284</u>
Less: valuation allowance	<u>(14,805)</u>
Net Carrying Value	<u><u>\$8,479</u></u>



Housing Loans

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

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

Oak Manor Townhouse

On January 7, 1991, the City loaned \$2.1 million to assist in the acquisition of an apartment complex to be used to provide rental housing for low and very low-income households. This loan bears interest at 3 percent, is due in annual installments until 2011 and is collateralized by a subordinated deed of trust. Under the terms of the loan agreement, loan payments are forgiven if the Corporation meets the objective of this project. During the year ended June 30, 2009, the objective was met. The annual loan payment was forgiven for the calendar year ending December 31, 2008.

Emerson Street Project

On November 8, 1994, the City loaned \$375 thousand for expenses necessary to acquire an apartment complex for the preservation of rental housing for low and very low-income households in the City. This loan is collateralized by a second deed of trust. The loan bears no interest until 2009 after which the loan bears interest at three percent per year. The principal balance is due in 2034.

Alma Single Room Occupancy Development

On December 13, 1996, the City loaned \$2.7 million to the Alma Place Associates, L.P. for the development of a 107-unit single room occupancy development. This loan bears interest at 3 percent and is collateralized by a subordinated deed of trust. Loan payments are deferred until 2014. The principal balance is due in 2041.

Barker Hotel

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



In July 2004, the City agreed to loan up to \$41 thousand to Palo Alto Housing Corporation to rehabilitate the interior of the Barker Hotel. The loan is funded entirely by Community Development Block Grant funds and is collateralized by a deed of trust on the property. Annual loan payments are deferred until certain criteria defined in the loan agreement are reached. The loan shall be forgiven if the borrower satisfactorily complies with all the terms and conditions of the loan agreement.

Sheridan Apartments

On December 8, 1998, the City loaned \$2.5 million to the Palo Alto Housing Corporation for the purchase and rehabilitation of a 57-unit apartment complex to be used for senior and low-income housing. The loan is funded by \$1.6 million in Community Development Block Grant Funds, and \$825 thousand in Housing In-Lieu funds. The note bears interest at 9 percent when available surplus cash from the project equals or exceeds 25 percent of interest calculated using 9 percent. When available surplus cash falls below this level, the note bears interest at 3 percent. The note is collateralized by a second deed of trust and an Affordability Reserve Account held by the Corporation. Annual loan payments are deferred until the Corporation accumulates \$1.0 million in an Affordability Reserve Account. The principal balance is due in 2033.

Oak Court Apartments

On August 18, 2003, in connection with the loan to Oak Court Apartments, L.P. discussed below, the City loaned \$5.9 million to the Palo Alto Housing Corporation for the purchase of land on which Oak Court Apartments, L.P. constructed a 53-unit rental apartment complex for low and very low-income households with children. The note bears interest of five percent and is secured by a deed of trust. Annually accrued interest is added to the principal balance: and note payments are due annually after 55 years, or beginning in 2058, unless the Corporation elects to extend the note until 2102, as define in the regulatory agreement.

Oak Court Apartments, L.P.

On August 18, 2003, the City loaned \$2.0 million to Oak Court Apartments, L.P. for the construction of a 53-unit rental apartment complex for low and very low-income households with children, which was completed in April 2005. The note bears no interest until certain criteria defined in the note are satisfied, at which time the note will bear an interest rate not to exceed three percent. The note is secured by a subordinate deed of trust. The principal balance is due in 2058.

Palo Alto Gardens Apartments

On April 22, 1999, the City loaned \$1.0 million to the Mid-Peninsula Housing Coalition for the purchase and rehabilitation of a 155-unit complex for the continuation of low-income housing. This loan is funded by \$659 thousand in Community Development Block Grant funds and \$341 thousand in Housing In-Lieu funds. There are two notes that bear interest at 3 percent and are secured by second deeds of trust and a City Affordability Reserve Account held by the Coalition. Annual loan payments are deferred until certain criteria defined in the notes are reached. Principal and interest payments began in FY 2008. The principal balance is due in 2039.

Community Working Group, Inc.

On May 13, 2002, the City loaned \$1.3 million to the Community Working Group, Inc. for predevelopment, relocation and acquisition of land for development of an 89-unit complex and homeless service center for very low-income households. The loan is funded by \$1.3 million dollars of Community Development Block Grant funds. The note bears no interest and is secured by a first deed of trust. No repayment of the \$1.3 million will be required, provided that compliance with the City’s agreement is maintained. After 89 years of compliance with the regulatory agreement, the City’s loan would convert to a grant and its deed of trust would be reconveyed.

**Opportunity Center Associates, L.P.**

On July 19, 2004, the City loaned \$750 thousand for a 55-year term to the Opportunity Center Associates, L.P. for construction of 89 units of rental housing for extremely low-income and very low-income households. The loan is funded by \$750 thousand of Residential Housing Funds. The note bears 3 percent interest and is secured by a deed of trust.

Home Rehabilitation

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

Executive Relocation Assistance Loans

The City Council may authorize a mortgage loan as part of a relocation assistance package to executive staff. The loans are secured by first deeds of trust, and interest is adjusted annually based on the rate of return of the invested funds of the City for the year ending June 30 plus one quarter of 1 percent. Principal and interest payments are due bi-weekly. Employees must pay off any outstanding balance of their loans within a certain period after ending employment with the City. As of June 30, 2009, the City had one outstanding employee home loan due in 2030.

Below Market Rate Assessment Loans

In December 2002, the City loaned \$53 thousand to Below Market Rate home owners with low incomes and /or very limited assets for capital repairs, special assessments and improvements of their properties. The loans bear interest at 3 percent and are secured by a deed of trust on each property. Loan payments are deferred until 2032. In 2009, the City did not receive interest payments.

Stevenson Housing Hot Water Loans

In July 2004, the City agreed to loan up to \$38 thousand to Palo Alto Senior Housing Project, Inc. to refurbish the hot water piping system at the Stevenson House Senior Housing facility. In April 2005, the City agreed to increase the loan by \$45 thousand, bringing the total loan to \$83 thousand. The loan is funded entirely by Community Development Block Grant funds and bears simple interest of 6 percent. Principal and interest payments are deferred until July 1, 2010, as long as the borrower continues to comply with all terms and conditions of the agreement.

Stevenson Housing Fire Alarm

In December 2006, the City agreed to loan up to \$48 thousand to Palo Alto Senior Housing Project, Inc. to repair and upgrade the existing fire alarm system at the Stevenson House Senior Housing facility. The loan is funded entirely by Community Development Block Grant funds and bears simple interest of 6 percent. Principal and interest payments are deferred until July 1, 2012, as long as the borrower continues to comply with all terms and conditions of the agreement.



Palo Alto Senior Housing Project Loans

In July 2003, the City agreed to loan up to \$45 thousand to Palo Alto Senior Housing Project for home improvements in the independent living facility for low-income seniors. The loan is funded entirely by Community Development Block Grant funds, bears interest at 6 percent and is secured by a deed of trust on the property. Principal and interest payments are deferred until 2009. Principal and interest on the loan shall be forgiven if the borrower satisfactorily complies with all the terms set forth in the July 2003 agreement.

In April 2008, the City provided \$47.6 thousand for the purpose of repairing and upgrading the fire alarm system at the Senior Housing facility.

Clara-Mateo Alliance Loans

In July 2003, the City agreed to loan up to \$200 thousand to Clara-Mateo Alliance for rehabilitation of the kitchen and the Elsa Segovia Center to provide services for the homeless. The loan is funded entirely by Community Development Block Grant funds, bears interest at 6 percent and is secured by a deed of trust on the property. Repayment of the loan will not be required unless the property is sold or the program terminated or changed to a use prior to July 1, 2009, that has not been approved by the City. Principal and interest on the loan shall be forgiven if the borrower satisfactorily complies with all the terms and conditions set forth in the July 2003 agreement.

Lytton Gardens Assisted Living

In June 2005, the City agreed to loan up to \$109 thousand to Community Housing, Inc. to upgrade and modernize the existing kitchens at the senior residential facility known as Lytton Gardens Assisted Living. The loan is funded entirely by Community Development Block Grant funds, and bears simple interest of 3 percent. Principal and interest payments are deferred until July 1, 2035, as long as the borrower continues to comply with all terms and conditions of the agreement.

Emergency Housing Consortium

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

Alma Garden Apartments

In March 2006, the City agreed to loan up to \$1.2 million to Community Working Group, Inc., to acquire a 10-unit multi-family housing complex known as Alma Garden Apartments. The loan is funded entirely by Community Development Block Grant funds. Principal and interest payments will be made as provided in the note until July 1, 2061, as long as the borrower continues to comply with all terms and conditions of the agreement.

Tree House Apartments

In March 2009, the City agreed to loan \$2.8 million to the Tree House Apartments, L.P. for the purchase of the real property located at 488 W. Charleston Road. On March 23, 2009, the City wired the full loan amount to an escrow account. \$1.8 million of the loan was funded by Community Development Block Grant funds; the remaining \$1.0 million was funded by Residential funds. Principal



and interest payments will be deferred for 55 years. However if the borrower has earned extra income, and if acceptable to the other entities providing final permanent sources of funds, payment of interest and principal based on the City's proportionate share of the project's residual receipts from net operating income shall be made by borrower. In no event shall full payment be made by the borrower later than concurrently with the expiration or earlier termination of the loan agreement which is March 23, 2064.



Note 6.....

CAPITAL ASSETS

Valuation

All capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Contributed capital assets are valued at their estimated fair market value on the date contributed. The City's policy is to capitalize all assets when costs are equal to/or exceed \$5,000 and the useful life exceeds three years. Infrastructure assets are capitalized when costs are equal to/or exceed \$100,000.

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

The City has recorded all its public domain (infrastructure) capital assets, which consists of Roadway, Recreation and Open Space, in its Citywide financial statements. GASB Statement 34 requires that all capital assets with limited useful lives be depreciated over their estimated useful lives. Alternatively, the "modified approach" may be used for certain capital assets. Depreciation is not provided under this approach, but all expenditures on these assets are expensed unless they are additions or improvements. The City has elected to use the depreciation method for its capital assets.

The purpose of depreciation is to spread the cost of capital assets equitably among all users over the life of these assets. The amount charged to depreciation expense each year represents that year's pro rata share of the cost of capital assets.

Depreciation has been provided on capital assets. Depreciation of all capital assets is charged as an expense against operations each year and the total amount of depreciation taken over the years, called accumulated depreciation, is reported on the balance sheet as a reduction in the book value of capital assets.

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



GOVERNMENTAL ACTIVITIES	Years
Buildings & structures	10-30
Equipment:	
Computer equipment	4
Office machinery & equipment	5
Machinery & equipment	10
Roadway network includes pavement, striping & legends, curbs, gutters & sidewalks, parking lots, traffic signage and bridges	5-40
Recreation and open space network includes major park facilities, park trails, bike paths and medians	25-40
 BUSINESS-TYPE ACTIVITIES	
Buildings and structures	25-60
Vehicles and heavy equipment	3-10
Machinery and equipment	10-50
Transmission and distribution systems	10-100

General Capital Assets

Changes in the City’s general capital assets during the year ended June 30, 2009, were (in thousands):

	Balance June 30, 2008	Additions	Retirements	Transfers	Balance June 30, 2009
<i>Governmental activities</i>					
Capital assets not being depreciated					
Land and improvements	\$73,179			\$2,271	\$75,450
Street trees	15,147	\$45	(\$140)		15,052
Construction in progress	37,369	21,038	(5,261)	(19,671)	33,475
Total capital assets not being depreciated	125,695	21,083	(5,401)	(17,400)	123,977
Capital assets being depreciated					
Buildings and improvements	99,696	12		3,500	103,208
Equipment	7,791	110			7,901
Roadway network	243,681			11,544	255,225
Recreation & open space network	13,856			2,356	16,212
Total capital assets being depreciated	365,024	122		17,400	382,546
Less accumulated depreciation					
Buildings and improvements	(56,748)	(1,893)			(58,641)
Equipment	(5,432)	(398)			(5,830)
Roadway network	(89,174)	(5,879)			(95,053)
Recreation & open space network	(5,124)	(379)			(5,503)
Total accumulated depreciation	(156,478)	(8,549)			(165,027)
Net governmental fund program					
Capital assets being depreciated	208,546	(8,427)		17,400	217,519
<i>Internal service fund capital assets</i>					
Construction in progress	7,151	2,081		(6,110)	3,122
Equipment	35,250	4,079	(132)	6,729	45,926
Accumulated depreciation	(24,700)	(1,095)	132	(619)	(26,282)
Net internal service capital assets	17,701	5,065			22,766
Governmental activity capital assets, net	\$351,942	\$17,721	(\$5,401)		\$364,262



Business-type Capital Assets

Changes in the City's Enterprise Fund capital assets during the year ended June 30, 2009, were (in thousands):

	Balance June 30, 2008	Additions	Retirements	Transfers	Balance June 30, 2009
<i>Business-type activities</i>					
Capital assets not being depreciated					
Land and improvements	\$1,953				\$1,953
Construction in progress	130,044	\$28,510		(\$55,465)	103,089
Total capital assets not being depreciated	131,997	28,510		(55,465)	105,042
Capital assets being depreciated					
Buildings and structures	19,591		(\$159)	11,275	30,707
Transmission, distribution, and treatment systems	481,446	47	(14,186)	44,190	511,497
Total capital assets being depreciated	501,037	47	(14,345)	55,465	542,204
Less accumulated depreciation					
Buildings and structures	(6,116)	(507)	46		(6,577)
Transmission, distribution, and treatment systems	(210,305)	(13,108)	8,872		(214,541)
Net capital assets being depreciated	(216,421)	(13,615)	8,918		(221,118)
Total depreciable assets	284,616	(13,568)	(5,427)	55,465	321,086
<i>Business-type activity capital assets, net</i>	<u>\$416,613</u>	<u>\$14,942</u>	<u>(\$5,427)</u>		<u>\$426,128</u>

Capital Asset Contributions

Some capital assets may be acquired using Federal and State grant funds, or they may be contributed by developers or other governments. Generally accepted accounting principles require that these contributions be accounted for as revenues at the time the capital assets are contributed.

Depreciation Allocation

Depreciation expense was charged to functions and programs based on their usage of the related assets. The amounts allocated to each function or program were as follows (in thousands):

<i>Governmental Activities</i>		<i>Business-Type Activities</i>	
City Manager	\$11	Water	\$1,102
Community Services	718	Electric	6,131
Fire	116	Fiber Optics	236
Police	60	Gas	1,589
Public Works	7,320	Wastewater Collection	1,453
Planning	54	Wastewater Treatment	2,081
Administrative Services	11	Refuse	636
Library Dept	259	Storm Drainage	387
Internal Service Funds	1,095		
	<u>\$9,644</u>		<u>\$13,615</u>

Construction in Progress and Completed Projects

Construction in progress during fiscal year 2009 is comprised of the following (in thousands):

	Expended to June 30, 2009
Governmental Activities:	
Americans with Disabilities	\$821
Animal Shelter Expansion & Renovation	1,580
Art Center Electrical & Mechanical Upgrades	185
Baylands Athletic Center Fencing Dugout	288
Buildings Study	175
Charleston/Arastradero Corridor Plan	781
Children's Theater System	207
Civic Center Infrastructure	6,915
College Terrace Library Improvements	662
College Terrace Parks Improvements	305
College Terrace Traffic Calming	143
Community Services Lighting Enhancements	210
Cubberley Community Center Campus Fire Alarm System	745
Cubberley Mechanical & Electrical Upgrades	171
Cubberley Turf Renovation	191
ECR/Ventura Signal	110
Fire Station Improvement	834
Fire Stations 3 & 4 Feasibility Study	188
Foothills Park Maintenance Building Rehabilitation	337
Greer Park Phase IV	169
Heritage Park Playground Public/Private Partnership	158
LATP Master Plan Study	136
Library Automation Service	210
Library Master Plan Project	974
Library Service Model Analysis	268
Lot S/L Garage (Downtown Parking Structure)	497
Lucie Stern Community Center Improvements	111
Mitchell Park Facilities Improvements	1,132
Mitchell Park Library	2,179
Municipal Service Center Improvements	176
Open Space Parking Improvements	622
Open Space Trails & Amenities	1,235
Other construction in progress	1,111
Park Backflow Replacement & Irrigation	260
Park Facilities Improvements	1,259
Police Mounted Video	196
Public Safety Building	3,555
Public Safety Mobile Data	164
Roofing Replacement	339
Roth Building Maintenance	161



Governmental Activities:(Continued)

San Antonio Road Median Improvements	1,083
San Antonio/101 Signal	234
San Mateo Drive Bridges	110
Sand Hill Road Bridge	173
School Site Irrigation	274
Security Systems Improvements	212
Sixteen ALS Monitor/Defibrillator	140
Stanford/Palo Alto Playing Fields	855
Street Lights Improvements	153
Tennis & Basketball Court Resurfacing	293
Traffic Signal Upgrades	188
Vehicle Replacement Fund	3,122
Total governmental construction in progress	<u><u>\$36,597</u></u>

Enterprise Funds:

Electric distribution system improvements	\$12,680
Gas system extension replacements and improvements	16,075
Other construction in progress	53,816
Other electrical improvements projects	322
Sewer system rehabilitation and extensions	3,663
Storm drainage structural and water quality improvements	880
Water quality control plant equipment replacement and lab facilities	6,486
Water system extension replacements and improvements	9,167
Total enterprise construction in progress	<u><u>\$103,089</u></u>

Allocations of Enterprise Fund administration and general expenses of \$6.44 million have been capitalized and included in amounts expended to June 30, 2009.

Note 7.....

GENERAL LONG-TERM OBLIGATIONS

The City’s Long-Term Obligations

Bond discounts and issuance costs of long-term debt issues are amortized over the life of the related debt. Gains or losses between the net book value of debt and funds placed in escrow to defease that debt are amortized over the remaining life of either the refunded debt or the refunding debt, whichever is shorter.

The City’s long-term debt issues and transactions, other than Special Assessment debt discussed in Note 8, were as follows (in thousands):

	Original Issue Amount	Balance June 30, 2008	Additions	Retirements	Balance June 30, 2009	Current Portion
Governmental Activity Debt:						
<i>General Long Term Obligations:</i>						
1998 Golf Course Certificates of Participation,						
4.00-5.00%, due 09/01/2018	\$7,750	\$4,750		\$335	\$4,415	\$355
2002A Civic Center Refinancing Certificates of Participation,						
2.00-4.00%, due 03/01/2012	3,500	1,540		365	1,175	380
2002B Downtown Parking Improvements Certificates of Participation						
4.55-6.00%, due 03/01/2022	3,555	2,115		100	2,015	105
Total Governmental Activity Debt	<u>\$14,805</u>	<u>\$8,405</u>		<u>\$800</u>	<u>\$7,605</u>	<u>\$840</u>
Business-type Activity Debt:						
<i>Enterprise Long Term Obligations:</i>						
Utility Revenue Bonds,						
1995 Series A, 5.00-6.25%, due 06/01/2020	\$8,640	\$5,649		\$330	\$5,319	\$350
1999 Refunding, 3.25-5.25%, due 06/01/2024	17,735	14,215		480	13,735	500
2002 Series A, 3.00-5.00%, due 06/01/2026	26,055	20,470		780	19,690	805
Energy Tax Credit Bonds,						
2007 Series A, 0%, due 12/15/2021	1,500	1,400		100	1,300	100
State Water Resources Loan,						
2007, 0%, due 6/30/2029	9,000	5,629	\$3,371		9,000	450
Less: unamortized discount/ issuance cost		(1,053)	(1,500)	(74)	(2,479)	
	<u>\$62,930</u>	<u>\$46,310</u>	<u>\$1,871</u>	<u>\$1,616</u>	<u>\$46,565</u>	<u>\$2,205</u>



Description of the City's Long-Term Debt Issues

1998 Golf Course COPs – In August 1998, the City's Public Improvement Corporation issued Golf Course Improvement COPs, Series 1998 in the amount of \$7.8 million to retire the 1978 Golf Course Lease Revenue Bonds, and to finance various improvements at the Palo Alto Public Golf Course, including upgrading five fairways and various traps, trees and greens, constructing new storm drain facilities, replacing the existing irrigation system, upgrading the driving range, and installing new cart paths. The 1998 COPs are secured by lease revenues received by the Public Improvement Corporation from golf course revenues or other unrestricted revenues of the City. Principal and interest are payable semi-annually each March 1 and September 1.

2002A Civic Center Refinancing COPs – On January 16, 2002 the City issued \$3.5 million of COPs to refund the City's 1992 COPs which were subsequently retired. Principal payments for the 2002A COPs are due annually on March 1 and interest payments semi-annually on March 1 and September 1 and are payable from lease revenues received by the Palo Alto Public Improvement Corporation from the City's available funds.

2002B Downtown Parking Improvement Project COPs – On January 16, 2002 the City issued \$3.6 million of COPs to finance the construction of certain improvements to the non-parking area contained in the City's Bryant /Florence Garage complex. Principal payments are due annually on March 1 and interest payments semi-annually on March 1 and September 1 from 4.6 percent to 6.5 percent, and are payable from lease revenues received by the Palo Alto Public Improvement Corporation from the City's available funds.

On January 25, 2005, the City defeased \$900 thousand of the 2002B Downtown Parking Improvements Certificates of Participation. Surplus cash from the Civic Center Refinancing and Downtown Parking Improvement Project Construction account were placed in an irrevocable trust to provide for future debt payments. Accordingly, the trust account assets and the liability for the defeased bonds are not included on the financial statements. The outstanding amount of the defeased debt at June 30, 2009 is \$740 thousand. The defeasance resulted in an overall debt service savings of \$1.5 million and an economic gain of \$462 thousand.

1995 Utility Revenue Bonds, Series A – The City issued Utility Revenue Bonds on February 1, 1995 to finance certain extensions and improvements to the City's Storm Drainage and Surface Water System. The Bonds are special obligations of the City payable solely from and secured by a pledge of and lien upon the revenues derived by the City from the funds, services and facilities of all Enterprise Funds except the Refuse Fund and Fiber Optic Fund. Principal payments are payable annually on June 1 and interest payments semi-annually on June 1 and December 1. A \$2.9 million 6.3 percent term bond is due June 1, 2020. In lieu of a reserve fund, the Bonds are secured by a Surety Bond issued by AMBAC Indemnity Corporation.

The pledge of future Net Revenues for the above funds ends upon repayment of the \$5.319 million in remaining debt service on the bonds which is scheduled to occur in 2020. For fiscal year 2009, Net Revenues, including operating revenues and non-operating interest earnings, amounted to \$262.660 million, and operating costs include operating expenses but not interest, depreciation or amortization and amounted to \$182.018 million. Net Revenues available for debt service amounted to \$80.642 million which represented coverage of 118.59 times over the \$680 thousand in debt service.



1999 Utility Revenue and Refunding Bonds, Series A – The City issued Utility Revenue Bonds on June 1, 1999, to refund the 1990 Utility Revenue Refunding Bonds, Series A and the 1992 Utility Revenue Bonds, Series A, and to finance rehabilitation of the Wastewater Treatment System’s two sludge incinerators. The 1990 Utility Revenue Refunding Bonds, Series A and the 1992 Utility Revenue Bonds, Series A, were subsequently retired.

The 1999 Bonds are special obligations of the City payable solely from and secured by a pledge of and lien upon certain net revenues derived by the City’s Sewer System and its storm and surface water system (the “Storm Drain System”). As of June 30, 2001, the 1999 Bonds had been allocated to and were repayable from net revenues of the following enterprise funds: Wastewater Collection (10.2 percent), Wastewater Treatment (64.6 percent) and Storm Drain (25.2 percent). Principal payments are payable annually on June 1 and interest payments semi-annually on June 1 and December 1. A \$3.1 million 5.3 percent term bond, and a \$5.1 million 5.3 percent term bond are due June 1, 2021 and 2024, respectively. In lieu of a reserve fund, the Bonds are secured by a Surety Bond issued by AMBAC Indemnity Corporation.

The pledge of future Net Revenues for the above funds ends upon repayment of the \$13.735 million in remaining debt service on the bonds which is scheduled to occur in 2024. For fiscal year 2009, Net Revenues, including operating revenues and non-operating interest earnings, amounted to \$48.65 million; and operating costs include operating expenses but not interest, depreciation or amortization and amounted to \$24.716 million. Net Revenues available for debt service amounted to \$23.934 million which represents coverage of 19.78 times over the \$1.21 million in debt service.

2002 Utility Revenue Bonds, Series A – On January 24, 2002, the City issued Utility Revenue Bonds to finance certain improvements to the City’s water utility system and the City’s natural gas utility system. Principal payments are due annually on June 1, and interest payments are due semi-annually on June 1 and December 1 from 3.0 percent to 5.0 percent. The 2002 Revenue Bonds are secured by net revenues generated by the Water Services and Gas Services Funds.

The pledge of future Net Revenues for the above funds ends upon repayment of the \$19.69 million in remaining debt service on the bonds which is scheduled to occur in 2026. For fiscal year 2009, Net Revenues, including operating revenues and non-operating interest earnings amounted to \$78.423 million; and operating costs include operating expenses but not interest, depreciation or amortization and amounted to \$49.902 million. Net Revenues available for debt service amounted to \$28.521 million which represented coverage of 15.48 times over the \$1.725 million in debt service.

2007 Electric System Clean Renewable Energy Tax Credit Bonds, Series A – In October 2007, the City issued \$1.5 million of Electric Utility Clean Renewable Energy Tax Credit Bonds (CREBs), 2007 Series A, to finance the City’s photovoltaic solar panel project. The Bonds do not bear interest. In lieu of receiving periodic interest payments, bondholders are allowed annual federal income tax credits in an amount equal to a credit rate for such CREBs multiplied by the outstanding principal amount of the CREBs owned by the bondholders. The Bonds are payable solely from and secured solely by a pledge of the Net Revenues of the Electric system and the other funds pledged therefore under the Indenture.

The pledge of future Electric Fund Net Revenues ends upon repayment of the \$1.3 million in remaining debt service on the bonds which is scheduled to occur in 2021. For fiscal year 2009, Net Revenues, including operating revenues and non-operating interest earnings, amounted to \$131.791 million; and operating costs include operating expenses but not interest, depreciation or amortization and amounted to \$106.263 million. Net Revenues available for debt service amounted to \$25.528 million which represented coverage of 255.28 times over the \$0.1 million in debt service.

State Water Resources Loan – In October 2007, the City approved the \$9.0 million loan agreement with State Water Resources Control Board (SWRCB) to finance the City’s Mountain View/Moffett Area reclaimed water pipeline project. Under the terms of the contract, the City has agreed to repay \$9.0 million to the State in exchange for receiving \$7.5 million in proceeds to be used to fund the Project. The difference between the repayment obligation and proceeds amounts to \$1.5 million and represents in-substance interest on the outstanding balance. Loan proceeds are drawn down as the project progresses and debt service payments commence on June 30, 2010. Concurrently with the loan, the City entered into various other agreements including a cost sharing arrangement with the City of Mountain View. Pursuant to that agreement, City of Mountain View agreed to finance a portion of the project with a \$5 million loan repayable to the City. This loan has been recorded as “Due from other government agencies” in the accompanying financial statements.

Debt Service Requirements (in thousands):

Debt service and capitalized lease requirements are shown below for all long-term debt.

For the Year Ending June 30	Governmental Activities			Business-Type Activities		
	Principal	Interest	Total	Principal	Interest	Total
2010	\$840	\$381	\$1,221	\$2,205	\$1,955	\$4,160
2011	870	345	1,215	2,280	1,880	4,160
2012	905	305	1,210	2,365	1,800	4,165
2013	530	264	794	2,455	1,713	4,168
2014	555	234	789	2,540	1,620	4,160
2015 -2019	3,285	689	3,974	14,314	6,493	20,807
2020 -2024	620	82	702	17,435	3,174	20,609
2025 -2029				5,450	242	5,692
Total	<u>\$7,605</u>	<u>\$2,300</u>	<u>\$9,905</u>	<u>49,044</u>	<u>\$18,877</u>	<u>\$67,921</u>

Reconciliation of long-term debt

Less unamortized original issue discount	<u>(2,479)</u>
Net long-term debt	<u>\$46,565</u>

Debt Call Provisions

Long-term debt as of June 30, 2009 is callable on the following terms and conditions:

	<u>Initial Call Date</u>	
<i>Governmental Activities Long Term Debt</i>		
1998 Certificates of Participation	09/01/2008	(3)
2002B Certificates of Participation	03/01/2011	(2)
<i>Business-Type Activities Long Term Debt</i>		
Utility Revenue Bonds -		
1999 Refunding	06/01/2009	(1)
2002 Series A	06/01/2012	(1)

- (1) Callable in inverse numerical order of maturity at par plus a premium of 2.0 percent beginning on the initial call date. The call price declines subsequent to the initial date.
- (2) Callable in any order specified by the City at par plus a premium of 1.0 percent beginning on the initial call date. The call price declines subsequent to the initial date.
- (3) Callable in any order specified by the Trustee at par plus a premium of 1.0 percent beginning on the initial call date. The call price declines subsequent to the initial date.

Leasing Arrangements

COPs and Capital Leases are issued for the purpose of financing the construction or acquisition of projects defined in each leasing arrangement. Projects are leased to the City for lease payments which, together with unspent proceeds of the leasing arrangement, will be sufficient to meet the debt service obligations of the leasing arrangement. At the termination of the leasing arrangement, title to the project will pass to the City.

Leasing arrangements are similar to debt; they allow investors to participate in a share of guaranteed payments which are made by the City. Because they are similar to debt, the present value of the total of the payments to be made by the City is recorded as long-term debt. The City’s leasing arrangements are included in long-term obligations discussed above.

Conduit Financing

On December 15, 1996, the City acted as a financial intermediary in order to assist Lytton Gardens Health Care Center in issuing Insured Revenue Refunding Bonds. The Bonds are payable solely from revenues collected by Lytton Gardens Health Care Center. The City has not included these Bonds in its basic financial statements since it is not legally or morally obligated for the repayment of the Bonds. At June 30, 2009, the amount of Bonds outstanding was \$7.4 million.



Long-term Debt without City Commitment

On July 23, 2007, the City approved the issuance of two variable rate demand Tax-Exempt Revenue Bonds by the ABAG Finance Authority in the amounts of \$160 million and \$180 million for the construction of Albert L. Schultz Jewish Community Center and a new continuing care retirement community, respectively. The Debt is payable by the borrowers, Albert L. Schultz Jewish Community Center and 899 Charleston, LLC. The City has no legal or moral liability with respect to the payment of these debts.



Note 8.....

SPECIAL ASSESSMENT DEBT Special Assessment Debt with no City Commitment

The California Avenue Parking Assessment District No. 92-13 issued Assessment Bonds of 1993, but the City has no legal or moral liability with respect to the payment of this debt, which is secured only by assessments on the properties in this District. Therefore, this debt is not included in Governmental Activities long-term debt of the City. At June 30, 2009, the District’s outstanding debt amounted to \$1.0 million.

The University Avenue Area Off-Street Parking Assessment District issued Assessment Bonds of Series 2001-A, but the City has no legal or moral liability with respect to the payment of this debt, which is secured only by assessments on the properties in the District. Therefore, this debt is not included in Governmental Activities long-term debt of the City. At June 30, 2009, the District’s outstanding debt amounted to \$8.14 million. A portion of the proceeds from the 2001 Bonds amounting to \$3.2 million was used to defease the 1977 University Avenue Area Off-Street Parking Assessment District Bonds and the 1989 University Avenue Area Off-street Parking Assessment District Refunding and Improvement Bonds.

The University Avenue Area Off-Street Parking Assessment District issued Assessment Bonds of Series 2002-A, but the City has no legal or moral liability with respect to the payment of this debt, which is secured only by assessments on the properties in the District. Therefore, this debt is not included in Governmental Activities long-term debt of the City. As of June 30, 2009, \$0.8 million of the bonds were called and the remaining outstanding debt amounted to \$28 million.



Note 9.....

LANDFILL CLOSURE AND POST-CLOSURE CARE

State and Federal laws and regulations require the City to properly close the Palo Alto Refuse Disposal Site (Palo Alto Landfill) after it stops accepting waste by constructing a final cover on top of the approximately 126 acre landfill to cap the wastes and to perform certain maintenance and monitoring activities at the site for a minimum of thirty years after closure. The first section of the landfill closed in 1991 was a 29 acre section designated “Phase I” costing \$1.6 million. Phase I was subsequently converted to a pastoral park (Byxbee Park) and opened to the public. The remaining sections of the landfill are designated as Phase IIA (22.5 acres closed in 1992 for \$904 thousand), Phase IIB (23.2 acres closed in 2000 for \$1.2 million) and Phase IIC a 51.2 acre active area currently being filled. Phase IIC is currently expected to be filled by 2011 and is projected for closure in 2012. The 30 years of post-closure maintenance costs will be paid after the State certifies the Phase IIC closure (expected in early 2013).

In accordance with State regulations, a final closure and post-closure maintenance plan was produced by a consultant and submitted to State and local regulatory agencies earlier this year. As part of this plan the City’s consultant updated cost forecasts for both the remaining Phase IIC closure and for the 30 year post-closure maintenance activities.

Landfill closure and post-closure liabilities for fiscal years 2009 and 2008 were \$11.0 million and \$7.9 million, respectively. Currently 97.8 percent of the landfill capacity has been used to date.

The City is required by State and Federal laws and regulations to make annual funding contributions to finance closure and post-closure care. In 2009 for post-closure maintenance, the City changed its financial assurance mechanism from an enterprise fund mechanism to a pledge of revenue agreement with the California Integrated Waste Management Board. The City is in compliance with these requirements for the year ended June 30, 2009, with the establishment of the fully funded liability for this purpose.

Note 10.....

NET ASSETS AND FUND BALANCES

Net Assets

Net assets are the excess of all the City’s assets over all its liabilities, regardless of fund. Net assets are divided into three categories and are described below:

Invested in Capital Assets, net of related debt describes the portion of net assets which is represented by the current net book value of the City’s capital assets, less the outstanding balance of any debt issued to finance these assets.

Restricted describes the portion of net assets which is restricted as to use by the terms and conditions of agreements with outside parties, governmental regulations, laws, or other restrictions which the City cannot unilaterally alter. These principally include bond proceeds received for use on capital projects, debt service requirements, and special revenue programs subject to limitations, defined regulations, and laws underlying such programs.

Unrestricted describes the portion of net assets which is not restricted as to use.

Fund Balances, Reserves and Designations

In the Fund financial statements, fund balances represent the net current assets of each fund. Net current assets generally represent a fund’s cash and receivables, less its liabilities. Portions of a fund’s balance may be reserved or designated for future expenditure.

At June 30, 2009, Governmental Funds reservations and designations included (in thousands):

	Major Funds		
	General Fund	Capital Projects Fund	Non- Major Funds
Reserved for:			
Encumbrances	\$3,659	\$11,247	\$81
Notes and loans	428		8,051
Interfund advances	1,100		
Inventory of materials and supplies	3,173		
Prepaid Items	1,775		
Debt service			1,412
Total Reserved Fund Balance	<u>\$10,135</u>	<u>\$11,247</u>	<u>\$9,544</u>
Unreserved, designated for:			
Unrealized gain on investment	\$2,441		\$541
Equity transfer stabilization	3,636		
Reappropriations	2,265	\$17,744	
Budget stabilization	24,747		
Infrastructure		7,016	
Total Unreserved/Designated Fund Balances	<u>\$33,089</u>	<u>\$24,760</u>	<u>\$541</u>



Reserve for **encumbrances** represents the portion of fund balance set aside for open purchase orders.

Reserves for **notes, loans, interfund advances, inventory of materials and supplies, and prepaid items** are the portions of fund balance set aside to indicate these items do not represent available, spendable resources even though they are a component of assets.

Reserve for **debt service** is the portion of fund balance legally restricted for the payment of principal and interest on long-term liabilities.

Designated for **unrealized gain on investment** is the portion of fund balance set aside for unrealized gains on investment.

Designated for **infrastructure** is the portion of fund balance set aside for use on infrastructure.

Designated for **equity transfer stabilization** is the portion of fund balance to replace required equity transfer by Gas, or Electric Enterprise Funds in the event the fund was unable to make its required equity transfer.

Designated for **reappropriations** is the portion of fund balance set aside for subsequent years' appropriations.

Designated for **budget stabilization** is the portion of fund balance to be used to supplement the regular budget when unexpected events such as state government action, a downturn in the economy or a natural disaster reduces revenue or creates obligations that significantly impact the current-year budget.

Internal Service Funds

At June 30, 2009, internal service fund net assets designations included (in thousands):

	Vehicle Replacement and Maintenance	Technology	Printing and Mailing Services	General Benefits and Insurance	Retiree Health Benefit	Total
Reserved net assets						
Commitments	\$1,248	\$1,266	\$9	\$461		\$2,984
Unreserved:						
Designated for:						
Future catastrophic losses				20		20
Retiree health care					\$26,362	26,362
Capital projects	2,340	6,868				9,208
Operating software replacement		180				180
Undesignated		52	75			127
	<u>\$3,588</u>	<u>\$8,366</u>	<u>\$84</u>	<u>\$481</u>	<u>\$26,362</u>	<u>\$38,881</u>

Reserve for **commitments** represents the portion of net assets set aside for open purchase orders.

Designated for **future catastrophic losses** is the portion of net assets to be used for unforeseen future losses.

Notes to Basic Financial Statements – Note 10

Designated for **retiree health care** represents the portion of net assets set aside to defer future costs of retiree health care coverage.

Designated for **capital projects** represents the portion of net assets set aside for adopted capital projects.

Designated for **operating software replacement** represents the portion of net assets set aside to defer future costs for operating software replacement.

Enterprise Funds

At June 30, 2009, Enterprise Fund net assets (in thousands):

	Water	Electric	Fiber Optics	Gas	Wastewater Collection	Wastewater Treatment	Refuse	Storm Drainage	Total
Unrestricted									
Rate stabilization									
Supply		\$41,442		\$8,733					\$50,175
Distribution		6,341		4,449					10,790
Operations	\$5,400		\$6,436		\$6,001	(\$15,602)	(\$2,844)	(\$1,098)	(1,707)
	5,400	47,783	6,436	13,182	6,001	(15,602)	(2,844)	(1,098)	59,258
Emergency plant									
replacement	1,000	1,000	1,000	1,000	1,000	2,160			7,160
Calaveras		64,535							64,535
Reappropriations	19,701	8,051	411	8,295	5,529	15,486	1,980	2,103	61,556
Commitments	410	2,849	196	3,769	1,593	10,812	1,041	203	20,873
Underground loan		717							717
Refuse Water							650		650
Resources Board									
Public benefit									
program		4,280							4,280
Central Valley Project		153							153
Debt Portion	108			132					240
	<u>\$26,619</u>	<u>\$129,368</u>	<u>\$8,043</u>	<u>\$26,378</u>	<u>\$14,123</u>	<u>\$12,856</u>	<u>\$827</u>	<u>\$1,208</u>	<u>\$219,422</u>
Restricted for Debt Service	<u>\$780</u>			<u>\$952</u>					<u>\$1,732</u>

As of July 1, 2008, the City recategorized the Fiber Optics enterprise Fund separately from the Electric Enterprise Fund. The effect of this change was to reflect Net Assets of \$12.265 million for the Fiber Optics Fund and to reduce Electric Fund Net Assets by a like amount.

The City Council has committed unreserved net assets for general contingencies, future capital and debt service expenditures including operating and capital contingencies for unusual or emergency expenditures.



Note 11.....

PENSION PLANS

CALPERS Safety and Miscellaneous Employees Plans

Substantially all permanent City employees are eligible to participate in pension plans offered by California Public Employees Retirement System (CALPERS) an agent for multiple employer defined benefit pension plans which acts as a common investment and administrative agent for its participating member employers. CALPERS provides retirement and disability benefits, annual cost of living adjustments and death benefits to plan members, who must be public employees and beneficiaries. The City's employees participate in the Safety (police and fire) and Miscellaneous (all other) Employee Plans. Benefit provisions under both Plans are established by State statute and City resolution. Benefits are based on years of credited service, equal to one year of full-time employment. Funding contributions for both Plans are determined annually on an actuarial basis as of June 30 by CALPERS.

Effective July 1, 2004, the separate Police and Fire Plans were combined into one Safety Plan. Prior actuarial valuation information for Safety is not available, since the plans were combined.

The Plans' provisions and benefits in effect at June 30, 2009, are summarized as follows:

	<u>Safety</u>	<u>Miscellaneous</u>
Benefit vesting schedule	5 years service	5 years service
Benefit payments	monthly for life	monthly for life
Retirement age	50	50
Monthly benefits, as a % of annual salary	3%	1.092-3%
Required employee contribution rates	9%	8%
Required employer contribution rates	23.938%	17.063%

The City's current labor contracts with Safety employees require it to pay employee contributions as well as its own. The Miscellaneous group contributes 2 percent of the employee contributions with the City paying the balance. Miscellaneous employee contributions are collected through payroll deductions and the City remits those contributions to CalPERS.

CALPERS determines contribution requirements using a modification of the Entry Age Normal Method. Under this method, the City's total normal benefit cost for each employee from date of hire to date of retirement is expressed as a level percentage of the related total payroll cost. Normal benefit cost under this Method is the level amount the employer must pay annually to fund an employee's projected retirement benefit. This level percentage of payroll method is used to amortize any unfunded actuarial liabilities. The actuarial assumptions used to compute contribution requirements are also used to compute the actuarial accrued liability. The City does not have a net pension obligation since it pays these actuarially required contributions monthly.

CALPERS uses the market related value method of valuing the Plan’s assets. An investment rate of return of 7.75 percent is assumed, including inflation at 3 percent. Annual salary increases are assumed to vary by duration of service. Changes in liability due to plan amendments, changes in actuarial assumptions, or changes in actuarial methods are amortized as a level percentage of payroll on a closed basis over twenty years. Investment gains and losses are tracked and amortized over 30 years.

The Plans’ actuarial value (which differs from market value) and funding progress over the most recently available three years is set forth below at their actuarial valuation date of June 30, 2007 (in thousands):

Safety Plan:

<i>Actuarial</i>						
Valuation Date	Entry Age Accrued Liability	Value of Assets	Unfunded (Overfunded) Liability	Funded Ratio	Annual Covered Payroll	Unfunded (Overfunded) Liability as a % of Payroll
2005	\$213,683	\$189,821	\$23,862	88.8%	\$18,953	125.9%
2006	230,186	202,408	27,778	87.9%	20,469	135.7%
2007	242,952	216,499	26,453	89.1%	20,907	126.5%

Miscellaneous Plan:

<i>Actuarial</i>						
Valuation Date	Entry Age Accrued Liability	Value of Assets	Unfunded (Overfunded) Liability	Funded Ratio	Annual Covered Payroll	Unfunded (Overfunded) Liability as a % of Payroll
2005	\$339,641	\$287,139	\$52,502	84.5%	\$60,954	86.1%
2006	363,774	311,105	52,669	85.5%	61,265	86.0%
2007	408,625	350,543	58,082	85.8%	61,883	93.9%

* On November 13, 2006, the City Council voted to increase the pension benefit for miscellaneous employees from 1.426-2.418 % to 2.0-2.7% effective the pay period inclusive of January 06, 2007. CALPERS revised the fiscal 2004-05 actuarial data for the impacts of this benefit enhancement.

Audited annual financial statements and ten-year trend information are available from CALPERS at P.O. Box 942709, Sacramento, CA 94229-2709.

Actuarially-required contributions for all plans for fiscal years 2009, 2008 and 2007 were \$7.6, \$25.5 and \$19.2, million, respectively. The City made these contributions as required, together with certain immaterial amounts required as the result of the payment of overtime and other additional employee compensation.



Note 12.....

RETIREE HEALTH BENEFITS

In addition to providing pension benefits, the City participates in the California Public Employees Medical and Health Care Act program to provide certain health care benefits for retired employees. Employees who retire directly from the City are eligible for retiree health benefits if they retire on or after age 50 with 5 years of service and are receiving a monthly pension from CalPERS.

For employees hired before January 1, 2004, and all PAPOA employees, the City pays for the entire cost of retiree health benefits for retirees for their lifetimes. The City also pays a portion of medical costs for dependents of retirees equal to 80 percent of the premiums for 2009 and increasing 5 percent per year until the City's share reaches 100 percent of dependent premiums for 2013 and beyond.

For management employees, fire fighter and fire chief association members hired on or after January 1, 2004, and service employees hired on or after January 1, 2005, the City pays for 50% of the above-described benefits after 10 years of service, and the city's portion increases by 5% for each additional year of service up to 20 years. For management, fire fighter and fire chief association members who retire on or after January 1, 2006, and for service employees who retire on or after January 1, 2007, the maximum premium amount the City will pay toward health insurance will be equal to the second highest CalPERS Bay Area Basic plan premium (currently the Blue Shield HMO premium).

During fiscal year 2008, the City implemented the provisions of Governmental Accounting Standards Board Statement No. 45, Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions. This Statement establishes uniform financial reporting standards for employers providing postemployment benefits (OPEB). As part of the implementation, the City elected to participate in an irrevocable trust to provide a funding mechanism for the OPEB and to apply the provisions of the statement on a prospective basis. The Trust, California Employers' Retirees Benefit Trust, is administrated by CalPERS and managed by a separately appointed board which is not under the control of City Council. This Trust is not considered a component unit of the City.

Funding Policy and Actuarial Assumptions

The City’s policy is to prefund these benefits by accumulating assets in the Trust Fund discussed above pursuant to City Council Resolution. The annual required contribution (ARC) was determined as part of a January 1, 2007 actuarial valuation using the entry age normal actuarial cost method. This is a projected benefit cost method, which takes into account those benefits that are expected to be earned in the future as well as those already accrued. The actuarial assumptions included (a) 7.75% investment rate of return, (b) 3.25% projected annual salary increase, and (c) 5% health inflation increase. The actuarial methods and assumptions used include techniques that smooth the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets. Actuarial calculations reflect a long-term perspective and actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. The calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing costs between the City and plan members to that point. Actuarially determined amounts are subject to revision at least biannually as results are compared to past expectations and new estimates are made about the future. The City’s OPEB unfunded actuarial accrued liability is being amortized as a level percentage of projected payroll using a 30-year open amortization period.

Generally accepted accounting principles permit assets to be treated as OPEB assets and deducted from the Actuarial Accrued Liability when such assets are placed in an irrevocable trust or equivalent arrangement. During the fiscal year ended June 30, 2009, the City made contributions and drew funds from the Net OPEB asset to fund the current year ARC. As a result, the City has calculated and recorded the Net OPEB Asset, representing the difference between the ARC, amortization and contributions, as presented below:

Annual required contribution	\$7,686
Amortization on the Net OPEB Asset	3,303
Interest on the Net OPEB Asset	(2,260)
Adjustment to annual required contribution	<u>1,043</u>
Annual OPEB Cost	<u>8,729</u>
Contributions made:	
Contributions to OPEB Trust	700
City portion of current year premiums paid	<u>5,204</u>
Contributions less than the ARC	\$2,825
Net OPEB obligation (asset) June 30, 2008	<u>(29,177)</u>
Net OPEB obligation (asset) June 30, 2009	<u><u>(\$26,352)</u></u>

The Plan's annual required contributions and actual contributions for fiscal years ended June 30, 2008 and 2009 are set forth below:

<u>Fiscal Year</u>	<u>Annual OPEB Cost</u>	<u>Actual Contribution</u>	<u>Percentage of OPEB Cost</u>	<u>Net OPEB Asset</u>
6/30/2008	\$9,313	\$38,490	413%	(\$29,177)
6/30/2009	8,729	5,904	67%	(26,352)

The Schedule of Funding Progress presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits. Trend data from the actuarial studies is presented below:

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets</u>	<u>Entry Age Actuarial Accrued Liability</u>	<u>Unfunded Actuarial Accrued Liability</u>	<u>Funded Ratio</u>	<u>Covered Payroll</u>	<u>Unfunded Actuarial Liability as Percentage of Covered Payroll</u>
1/1/2007		\$102,237	(\$102,237)	0%	\$97,600	(104.8%)
1/1/2009	\$24,616	129,661	(105,045)	18.98%	98,940	(106.2%)

In the fiscal year ended June 30, 1993, the City received a \$6.1 million refund from the California Public Retirement System ("CALPERS") through the passage of Assembly Bill (AB) 702. This amount was placed in a separate fund to defer future costs of retiree health care coverage. During the fiscal year ended June 30, 1995, the City established and transferred the amount to a separate fund which is now accounted for as an Internal Service Fund.

The Retiree Fund's net assets consist of the following for the fiscal year ended June 30, 2009 (in thousands):

<u>Retiree Health Benefits</u>	<u>2009</u>	<u>2008</u>
Net assets, beginning of year	\$29,756	\$30,719
Interest earnings	50	970
Unrealized gain (loss) on investments	(202)	567
Interdepartmental charges	5,785	7,133
Compensated benefits	(8,963)	(9,569)
Transfers in	(64)	(64)
	<u>\$26,362</u>	<u>\$29,756</u>
Net assets, end of year		



Note 13.....

DEFERRED COMPENSATION PLAN

City employees may defer a portion of their compensation under City sponsored Deferred Compensation Plans created in accordance with Internal Revenue Code Section 457. Under these Plans, participants are not taxed on the deferred portion of their compensation until distributed to them; distributions may be made only at termination, retirement, death or in an emergency as defined by the Plans.

The laws governing deferred compensation plan assets now require plan assets to be held by a Trust for the exclusive benefit of plan participants and their beneficiaries. Since the assets held under these plans are not the City’s property and are not subject to City control, they have been excluded from these financial statements.

Note 14.....

RISK MANAGEMENT

Coverage

The City provides dental coverage to employees through programs which are administered by a service agent. The City is self-insured for the dental coverage.

The City has a workers’ compensation insurance policy with coverage up to the statutory limit set by the State of California. The City retains the risk for the first \$500 thousand in losses for each accident and employee under this policy.

The City also has public employee dishonesty insurance with a \$5 thousand deductible and coverage up to \$1.0 million per loss. The City’s property and machinery insurance policy has various deductibles and various coverages based on the kind of machinery.

The City is a member of the Authority for California Cities Excess Liability (ACCEL) which provides general liability, including auto liability, insurance coverage up to \$45.0 million per occurrence. The City retains the risk for the first \$1.0 million in losses for each occurrence under this policy.

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

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



During the fiscal year ended June 30, 2009, the City contributed \$730 thousand to ACCEL for current year coverage.

Audited financial statements are available from ACCEL at 160 Spear Street, San Francisco, California 94105-2709.

Claims Liability

The City provides for the uninsured portion of claims and judgments in the General Benefits and Insurance Internal Service Fund. Claims and judgments, including a provision for claims incurred but not reported, are recorded when a loss is deemed probable of assertion and the amount of the loss is reasonably determinable. As discussed above, the City has a coverage for such claims, but it has retained the risk for the deductible or uninsured portion of these claims.

The City’s liability for uninsured claims is limited to dental, general liability, and workers’ compensation claims, as discussed above, and was estimated by management based on prior years’ claims experience as follows as of June 30 (in thousands):

	<u>Year Ended June 30</u>	
	<u>2009</u>	<u>2008</u>
Beginning Balance	\$23,526	\$21,130
Liability for current and prior fiscal year claims and claims incurred but not reported (IBNR)	1,987	6,466
Claims paid	<u>(4,075)</u>	<u>(4,070)</u>
Ending Balance	<u>\$21,438</u>	<u>\$23,526</u>
Current Portion	<u>\$5,855</u>	<u>\$7,356</u>



Note 15.....

JOINT VENTURES

General

The City participates in joint ventures through Joint Powers Authorities (JPAs) established under the Joint Exercise of Powers Act of the State of California. As separate legal entities, these JPAs exercise full powers and authorities within the scope of the related Joint Powers Agreement, including the preparation of annual budgets, accountability for all funds, the power to make and execute contracts and the right to sue and be sued. Obligations and liabilities of the JPAs are not those of the City.

Each JPA is governed by a board consisting of representatives from each member agency. Each board controls the operations of its respective JPA, including selection of management and approval of operating budgets, independent of any influence by member agencies beyond their representation on the Board.

Northern California Power Agency

The City is a member of Northern California Power Agency (NCPA), a joint powers agency which operates under a joint powers agreement among fifteen public agencies. The purpose of NCPA is to use the combined strength of its members to purchase, generate, sell and interchange electric energy and capacity through the acquisition and use of electrical generation and transmission facilities. Each agency member has agreed to fund a pro rata share of certain assessments by NCPA and enter into take-or-pay power supply contracts with NCPA. While NCPA is governed by its members, none of its obligations are those of its members unless expressly assumed by them.

During the year ended June 30, 2009, the City incurred expenses totaling \$79.1 million for purchased power and assessments earned by NCPA.

The City’s interest in NCPA projects and reserves, as computed by NCPA, was \$3.3 million at June 30, 2009. This amount represents the City’s portion of funds which resulted from the settlement with third parties of issues with financial consequences and reconciliations of several prior years’ budgets for programs. It is recognized that all the funds credited to the City are linked to the collection of revenue from the City’s ratepayers, or to the settlement of disputes relating to electric power supply and that the money was collected from the City’s ratepayers to pay power bills. Additionally, the NCPA Commission identified and approved the funding of specific reserves for working capital, accumulated employees post-retirement medical benefits, and billed property taxes for the geothermal project. The Commission also identified a number of contingent liabilities that may or may not be realized, the cost of which in most cases is difficult to estimate at this time. One such contingent liability is the steam field depletion which will require funding to cover debt service and operational costs in excess of the expected value of the electric power. The General Operating Reserve is intended to minimize the number and amount of individual reserves needed for each project, protect NCPA’s financial condition and maintain its credit worthiness. These funds are available on demand, but the City has left them with NCPA as a reserve against these contingencies identified by NCPA.



Members of NCPA may participate in an individual project of NCPA without obligation for any other project. Member assessments collected for one project may not be used to finance other projects of NCPA without the member's permission.

Geothermal Projects

A purchased power agreement with NCPA obligated the City for 6.2 percent and 6.2 percent, respectively, of the operating costs and debt service of the two NCPA 110-megawatt geothermal steam powered generating plants, Project Number 2 and Project Number 3.

The City's participation in the Geothermal Project was sold to Turlock Irrigation District in October 1984. Accordingly, the City is liable for payment of outstanding geothermal related debt only in the event that Turlock fails to make specified payments. Total outstanding debt of the NCPA Geothermal Project at June 30, 2009 is \$128 million. The City's participation in this project was 6.2 percent, or \$7.9 million.

NCPA's Geothermal Project has experienced a greater than originally anticipated decline in steam production from geothermal wells on its leasehold property. Results of the continuing well analysis program indicate that the potential productive capacity of the geothermal steam reservoir is less than originally estimated. Therefore, NCPA has modified the operations of the Geothermal Project to reduce the average annual output from past levels. As a result, the per unit cost of energy generated by the projects will be higher than anticipated.

NCPA will continue to monitor the wells while pursuing alternatives for improving and extending reservoir performance, including supplemental water re-injection, plant equipment modifications, and changes in operating methodology. NCPA, along with other steam field operators, has observed a substantial increase in steam production in the vicinity of re-injection wells and is attempting to increase water re-injection at strategic locations. NCPA, other steam developers, and the Lake County Sanitation District are constructing a wastewater pipeline project that will greatly increase the amount of water available for re-injection.

Calaveras Hydroelectric Project

In July 1981, NCPA agreed with Calaveras County Water District to purchase the output of the North Fork Stanislaus River Hydroelectric Development Project and to finance its construction. Debt service payments to NCPA began in February 1990 when the project was declared substantially complete and power was delivered to the participants. Under its power purchase agreement with NCPA, the City is obligated to pay 22.9 percent of this Project's debt service and operating costs. At June 30, 2009, the book value of this Project's plant, equipment and other assets was \$498.3 million, while its long-term debt totaled \$491.6 million and other liabilities totaled \$3.8 million. The City's share of the Project's long-term debt amounted to \$113.4 million at that date.

Geothermal Public Power Line

In 1983, NCPA, Sacramento Municipal Utility District, the City of Santa Clara and the Modesto Irrigation District (joint owners) initiated studies for a Geothermal Public Power Line (GPPL) which would carry power generated at several existing and planned geothermal plants in the Geysers area to a location where the joint owners could receive it for transmission to their load centers. NCPA has an 18.5 percent share of this Project and the City has an 11.1 percent participation in NCPA's share. In 1989, the development of the proposed Geothermal Public Power Line was discontinued because NCPA was able to contract for sufficient transmission capacity to meet its needs in the Geysers.

However, because the project financing provided funding for an ownership interest in a PG&E transmission line, a central dispatch facility and a performance bond pursuant to the Interconnection Agreement with PG&E, as well as an ownership interest in the proposed GPPL, NCPA issued \$16.0 million in long-term, fixed-rate revenue bonds in November 1989 to defease the remaining variable rate refunding bonds used to refinance this project. The City is obligated to pay its 11.1 percent share of the related debt service, but debt service costs are covered through NCPA billing mechanisms that allocate the costs to members based on use of the facilities and services.

At June 30, 2009, the book value of this Project’s plant, equipment and other assets was \$1.7 million, while its long term debt totaled \$875 thousand. The City’s share of the Project’s long-term debt amounted to \$97 thousand at that date.

NCPA Financial Information

NCPA’s financial statements can be obtained from NCPA, 180 Cirby Way, Roseville, CA 95678.

Transmission Agency of Northern California (TANC)

The City is a member of a joint powers agreement with 14 other entities in the Transmission Agency of Northern California (TANC). TANC’s purpose is to provide electrical transmission or other facilities for the use of its members. While governed by its members, none of TANC’s obligations are those of its members unless expressly assumed by them. The City was obligated to pay 4.0 percent of TANC’s debt-service and operating costs. However, a Resolution was approved authorizing the execution of a Long-Term Layoff Agreement (LTLA) between the Cities of Palo Alto and Roseville. These two agencies desired to “layoff” their entitlement rights to the California-Oregon Transmission Project (COTP), (and Roseville’s South of Tesla entitlement rights), for a period of 15 years to those acquiring Members (Sacramento Municipal Utility District, Turlock Irrigation district, and Modesto Irrigation District). The effective date of this Agreement was February 1, 2009. As a result, the City is obligated to pay zero percent of TANC’s debt-service and operating costs starting February 1, 2009 for a period of fifteen years.

According to the 1985 Project Agreement with TANC for the development of the California-Oregon Transmission Project (COTP) and subsequent related project agreements, the City is obligated to pay its share of the project’s costs, including debt service, and is entitled to the use of a percentage of the project’s transmission or transfer capacity. TANC has issued four series of Revenue Bonds and Commercial Paper Notes totaling \$435.8 million as of June 30, 2009. The City’s share of this debt is zero due to the LTLA mentioned above.

Construction of the COTP was complete as of June 30, 1993. The transmission line was energized March 24, 1993. Because funding of certain participants’ shares in the project was needed pending approval of their applications for participation, TANC issued \$93.8 million of Commercial Paper debt backed by a Letter of Credit. The City’s share of the Commercial Paper was zero at June 30, 2009, due to the LTLA mentioned above. Shares and obligations of the existing participants could increase pending final project subscription.

TANC Financial Information

TANC’s financial statements can be obtained from TANC, P.O. Box 15129, Sacramento, CA 95851.

Note 16.....

COMMITMENTS AND CONTINGENCIES

Palo Alto Unified School District – The City leases a portion of the former Cubberley School site and eleven extended day care sites from the Palo Alto Unified School District (PAUSD). The lease is part of a larger agreement which includes a covenant not to develop certain properties owned by the PAUSD. The lease term expired in December 2004, with an option for an additional ten-year term. The City renewed the lease for 10 years in 2005, with the lease expiring in 12/31/2014. In December 2014, the City has an option for an additional five-year term to expire on 12/31/2019. The City's rent for the facilities is \$5.0 million per year plus insurance, repairs and maintenance work to be completed, which are not to exceed \$250 thousand per year. This lease is cancelable upon 90 days' written notice in the event funds are not appropriated by the City. In addition, the lease is contingent upon authorization by the Palo Alto electorate if it exceeds the City's Proposition 4 (Gann) appropriations limitation in any fiscal year. Lease expenditures for the year ended June 30, 2009 amounted to \$6.6 million.

Future minimum annual lease and covenant payments are as follows (in thousands):

<u>Year ending June 30:</u>	<u>Payments</u>
2010	6,669
2011	6,878
2012	7,084
2013	7,297
2014	7,516
2015-2019	<u>41,092</u>
	<u><u>\$76,536</u></u>

Palo Alto Sanitation Company – In 1999 the City, under the provisions of a new agreement, contracted with the Palo Alto Sanitation Company (PASCO) for services related to residential and commercial refuse collection, curbside recycling, and other operation special programs. The new agreement has a term of seven years and ten months from the effective date of September 1, 1999. The new contract revised the method by which compensation is paid to PASCO to be more in-line with the industry standard. The method establishes compensation based on the relationship between costs and profits and includes periodic performance reviews. In 2008-09 this resulted in payments to PASCO of \$9.5 million.

City of Palo Alto Regional Water Quality Control Plant – The cities of Palo Alto, Mountain View and Los Altos (the Partners) participate jointly in the cost of maintaining and operating the City of Palo Alto Regional Water Quality Control Plant and related system (the Plant). The City is the owner and administrator of the Plant which provides the transmission, treatment and disposal of sewage for the Partners. The cities of Mountain View and Los Altos are entitled to use a portion of the capacity of the Plant for a specified period of time. Each partner has the right to rent unused capacity from/to the other partners. The expenses of operations and maintenance are paid quarterly by each partner based on its pro rata share of treatment costs. Additionally, joint system revenues are shared by the partners in the same ratio as expenses are paid. The amended agreement has a term of fifty years beginning from the original signing in October 1968, but may be terminated by any partner upon ten years' notice to the other partners. All sewage treatment property, plant and equipment are included in the Wastewater Treatment Enterprise Fund's capital assets balance at June 30, 2009. If the City initiates the termination of the contracts, it is required to pay the other partners their unamortized contribution towards the capital assets.

Solid Waste Materials Recovery and Transfer Station (SMaRT Station) – On June 9, 1992, the City, along with the City of Mountain View, signed a Memorandum of Understanding (MOU) with the City of Sunnyvale (Sunnyvale) to participate in the construction and operation of the SMaRT station which recovers recyclable materials from the municipal solid waste delivered from participating cities. Per the MOU, the City has capacity share of 21.3 percent of this facility and reimburses its proportionate capacity share of design, construction, and operation costs to Sunnyvale.

On December 1, 1992, the Sunnyvale Financing Authority issued \$24.6 million in revenue bonds to finance the design and construction costs of the SMaRT Station. During the fiscal year ending June 30, 2003, the 1992 bonds were refunded by issuing the 2003 Solid Waste Revenue Bonds in the amount of \$20.6 million. Even though these bonds are payable from and secured by the net revenues of Sunnyvale’s Utilities Enterprise, the City is obligated to reimburse Sunnyvale 21.3 percent of total debt service payments related to these bonds. The City’s portion of remaining principal balance for SMaRT revenue bonds as of June 30, 2009 is \$2.9 million. During the year ended June 30, 2009, the City paid \$413.2 thousand as its portion of current debt service.

In fiscal 2007-08, the members agreed to finance an Equipment Replacement Project from existing reserves and proceeds from the Solid Waste Revenue Bond, Series 2007. The City has committed to repay 27.8 percent of the remaining debt service on the Bonds. The City’s portion of the Bonds amounts to \$2.1 million as of June 30, 2009.

UTILITIES ENERGY RESOURCE MANAGEMENT

Energy Markets in the United States and California

U.S. and California electric and gas prices continued to be volatile during the year. The City purchased electricity in fiscal year 2009 in conformance with the Council-approved Long-term Electric Acquisition Plan (LEAP) established in 2001 and last modified in March 2007. Due to the City’s commodity purchase strategy, whereby purchases are made on a 3-year forward basis in a laddered fashion, the City’s electric and gas utility customers enjoyed stable rates in fiscal year 2009 compared to what they would have paid if exposed to volatile market prices during the year. The City’s average natural gas commodity cost for the gas pool customers was \$8.30/MMBtu compared to a spot market price of \$5.81/MMBtu. The primary reason the City’s natural gas costs were higher than market was due to a dramatic drop in spot market prices in fiscal year 2009 after gas had been purchased and costs were locked in. The City’s average wholesale electric commodity purchase cost during the fiscal year was approximately 5.6 ¢/kWh while the average spot market prices were approximately 5.3 ¢/kWh. The primary reason the electric costs were higher than market prices was due to a lack of availability of low-cost hydroelectric power.

Due to the dry hydrologic conditions in 2007 and 2008, the hydroelectric supplies were at low levels during the year and resulted in the need for the City to purchase high-cost power during the year from the market. Hydro-electric production accounted for only 36 percent of the City’s electric supply in fiscal year 2009 instead of 50 percent in a normal hydrologic year. These hydroelectric supplies derive from two sources – from contract with the Western Area Power Administration and from the City’s partial ownership of the Calaveras Hydroelectric Project. Wind and landfill gas resources accounted for 13 percent of the electric supply in fiscal year 2009, with the balance purchased from the wholesale electric market. The City transacts with qualified suppliers for the market purchases; and the Northern California Power Agency (NCPA), which provides scheduling services for the City, buys and sells electricity within the month as needed to meet the City’s demands.

Incidental sales of surplus energy resulted in revenues of \$3.31 million during the year. (The expense associated with the surplus energy sold from the overall electric supply portfolio was calculated at \$3.30 million during the year, and is shown separately on the Statement of Revenues, Expenses and Changes in Net Assets.)

During fiscal year 2009, the City executed a 15-year assignment of its full share of ownership and obligations in the California Oregon Transmission Project (COTP). The assignment resulted in lower cost to serve the City’s electric rate payers in fiscal year 2009 and is projected to continue saving the City throughout the term of the assignment.

The California Independent System Operation (CAISO) is authorized to allocate to all electric load serving entities, including publicly-owned utilities such as the City, the cost responsibility for the local generation capacity required to maintain transmission reliability on the CAISO-controlled electric grid. This is expected to result in higher costs to Palo Alto’s electric utility customers.

The City has executed Electric and Gas Master Agreements with suppliers to procure electricity and natural gas supplies. The table below outlines the electric and natural gas commodity supply commitments made by the City with these suppliers as of June 30, 2009. Monthly payments are made to suppliers upon delivery of supplies for the month. The City’s procurement plans conform to the Council-approved Energy Risk Management Policies. These include a formal oversight role (Middle Office) within the Administrative Services Department. A quarterly energy risk management report is provided to the Council as part of this oversight role.

Forward Electricity Commodity Supply Commitments as of June 30, 2009

Supplier	FY 2010	FY 2011	FY 2012	Total
JPMorgan Chase	\$ 5,413,894	\$ -	\$ -	\$ 5,413,894
Powerex	\$ 2,965,260	\$ 2,911,951	\$ 3,078,794	\$ 8,956,005
Sempra	\$ 1,520,737	\$ 2,595,575	\$ -	\$ 4,116,312
SENA	\$ 8,737,635	\$ 2,982,150	\$ -	\$ 11,719,785
	\$ 18,637,526	\$ 8,489,676	\$ 3,078,794	\$ 30,205,996
Average Cost (cents/kWh)	5.27 ¢	5.53 ¢	5.58 ¢	5.37 ¢

Forward Natural Gas Commodity Supply Commitments as of June 30, 2009

Supplier	FY 2010	FY 2011	FY 2012	Total
BP	\$ 2,760,020	\$ 4,016,657	\$ 2,004,405	\$ 8,781,083
Powerex	\$ 3,425,610	\$ 568,295	\$ 768,135	\$ 4,762,040
Sempra	\$ 3,016,282	\$ 1,080,832	\$ 645,190	\$ 4,742,305
SENA	\$ 6,709,356	\$ 8,612,848	\$ 1,390,920	\$ 16,713,123
	\$ 15,911,268	\$ 14,278,632	\$ 4,808,650	\$ 34,998,551
Average Cost (\$/MMBtu)	\$7.72	\$7.86	\$7.16	\$7.70

The City’s natural gas transportation contract with the Pacific Gas and Electric Company (PG&E) went into effect starting January 1, 2008, and will be in place until the end of 2010. This contract, commonly known as Gas Accord IV, between PG&E and its transportation customers provides the City’s retail customers stable transportation costs. This contract is not substantially different from the last agreement that went into effect in 2005.



Future Outlook

Electric

The market price for fossil fuel based electricity is projected to be relatively low for the next 12 months – at 4 to 6¢/kWh – but in the longer term it is expected to return to a higher level of 6 to 8¢/kWh. The price premium commanded by renewable energy projects has increased considerably in the last year and is expected to remain high in the foreseeable future. The higher prices will result in higher costs to meet the City’s renewable energy supply targets.

The Council increased the renewable resource supply targets in March 2007. The current target is to meet 20 percent of the Citywide load with renewable resource supplies by 2008, 30 percent by 2012, and 33 percent by 2015. Though the City has made considerable progress in securing renewable energy supplies, due to; the unavailability of short-term renewable energy supplies, delay in start date for projects for which commitments have already been made and a large demand for renewable energy supplies in the Western U.S., the City fell slightly short of meeting the 20 percent target for 2008. Renewable supplies accounted for approximately 17 percent of supplies during calendar year 2008 with short-term purchases accounting for about 3 percent. Going forward, the portion of the City’s electricity demand met by renewable supplies is expected to remain at 17 percent in calendar year 2009 before rising to 19 percent in 2010 and 22 percent in 2011.

PaloAltoGreen, the City’s volunteer green power program, currently accounts for an additional 6 percent of the City’s energy needs from renewable resources. The City is also in the process of implementing a program to encourage small-scale ultra-clean distributed generation and cogeneration applications within the city. Additionally, the City is in the process of reviewing all utility programs, including PaloAltoGreen, to ensure that programs are aligned to reduce greenhouse gas emissions associated with the City’s energy supplies.

The CAISO implemented its Market Redesign and Technology Update (MRTU) in April 2009. MRTU introduced a number of initiatives with the stated goals of reliable and efficient operation of the transmission grid. An underlying component of MRTU is the use of location-specific prices for the scheduling of energy transactions, which could lead to cost increases for transmission services for the City.

The City continues to follow the development of laws and associated regulations related to implementation of AB 32 (California Global Warming Solutions Act of 2006, Chaptered 9/27/2006). In December 2008, the California Air Resources Board (CARB) approved the Scoping Plan, which is the primary guidance document for shaping how California will reduce its greenhouse gas (GHG) emissions to 1990 levels by 2020 as called for by AB 32. The scoping plan has a range of GHG reduction actions which include direct regulations, alternative compliance mechanisms, monetary and non-monetary incentives, voluntary actions, market-based mechanisms such as a cap-and-trade system, and an AB 32 cost of implementation fee regulation to fund the program. CARB is tasked with completing the majority of the work in designing the implementation details by December 31, 2010, with most regulations and other initiatives adopted by the start of 2011. This means more than 20 Scoping Plan measures are planned to be adopted by ARB in 2009 and 2010.

Natural Gas

Long-term market prices for natural gas have fallen to just under \$0.70 per therm. While declining production in the U.S. and Canada and increasing U.S. and international demand resulting from economic recovery may put pressure on gas prices in the long term, over supply and low demand are forecasted for the next two years. Market price volatility is expected to remain high in the short term due to the uncertainty in the financial markets. The City expanded the gas laddering strategy from 3 to 5 years using both fixed-price and capped-price products to hedge the gas utility supply portfolio. The City will also examine additional strategies to control commodity cost.



In February 2008, Council approved a new plan to implement a voluntary customer program similar to PaloAltoGreen for non-fossil fuel gas supplies. The City is in the process of evaluating biomethane supply resources for the program.

Water

The City's water use during fiscal year 2009 decreased about 8.5 percent from the prior year. Usage is highly dependent on weather conditions, but has remained essentially flat for the past 10 years. Current water usage is only 65 percent of what it was in 1975. The drop in usage in fiscal year 2009 may be attributed to customer response to the call for water conservation due to dry conditions that was issued in April 2008 by the San Francisco Public Utilities Commission (SFPUC). Because of the lower water usage, water supply costs for fiscal year 2009 increased only 1 percent from fiscal year 2008, even though there was a 10 percent increase in the wholesale water rate in fiscal year 2009.

Water supply costs are expected to trend upward as the SFPUC implements a much delayed, but essential, upgrade to the regional water system facilities, the Water System Improvement Program (WSIP). Costs for the WSIP are now expected to be about \$4.5 billion. Estimates for these increased costs have been factored into the City's long-term water supply cost projections.

Palo Alto is a member of the Bay Area Water Supply and Conservation Agency (BAWSCA), which represents all the agencies that buy water on a wholesale basis from San Francisco. The relationship between each of the BAWSCA agencies and the City and County of San Francisco is specified in a 25-year water service contract, which expired on June 30, 2009. Each agency, including Palo Alto, has approved a new 25-year Water Supply Agreement with San Francisco effective on July 1, 2009. The new contract contains the same mechanism for cost allocation as in the old contract and the contract has other improvements regarding water quality and fair treatment in water supply emergencies. However, a new supply limitation will require that the BAWSCA agencies work together to reduce long-term demand so that additional diversions from the Tuolumne River are minimized or eliminated.

During fiscal year 2009, the City continued the planning phase for expanding the recycled water distribution system in Palo Alto by completing a Recycled Water Facility Plan. This plan provides more detailed design information on the project. The environmental documents, which are necessary to compete for grant funding opportunities, are expected to be completed in fiscal year 2010.

Contingent Liabilities

Many of the uncertainties faced by the Utilities Department as an aftermath of the 2000-01 energy crisis have been resolved, however, a number of uncertainties remain. The Ninth Circuit Court has determined that the Federal Energy Regulatory Commission (FERC) lacked authority under the Federal Power Act to grant refund relief against governmental agencies, and the United States Supreme Court declined to review that decision. Nonetheless a number of entities ("the California Parties") have filed suit against the NCPA and other municipal utilities seeking refunds for sales made to the CAISO and Power Exchange during the energy crisis. The suit was filed in the Superior Court in Los Angeles in April 2007. Another dispute between the Western Area Power Administration and PG&E regarding PG&E's claim to recover certain CAISO related costs has also not been resolved.

Litigation – The City is subject to litigation arising in the normal course of business. In the opinion of the City Attorney, there is no pending litigation, claims or assessments that are likely to have a material adverse effect on the City's financial condition.



Sales Tax Adjustment - On April 14, 1999, the State Board of Equalization informed the City that it had been allocated and paid \$594 thousand in sales and taxes in error and that the City was obligated to refund these taxes from future sales tax revenues. The City is in process of challenging the Board's findings. However, as of June 30, 2009, the issue had not been settled and the refund had not been returned.

Grant Programs - The City participates in Federal and State grant programs. These programs have been audited by the City's independent accountants in accordance with the provisions of the Federal Single Audit Act amendments of 1996 and applicable State requirements. No cost disallowances were proposed as a result of these audits; however, these programs are still subject to further examination by the grantors and the amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time. The City expects such amounts, if any, to be immaterial.



Non-major Governmental Funds.....

STREET IMPROVEMENT

This fund accounts for revenues received from state gas tax, allocations must be spent on the construction and maintenance of the road network system of the City.

FEDERAL REVENUE

This fund accounts for grant funds received under the Community Development Act of 1974 and HOME Investment Grant Programs, for activities approved and subject to federal regulations.

HOUSING IN-LIEU

This fund accounts for revenues from commercial and residential developers to provide housing under the City's Below Market Rate program.

SPECIAL DISTRICTS

This fund accounts for revenues from parking permits and for maintenance of various parking lots within the City's parking districts.

TRANSPORTATION MITIGATION

This fund accounts for revenues from fees or contributions required for transportation mitigation issues encountered as a result of City development.

LOCAL LAW ENFORCEMENT

This fund accounts for revenues received in support of City's law enforcement program.

ASSETS SEIZURE

This fund accounts for seized property and funds associated with drug trafficking. Under California Assembly Bill No. 4162, the monies are released to the City for specific expenditures related to law enforcement activities.

DEVELOPER'S IMPACT FEE

This fund accounts for fees imposed on new developments to be used for parks, community centers and libraries.

REDEVELOPMENT AGENCY ADMINISTRATION

This fund accounts for the activities of administrating the Redevelopment Agency.

DOWNTOWN BUSINESS IMPROVEMENT DISTRICT

The Downtown Business Improvement District Fund was established to account for the activities of the Palo Alto Downtown Business Improvement District, which was established to enhance the viability of the downtown business district.

GOLF COURSE

This fund accounts for revenues received from the General Fund to provide payment of principal and interest associated with Certificates of Participation issued for the City's golf course.

CIVIC CENTER REFINANCING

This fund accounts for revenues received from the General Fund to provide payment of principal and interest associated with the 2002A Civic Center Refinancing Certificates of Participation as they become due.





Non-major Governmental Funds

DOWNTOWN PARKING IMPROVEMENT

This fund accounts for revenues received from the General Fund to provide payment of principal and interest associated with the 2002B Downtown Parking Improvement Certificate of Participation as they become due.

SPECIAL ASSESSMENT DEBT

This fund accumulates monies for payments of special assessment improvement bonds which are financed by assessments placed on property owners within the University Avenue and California Avenue Parking District.

EYERLY FAMILY

This fund accounts for the revenues received from assets donated by Mr. and Mrs. Fred Eyerly for the City and or its citizenry.



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City of Palo Alto - Non-Major Governmental Funds
Combining Balance Sheets- June 30, 2009
(In thousands of dollars)

	<u>SPECIAL REVENUE FUNDS</u>					
	<u>Street Improvement</u>	<u>Federal Revenue</u>	<u>Housing In-Lieu</u>	<u>Special Districts</u>	<u>Transportation Mitigation</u>	<u>Local Law Enforcement</u>
ASSETS						
Cash and investments:						
Available for operations	\$1,379	\$25	\$3,898	\$852	\$4,127	\$155
Cash and investments with fiscal agent						
Receivables:						
Accounts	85	128				29
Interest	8		62	8	34	2
Notes		4,460	3,591			
Total Assets	<u>\$1,472</u>	<u>\$4,613</u>	<u>\$7,551</u>	<u>\$860</u>	<u>\$4,161</u>	<u>\$186</u>
LIABILITIES						
Accounts payable		\$45	\$196			
Interfund payable		105				\$5
Total Liabilities		<u>150</u>	<u>196</u>			<u>5</u>
FUNDEQUITY						
Reserved for:						
Encumbrances		26	30			20
Notes receivable		4,460	3,591			
Debt service						
Unreserved, designated for:						
Special Revenue Funds						
Unrealized gain on investments	\$26		212	\$26	\$113	5
Special revenue projects			3,522	834	4,048	156
Special revenue reappropriations	854					
Unreserved, undesignated:						
Permanent Fund						
Special Revenue Funds	592	(23)				
Total Fund Balances	<u>1,472</u>	<u>4,463</u>	<u>7,355</u>	<u>860</u>	<u>4,161</u>	<u>181</u>
Total Liabilities and Fund Balances	<u>\$1,472</u>	<u>\$4,613</u>	<u>\$7,551</u>	<u>\$860</u>	<u>\$4,161</u>	<u>\$186</u>



SPECIAL REVENUE FUNDS			DEBT SERVICE FUNDS			
Assets Seizure	Developer's Impact Fee	Redevelopment Agency	Downtown Business Improvement District	Golf Course	Civic Center Refinancing	Downtown Parking Improvement
	\$4,017		\$24	\$13 776	\$16 350	\$7 238
	48		84	12		
	<u>\$4,065</u>		<u>\$108</u>	<u>\$801</u>	<u>\$366</u>	<u>\$245</u>
			\$5			
				\$801	\$366	\$245
	\$159					
	3,906		103			
	4,065		108	801	366	245
	<u>\$4,065</u>		<u>\$108</u>	<u>\$801</u>	<u>\$366</u>	<u>\$245</u>

(Continued)



City of Palo Alto - Non-Major Governmental Funds

Combining Balance Sheets- June 30, 2009

(In thousands of dollars)

	<u>PERMANENT FUND</u>	Total Non-major Governmental Funds
	<u>Eyerly Family</u>	<u></u>
ASSETS		
Cash and investments:		
Available for operations	\$1,305	\$15,818
Cash and investments with fiscal agent		1,364
Receivables:		
Accounts		326
Interest	12	186
Notes		8,051
	<u> </u>	<u> </u>
Total Assets	<u>\$1,317</u>	<u>\$25,745</u>
LIABILITIES		
Accounts payable	\$9	\$250
	<u> </u>	<u>110</u>
Total Liabilities	<u>9</u>	<u>360</u>
FUND EQUITY		
Reserved for:		
Encumbrances		81
Notes receivable		8,051
Debt service		1,412
Unreserved, designated for:		
Special Revenue Funds		
Unrealized gain on investments		541
Special revenue projects		8,560
Special revenue reappropriations		854
Unreserved, undesignated:		
Permanent Fund	1,308	1,308
Special Revenue Funds		4,578
	<u>1,308</u>	<u>25,385</u>
	<u>\$1,317</u>	<u>\$25,745</u>



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City of Palo Alto - Non-Major Governmental Funds
Combining Statements of Revenues, Expenditures and
Changes in Fund Balances -
For the Year Ended June 30, 2009
(In thousands of dollars)

	SPECIAL REVENUE FUNDS					
	Street Improvement	Federal Revenue	Housing In-Lieu	Special Districts	Transportation Mitigation	Local Law Enforcement
REVENUES						
Special assessments						
Other taxes and fines	\$1,025				\$128	
Charges for services					68	
From other agencies:						
Community Development Block Grant		\$1,494				
State of California			\$1,000			\$62
Other revenue from other agencies		135				29
Permit and licenses				\$208		
Return on investment	37	38	335	45	190	9
Rental income			10			
Other:						
Housing In-Lieu - residential			10			
Housing In-Lieu - commercial			397			
University Avenue Parking				810		
California Avenue Parking				99		
Other fees			38		40	
Total Revenues	<u>1,062</u>	<u>1,667</u>	<u>1,790</u>	<u>1,162</u>	<u>426</u>	<u>100</u>
EXPENDITURES						
Current:						
Planning and Community Environment		571	382			
Public Safety - Police						65
Non Departmental		73	3,653			
Debt service:						
Principal retirement						
Interest and fiscal charges						
Total Expenditures		<u>644</u>	<u>4,035</u>			<u>65</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>1,062</u>	<u>1,023</u>	<u>(2,245)</u>	<u>1,162</u>	<u>426</u>	<u>35</u>
OTHER FINANCING SOURCES (USES)						
Transfers in	1,800			31	1,590	
Transfers (out)	(1,771)			(1,084)	(82)	
Total Other Financing Sources (Uses)	<u>29</u>			<u>(1,053)</u>	<u>1,508</u>	
Net Change in Fund Balance	1,091	1,023	(2,245)	109	1,934	35
Fund balances at the beginning of year	381	3,440	9,600	751	2,227	146
Fund balances at end of year	<u>\$1,472</u>	<u>\$4,463</u>	<u>\$7,355</u>	<u>\$860</u>	<u>\$4,161</u>	<u>\$181</u>



SPECIAL REVENUE FUNDS				DEBT SERVICE FUNDS		
Assets Seizure	Developer's Impact Fee	Redevelopment Agency	Downtown Business Improvement District	Golf Course	Civic Center Refinancing	Downtown Parking Improvement
			\$96			
	\$296		3	\$54	\$3	\$2
	436					
	732		99	54	3	2
			103			
				335	365	100
				222	59	135
			103	557	424	235
	732		(4)	(503)	(421)	(233)
	35	\$6		526	412	225
	(1,090)	(6)				
	(1,055)			526	412	225
	(323)		(4)	23	(9)	(8)
	4,388		112	778	375	253
	\$4,065		\$108	\$801	\$366	\$245

(Continued)



City of Palo Alto - Non-Major Governmental Funds
Combining Statements of Revenues, Expenditures and
Changes in Fund Balances -
For the Year Ended June 30, 2009
(In thousands of dollars)

	PERMANENT FUND	
	Eyerly Family	Total Non-major Governmental Funds
REVENUES		
Special assessments		\$96
Other taxes and fines		1,153
Charges for services		68
From other agencies:		
Community Development Block Grant		1,494
State of California		1,062
Other revenue from other agencies		164
Permit and licenses		208
Return on investment	\$73	1,085
Rental income		10
Other:		
Housing In-Lieu - residential		10
Housing In-Lieu - commercial		397
University Avenue Parking		810
California Avenue Parking		99
Other fees	517	1,031
Total Revenues	<u>590</u>	<u>7,687</u>
EXPENDITURES		
Current:		
Planning and Community Environment		953
Public Safety - Police		65
Non Departmental	13	3,842
Debt service:		
Principal retirement		800
Interest and fiscal charges		416
Total Expenditures	<u>13</u>	<u>6,076</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>577</u>	<u>1,611</u>
OTHER FINANCING SOURCES (USES)		
Transfers in		4,625
Transfers (out)		(4,033)
Total Other Financing Sources (Uses)		<u>592</u>
Net Change in Fund Balance	577	2,203
Fund balances at the beginning of year	731	23,182
Fund balances at end of year	<u>\$1,308</u>	<u>\$25,385</u>



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City of Palo Alto - Non-major Governmental Funds
Combining Statement of Revenues, Expenditures and
Changes in Fund Balances -Budget and Actual
For the Year Ended June 30, 2009
(In thousands of dollars)

	SPECIAL REVENUE FUNDS					
	Street Improvement			Federal Revenue		
	Budget	Actual	Variance Positive (Negative)	Budget	Actual	Variance Positive (Negative)
REVENUES						
Special assessments						
Other taxes and fines	\$746	\$1,025	\$279			
Charges for services						
From other agencies:						
Community Development Block Grant State of California				\$676	\$1,494	\$818
Other revenue from other agencies				674	135	(539)
Permit and licenses						
Return on investment	7	37	30		38	38
Rental income						
Other:						
Housing In-Lieu - residential						
Housing In-Lieu - commercial						
University Avenue Parking						
California Avenue Parking						
Other fees				7		(7)
Total Revenues	753	1,062	309	1,357	1,667	310
EXPENDITURES						
Current operations:						
Planning and Community Environment				2,347	571	1,776
Public Safety - Police						
Non Departmental					28	(28)
Debt service:						
Principal retirement						
Interest and fiscal charges						
Total Expenditures				2,347	599	1,748
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	753	1,062	309	(990)	1,068	2,058
OTHER FINANCING SOURCES (USES)						
Transfers in	1,800	1,800				
Transfers (out)	(1,771)	(1,771)				
Total Other Financing Sources (Uses)	29	29				
Net Change in Fund Balance - Budget Basis	\$782	1,091	\$309	(\$990)	1,068	\$2,058
Nonbudgeted transactions- valuation allowance					(45)	
Fund balances at the beginning of year		381			3,440	
Fund balances at end of year		<u>\$1,472</u>			<u>\$4,463</u>	



SPECIAL REVENUE FUNDS

Housing In-Lieu			Special Districts			Transportation Mitigation		
Budget	Actual	Variance Positive (Negative)	Budget	Actual	Variance Positive (Negative)	Budget	Actual	Variance Positive (Negative)
						\$82	\$128 68	\$128 (14)
\$1,000	\$1,000							
253	335	\$82	\$27	\$208 45	\$208 18	75	190	115
920	10	(910)						
300	397	97	1,034	810	(224)	480		(480)
			134	99	(35)			
690	38	(652)					40	40
3,172	1,790	(1,382)	1,195	1,162	(33)	637	426	(211)
1,937	382	1,555						
3,691	3,653	38						
5,628	4,035	1,593						
(2,456)	(2,245)	211	1,195	1,162	(33)	637	426	(211)
			31	31		1,590	1,590	
			(1,250)	(1,084)	166	(82)	(82)	
			(1,219)	(1,053)	166	1,508	1,508	
<u>(\$2,456)</u>	<u>(2,245)</u>	<u>\$211</u>	<u>(\$24)</u>	<u>109</u>	<u>\$133</u>	<u>\$2,145</u>	<u>1,934</u>	<u>(\$211)</u>
	9,600			751			2,227	
	<u>\$7,355</u>			<u>\$860</u>			<u>\$4,161</u>	

(Continued)



City of Palo Alto - Non-major Governmental Funds

Combining Statement of Revenues, Expenditures and

Changes in Fund Balances -Budget and Actual

For the Year Ended June 30, 2009

(In thousands of dollars)

	SPECIAL REVENUE FUNDS					
	Local Law Enforcement			Developer's Impact Fee		
	Budget	Actual	Variance Positive (Negative)	Budget	Actual	Variance Positive (Negative)
REVENUES						
Special assessments						
Other taxes and fines						
Charges for services						
From other agencies:						
Community Development Block Grant						
State of California	\$101	\$62	(\$39)			
Other revenue from other agencies		29	29			
Permit and licenses						
Return on investment	8	9	\$1	\$123	\$296	\$173
Rental income						
Other:						
Housing In-Lieu - residential						
Housing In-Lieu - commercial						
University Avenue Parking						
California Avenue Parking						
Other fees				553	436	(117)
Total Revenues	109	100	(9)	676	732	56
EXPENDITURES						
Current operations:						
Planning and Community Environment						
Public Safety - Police	139	65	74			
Non Departmental						
Debt service:						
Principal retirement						
Interest and fiscal charges						
Total Expenditures	139	65	74			
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(30)	35	65	676	732	56
OTHER FINANCING SOURCES (USES)						
Transfers in				35	35	
Transfers (out)				(1,090)	(1,090)	
Total Other Financing Sources (Uses)				(1,055)	(1,055)	
Net Change in Fund Balance - Budget Basis	(\$30)	35	\$65	(\$379)	(323)	\$56
Nonbudgeted transactions- valuation allowance						
Fund balances at the beginning of year		146			4,388	
Fund balances at end of year		\$181			\$4,065	



SPECIAL REVENUE FUNDS						DEBT SERVICE FUNDS		
Redevelopment Agency			Downtown Business Improvement District			Golf Course		
Budget	Actual	Variance Positive (Negative)	Budget	Actual	Variance Positive (Negative)	Budget	Actual	Variance Positive (Negative)
			\$160	\$96	(\$64)			
			1	3	2	\$31	\$54	\$23
			161	99	(62)	31	54	23
			164	103	61			
						335	335	
						222	222	
			164	103	61	557	557	
			(3)	(4)	(1)	(526)	(503)	23
\$9	\$6	(\$3)				526	526	
(9)	(6)	3						
						526	526	
			(\$3)	(4)	(\$1)		23	\$23
				112			778	
				\$108			\$801	

(Continued)



City of Palo Alto - Non-major Governmental Funds
Combining Statement of Revenues, Expenditures and
Changes in Fund Balances -Budget and Actual
For the Year Ended June 30, 2009
(In thousands of dollars)

	DEBT SERVICE FUNDS					
	Civic Center Refinance			Downtown Parking Improvement		
	Budget	Actual	Variance Positive (Negative)	Budget	Actual	Variance Positive (Negative)
REVENUES						
Special assessments						
Other taxes and fines						
Charges for services						
From other agencies:						
Community Development Block Grant						
State of California						
Other revenue from other agencies						
Permit and licenses						
Return on investment	\$12	\$3	(\$9)	\$10	\$2	(\$8)
Rental income						
Other:						
Housing In-Lieu - residential						
Housing In-Lieu - commercial						
University Avenue Parking						
California Avenue Parking						
Other fees						
Total Revenues	12	3	(9)	10	2	(8)
EXPENDITURES						
Current operations:						
Planning and Community Environment						
Public Safety - Police						
Non Departmental						
Debt service:						
Principal retirement	365	365		100	100	
Interest and fiscal charges	59	59		135	135	
Total Expenditures	424	424		235	235	
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(412)	(421)	(9)	(225)	(233)	(8)
OTHER FINANCING SOURCES (USES)						
Transfers in	412	412		225	225	
Transfers (out)						
Total Other Financing Sources (Uses)	412	412		225	225	
Net Change in Fund Balance - Budget Basis		(9)	(\$9)		(8)	(\$8)
Nonbudgeted transactions- valuation allowance						
Fund balances at the beginning of year		375			253	
Fund balances at end of year		\$366			\$245	



PERMANENT FUND			TOTAL		
Eyerly Family			Non-major Governmental Funds		
Budget	Actual	Variance Positive (Negative)	Budget	Actual	Variance Positive (Negative)
			\$160	\$96	(\$64)
			746	1,153	407
			82	68	(14)
			676	1,494	818
			1,101	1,062	(39)
			674	164	(510)
				208	208
	\$73	\$73	547	1,085	538
			9	10	1
			920	10	(910)
			300	397	97
			1,514	810	(704)
			134	99	(35)
	517	517	1,250	1,031	(219)
	590	590	8,113	7,687	(426)
			4,284	953	3,331
			139	65	74
	13	(13)	3,855	3,797	58
			800	800	
			416	416	
	13	(13)	9,494	6,031	3,463
	577	577	(1,381)	1,656	3,037
			4,628	4,625	(3)
			(4,202)	(4,033)	169
			426	592	166
	577	\$577	(\$955)	2,248	\$3,203
				(45)	
	731			23,182	
	\$1,308			\$25,385	



Non-major Governmental Funds

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Internal Service Funds

Introduction

Internal Service Funds are used to finance and account for special activities and services performed by a designated department for other departments in the City on a cost reimbursement basis.

VEHICLE REPLACEMENT AND MAINTENANCE

This fund accounts for the maintenance and replacement of vehicles and equipment used by all City departments. The source of revenue is an accumulation of resources.

TECHNOLOGY

This fund accounts for replacement and upgrade of technology, and covers four primary areas used by all City departments: desktop, infrastructure, applications, and technology research and development. The source of revenue is an accumulation of resources.

PRINTING AND MAILING SERVICES

This fund accounts for central duplicating, printing and mailing services provided to all City departments. Source of revenue for this fund is on reimbursement of costs for services and supplies purchased by other departments.

GENERAL BENEFITS AND INSURANCE

This fund accounts for the administration of compensated absences and health benefits, and the City's self-insured workers' compensation and general liability programs.

RETIREE HEALTH BENEFIT

This fund accounts for the retiree health benefits.



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City of Palo Alto - Internal Service Funds

Combining Statements of Net Assets - June 30, 2009

(In thousands of dollars)

	Vehicle Replacement and Maintenance	Technology	Printing and Mailing Services	General Benefits and Insurance	Retiree Health Benefit	Total
ASSETS						
Current Assets:						
Cash and investments available for operations	\$4,442	\$9,113	\$93	\$35,675	\$9	\$49,332
Accounts receivable, net	28					28
Interest receivable	54	162		373	1	590
Inventory of materials and supplies	467					467
Prepaid items					26,352	26,352
Total Current Assets	4,991	9,275	93	36,048	26,362	76,769
Noncurrent Assets:						
Capital assets, nondepreciable	3,122					3,122
Capital assets, net of depreciation	9,090	10,536	18			19,644
Total Noncurrent Assets	12,212	10,536	18			22,766
Total Assets	17,203	19,811	111	36,048	26,362	99,535
LIABILITIES						
Current Liabilities:						
Accounts payable and accrued liabilities	1,376	826		1,104		3,306
Accrued salaries and benefits	27	83	9	357		476
Accrued compensated absences				4,054		4,054
Accrued claims payable - current				5,855		5,855
Total Current Liabilities	1,403	909	9	11,370		13,691
Long-term Liabilities:						
Accrued compensated absences				8,614		8,614
Accrued claims payable				15,583		15,583
Total Long-term Liabilities				24,197		24,197
Total Liabilities	1,403	909	9	35,567		37,888
NET ASSETS						
Investment in capital assets	12,212	10,536	18			22,766
Unrestricted	3,588	8,366	84	481	26,362	38,881
Total Net Assets	\$15,800	\$18,902	\$102	\$481	\$26,362	\$61,647



**City of Palo Alto - Internal Service Funds
 Combining Statements of Revenues, Expenses and
 Changes in Net Assets - For the Year Ended June 30, 2009**

(In thousands of dollars)

	Vehicle Replacement and Maintenance	Technology	Printing and Mailing Services	General Benefits and Insurance	Retiree Health Benefit	Total
OPERATING REVENUES						
Charges for services	\$8,119	\$3,768	\$1,420	\$36,817	\$5,785	\$55,909
Total Operating Revenues	8,119	3,768	1,420	36,817	5,785	55,909
OPERATING EXPENSES						
Administration and general	795	11,149	1,504	1,712	1,077	16,237
Operations and maintenance	7,793					7,793
Depreciation and amortization	1,782	531	3			2,316
Claim payments and change in estimated self-insured liability				2,168		2,168
Compensated absences and other benefits	119			37,677	7,886	45,682
Total Operating Expenses	10,489	11,680	1,507	41,557	8,963	74,196
Total Operating Income (Loss)	(2,370)	(7,912)	(87)	(4,740)	(3,178)	(18,287)
NONOPERATING REVENUES (EXPENSES)						
Return on investment	321	903	(10)	1,936	(152)	2,998
Gain (loss) on disposal of capital assets	29					29
Other nonoperating revenues (expense)		59	4			63
Total Nonoperating Revenues	350	962	(6)	1,936	(152)	3,090
Income (Loss) Before Transfers	(2,020)	(6,950)	(93)	(2,804)	(3,330)	(15,197)
Transfers in	355	6,365				6,720
Transfers (out)	(27)	(105)	(8)		(64)	(204)
Change in Net Assets	(1,692)	(690)	(101)	(2,804)	(3,394)	(8,681)
Net assets at beginning of year	17,492	19,592	203	3,285	29,756	70,328
Net assets at end of year	\$15,800	\$18,902	\$102	\$481	\$26,362	\$61,647



City of Palo Alto - Internal Service Funds

Combining Statements of Cash Flows - For the Fiscal Year Ended June 30, 2009

(In thousands of dollars)

	Vehicle Replacement and Maintenance	Technology	Printing and Mailing Services	General Benefits and Insurance	Retiree Health Benefit	Total
CASH FLOW FROM OPERATING ACTIVITIES						
Receipts from customers	\$8,141	\$4,050	\$1,420	\$36,817	\$5,785	\$56,213
Payments to suppliers	(6,607)					(6,607)
Payments to employees	(909)	(11,705)	(1,503)	(37,185)	(6,138)	(57,440)
Claims paid				(4,256)		(4,256)
Other receipts		59	4			63
Net cash provided by operating activities	625	(7,596)	(79)	(4,624)	(353)	(12,027)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES						
Transfers in	355	6,365				6,720
Transfers (out)	(27)	(105)	(8)		(64)	(204)
Cash flows from noncapital financing activities	328	6,260	(8)		(64)	6,516
CASH FLOWS FROM CAPITAL FINANCING ACTIVITIES						
Acquisition and construction of capital assets	(1,991)	(5,390)				(7,381)
Proceeds from sale of capital assets	29					29
Cash flows from capital financing activities	(1,962)	(5,390)				(7,352)
CASH FLOWS FROM INVESTING ACTIVITIES						
Interest and dividends on pooled investments	328	928	(7)	1,966	42	3,257
Net Cash Flows	(681)	(5,798)	(94)	(2,658)	(375)	(9,606)
Cash and investments at beginning of year	5,123	14,911	187	38,333	384	58,938
Cash and investments at end of year	\$4,442	\$9,113	\$93	\$35,675	\$9	\$49,332
CASH FLOWS FROM OPERATING ACTIVITIES						
Operating income (loss)	(\$2,370)	(\$7,912)	(\$87)	(\$4,740)	(\$3,178)	(\$18,287)
Adjustments to reconcile operating income (loss) to cash flows from operating activities:						
Depreciation and amortization	1,782	531	3			2,316
Other		59	4			63
Changes in assets and liabilities:						
Accounts receivable	22	282				304
Inventory of materials and supplies	120	(67)	(1)	13		65
Prepaid items					2,825	2,825
Accounts and other payables	1,074	(477)	3	2,191		2,791
Accrued compensated absences	(3)	(12)	(1)			(16)
Interfund payment						
Accrued claims payable				(2,088)		(2,088)
Net cash provided by operating activities	\$625	(\$7,596)	(\$79)	(\$4,624)	(\$353)	(\$12,027)



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Fiduciary Funds.....

Introduction

Fiduciary Funds are used to account for assets held by the City acting in a fiduciary capacity for other entities and individuals. The funds are operated to carry out the specific actions required by the trust agreements, ordinances and other governing regulations.

Fiduciary Funds are presented separately from the Citywide and Fund financial statements.

Agency Funds are custodial in nature and do not involve measurement of results of operations. The City maintains three agency funds, as follows:

CALIFORNIA AVENUE PARKING ASSESSMENT DISTRICT

This fund accounts for receipts and disbursements associated with the 1993 Parking District No. 92-13 Assessment Bonds.

CABLE JOINT POWERS AUTHORITY

The fund was established to account for the activities of the cable television system on behalf of the members.

UNIVERSITY AVENUE AREA PARKING ASSESSMENT DISTRICT

The fund accounts for the receipts and disbursements associated with the Series 2001-A University Avenue Area Off-Street Parking Assessments Bonds.

City of Palo Alto - Agency Funds

Statement of Changes in Assets and Liabilities -

For the Fiscal Year Ended June 30, 2009

(In thousands of dollars)

	Balance June 30, 2008	Additions	Reductions	Balance June 30, 2009
<u>California Avenue Parking Assessment District</u>				
ASSETS				
Cash and investments available for operations	\$254		\$16	\$238
LIABILITIES				
Due to bondholders	\$254		\$16	\$238
<u>Cable Joint Powers Authority</u>				
ASSETS				
Cash and investments available for operations	\$813	\$55		\$868
Interest receivable	10		1	9
Total assets	\$823	\$55	\$1	\$877
LIABILITIES				
Due to other governments	\$823	\$55	\$1	\$877
<u>University Avenue Area Parking Assessment District</u>				
ASSETS				
Cash and investments with fiscal agents	\$6,099		\$37	\$6,062
Interest receivable	35		2	33
Total assets	\$6,134		\$39	\$6,095
LIABILITIES				
Due to bondholders	\$6,134		\$39	\$6,095
<u>Total Agency Funds</u>				
ASSETS				
Cash and investments available for operations	\$1,067	\$55	\$16	\$1,106
Cash and investments with fiscal agents	6,099		37	6,062
Interest receivable	45		3	42
Total assets	\$7,211	\$55	\$56	\$7,210
LIABILITIES				
Due to bondholders	\$6,388		\$55	\$6,333
Due to other governments	823	55	1	877
Total liabilities	\$7,211	\$55	\$56	\$7,210



Statistical Section.....

The statistical section contains comprehensive statistical data which relates to physical, economic, social and political characteristics of the City. It is intended to provide users with a broader and more complete understanding of the City and its financial affairs than is possible from the financial statements and supporting schedules included in the financial section.

In this section, readers will find comparative information related to the City's revenue sources, expenditures, property tax valuations, levies and collections, general obligation bonded debt, utility revenue debt service, demographics and pension plan funding. Where available, the comparative information is presented for the last ten fiscal years.

In addition, this section presents information related to the City's legal debt margin computation, principal taxpayers, notary and security bond coverages, and other miscellaneous statistics pertaining to services provided by the City.

In contrast to the financial section, the statistical section information is not usually subject to independent audit.

Financial Trends

These schedules contain trend information to help the reader understand how the City's financial performance and well being have changed over time:

1. Net Assets by Component
2. Changes in Net Assets
3. Fund Balances of Governmental Funds
4. Changes in Fund Balance of Governmental Funds

Revenue Capacity

These schedules contain information to help the reader assess the City's most significant local revenue sources, property tax and electric charges:

1. Electric Daily Loads and Top Customers by Usage
2. Electric Operating Revenue by Source
3. Assessed Value of Taxable Property
4. Property Tax Rates, All Overlapping Governments
5. Property Tax Levies and Collections
6. Principal Property Taxpayers

Debt Capacity

These schedules present information to help the reader assess the affordability of the City's current levels of outstanding debt and the City's ability to issue additional debt in the future:

1. Ratio of Outstanding Debt by Type
2. Computation of Direct and Overlapping Debt
3. Computation of Legal Bonded Debt Margin
4. Revenue Bond Coverage

Demographic and Economic Information

These schedules offer demographic and economic indicators to help the reader understand the environment within which the City's financial activities take place:

1. Taxable Transaction by Type of Business
2. Demographic and Economic Statistics
3. Principal Employers

Operating Information

These schedules contain service and infrastructure data to help the reader understand how the information in the City's financial report relates to the services the City provides and the activities it performs:

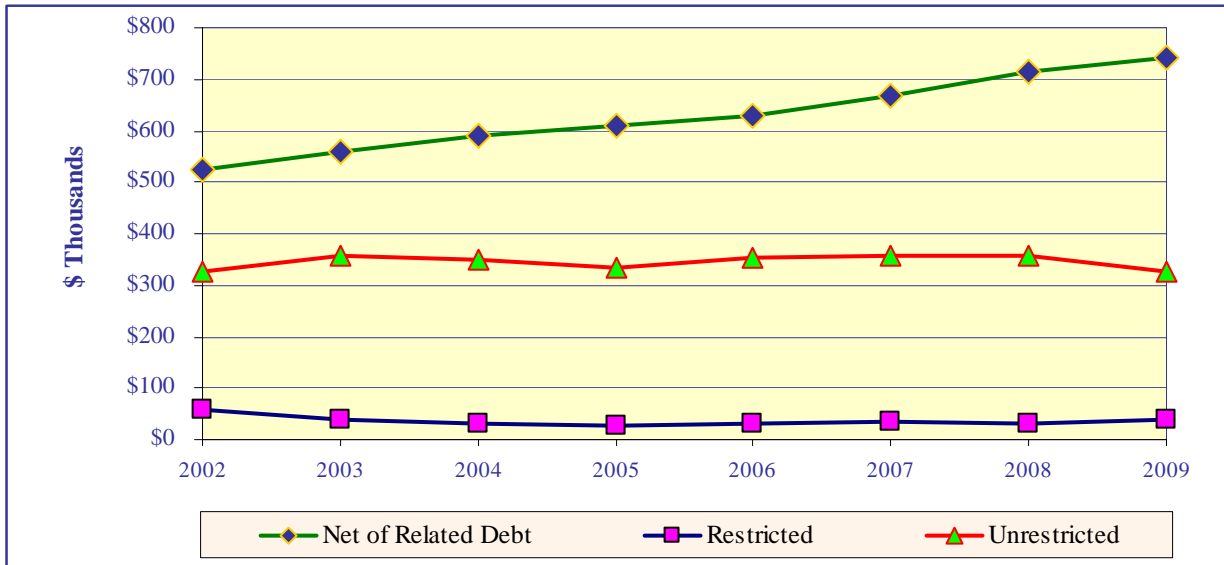
1. Full-Time Equivalent City Government Employees by Function
2. Operating Indicators by Function/Program
3. Capital Asset Statistics by Function/Program
4. Insurance Coverage

Sources

Unless otherwise noted, the information in these schedules is derived from the Comprehensive Annual Financial Reports for the relevant year. The City implemented GASB Statement 34 in 2002; schedules presenting government-wide information include information beginning in that year.



City of Palo Alto - Net Assets by Component
Last Eight Fiscal Years (\$000)
(Accrual Basis of Accounting)



Fiscal Year Ended June 30,

	2002	2003	2004	2005	2006	2007	2008	2009
Governmental activities								
Invested in capital assets, net of related debt	\$252,183	\$279,306	\$297,125	\$305,225	\$311,335	\$326,411	\$343,537	\$356,657
Restricted	56,785	37,112	30,417	27,273	29,885	32,576	27,428	36,632
Unrestricted	117,113	130,463	123,762	117,301	123,823	127,190	130,460	118,133
Total governmental activities net assets	\$426,081	\$446,881	\$451,304	\$449,799	\$465,043	\$486,177	\$501,425	\$511,422
Business-type activities								
Invested in capital assets, net of related debt	\$270,622	\$279,885	\$294,197	\$303,473	\$318,738	\$342,922	\$370,303	\$384,313
Restricted	1,728	1,728	1,798	1,750	1,732	1,732	1,732	1,732
Unrestricted	210,990	228,308	226,278	215,128	228,032	230,912	226,539	208,025
Total business-type activities net assets	\$483,340	\$509,921	\$522,273	\$520,351	\$548,502	\$575,566	\$598,574	\$594,070
Primary government								
Invested in capital assets, net of related debt	\$522,805	\$559,191	\$591,322	\$608,698	\$630,073	\$669,333	\$713,840	\$740,970
Restricted	58,513	38,840	32,215	29,023	31,617	34,308	29,160	38,364
Unrestricted	328,103	358,771	350,040	332,429	351,855	358,102	356,999	326,158
Total primary government net assets	\$909,421	\$956,802	\$973,577	\$970,150	\$1,013,545	\$1,061,743	\$1,099,999	\$1,105,492

Source: Annual Financial Statements

Note: The City implemented GASB Statement 34 in fiscal year 2002. Therefore this calculation is included only for fiscal years subsequent to that date.

City of Palo Alto - Changes in Net Assets

Last Eight Fiscal Years (\$000)
(Accrual Basis of Accounting)

	Fiscal Year Ended June 30,							
	2002	2003	2004	2005	2006	2007	2008	2009
Expenses								
Governmental Activities:								
City Council	\$238	\$234	\$269	\$130	\$141	\$180	\$323	\$394
City Manager	1,765	1,565	1,663	1,725	1,563	1,760	2,273	2,085
City Attorney	2,410	2,028	2,300	2,653	2,598	2,390	2,653	2,575
City Clerk	633	598	808	770	945	900	1,241	1,098
City Auditor	583	646	668	764	843	838	1,379	2,053
Administrative Services **	10,138	9,723	6,271	6,982	6,972	6,419	15,477	17,784
Human Resources	2,166	1,728	2,078	2,410	2,546	2,472	2,806	3,448
Public Works	15,656	13,702	14,460	16,400	17,596	16,645	18,565	21,270
Planning and Community Environment	7,311	7,485	8,898	10,162	9,931	12,929	16,388	12,940
Police	19,049	19,273	20,414	22,416	23,411	23,861	27,740	29,288
Fire	16,870	16,859	17,308	18,127	18,747	19,530	22,386	23,199
Community Services	19,850	19,633	20,864	17,240	17,296	15,729	17,736	19,862
Library				4,835	5,323	5,347	6,321	6,244
Non-Departmental **	8,412	7,449	7,618	12,474	10,400	12,133	0	0
Interest on Long Term Debt	1,094	675	635	693	512	477	438	404
Total Governmental Activities Expenses	\$106,175	\$101,598	\$104,254	\$117,781	\$118,824	\$121,610	\$135,726	\$142,644
Business-Type Activities:								
Water	\$12,722	\$13,237	\$16,047	\$14,969	\$15,881	\$16,794	\$18,842	\$20,271
Electric	98,405	73,744	73,545	73,051	91,570	99,294	108,032	122,268
Fiber Optics *	0	0	0	0	0	0	0	1,284
Gas	28,778	22,270	22,994	26,656	29,107	30,690	37,211	34,603
Wastewater Collection	8,489	8,712	9,203	8,907	11,005	10,085	12,023	14,875
Wastewater Treatment	13,287	14,312	14,868	17,457	16,747	15,901	18,902	36,896
Refuse	23,750	24,635	24,282	24,959	26,989	25,372	28,827	37,217
Storm Drainage	2,188	2,489	2,975	3,336	2,673	2,517	3,202	2,943
External Services	349	583	688	760	868	767	984	0
Total Business-Type Activities Expenses	187,968	159,982	164,602	170,095	194,840	201,420	228,023	270,357
Total Primary Government Expenses	\$294,143	\$261,580	\$268,856	\$287,876	\$313,664	\$323,030	\$363,749	\$413,001
Program Revenues								
Governmental Activities								
Charges for Services:								
City Council								
City Manager								
City Attorney		\$92	\$64	\$22	\$22	\$13	\$16	\$12
City Clerk	\$1	1	1		2			
City Auditor		1						
Administrative Services	12	406	815	480	627	835	870	726
Human Resources						11		
Public Works	320	1,058	260	573	805	968	1,310	1,169
Planning and Community Environment	4,062	5,119	3,074	4,090	5,509	6,267	5,498	4,704
Police	3,966	3,396	4,415	3,801	4,178	4,179	4,274	3,947
Fire	7,976	7,811	7,565	8,555	9,078	9,610	9,418	10,723
Community Services	7,793	7,537	7,846	7,592	10,803	9,128	10,314	8,522
Library				133	129	146	176	177
Operating Grants and Contributions	5,568	4,468	4,213	3,677	3,976	5,642	4,029	3,599

* Prior to 2009, Fiber Optics was included in Electric

** Beginning in 2008, includes expenditures classified as Non-departmental in prior years (GFOA recommendation)



City of Palo Alto - Changes in Net Assets

Last Eight Fiscal Years (\$000)

(Accrual Basis of Accounting)

	Fiscal Year Ended June 30,							
	2002	2003	2004	2005	2006	2007	2008	2009
Capital Grants and Contributions	32,380	635	1,990	804	3,156	1,756	1,930	3,810
Total Government Activities Program Revenues	62,078	30,524	30,243	29,727	38,285	38,555	37,835	37,389
Business-Type Activities:								
Charges for Services:								
Water	16,034	17,654	21,993	21,041	21,108	23,495	26,510	27,120
Electric	93,755	91,622	92,617	88,737	119,418	102,549	103,833	119,320
Fiber Optics *	0	0	0	0	0	0	0	3,336
Gas	41,658	29,714	24,839	31,206	36,977	42,221	49,021	47,838
Wastewater Collection	9,292	10,676	12,647	12,041	13,801	14,848	15,102	14,486
Wastewater Treatment	13,987	13,556	14,744	15,982	18,778	16,957	22,889	28,425
Refuse	21,777	21,691	21,923	23,387	24,795	25,532	28,805	29,101
Storm Drainage	2,221	2,192	2,170	2,484	5,174	5,181	5,450	5,505
External Services	380	605	585	766	854	789	112	0
Capital Grants and Contributions	185					756	1,594	639
Total Business-Type Activities Program Revenue	199,289	187,710	191,518	195,644	240,905	232,328	253,316	275,770
Total Primary Government Program Revenues	\$261,367	\$218,234	\$221,761	\$225,371	\$279,190	\$270,883	\$291,151	\$313,159
Net (Expense)/Revenue								
Governmental Activities	(\$44,097)	(\$71,074)	(\$74,011)	(\$88,054)	(\$80,539)	(\$83,055)	(\$97,891)	(\$105,255)
Business-Type Activities	11,321	27,728	26,916	25,549	46,065	30,908	25,293	5,413
Total Primary Government Net Expense	(\$32,776)	(\$43,346)	(\$47,095)	(\$62,505)	(\$34,474)	(\$52,147)	(\$72,598)	(\$99,842)
General Revenues and Other Changes in Net Assets								
Governmental Activities:								
Taxes:								
Property Taxes	\$13,270	\$13,882	\$13,707	\$16,657	\$18,731	\$21,466	\$23,084	\$25,432
Sales Taxes	20,085	18,041	18,151	19,308	20,315	22,194	22,623	20,089
Utilities Users Taxes	6,457	7,067	7,152	7,269	8,759	9,356	10,285	11,030
Transient Occupancy Tax	6,615	5,333	5,489	5,686	6,393	6,709	7,976	7,111
Other taxes	6,284	7,275	8,493	5,580	7,033	6,293	6,261	3,364
Investment Earnings	10,589	10,213	326	4,988	2,567	8,747	12,313	8,525
Rents and Miscellaneous	18,524	15,333	10,165	12,997	10,440	13,670	11,896	15,682
Transfers	13,334	14,730	14,951	14,064	21,545	15,754	18,701	24,020
Total Government Activities	95,158	91,874	78,434	86,549	95,783	104,189	113,139	115,253
Business-Type Activities:								
Investment Earnings	15,620	13,583	387	8,093	3,631	11,910	16,416	14,103
Special Item				(21,500)				
Transfers	(13,334)	(14,730)	(14,951)	(14,064)	(21,545)	(15,754)	(18,701)	(24,020)
Total Business-Type Activities	2,286	(1,147)	(14,564)	(27,471)	(17,914)	(3,844)	(2,285)	(9,917)
Total Primary Government	\$97,444	\$90,727	\$63,870	\$59,078	\$77,869	\$100,345	\$110,854	\$105,336
Change in Net Assets								
Governmental Activities	\$51,061	\$20,800	\$4,423	(\$1,505)	\$15,244	\$21,134	\$15,248	\$9,998
Business-Type Activities	13,607	26,581	12,352	(1,922)	28,151	27,064	23,008	(4,504)
Total Primary Government	\$64,668	\$47,381	\$16,775	(\$3,427)	\$43,395	\$48,198	\$38,256	\$5,494

Source: Annual Financial Statements

* Prior to 2009, Fiber Optics was included in Electric

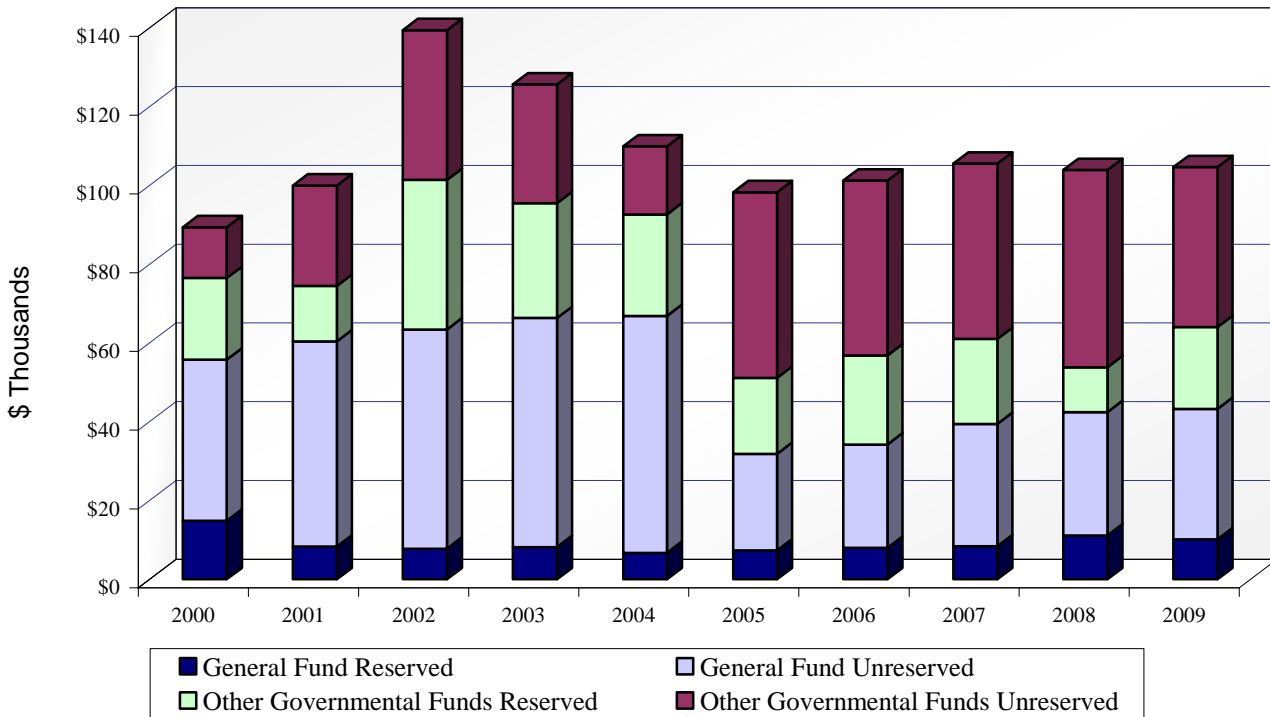
Note: The City implemented GASB Statement 34 in fiscal year 2002.

Therefore this calculation is included only for fiscal years subsequent to that date.

City of Palo Alto - Fund Balances of Governmental Funds

Last Ten Fiscal Years (\$000)

(Modified Accrual Basis of Accounting)



Fiscal Year Ended June 30,

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
General Fund										
Reserved	\$14,838	\$8,282	\$7,780	\$8,156	\$6,735	\$7,332	\$7,966	\$8,392	\$11,102	\$10,135
Unreserved	40,927	52,114	55,653	58,151	60,087	24,498	26,251	31,016	31,313	33,089
Total General Fund	\$55,765	\$60,396	\$63,433	\$66,307	\$66,822	\$31,830	\$34,217	\$39,408	\$42,415	\$43,224 (a)
All Other Governmental Funds										
Reserved	\$20,717	\$14,086	\$37,924	\$29,174	\$25,790	\$19,305	\$22,597	\$21,614	\$11,403	\$20,791
Unreserved, reported in:										
Special revenue funds	4,908	7,466	18,263	7,428	6,875	7,643	7,063	10,847	15,379	14,533
Capital project funds	7,987	18,005	19,772	22,705	10,419	39,431	37,315	33,646	33,947	24,760
Permanent funds									731	1,308
Total all other governmental funds	\$33,612	\$39,557	\$75,959	\$59,307	\$43,084	\$66,379	\$66,975	\$66,107	\$61,460	\$61,392

Source: Annual Financial Statements

Note: (a) The change in total fund balance for the General fund is explained in the "Management's Discussion and Analysis".

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**City of Palo Alto - Changes in Fund Balance of Governmental Funds
Last Ten Fiscal Years (\$000)**

(Modified Accrual Basis of Accounting)

	Fiscal Year Ended June 30,				
	2000	2001	2002	2003	2004
Revenues					
Sales tax	\$22,867	\$25,786	\$20,085	\$18,041	\$18,151
Property tax	10,770	12,110	13,231	13,821	13,707
Other taxes	23,582	26,160	20,485	21,070	22,427
Permits and licenses	12,408	12,743	2,901	3,161	2,563
Fines, forfeits and penalties	1,703	1,873	2,181	2,124	2,884
Interest and rentals	13,874	17,432	19,547	19,981	11,480
From other agencies	3,282	2,208	3,860	3,776	4,661
Charges for services	5,053	5,466	16,667	16,798	16,018
Other	6,213	7,590	8,580	5,095	1,681
Total Revenues	99,752	111,368	107,537	103,867	93,572
Expenditures					
Administration (1)	15,772	18,557	18,235	17,521	13,862
Public works	8,827	9,522	9,549	9,858	8,031
Planning and community environment	6,639	6,652	7,378	7,721	8,793
Police	17,666	18,306	19,047	19,719	19,962
Fire	14,512	15,973	16,722	16,841	16,891
Community services	17,858	18,469	19,499	19,793	19,934
Library (2)					
Non-departmental	6,927	14,487	8,259	7,442	7,598
Special revenue and capital projects	13,151	11,089	16,960	33,584	22,289
Debt service - Principal payments	1,775	1,895	465	875	780
Debt Service - Interest and fiscal fees	1,026	922	686	696	639
Total Expenditures	104,153	115,872	116,800	134,050	118,779
Excess (deficiency) of revenues over (under) expenditures	(4,401)	(4,504)	(9,263)	(30,183)	(25,207)
Other Financing Sources (Uses)					
Transfers in	27,795	26,150	27,389	31,402	28,632
Transfers (out)	(15,418)	(14,487)	(14,444)	(16,603)	(19,133)
Contribution from assessment district		4,112	31,823	425	
Proceeds from long term debt			7,055		
Payments to refunded bond escrow		(705)	(3,820)		
Total other financing sources (uses)	12,377	15,070	48,003	15,224	9,499
Net Change in fund balances	\$7,976	\$10,566	\$38,740	(\$14,959)	(\$15,708)
Debt service as a percentage of noncapital expenditures	(a)	(a)	1.1%	1.6%	1.5%

Source: Annual Financial Statements

- Note:** (a) The City implemented GASB Statement 34 in fiscal year 2002. Therefore this calculation is included only for fiscal years subsequent to that date.
- (1) Comprised of the following departments: City Council, City Manager, City Attorney, City Clerk, City Auditor, Administrative Services and Human Resources.
- (2) Prior to 2005, Library was included in Community Services.



Fiscal Year Ended June 30,

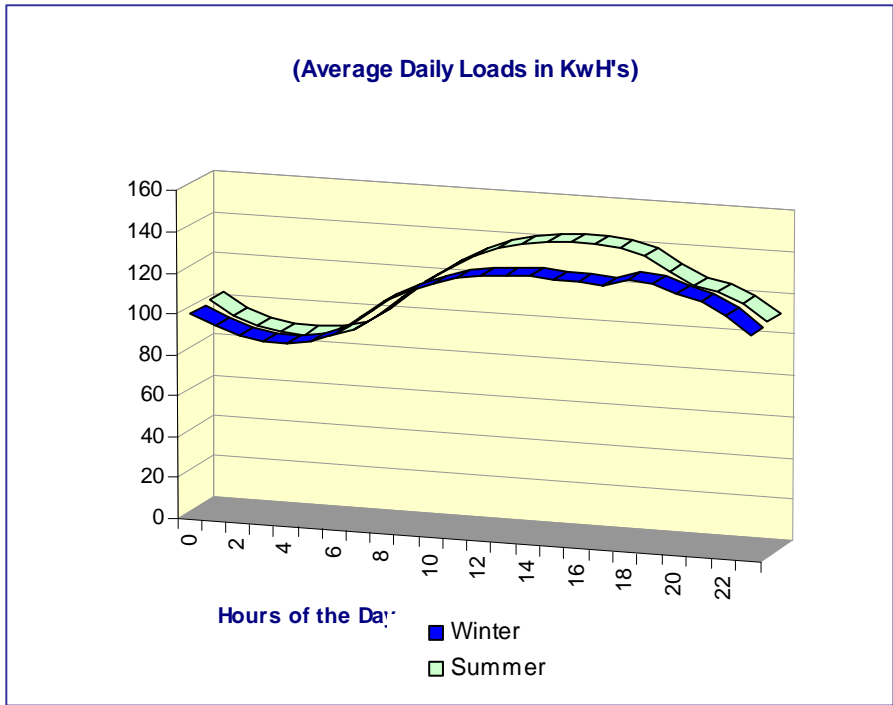
2005	2006	2007	2008	2009
\$19,308	\$20,315	\$22,194	\$22,623	\$20,089
16,657	18,731	21,466	23,084	25,432
19,941	23,712	23,698	25,202	24,843
3,183	4,305	4,711	4,761	4,033
2,096	2,128	2,517	2,183	0
14,968	13,776	17,750	20,507	19,183
2,757	5,931	3,448	4,300	5,984
17,159	18,672	19,929	19,610	19,837
4,269	4,058	7,503	4,713	6,223
100,338	111,628	123,216	126,983	125,624
14,509	14,299	14,399	16,250	16,002
9,060	9,036	9,256	10,072	10,064
9,692	9,292	11,874	9,861	10,462
21,117	22,279	23,305	27,006	27,053
17,615	18,114	19,146	21,644	21,904
16,298	19,740	16,533	17,138	17,451
4,800	5,170	5,260	6,219	5,985
9,028	10,389	12,122	14,089	10,765
21,317	13,243	17,478	21,626	21,485
785	810	850	885	800
583	523	489	451	416
124,804	122,895	130,712	145,241	142,387
(24,466)	(11,267)	(7,496)	(18,258)	(16,763)
60,429	26,640	27,701	33,437	39,903
(46,622)	(12,390)	(15,882)	(16,819)	(22,399)
(1,038)				
12,769	14,250	11,819	16,618	17,504
(\$11,697)	\$2,983	\$4,323	(\$1,640)	\$741
1.3%	1.2%	1.2%	1.1%	1.0%

City of Palo Alto - Electric Daily Loads and Top Customers by Usage

June 30, 2009

(in thousands of KWh)

# Kilowatt Hours		
Daily Hours	(Oct-Mar) Winter	(Apr-Sep) Summer
0	95,288	88,414
1	93,479	86,138
2	89,032	84,096
3	88,996	85,456
4	89,931	89,506
5	93,012	94,110
6	100,173	102,378
7	108,614	110,258
8	116,654	114,795
9	124,265	119,533
10	131,112	123,242
11	135,320	124,340
12	138,153	125,022
13	139,793	124,715
14	141,055	125,943
15	140,296	124,574
16	138,838	124,258
17	135,546	126,725
18	129,127	125,008
19	122,847	121,131
20	121,464	117,806
21	116,462	111,038
22	108,551	102,238
23	100,547	91,975



Source: City of Palo Alto, Utilities Resource Management

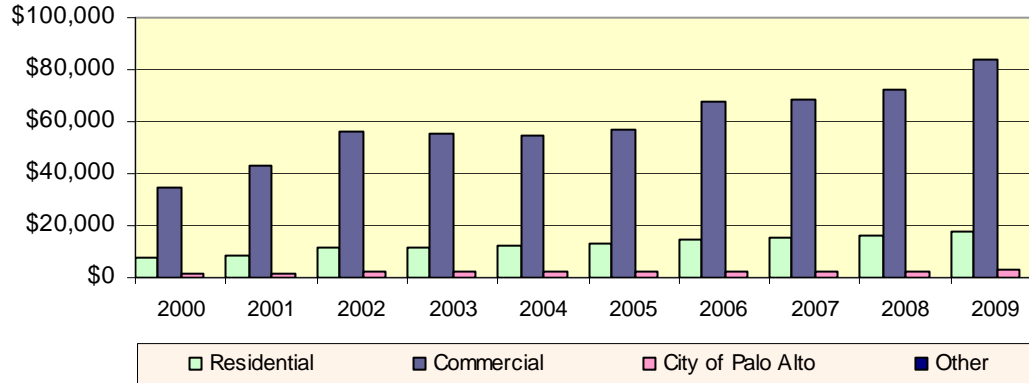
Top Ten Electric Customers by Usage

Customer (alphabetical order)	Type of Business	KWh's	% of System Total
City Of Palo Alto	Municipal		
CPI-David Morman	Research in Physical Science		
Hew lett Packard	Computer		
Space System Loral	Satellite & Satellite Systems		
Stanford Hines Interests	Property Management		
Stanford Hospital	Hospital		
Syntex/J Meek-MS#SS-200	Technology in Occupational Risk Mgmt		
Varian Medical Systems	Manufacturing of Medical Equipment		
Veterans Admin Hospital	Hospital		
VMWare Inc.	Computer		
Total		367,221,326	36.50 %

Source: City of Palo Alto, Utilities Department



City of Palo Alto - Electric Operating Revenue by Source Last Ten Fiscal Years (\$000)



Fiscal Year	Residential	Commercial	City of Palo Alto	Other	Total
2000	7,987	34,826	1,415	29	44,256
2001	8,489	43,460	1,545	5	53,499
2002	11,377	56,214	1,925	6	69,521
2003	11,657	55,353	2,004	24	69,039
2004	12,245	54,881	2,047	66	69,240
2005	13,009	56,683	2,222	67	71,981
2006	14,973	67,389	2,395	97	84,854
2007	15,150	68,214	2,397	69	85,829
2008	16,109	72,632	2,571	0	91,312
2009	17,939	83,710	2,823	0	104,472

Top Ten Electric Revenue

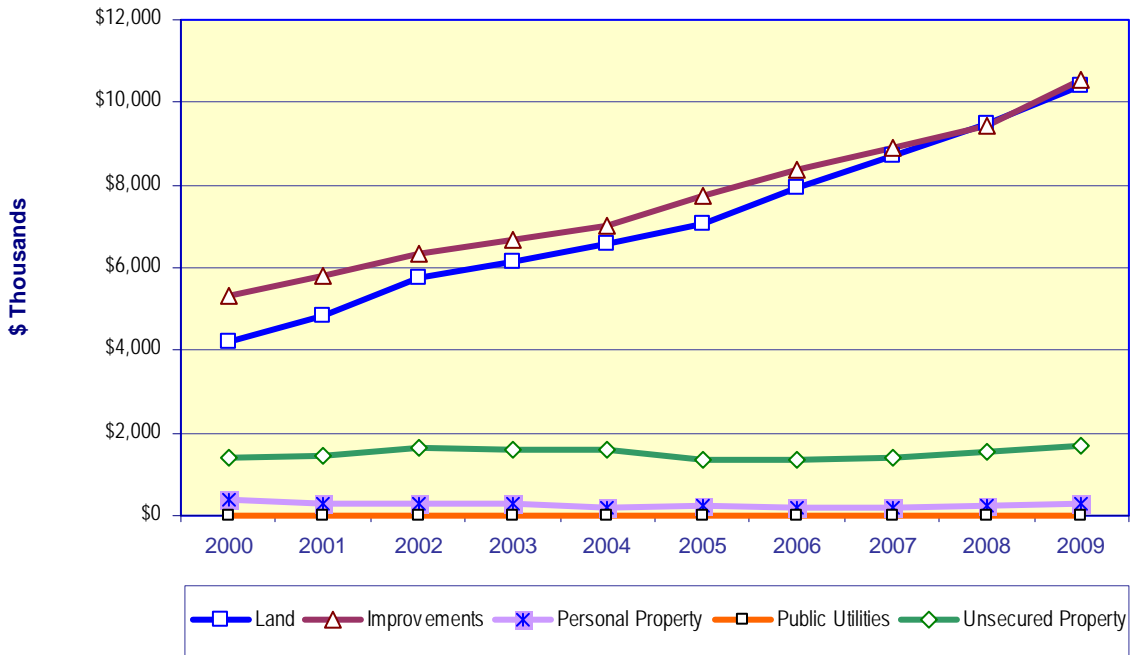
Customer (alphabetical order)	Type of Business	Net Charges	% of System Total
City of Palo Alto	Municipal		
CPI-David Morman	Research		
Hewlett Packard	Computer		
Space System Loral/MS-AC-1	Satellite System		
Stanford Hines Interests	Property Mgmt		
Stanford Hospital	Hospital		
Syntex/J Meek-MS#SS-200	Technology		
Varian Medical Systems	Manufacturing		
Veterans Admin Hospital	Hospital		
VMWare, Inc.	Computer		
Total		\$ 35,263,479	15.15%

Source: City of Palo Alto, Utilities Department

Notes: Revenue includes all utilities (metered and non-metered), revenue adjustments, and Primary Voltage discount. Does not include CEC surcharge, UUT, Solar and Rap discounts, and deposits.

FY 2008 net charges were overstated due to all utility services being included. FY 2008 should have been stated with net charges being \$28,132,971.

City of Palo Alto - Assessed Value of Taxable Property
Last Ten Fiscal Years (\$000)



Fiscal Year	Net Local Secured Roll			Subtotal			Less		Total Assessed Value	Total Direct Tax Rate
	Land	Improvements	Personal Property	Net Local Secured Roll	Public Utilities	Unsecured Property	Exemptions Net of State Aid	Total		
2000	4,187,357	5,335,026	394,198	9,916,581	3,362	1,415,999	802,164	10,533,778	1%	
2001	4,849,233	5,816,633	280,958	10,946,824	3,309	1,473,678	813,896	11,609,915	1%	
2002	5,744,675	6,347,719	292,812	12,385,206	3,371	1,627,594	913,475	13,102,696	1%	
2003	6,140,438	6,692,162	309,386	13,141,986	3,859	1,612,179	951,807	13,806,217	1%	
2004	6,588,474	6,996,106	195,859	13,780,439	3,956	1,582,368	1,196,546	14,170,217	1%	
2005	7,075,300	7,722,660	220,585	15,018,545	4,150	1,354,310	1,402,039	14,974,966	1%	
2006	7,941,482	8,364,668	174,666	16,480,816	4,084	1,361,117	1,595,871	16,250,146	1%	
2007	8,725,485	8,915,623	213,154	17,854,262	3,923	1,391,284	1,639,856	17,609,613	1%	
2008	9,497,746	9,453,436	228,875	19,180,057	3,174	1,536,584	1,797,327	18,922,488	1%	
2009	10,420,139	10,527,617	303,688	21,251,444	2,573	1,702,884	1,871,292	21,085,609	1%	

Source: County of Santa Clara Assessor's Office

Note: Beginning in fiscal year 1988-89, Chapter 921 of the Statutes of 1987 requires the establishment of a single county-wide tax rate area for the assignment of the assessed value of certain types of state-assessed utility property and sets forth formulas for the determination of county-wide tax rates for this particular type of property.

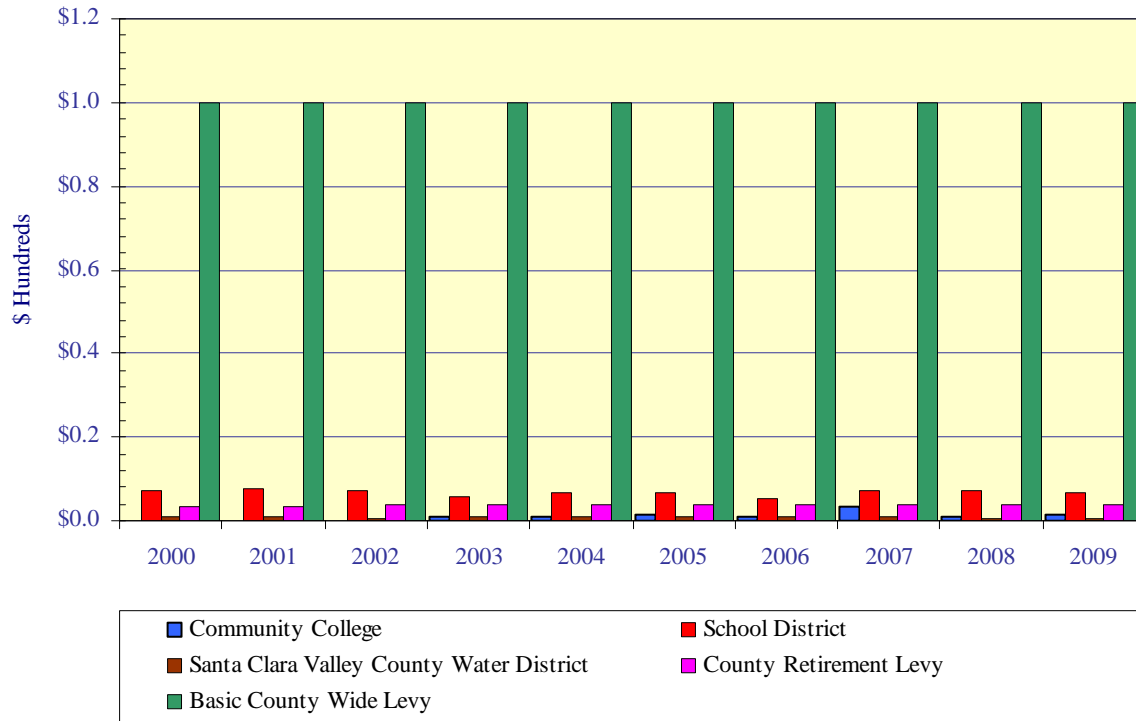
The State Constitution requires property to be assessed at one hundred percent of the most recent purchase price, plus an increment of no more than two percent annually, plus any local over-rides. These values are considered to be full market values.



City of Palo Alto - Property Tax Rates

All Overlapping Governments

Last Ten Fiscal Years



Fiscal Year	Basic County Wide Levy	County Retirement Levy	Santa Clara Valley Water District	School District	Community College	Total
2000	1.0000	0.0319	0.0085	0.0740	0.0000	1.1144
2001	1.0000	0.0356	0.0075	0.0771	0.0000	1.1202
2002	1.0000	0.0364	0.0062	0.0727	0.0000	1.1153
2003	1.0000	0.0388	0.0072	0.0586	0.0108	1.1154
2004	1.0000	0.0388	0.0087	0.0666	0.0110	1.1251
2005	1.0000	0.0388	0.0092	0.0680	0.0129	1.1289
2006	1.0000	0.0388	0.0078	0.0526	0.0119	1.1111
2007	1.0000	0.0388	0.0072	0.0720	0.0346	1.1526
2008	1.0000	0.0388	0.0071	0.0702	0.0113	1.1274
2009	1.0000	0.0388	0.0061	0.0674	0.0123	1.1246

Source: County of Santa Clara, Tax Rates and Information

City of Palo Alto - Property Tax Levies and Collections

Last Ten Fiscal Years (\$000)

<u>Fiscal Year</u>	<u>Total Tax Levy (a)</u>	<u>Current Tax Collections</u>	<u>Percent of Levy Collected</u>	<u>Delinquent Tax Collections (b)</u>	<u>Total Tax Collections</u>	<u>Percent of Total Tax Collections to Tax Levy</u>
2000	10,770	10,770	100%	-	10,770	100%
2001	12,110	12,110	100%	-	12,110	100%
2002	13,231	13,231	100%	-	13,231	100%
2003	13,821	13,821	100%	-	13,821	100%
2004	13,707	13,707	100%	-	13,707	100%
2005	16,657	16,657	100%	-	16,657	100%
2006	18,731	18,731	100%	-	18,731	100%
2007	21,466	21,466	100%	-	21,466	100%
2008	23,084	23,084	100%	-	23,084	100%
2009	25,432	25,432	100%	-	25,432	100%

Source: County of Santa Clara Assessor's Office

Note: Current tax collections beginning in 1993 have been reduced by a mandatory tax reallocation imposed by the State of California.

- (a) During fiscal year 1995, the County began providing the City 100% of its tax levy under an agreement which allows the County to keep all interest and delinquency charges collected.
- (b) Effective with the fiscal year 1993-94, the City is on the Teeter Plan, under which the County of Santa Clara pays the full tax levy due. All prior delinquent taxes were also received in that fiscal year.



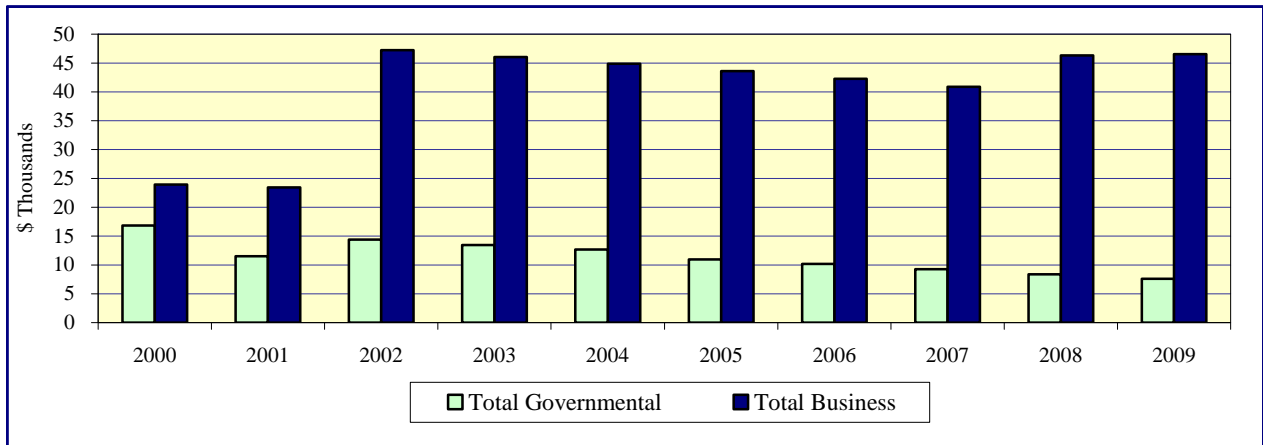
City of Palo Alto - Principal Property Tax Payers

Current Year and Nine Years Ago (\$000)

Taxpayer	FY 2009			FY 2000		
	Taxable Assessed Value	Rank	Percentage of Total City Taxable Assessed Value	Taxable Assessed Value	Rank	Percentage of Total City Taxable Assessed Value
Leland Stanford Jr University	\$3,288,925	1	15.6%	\$1,795,791	1	17.0%
Space System /Loral Inc.	\$182,172	2	0.9%	194,548	2	1.8%
Arden Realty Limited Partnership	\$109,703	3	0.5%			0.0%
Whisman Ventures, LLC	\$102,479	4	0.5%			0.0%
ECI 2 Bayshore LLC / ECI Hamilton LLC	\$66,421	5	0.3%			0.0%
Blackhawk Parent LLC	\$48,960	6	0.2%			0.0%
Pacific Hotel Dev Venture L P	\$42,829	7	0.2%			0.0%
300 / 400 Hamilton Associates	\$40,413	8	0.2%			0.0%
505 Hamilton Avenue Partners L.P.	\$39,355	9	0.2%			0.0%
Ronald & Ann Williams Charit Foundation	\$39,189	10	0.2%			0.0%
Sun Microsystems Inc.			0.0%	69,529	3	0.7%
Harbor Investments Partners			0.0%	54,700	5	0.5%
Embarcadero Bayshore Invts. Et A1			0.0%	29,464	7	0.3%
Digital Equipment Corporation			0.0%	25,782	8	0.2%
Embarcadero Place Corporation			0.0%	62,000	4	0.6%
Cowper-Hamilton Associates			0.0%	38,397	6	0.4%
Hyatt Equities, LLC			0.0%	23,529	9	0.2%
Seabiscuit LLC Et A1			0.0%	22,611	10	0.2%
Subtotal	\$3,960,446		18.8%	\$2,316,351		22.0%
Total Net Assessed Valuation:						
FY 2009	\$21,085,609					
FY 2000	\$10,533,778					

Source: County of Santa Clara compiled by Hunt Consulting, LLC

City of Palo Alto - Ratio of Outstanding Debt by Type
Last Ten Fiscal Years (\$000)



Governmental Activities

Fiscal Year	Certificates of Participation	Special Assessment Debt	Capital Lease Obligations	Total
2000	11,625	4,670	537	16,832
2001	10,700	670	113	11,483
2002	13,695	595	84	14,374
2003	12,905	510	57	13,472
2004	12,215	420	25	12,660
2005	10,625	325	0	10,950
2006	9,915	225	0	10,140
2007	9,175	115	0	9,290
2008	8,405	0	0	8,405
2009	7,605	0	0	7,605

Business-Type Activities

Fiscal Year	Utility Revenue Bonds	Total	Total Primary Government	Percentage of Assessed Value (a)	Percentage of Personal Income (b)	Per Capita (c)
2000	23,935	23,935	40,767	0.39 %	1.02%	\$0.66
2001	23,465	23,465	34,948	0.30 %	1.03%	\$0.57
2002	47,210	47,210	61,584	0.47 %	2.04%	\$1.02
2003	46,069	46,069	59,541	0.43 %	1.97%	\$0.98
2004	44,862	44,862	57,522	0.38 %	1.87%	\$0.95
2005	43,598	43,598	54,548	0.34 %	1.67%	\$0.88
2006	42,288	42,288	52,428	0.32 %	1.53%	\$0.84
2007	40,887	40,887	50,177	0.28 %	1.46%	\$0.80
2008	46,310	46,310	54,715	0.29 %	1.54%	\$0.86
2009	46,565	46,565	54,170	0.26 %	1.47%	\$0.84

Sources: City of Palo Alto

(a) County of Santa Clara (assessed value)

(b) Per capita personal income are only available for Santa Clara County.

Personal income is the product of the countywide per capita amount and the City's population.

(c) State of California, Department of Finance (population)

California State Department of Transportation Forecasts

Note: Debt amounts exclude any premiums, discounts, or other amortization amounts.

Details regarding the City's outstanding debt can be found in the notes to the financial statements.

City of Palo Alto - Computation of Direct and Overlapping Debt
June 30, 2009

FY 2009 Assessed Valuation	<u><u>\$21,085,609,000</u></u>		
	Total Debt Outstanding	Percentage Applicable To City of Palo Alto (a)	Amount Applicable To City of Palo Alto
<u>OVERLAPPING TAX AND ASSESSMENT DEBT:</u>			
Santa Clara County	\$350,000,000	7.784%	\$27,244,000
Santa Clara Valley Water District, Zone W-1	1,390,000	0.456%	6,338
Foothill-DeAnza Community College District	482,349,288	23.332%	112,541,736
Palo Alto Unified School District	215,619,249	89.250%	192,440,180
Fremont Union High School District	208,080,000	0.006%	12,485
Mountain View-Los Altos Union High School District	35,638,260	1.024%	364,936
Cupertino Union School District	124,159,021	0.001%	1,242
Los Altos School District	94,359,000	0.992%	936,041
Whisman School District	21,586,425	3.730%	805,174
El Camino Hospital District	145,820,000	0.095%	138,529
City of Palo Alto Special Assessment Bonds	36,625,000	100.000%	36,625,000
Santa Clara Valley Water District Benefit Assessment District	161,485,000	7.784%	12,569,992
TOTAL OVERLAPPING TAX AND ASSESSMENT DEBT	<u><u>\$1,877,111,243</u></u>		<u><u>\$383,685,653</u></u>
<u>DIRECT AND OVERLAPPING GENERAL FUND DEBT:</u>			
Santa Clara County General Fund Obligations	\$862,655,000	7.784%	\$67,149,065
Santa Clara County Pension Obligations	389,174,822	7.784%	30,293,368
Santa Clara County Board of Education Certificates of Participation	14,530,000	7.784%	1,131,015
Foothill-DeAnza Community College District Certificates of Participation	25,605,000	23.332%	5,974,159
Mountain View-Los Altos Union High School District Certificates of Participation	6,880,000	1.024%	70,451
Cupertino Union School District Certificates of Participation	1,215,000	0.001%	12
City of Palo Alto General Fund Obligations	7,605,000	100.000%	7,605,000
Santa Clara County Vector Control District Certificates of Participation	4,125,000	7.784%	321,090
Midpeninsula Regional Open Space Park District General Fund Obligations	116,673,031	13.545%	15,803,362
TOTAL DIRECT AND OVERLAPPING GENERAL FUND DEBT	<u><u>\$1,428,462,853</u></u>		<u><u>\$128,347,522</u></u>
COMBINED TOTAL DEBT	<u><u>\$3,305,574,096</u></u>		<u><u>\$512,033,175</u></u> (b)

Note: (a) Percentage of overlapping agency's assessed valuation located within boundaries of the city.

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

Ratios to Assessed Valuation

Combined Direct Debt (\$7,605,000)	0.04%
Total Overlapping Tax and Assessment Debt	1.82%
Combined Total Debt	2.41%

STATE SCHOOL BUILDING AID REPAYABLE AS OF 06/30/09: \$0

Source: California Municipal Statistics, Inc.

City of Palo Alto - Computation of Legal Bonded Debt Margin

June 30, 2009

(in thousands of dollars)

Assessed Valuation:

Secured property assessed value, net of exempt real property	\$21,085,609
---	--------------

Bonded debt limit 3.75% of assessed value (a)	\$790,710
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Amount of debt subject to limit: (b)

Certificates of participation	7,605
Special assessment debt with government commitment	0
Total Debt	7,605

Less amount of debt not subject to limit	7,605
--	-------

Amount of debt subject to limit	0
---------------------------------	---

Legal bonded debt margin	\$790,710
---------------------------------	-----------

Fiscal Year	Debt Limit	Total Net Debt Applicable to Limit	Legal Debt Margin	Total net debt applicable to the limit as a percentage of debt limit
2000	395,017	0	395,017	0.00%
2001	435,372	0	435,372	0.00%
2002	491,351	0	491,351	0.00%
2003	516,615	0	516,615	0.00%
2004	561,561	0	561,561	0.00%
2005	609,378	0	609,378	0.00%
2006	609,377	0	609,377	0.00%
2007	660,360	0	660,360	0.00%
2008	709,593	0	709,593	0.00%
2009	790,710	0	790,710	0.00%

Source: Annual Financial Statements

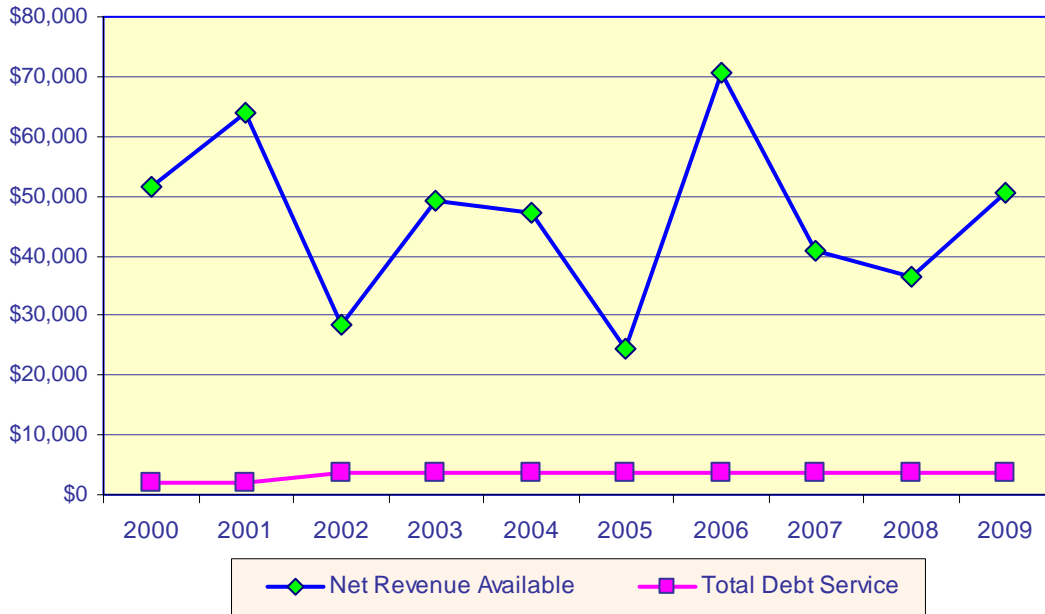
- Notes:**
- (a) California Government Code, Section 43605 sets the debt limit at 15%. The Code section was enacted prior to the change in basing assessed value to full market value when it was previously 25% of market value. Thus, the limit shown as 3.75% is one-fourth the limit to account for the adjustment of showing assessed valuation at full cash value. Prior year limits have been adjusted to conform to the current year methodology.
 - (b) In accordance with California Government Code Section 43605, only the City's general obligation bonds are subject to the legal debt limit of 15%. As of June 30, 2009, the City had no general obligation bonds outstanding. The above does not include debt recorded in the Enterprise Funds because such debt is not subject to legal debt margin.
Special assessment debt excludes debt where there is no government commitment.



City of Palo Alto - Revenue Bond Coverage

Water, Electric, Gas, Wastewater Collection, Wastewater Treatment and Storm Drainage Funds

Last Ten Fiscal Years (\$000)



Fiscal Year	Gross Revenue	Direct Operating Expenditures	Net Revenue Available for Debt Services (a)	Debt Service			Coverage
				Principal	Interest	Total	
2000	130,550	78,880	51,670	545	1,363	1,908	27.08
2001	197,022	133,012	64,010	555	1,342	1,897	33.74
2002	176,947	148,345	28,602	1,955	1,660	3,615	7.91
2003	165,414	116,268	49,146	1,255	2,354	3,609	13.62
2004	169,047	121,988	47,059	1,310	2,307	3,617	13.01
2005	171,493	147,123	24,370	1,365	2,257	3,622	6.73
2006	214,944	144,465	70,479	1,410	2,203	3,613	19.51
2007	205,258	164,340	40,918	1,465	2,147	3,612	11.33
2008	222,799	186,285	36,514	1,525	2,088	3,613	10.11
2009	246,028	195,489	50,539	1,590	2,024	3,614	13.98

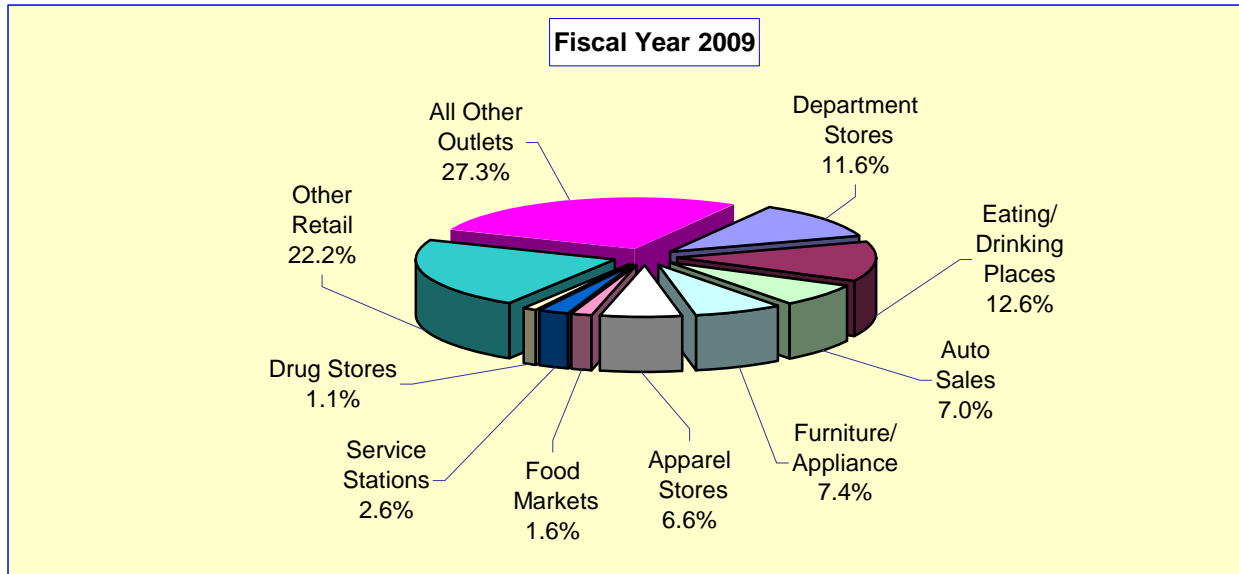
Source: Annual Financial Statements

Note: (a) Excludes depreciation and amortization expense.

Details regarding the City's outstanding debt can be found in the notes to the financial statements.

FY 2008 Principal for Debt Service was restated due to correction of data.

City of Palo Alto- Taxable Transactions by Type of Business
Last Ten Fiscal Years (\$000)



RETAIL STORES

Fiscal Year	Department Stores	Eating/Drinking Places	Auto Sales	Furniture/Appliance	Apparel Stores	Food Markets	Service Stations	Drug Stores	Other Retail	Retail Stores Total	All Other Outlets	Total
2000	3,011	2,379	2,724	1,845	1,226	347	323	173	4,169	16,197	6,386	22,583
2001	3,112	2,551	3,118	1,824	1,343	351	417	186	4,706	17,608	7,270	24,878
2002	2,646	2,321	2,533	1,593	1,171	371	379	180	3,674	14,868	5,009	19,877
2003	2,316	2,172	2,094	1,455	1,114	375	388	171	2,811	12,896	4,834	17,730
2004	2,425	2,168	1,958	1,479	1,186	351	437	168	3,698	13,870	3,997	17,867
2005	2,621	2,206	1,966	1,176	1,310	356	533	317	3,590	14,075	5,139	19,214
2006	2,664	2,306	2,062	1,168	1,346	370	595	392	4,244	15,147	5,042	20,189
2007	2,751	2,486	1,954	1,109	1,485	374	602	203	5,075	16,039	5,185	21,224
2008	2,685	2,566	1,731	1,685	1,497	349	622	405	4,682	16,222	5,066	21,288
2009	2,251	2,443	1,358	1,431	1,258	315	493	214	4,284	14,047	5,277	19,324

Source: California State Board of Equalization, compiled by MBIA Muniservices Company

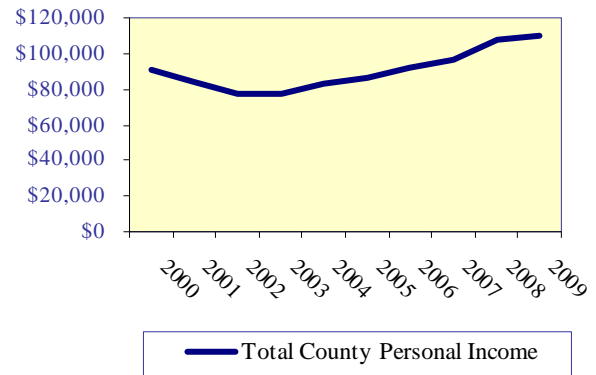
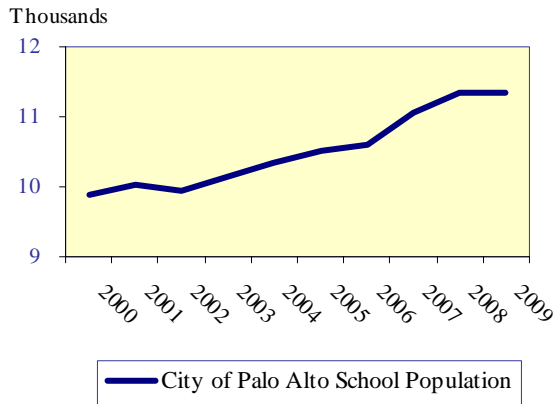
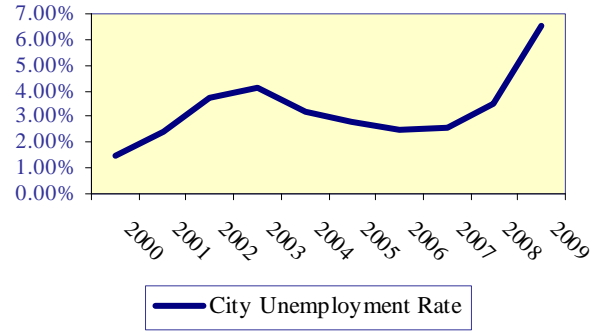
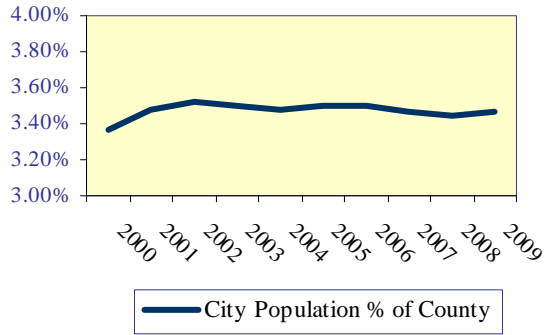
**SALES TAX RATES FOR THE
 FISCAL YEAR ENDED JUNE 30, 2009**

State Funds	7.00%
County Transportation Fund (Transportation Development Act)	0.25%
County Transportation Fund	1.00%
City	1.00%
	9.25%

Source: California State Board of Equalization

City of Palo Alto - Demographic and Economic Statistics

Last Ten Fiscal Years



Fiscal Year	City of Palo Alto Population	City of Palo Alto Unemployment Rate (%)	City of Palo Alto School Population	Santa Clara County Population	City Population % of County	Santa Clara Total County Personal Income (\$000)
2000	58,500	1.5%	9,881	1,736,700	3.37%	91,386,181
2001	60,200	2.4%	10,031	1,728,680	3.48%	83,838,707
2002	60,500	3.7%	9,952	1,719,565	3.52%	77,548,912
2003	60,465	4.1%	10,151	1,729,917	3.50%	77,680,349
2004	60,246	3.2%	10,341	1,731,422	3.48%	82,638,917
2005	61,674	2.8%	10,527	1,759,585	3.51%	86,400,000 *
2006	62,148	2.5%	10,607	1,773,258	3.50%	91,600,000 *
2007	62,615	2.6%	11,056	1,808,056	3.46%	96,900,000 *
2008	63,367	3.5%	11,329	1,837,075	3.45%	107,900,000 *
2009	64,484	6.5%	11,329	1,857,621	3.47%	109,700,000 *

Source: California State Department of Finance
 State Employment Development Office
 Palo Alto Unified School District

* California State Department of Transportation Forecasts

City of Palo Alto - Principal Employers

Current Year and Nine Years Ago

Employer	FY 2009		FY 2000	
	Number of Employees	Rank	Number of Employees	Rank
Stanford University	9,821	1	5,000 +	1
Stanford University Medical Center/Hospital	5,025	2	750 - 1,000	10
Veteran's Affairs Palo Alto Health Care System	3,500	3	1,000 +	9
Lucile Packard Children's Hospital	3,326	4		
Hewlett-Packard Company	2,001	5	1,000	8
Palo Alto Medical Foundation	2,000	6	1,500 +	6
Space Systems Loral	1,700	7	2,700	2
Wilson Sonsini Goodrich Rosati	1,500	8		
Palo Alto Unified School District	1,304	9	1,636	4
City of Palo Alto	1,100	10		
Varian Associates			1,500 - 2,000	3
Alza Corporation			1,500 +	5
Roche Bioscience			1,000 - 1,500	7

Total City Day Population

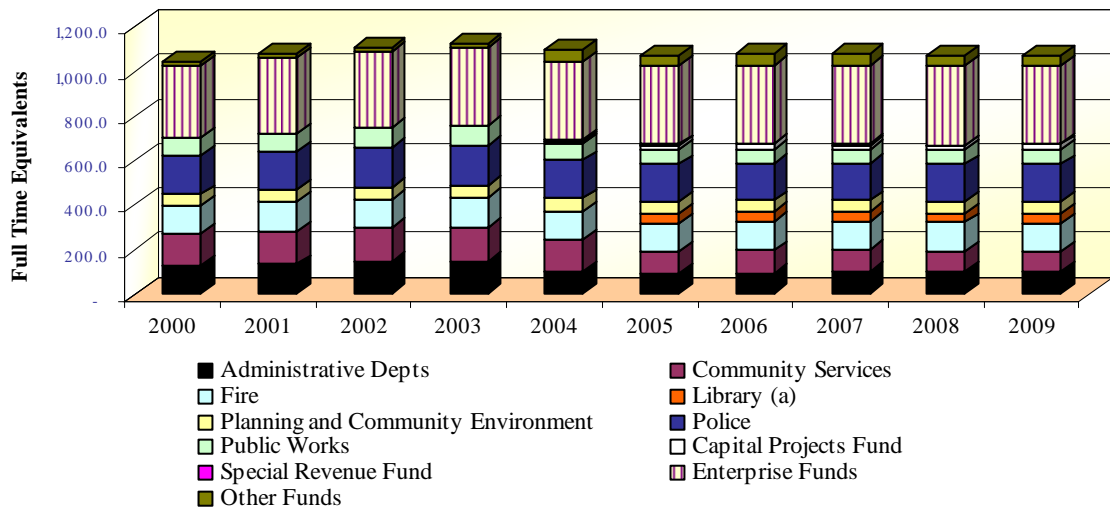
64,484

Source: FY 2009: www.ReferenceUSA.com, www.stanfordhospital.org, www.lpch.org, www.pausd.org
 FY 2000: Palo Alto Weekly



City of Palo Alto - Full-Time Equivalent City Government Employees by Function

Last Ten Fiscal Years



	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Governmental Funds										
General Fund										
Administrative Depts	126.35	133.35	143.60	145.10	101.10	96.24	96.65	99.05	98.65	97.80
Community Services	142.25	152.00	153.00	153.00	144.75	98.25	99.25	97.25	96.25	96.50
Fire	128.00	129.00	129.00	132.50	128.50	126.00	127.00	127.00	127.00	126.69
Library (a)						44.00	44.25	43.75	43.75	43.75
Planning and Community Environment	51.00	52.00	56.50	59.00	54.80	53.30	53.30	53.30	53.30	53.30
Police	173.00	173.00	176.50	177.50	171.00	164.50	164.00	163.00	163.00	164.00
Public Works	83.42	85.98	87.05	93.05	76.20	67.90	67.90	67.90	67.90	69.23
Capital Projects Fund					12.70	20.20	20.20	20.00	20.00	20.67
Special Revenue Fund					1.20	1.20	1.20	1.20	1.20	1.20
Enterprise Funds										
Public Works Department (Refuse, Storm Drain, Wastewater Treatment)	107.58	109.52	110.45	110.45	111.35	112.65	112.65	112.65	112.65	113.55
Utilities Department (Administrative, Electric, Gas, Wastewater Collection, Water)	215.50	224.50	230.50	229.50	233.75	233.90	235.90	234.90	234.90	238.01
CPA External Services (b)			4.00	7.00	5.70	6.00	6.00	5.80	5.80	
Other Funds										
Printing and Mailing	5.15	5.15	4.15	4.15	4.15	4.70	4.60	4.65	4.05	4.05
Technology					33.15	29.56	29.60	29.80	29.80	30.65
Equipment Management	14.00	14.00	15.00	15.00	16.00	16.00	16.00	16.20	16.20	16.20
Total	1,046.25	1,078.50	1,109.75	1,126.25	1,094.35	1,074.40	1,078.50	1,076.45	1,074.45	1,075.60

Source: City of Palo Alto - Adopted Operating Budget

Notes: (a) Library became its own entity effective 2005, originally part of Community Services.

(b) CPA External Services of the original 5.80 FTE, .80 FTE was transferred to the Technology Fund and 5.00 FTE was eliminated.

City of Palo Alto - Operating Indicators by Function/Program
Last Ten Fiscal Years

Function / Program	Fiscal Year		
	2000	2001	2002
Public Safety:			
Fire:			
Number of Fire Hydrants	1,708	1,729	1,741
Planning & Community Environment			
Number of Housing Units	25,732	26,048	26,841
Commercial & Industrial Space - Million Sq Ft	27.3	27.3	27.3
Electric Utility			
Number of Customer Accounts	27,533	28,097	28,348
Million of KWH Sold	1,134	1,057	997
Fiber Optics Utility			
Number of Fiber Optic Connections	53	41	30
Water Utility			
Number of Customer Accounts	18,921	19,335	19,437
Million CCF Sold	6.6	5.9	5.9
Gas Utility			
Number of Customer Accounts	23,154	23,101	23,116
Million Therms Sold	37.0	36.7	33.7
Waste Water			
Number of Customer Accounts	21,973	21,752	21,772
Millions of Gallons Processed	9,834	9,243	8,699

Source: City of Palo Alto
 State of California, Dept of Finance (housing units)

Note: Fiscal Years 2004-2006, number of fire hydrants are restated due to change in source of data.
 Fiscal Years 2007 and 2008, for Water Utility - Million CCF Sold, are restated due to correction of measuring units.



Fiscal Year

2003	2004	2005	2006	2007	2008	2009
1,746	1,874	1,873	1,919	1,944	1,948	1,949
26,934 27.3	27,019 27.3	27,522 27.3	27,767 27.3	27,763 27.3	27,938 27.3	28,291 27.3
28,408 957	28,482 958	28,539 959	28,653 966	28,684 978	29,024 977	28,527 996
23	18	39	22	23	27	26
19,487 5.6	19,557 6.0	19,605 5.3	19,645 5.2	19,726 5.4	19,942 5.5	19,442 5.7
23,169 31.8	23,216 31.5	23,300 32.0	23,353 31.5	23,357 31.3	23,502 32.2	23,090 30.6
21,819 8,704	21,830 8,238	21,825 8,395	21,784 8,972	21,835 9,220	21,990 8,510	22,210 7,958

City of Palo Alto - Capital Asset Statistics by Function/Program

Last Ten Fiscal Years

Function/Program	Fiscal Year			
	2000	2001	2002	2003
Public Safety:				
Fire:				
Fire Stations	8	8	8	8
Fire Apparatus	23	24	25	22
Police:				
Police Stations	1	1	1	1
Police Patrol Vehicles	29	33	33	33
Community Services				
Acres - Downtown/Urban Parks	170	170	170	170
Acres - Open Space	3,731	3,731	3,731	3,731
Parks and Preserves	35	33	34	34
Golf Course	1	1	1	1
Tennis Courts	52	52	52	52
Athletic Center	1	1	1	1
Community Centers	4	4	4	4
Theatres	3	3	3	3
Cultural Center/Art Center	1	1	1	1
Junior Museum and Zoo	1	1	1	1
Swimming Pools	1	1	1	1
Nature Center	2	2	2	2
Libraries				
Libraries	6	6	6	6
Public Works				
Number of Trees Maintained	39,923	38,094	37,941	34,939
Electric Utility				
Overhead Pole Miles	228	227	227	227
Underground Trench Miles	209	220	186	186
Water Utility				
Miles of Water Mains	221	222	226	226
Gas Utility				
Miles of Gas Mains	170	201	207	207
Waste Water				
Miles of Sanitary Sewer Lines	219	218	202	202

Source: City of Palo Alto



Fiscal Year

2004	2005	2006	2007	2008	2009
8	8	8	8	8	8
23	25	25	25	23	28
1	1	1	1	1	1
30	30	30	30	30	30
170	170	170	157	157	157
3,731	3,731	3,731	3,744	3,744	3,744
34	35	35	36	36	36
1	1	1	1	1	1
52	52	52	51	51	51
1	1	1	4	4	4
4	4	4	4	4	4
3	3	3	3	3	3
1	1	1	1	1	1
1	1	1	1	1	1
1	1	1	1	1	1
2	2	2	3	3	3
5	5	5	5	5	5
35,440	35,096	34,841	34,556	35,322	35,255
227	225	217	194	193	193
186	188	210	252	253	253
226	226	217	217	217	214
207	207	207	207	207	207
202	202	202	202	202	207

City of Palo Alto - Insurance Coverage.....
June 30, 2009

TYPE	COVERAGE (Deductible)	LIMITS	COMPANY	EXPIRATION DATE
PROPERTY LOSS				
Blanket	All real & personal property (\$10,000 deductible), Fine Arts (\$2,500 deductible)	\$360,801,026	CA Public Entity Property Program	07/01/10
Boiler & Machinery	All real & personal property (\$25,000 deductible)	\$1,000,000 maximum all risk per occurrence limit \$1,000,000 minimum contingent business interruption	CA Public Entity Property Program	07/01/10
Flood Insurance	All real property 1305 Middlefield Road (\$1,000 deductible)	\$500,000	Hartford Fire Insurance Co.	04/07/10
FINANCIAL LOSS				
Employee Dishonesty	Position bond-faithful performance per loss (\$5,000 deductible)	\$1,000,000 / \$4,000,000 x \$1,000,000 per occurrence for City Mgr. & Director of ASD	Fidelity & Deposit Co.	03/22/12
UMBRELLA EXCESS LIABILITY				
	City is a member of an insurance pool participating with a number of other California cities (\$1,000,000 self-insured retention)	\$50,000,000 annual aggregate	Everest Ins. Co. Lexington Ins Co.	07/01/10
Trustees Errors and Omissions	Bodily injury and property damage liability Errors and omissions liability			
SPECIAL LIABILITY				
Volunteers Accident	Medical - Each person / (\$100 deductible)	\$20,000	Life Insurance Co. of North America	02/03/10
Special Events	Bodily injury	\$1,000,000 per occurrence	Axis Surplus Insurance Company	01/01/10
EMPLOYEE BENEFIT				
Travel Accident	Indemnity, based on salary	\$1,500,000 per accident	Life Insurance Co. of North America	06/01/10
EMPLOYEE HEALTH PLAN				
	The City participates in the California Public Employees' Medical and Health Care Act (PEMHCA) program to provide medical benefits to employees and retirees			
WORKERS' COMPENSATION				
	City is self-insured for first \$500,000 liability	\$500,000 per occurrence		07/01/10
EXCESS WORKERS' COMPENSATION				
	Pooled Retention	\$4,000,000 limit per occurrence Workers Comp and Employers Liability	CA. Public Entity Insurance Authority	07/01/10
	Reinsured Layer	\$45,000,000 workers comp per occurrence, excess of pooled retention limit, includes \$5,000,000 employers liability	ACB American Insurance Co.	07/01/10

Source: Human Resources Dept, City of Palo Alto



Single Audit Index.....

Schedule of Current Year Findings and Questioned Costs 161

Section I - Summary of Auditor’s Results..... 161

Section II - Financial Statement Findings 162

Section III - Federal Award Findings and Questioned Costs 162

Section IV - Status of Prior Year Findings
and Questioned Costs..... 162

Schedule of Expenditures of Federal Awards 163

Notes to Schedule of Expenditures of Federal Awards 165

Report On Internal Control over Financial Reporting and On Compliance
And Other Matters Based on an Audit of Financial Statements
Performed In Accordance With Government Auditing Standards..... 167

Report On Compliance with Requirements Applicable To
Each Major Program and On Internal Control Over Compliance
In Accordance With OMB Circular A-133 169



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Single Audit Section.....

This section provides an overview of grant awards received from the Federal government. The Single Audit Act Amendments of 1996 require local governments to report and audit Federal funds separately from their Basic Financial Statements.



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Schedule of Findings.....

CITY OF PALO ALTO
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
For The Year Ended June 30, 2009

SECTION I—SUMMARY OF AUDITOR’S RESULTS

Financial Statements

Type of auditor’s report issued:		Unqualified		
Internal control over financial reporting:				
• Material weakness(es) identified?		Yes	<u> X </u>	No
• Significant deficiency(ies) identified that are not considered to be material weaknesses?	<u> X </u>	Yes		None Reported
Noncompliance material to financial statements noted?		Yes	<u> X </u>	No

Federal Awards

Type of auditor’s report issued on compliance for major programs:		Unqualified		
Internal control over major programs:				
• Material weakness(es) identified?		Yes	<u> X </u>	No
• Significant deficiency(ies) identified that are not considered to be material weaknesses?		Yes	<u> X </u>	None Reported
Any audit findings disclosed that are required to be reported in accordance with section 510(a) of OMB Circular A-133?		Yes	<u> X </u>	No

Identification of major programs:

CFDA#(s)	Name of Federal Program or Cluster
66.458	Environmental Protection Agency - State Water Resources Control Board Loan
97.044	U.S. Department of Homeland Security - Assistance to Firefighters Grant

Dollar threshold used to distinguish between type A and type B programs: \$300,000

Auditee qualified as low-risk auditee? X Yes No



SECTION II – FINANCIAL STATEMENT FINDINGS

Our audit did not disclose any significant deficiencies, or material weaknesses or instances of noncompliance material to the basic financial statements. However, we did communicate other matters to the City Council in our separate Memorandum on Internal Control dated October 23, 2009 which is an integral part of our audits and should be read in conjunction with this report.

SECTION III – FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

Our audit did not disclose any findings or questioned costs required to be reported in accordance with section 510(a) of OMB Circular A-133.

**SECTION IV - STATUS OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS –
Prepared by Management**

Financial Statement Prior Year Findings

There were no prior year Financial Statement Findings reported.

Federal Award Prior Year Findings and Questioned Costs

There were no prior year Federal Award Findings and Questioned Costs reported.



CITY OF PALO ALTO
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
 FOR THE FISCAL YEAR ENDED JUNE 30, 2009

Program Name	Identifying Pass-Through Grant Number	Catalog of Federal Domestic Assistance Number	Program Expenditures
Department of Housing and Urban Development			
Community Development Block Grant Program	B-08-MC-06-0020		
Program Expenditures		14.218	121,376
Subgrants:			
Emergency Housing Consortium			7,500
OMBUDSMAN Program			7,800
Palo Alto Housing Corporation-Banker Counseling			30,000
New Housing Development			21,264
Clara Mateo Alliance Shelter			29,500
Clara Mateo Alliance Family Shelter			29,500
Shelter Network Haven Housing			8,500
InnVision			86,000
Project Sentinel - Fair Housing			26,800
Stevenson Housing - Windows/Doors			88,569
Stevenson Housing - Radiant Heating			143,300
Total CDBG Expenditures		14.218	<u>600,109</u>
Department of Transportation			
(Passed through California Department of Transportation)			
Intragency Hazardous Materials Public Sector Training and Planning Grants	OES ID #085-55282	20.703	<u>8,533</u>
Total Expenditures from Governor's office			<u>8,533</u>
Department of Energy	DE-FG36-03GO13066	81.087	<u>779,328</u>
Office of Water, Environmental Protection Agency			
(Passed through California State Water Resources Control Board)			
	Contract # 07-814-550-0 Loan # C-06-4132-110	66.458	<u>1,870,785</u>
U.S. Department of Homeland Security			
Assistance to Firefighter Grant	EMW-2008-FO-12589	97.044	<u>188,216</u>
TOTAL FEDERAL FINANCIAL AWARDS			<u><u>\$3,446,971</u></u>

See Notes to Schedule of Expenditures of Federal Awards



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NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Note 1.....

REPORTING ENTITY

The Schedule of Expenditure of Federal Awards (the Schedule) includes expenditures of federal awards for the City of Palo Alto, California and its component units as disclosed in the notes to the Basic Financial Statements.

Note 2.....

BASIS OF ACCOUNTING

Basis of accounting refers to *when* revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements, regardless of the measurement focus applied. All governmental funds and agency funds are accounted for using the modified accrual basis of accounting. All proprietary funds are accounted for using the accrual basis of accounting. Expenditures of Federal Awards reported on the Schedule are recognized when incurred.

OMB Circular A-133 requires that certain adjustments be made to expenditures recognized when incurred. The adjustments applicable to the City are summarized below:

Expenditure of Long-Term Debt Proceeds – In this fiscal year, the City received proceeds from long-term debt funded by the federal government passed through the California State Water Resources Control Board. In accordance with OMB Circular A-133, section .205(d) the City included current year expenditures of such proceeds on the Schedule of Expenditures of Federal Awards.

During FY 2009, the City expended \$1,870,785 in costs under the Office of Water, Environmental Protection Agency, Capitalization Grants For Clean Water State Revolving Funds Program (CFDA #66.458). As of June 30, 2009, the City had received \$1,459,975 in remittances from the State with another \$410,810 received subsequent to June 2009 as reimbursement of the above costs.

Note 3.....

DIRECT AND INDIRECT (PASS-THROUGH) FEDERAL AWARDS

Federal awards may be granted directly to the City by a federal granting agency or may be granted to other government agencies which pass-through federal awards to the City. The Schedule includes both of these types Federal award programs when they occur.



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Independent Auditor Reports.....

MAZE & ASSOCIATES

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REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

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

We have audited the financial statements of the City of Palo Alto as of and for the year ended June 30, 2009, and have issued our report thereon dated October 23, 2009. We conducted our audit in accordance with generally accepted auditing standards 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.

Internal Control over Financial Reporting

In planning and performing our audit, we considered the City's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the City's internal control over financial reporting.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the City's financial statements that is more than inconsequential will not be prevented or detected by the City's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the City's internal control.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

A Professional Corporation

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the City's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance and other matters that are required to be reported under *Government Auditing Standards*.

We have also issued a separate Memorandum on Internal Control dated October 23, 2009 which is an integral part of our audits and should be read in conjunction with this report.

This report is intended solely for the information and use of City Council, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Mage & Associates

October 23, 2009

MAZE & ASSOCIATES

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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

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

Compliance

We have audited the compliance of the City of Palo Alto with the types of compliance requirements described in the OMB Circular A-133 *Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2009. The City's major federal programs are identified in Section I - Summary of Auditor's Results included in the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the City's management. Our responsibility is to express an opinion on the City's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City's compliance with those requirements.

In our opinion, the City complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2009.

Internal Control over Compliance

The management of the City is responsible for establishing and maintaining effective internal controls over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of City's internal control over compliance.

A Professional Corporation

A *control deficiency* in a City's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the City's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the City's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the City's internal control.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider material weaknesses, as defined above.

Schedule of Expenditures of Federal Awards

We have audited the financial statements of the City as of and for the year ended June 30, 2009, and have issued our report thereon dated October 23, 2009. Our audit was performed for the purpose of forming opinions on the financial statements. The accompanying schedule of expenditures of federal awards is presented for the purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

The City's response to the findings identified in our audit is described in the accompanying schedule of findings and questioned costs. We did not audit the City's response and, accordingly, we express no opinion on it.

This report is intended solely for the information and use of City Council, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Maze + Associates

October 23, 2009

The City of Palo Alto is located in northern Santa Clara County, approximately 35 miles south of the City of San Francisco and 12 miles north of the City of San Jose. Spanish explorers named the area for the tall, twin-trunked redwood tree they camped beneath in 1769. Palo Alto incorporated in 1894 and the State of California granted its first charter in 1909.

AMERICANS WITH DISABILITIES ACT STATEMENT

In compliance with Americans with Disabilities Act (ADA) of 1990, this document may be provided in other accessible formats.

For information contact:

ADA Coordinator
250 Hamilton Avenue
(650) 329-2550
ada@cityofpaloalto.org

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