

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

1. Summary of Significant Accounting Policies

The basic financial statements of the City of Los Altos, California (the City) have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental agencies. The Governmental Accounting Standards Board (GASB) is the accepted standard setting body for establishing governmental accounting and financial reporting principles. The more significant of the City's accounting policies are described below.

a) Reporting Entity

The City incorporated in 1952. The City operates under an elected Council and appointed City Manager form of government and provides the following services: public safety, recreation, community development, public works, capital improvements, and general supporting administrative services. The City has no component units.

b) Basis of Presentation, Measurement Focus and Basis of Accounting

The accounts of the City are organized on the basis of funds, each of which is considered a separate accounting entity. The operations of each fund are accounted for within a separate set of self-balancing accounts which includes its assets, liabilities, fund equity, revenues and expenditures or expenses, as appropriate. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with finance-related legal and contractual provisions. The minimum number of funds is maintained consistent with such provisions and managerial requirements.

Government-wide and Fund Financial Statements

The City's Government-wide Financial Statements include a Statement of Net Position and a Statement of Activities and Changes in Net Position. These statements present summaries of governmental activities and business-type activities for the City, the primary government, accompanied by a total column. Fiduciary activities of the City are not included in these statements.

These basic financial statements are presented on an "economic resources" measurement focus and the accrual basis of accounting. Accordingly, all of the City's assets and liabilities, including capital assets, as well as infrastructure assets and long-term liabilities, are included in the accompanying Statement of Net Position. The Statement of Activities and Changes in Net Position presents changes in the net position of the City. Under the accrual basis of accounting, revenues are recognized in the period in which they are earned while expenses are recognized in the period in which the liability for goods or services is incurred.

Certain types of transactions are reported as program revenues for the city in three categories:

- Charges for services
- Operating grants and contributions
- Capital grants and contributions

CITY OF LOS ALTOS, CALIFORNIA
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Fiscal year ended June 30, 2013

1. Significant Accounting Policies, continued

b) Basis of Presentation, Measurement Focus and Basis of Accounting, continued

Certain eliminations have been made as prescribed by GASB Statement No. 34 in regards to inter-fund activities, payables, and receivables. All internal balances in the Statement of Net Position have been eliminated except those representing balances between the governmental activities and the business-type activities, which are presented as internal balances and eliminated in the total primary government column. In the Statement of Activities and Changes in Net Position internal service fund transactions have been eliminated; however, those transactions between governmental and business-type activities have not been eliminated. The following inter-fund activities have been eliminated:

- Due to, due from other funds
- Transfers in, transfers out
- Internal service fund transactions

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989 are generally followed by the proprietary funds in both the Government-Wide and Proprietary Fund financial statements to the extent that those standards do not conflict with or contradict guidance of the GASB. Governments also have the option of following subsequent private-sector guidance for their business-type activities and Enterprise Funds, subject to the same limitations. The City has elected not to follow subsequent private-sector guidance.

Governmental Fund Financial Statements

Governmental fund financial statements include a Balance Sheet and a Statement of Revenues, Expenditures and Changes in Fund Balances for all major governmental funds and non-major funds in the aggregate. An accompanying schedule is included to reconcile and explain the differences in fund balances as presented in these statements to the net position presented in the Government-Wide financial statements.

Governmental funds are accounted for on a spending or “*current financial resources*” measurement focus and the modified accrual basis of accounting. Accordingly, only current assets and current liabilities are included on the balance sheets. The Statement of Revenues, Expenditures and Changes in Fund Balances present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets. Under the modified accrual basis of accounting, revenues are recognized in the accounting period in which they become both measurable and available to finance expenditures of the current period.

Revenues are recorded when received in cash, except that revenues subject to accrual (generally 60 days after year-end) are recognized when due. The City’s primary revenue sources, which have been treated as susceptible to accrual by the City, are: property tax, sales tax, hotel tax, special assessments, intergovernmental revenues, other taxes, interest revenue, rental revenue and certain charges for services. Expenditures are recorded in the accounting period in which the related fund liability is incurred and are accrued accordingly.

Deferred revenues arise when potential revenues do not meet both the “measurable” and “available” criteria for recognition in the current period. Deferred revenues also arise when the government receives resources before it has a legal claim to them, as when grant monies are received prior to incurring qualifying expenditures. In subsequent periods when both revenue recognition criteria are met or when the government has a legal claim to the resources, the deferred revenue is removed from the balance sheet and revenue is recognized.

CITY OF LOS ALTOS, CALIFORNIA
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Fiscal year ended June 30, 2013

1. Significant Accounting Policies, continued

b) Basis of Presentation, Measurement Focus and Basis of Accounting, continued

Governmental Fund Financial Statements, continued

The reconciliation of the Fund Financial Statements to the Government-wide Financial Statements is provided to explain the differences created by the integrated approach of GASB Statement No. 34.

Proprietary Fund Financial Statements

Proprietary Fund financial statements include a Statement of Net Position, a Statement of Revenues, Expenses and Change in Net Position, and a Statement of Cash Flows for all proprietary funds.

A column representing the City's internal service funds, those funds that support agency wide shared service costs, is also presented in these statements. These internal service balances and activities are combined with the governmental activities in the Government-wide Financial Statements.

Proprietary Funds are accounted for using the "economic resources" measurement focus and the accrual basis of accounting. Accordingly, all assets and liabilities (whether current or noncurrent) are included on the Statement of Net Position. The Statement of Revenues, Expenses and Change in Fund Net Position presents increases (revenues) and decreases (expenses) in total net position. Under the accrual basis of accounting, revenues are recognized in the period in which they are earned while expenses are recognized in the period in which liability for goods or services is incurred.

Proprietary Funds distinguish operating revenues and expenses and non-operating items. Operating revenues and expenses generally result from providing services in connection with the fund's principal ongoing operations. The principal operating revenues of the City's enterprise and internal service funds are charges for customer services, including sewer charges, solid waste fees, and support charges. Operating expenses for enterprise funds and internal service funds include the cost of services, administrative expenses, and depreciation on capital assets. All other revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

Fiduciary Fund Financial Statements

Fiduciary Fund financial statements include a Statement of Fiduciary Net Position. The City's Fiduciary Funds are comprised of agency funds used to account for the operating activities and for the special assessment collections pertaining to the North County Library Authority, Raymundo & Avalon Curb and Gutter Districts, and Blue Oak Lane Sewer Improvements. Agency Funds are custodial in nature (assets equal liabilities), do not involve the measurement of results of operations, and are accounted for on the accrual basis of accounting.

Internal Service Funds

Internal Service Funds account for services provided to other departments pertaining to the employee self-insurance dental program, unemployment insurance, workers' compensation insurance and liability insurance, all of which are funded on a cost reimbursement basis as budget projections and valuations develop.

CITY OF LOS ALTOS, CALIFORNIA
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Fiscal year ended June 30, 2013

1. Significant Accounting Policies, continued

b) Basis of Presentation, Measurement Focus and Basis of Accounting, continued

Major Funds

The City reports the following major governmental funds:

General Fund - accounts for all financial resources necessary to carry out basic governmental activities of the City that are not accounted for in another funds. The General Fund supports essential City services such as police, fire, street and parks maintenance, public works, and community development and recreation activities.

Real Property Proceeds Fund - accounts for the proceeds from the sale of real property.

Capital Project Fund - accounts for the acquisition and construction of major general government capital projects and plans that are financed by resources other than proprietary funds.

Equipment Replacement Fund - accounts for the revenues and expenditures related to the replacement of certain City equipment and vehicles.

Community Facilities Renewal Fund - accounts for the revenues and expenditures related to the community facilities renewal efforts.

The City reports the following major proprietary funds:

Sewer Fund - accounts for the operation (including waste water treatment) of the City's sewer treatment activities, a self-supporting activity which provides services on a user charge basis.

Solid Waste Fund - accounts for the administration and support of contracted solid waste services, a self-supporting user-charge for service activity.

Storm Drain Fund -accounts for the operation of the City's urban runoff and storm drain activities.

c) New Accounting Pronouncements

During fiscal year 2012-13, the City implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows and Resources, and Net Position* (GASB 63). The most notable impact of GASB 63 was the renaming of “net assets” to “net position” to reflect the difference between assets and liabilities and provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources.

d) Recognition of Interest Liability

In the Governmental Fund Financial Statements, interest expenditures on long-term debt are recognized when payment is made. In the Government-wide Financial Statements and Proprietary Fund Financial Statements interest expense is recognized as the liability is incurred.

e) Use of Restricted and Unrestricted Net Assets

When an expense is incurred for purposes for which both restricted and unrestricted net assets are available, the City’s policy is to apply restricted net assets first.

CITY OF LOS ALTOS, CALIFORNIA
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Fiscal year ended June 30, 2013

1. Significant Accounting Policies, continued

f) Cash, Cash Equivalents and Investments

The City pools its available cash for investment purposes. The City considers pooled cash and investment amounts, with original maturities of three months or less, to be cash equivalents.

In accordance with GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, highly liquid market investments with maturities of one year or less at time of purchase are stated at amortized cost. All other investments are stated at fair value. Market value is used as fair value for those securities for which market quotations are readily available.

The City participates in an investment pool managed by the State of California known as the Local Agency Investment Fund (LAIF) which has invested a portion of the pool funds in Structured Notes and Asset-backed Securities. LAIF's investments are subject to credit risk with the full faith and credit of the State of California collateralizing these investments. In addition, these Structured Notes and Asset-backed Securities are subject to market risk as to change in interest rates.

The City places liquid assets in a co-managed investment account with the goal of enhancing the diversity of its investment holdings. This portfolio complies with state code investment requirements and is subject to a more restrictive City adopted investment policy. Such funds are held independently in City established investment custodial accounts.

For purposes of reporting cash flows, the City considers each fund's share in the cash and investments pool to be cash and cash equivalents including cash with fiscal agents.

g) Inventories

Inventory, mainly consisting vehicle fuel and paper supplies, is stated at cost on an average cost basis and is controlled by a perpetual inventory system which is adjusted to reflect periodic physical counts. Inventories are recorded as expenditures in the General Fund and charged to departments as consumed.

h) Restricted Cash

Fiscal agents acting on behalf of the City hold investment funds arising from the proceeds of long-term debt issuances. The funds may be used for specific capital outlays or for the payment of certain bonds, certificate of participation and have been invested only as permitted by specific State statutes or applicable City ordinance, resolution or bond indenture.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

1. Significant Accounting Policies, continued

i) Compensated Absences

Government-wide Financial Statements

For governmental and business-type activities, compensated absences are recorded as expenses and liabilities as the time is earned by employees.

Fund Financial Statements

For Governmental Funds, compensated absences are recorded as expenditures in the years paid. The General Fund is typically used to pay out compensated absences that arise in the course of any one year. Unpaid and accumulated liabilities for some compensated absences accrue to future resources. In Proprietary Funds, compensated absences are expensed to the various funds in the period they are earned, and such fund's share of the unpaid liability is recorded as a long-term liability of the fund.

j) Property Taxes

Santa Clara County (County) assesses all properties in the City, and it bills, collects and distributes property taxes to the City. Both secured and unsecured property taxes are levied on January 1. The County assesses properties and it 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 July 1 for the fiscal year.

Secured property tax is due in two installments, on November 1 and February 1, and it becomes delinquent after December 10 and April 10, respectively. The City and the County adopted the "alternative method of property tax distribution" known as the Teeter Plan that authorizes the County to allocate 100% of the secured property tax based on levy instead of collection and to retain all delinquent penalties and interest. Unsecured property tax is due on July 1 and becomes delinquent after August 31. Distribution of the unsecured property taxes is based on collections. Collection of delinquent accounts is the responsibility of the County, which retains all penalties. The County also distributes both penalties and interest collected for delinquent unsecured property taxes.

k) Capital Assets

Capital assets are valued at historical cost or estimated historical cost if actual historical cost was not available. Donated capital assets are valued at their estimated fair market value on the date donated. City policy has set the capitalization threshold for reporting capital assets at \$5,000 for equipment, \$25,000 for Building and Facility Improvements and \$100,000 for Infrastructure.

Depreciation is recorded on a straight-line basis over estimated useful lives of the assets as follows:

Buildings	50 years
Improvements	30-50 years
Equipment	3-10 years
Infrastructure	30-100 years

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

1. Significant Accounting Policies, continued

k) Capital Assets, continued

In accordance with GASB Statement No. 34, the City has included all infrastructures in its Statement of Net Position.

The City defines infrastructure as basic physical assets that allow the City to function. The assets include the street system. Each major infrastructure system can be divided into subsystems. For example, the street system can be subdivided into pavement, streetlights and traffic control devices (signs, signals and pavement markings). These subsystems were not delineated in the Government-wide Financial Statements. The appropriate operating department maintains information regarding the subsystems.

For all infrastructure systems, the City has elected to use the Basic Approach, as defined by GASB Statement No. 34, for infrastructure reporting. The valuation of the City's infrastructure assets are determined based on the original cost using one of the following methods:

- 1) Use of historical records where available
- 2) Standard unit costs appropriate for the construction/acquisition date of the asset
- 3) Present replacement cost indexed by a reciprocal factor of the price increase from the construction/acquisition date to the current date

Accumulated depreciation, defined as the total depreciation from the date of construction/acquisition to the current date, was computed on a straight-line method. The book value was then computed by deducting the accumulated depreciation from the original cost.

l) Long-Term Debt

Government-wide Financial Statements

Long-term debt and other financial obligations are reported as liabilities in the appropriate activities.

Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable premium or discount. Issuance costs are reported as deferred charges.

Fund Financial Statements

The Governmental Fund Financial Statements do not present long-term debt, which are shown in the Reconciliation of the Governmental Funds Balance Sheet to the Government-wide Statement of Net Position.

Governmental Funds recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuance are reported as other financing sources while discounts on debt issuance are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

Proprietary Fund Financial Statements use the same principles as those used in the Government-wide Financial Statements.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

1. Significant Accounting Policies, continued

m) Unearned Revenue

Government-wide Financial Statements

In the Government-wide Financial Statements, deferred revenue is recognized for transactions for which revenue has not yet been earned. Typical transactions recorded as deferred revenues in the Government-wide Financial Statements are long-term loans receivable and prepaid charges for services.

n) Deferred Revenue

Fund Financial Statements

In the Fund Financial Statements, deferred revenue is recorded when transactions have not yet met the revenue recognition criteria based on the modified accrual basis of accounting. The City records deferred revenue for transactions for which revenues have not been earned, or for which funds are not available to meet current financial obligations. Typical transactions for which deferred revenue is recorded are grants received but not yet earned or available, interest on inter-fund advances receivable, long-term assessments and long-term loans receivable.

o) Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities. In addition, estimates affect the reported amount of expenses. Actual results could differ from these estimates and assumptions.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

2. Cash, Cash Equivalents, and Investments

a) Cash Deposits

The City's cash and investments at June 30, 2013 are presented as follows:

Cash and investments	\$ 54,101,648
Cash and investments held by bond trustee	171,996
Fiduciary funds:	
Cash and investments	<u>1,967,699</u>
Total cash and investments	<u><u>\$ 56,241,343</u></u>

Cash and investments consist of the following as of June 30, 2013:

Cash on hand	\$ 2,170
Deposits with financial institutions	1,946,598
Investments:	
Bond trust investments	261,778
Liquid investments	32,866,612
Managed investments	<u>21,164,185</u>
Total cash and investments	<u><u>\$ 56,241,343</u></u>

b) Investments

Under the provisions of the City's investment policy and in accordance with Section 53601 of the California Government Code, the City is authorized to invest or deposit in the following:

Authorized Investment Type	Maximum Maturity	Maximum Percentage Allowed	Maximum Investment in One Issuer
Local Agency Investment Fund	N/A	N/A	\$50 M
Money Market Mutual Funds	N/A	20%	10%
Certificates of Deposit	3 years	50%	10%
Bankers' Acceptances	180 days	20%	10%
Commercial Paper	180 days	20%	10%
Repurchase Agreements	15 days	30%	N/A
U.S. Treasury Bills, Notes and Bonds	5 years	N/A	N/A
U.S. Government-Sponsored Enterprise Agencies	5 years	N/A	20%
Medium Term Corporate Notes	3 years	15%	5%

CITY OF LOS ALTOS, CALIFORNIA
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Fiscal year ended June 30, 2013

2. Cash, Cash Equivalents, and Investments, continued

c) Risk Disclosures

Interest Risk

Interest rate risk is the market rate changes that adversely affect the fair value of an investment. Generally, the sensitivity of an investment fair value to changes in market rates is greater when the maturity of the investment is longer.

Investments held in City Treasury grouped by maturity date at June 30, 2013, are shown below:

Investment Type	Remaining Maturity (in Years)			Total
	1 Year or Less	2 Years	3 Years	
Money Market	\$ 358,573	\$ -	\$ -	\$ 358,573
Government Sponsored Enterprises				
Treasury and agencies:				
Federal Home Loan Bank Bonds (FHLB)	-	-	1,186,512	1,186,512
Federal Home Loan Mrtg. Corp. Notes (FHLMC)	-	-	2,484,250	2,484,250
Federal National Mortg. Assn. Notes (FNMA)	-	-	4,440,106	4,440,106
Federal Farm Credit Bank (FFCB)	-	1,003,710	2,836,245	3,839,955
U.S. Securities	2,003,750	3,362,855	2,044,145	7,410,750
U.S. Corporate Notes	-	-	1,444,039	1,444,039
Local Agency Investment Funds (LAIF)	32,866,612	-	-	32,866,612
Trust Bond Funds	261,778	-	-	261,778
Total investments	\$ 35,490,713	\$ 4,366,565	\$ 14,435,297	54,292,575
Demand Deposits and Cash on Hand				1,948,768
Total cash and investments				\$ 56,241,343

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

2. Cash, Cash Equivalents, and Investments, continued

c) Risk Disclosures, continued

Credit Risk

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

At June 30, 2013, the City's deposit and investments were rated as follows:

Investment Type	Credit Quality Ratings		Market Value
	Moody's	S&P	
Cash on hand	Not Rated	Not Rated	\$ 2,170
US Bank General Checking	Not Rated	Not Rated	1,946,598
Money Market	Aaa	AA+	358,573
Securities of U.S. Government Agencies:			
Federal Home Loan Bank Bonds (FHLB)	Aaa	AA+	1,186,511
Federal Home Loan Mrtg. Corp. Notes (FHLMC)	Aaa	AA+	2,484,250
Federal National Mortg. Assn. Notes (FNMA)	Aaa	AA+	4,440,106
Federal Farm Credit Bank (FCCB)	Aaa	AA+	3,839,955
U.S. Securities	Aaa	AA+	7,410,750
Corporate Notes:			
General Electric Corp	Aa3	AA+	649,385
WalMart Stores, Inc.	Aa2	AA	794,655
Trust Bond Funds - Held by City	Not Rated	Not Rated	211,778
Trust Bond Funds - Held by Trustee	Not Rated	Not Rated	50,000
Local Agency Investment Funds (LAIF)	Not Rated	Not Rated	32,866,612
Total investments			<u>\$ 56,241,343</u>

Custodial Credit Risk – Deposits

This is the risk that in the event of a bank failure, the City's deposits may not be returned to it. The City does not have a policy for custodial credit risk for deposits. However, the California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure public deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits and letters of credit issued by the Federal Home Loan Bank of San Francisco having a value of 105% of the secured deposits.

As of June 30, 2013, the City's bank balance was \$2,515,563 and the corresponding carrying book balance was \$2,158,376. Of the bank balance, \$250,000 was covered by federal depository insurance and \$2,265,563 was collateralized.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

2. **Cash, Cash Equivalents, and Investments**, continued

c) Risk Disclosures, continued

Custodial Credit Risk – Investments

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, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and the City's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for investments.

Investment in State Investment Pool

The City is a voluntary participant in LAIF that is regulated by the California Government Code under the oversight of the Treasurer of the State of California. The fair value of the City's investment in this pool as reported in the accompanying financial statements is based upon the Entity's pro-rata share of the fair value provided by LAIF for the entire LAIF portfolio (in relation to the amortized cost of that portfolio).

As of June 30, 2013, the City held \$32,866,612 in LAIF, which had invested 1.96% of the pool investment funds in Structured Notes and Asset-Backed Securities, as compared to 2.75% in the previous year. The LAIF fair value factor of 1.000273207 was used to calculate the fair value of the investments in LAIF.

CITY OF LOS ALTOS, CALIFORNIA
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Fiscal year ended June 30, 2013

3. Interfund Transactions

Transfers

Transfers between funds during the fiscal year ended June 30, 2013 were as follows:

Transfer From	Transfer To	Amount
General Fund	Capital Project	\$ 564,000 (a)
	Equipment Replacement	100,000 (b)
	Community Facility Fund	100,000 (g)
	Storm Drain	231,933 (d)
	Workers Compensation Fund	250,000 (c)
	Debt Service Funds	165,000 (c)
		<u>1,410,933</u>
Nonmajor Governmental Funds	General Fund	282,395 (e) (f)
	Capital projects	1,231,717 (a)
		<u>1,514,112</u>
		<u>\$ 2,925,045</u>

Interfund transfers were principally used for the following purposes:

- (a) Fund capital projects
- (b) Replace public safety and public works vehicles
- (c) Maintain minimum fund balance in debt service and Workers Comp. funds
- (d) Support the operations of the storm drain fund
- (e) Public safety related funds paid to the General Fund
- (f) Gas tax to support street projects
- (g) Support facility replacments

Transfers are used to move unrestricted general fund revenues to finance various programs accounted for in other funds based on budgetary authorizations. Transfers are also used to move revenues from the general fund to the debt service fund as principal and interest payments become due and to fund assigned and approved capital projects. Additionally, Transfers are made to and from the Capital Improvement Program fund in line with approved and appropriated project dollar sources.

A substantial volume of capital projects were expended and/or completed.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

4. Capital Assets

a) Government-wide Financial Statements

At June 30, 2013, the City's capital assets consisted of the following:

	Governmental Activities	Business-Type Activities	Total
Nondepreciable assets:			
Construction in progress	\$ 4,075,554	\$ 379,320	\$ 4,454,874
Land	11,539,449	-	11,539,449
Total nondepreciable assets	<u>15,615,003</u>	<u>379,320</u>	<u>15,994,323</u>
Depreciable assets:			
Buildings	21,637,868	14,862,078	36,499,946
Improvements	5,079,055	-	5,079,055
Machinery and equipment	4,231,706	819,477	5,051,183
Infrastructure	25,495,035	1,969,221	27,464,256
Total depreciable assets	<u>56,443,663</u>	<u>17,650,776</u>	<u>74,094,439</u>
Less accumulated depreciation	<u>(20,291,336)</u>	<u>(11,256,677)</u>	<u>(31,548,013)</u>
Total depreciable assets, net	<u>36,152,327</u>	<u>6,394,099</u>	<u>42,546,426</u>
Total capital assets	<u>\$ 51,767,330</u>	<u>\$ 6,773,419</u>	<u>\$ 58,540,749</u>

The following is a summary of capital assets for governmental activities for the year ended June 30, 2013:

	Balances at July 1, 2012	Additions	Deletions	Transfers	Balances at June 30, 2013
Governmental activities:					
Nondepreciable assets:					
Construction in progress	\$ 4,522,348	\$ 2,593,392	\$ -	\$ (3,040,186)	\$ 4,075,554
Land	11,539,449	-	-	-	11,539,449
Total nondepreciable assets	<u>16,061,797</u>	<u>2,593,392</u>	<u>-</u>	<u>(3,040,186)</u>	<u>15,615,003</u>
Depreciable assets:					
Buildings	21,637,868	-	-	-	21,637,868
Improvements	5,079,055	-	-	-	5,079,055
Machinery and equipment	4,183,173	189,309	(140,776)	-	4,231,706
Infrastructure	22,082,803	372,046	-	3,040,186	25,495,035
Total depreciable assets	<u>52,982,899</u>	<u>561,355</u>	<u>(140,776)</u>	<u>3,040,186</u>	<u>56,443,664</u>
Less accumulated depreciation:					
Buildings	(7,600,599)	(454,499)	-	-	(8,055,098)
Improvements	(1,345,701)	(138,843)	-	-	(1,484,544)
Machinery and equipment	(2,919,966)	(378,240)	121,614	-	(3,176,592)
Infrastructure	(6,907,541)	(667,562)	-	-	(7,575,103)
Total accumulated depreciation	<u>(18,773,807)</u>	<u>(1,639,144)</u>	<u>121,614</u>	<u>-</u>	<u>(20,291,337)</u>
Net depreciable assets	<u>34,209,092</u>	<u>(1,077,789)</u>	<u>(19,162)</u>	<u>3,040,186</u>	<u>36,152,327</u>
Capital assets, net	<u>\$ 50,270,889</u>	<u>\$ 1,515,603</u>	<u>\$ (19,162)</u>	<u>\$ -</u>	<u>\$ 51,767,330</u>

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

4. Capital Assets, continued

a) Government-wide Financial Statements, continued

The governmental activities depreciation expenses for capital assets for the year ended June 30, 2013 are as follows:

Public safety	\$ 239,233
Public works	783,466
Community/cultural services	475,376
Community development	8,392
General government	132,677
Total depreciation expense	\$ 1,639,144

The following is a summary of capital assets for business-type activities:

	Balances at July 1, 2012	Additions	Deletions	Transfers	Balances at June 30, 2013
Business-type activities:					
Nondepreciable assets:					
Construction in progress	\$ 1,047,796	\$ 252,059	\$ -	\$ (920,535)	\$ 379,320
Total nondepreciable assets	1,047,796	252,059	-	(920,535)	379,320
Depreciable assets:					
Buildings	13,183,486	758,059	-	920,535	14,862,080
Infrastructure	1,969,221	-	-	-	1,969,221
Machinery and equipment	782,992	36,483	-	-	819,475
Total depreciable assets	15,935,699	794,542	-	920,535	17,650,776
Less accumulated depreciation:					
Buildings	(8,532,253)	(173,932)	-	-	(8,706,185)
Infrastructure	(1,969,221)	-	-	-	(1,969,221)
Machinery and equipment	(530,323)	(50,948)	-	-	(581,271)
Total accumulated depreciation	(11,031,797)	(224,880)	-	-	(11,256,677)
Net depreciable assets	4,903,902	569,662	-	920,535	6,394,099
Capital assets, net	\$ 5,951,698	\$ 821,721	\$ -	\$ -	\$ 6,773,419

Depreciation expense for business-type activities related to the Sewer Fund amounted to \$224,880 for the year ended June 30, 2013.

b) Fund Financial Statements

The Governmental Fund Financial Statements do not present capital assets, which are shown in the Reconciliation of the Governmental Funds Balance Sheet to the Government-wide Statement of Net Position.

The capital assets of the enterprise funds in the Proprietary Fund Financial Statements are the same as those shown in the business-type activities of the Government-wide Financial Statements.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

5. Net Pension Asset

In FY 2009-10, the City prepaid a major portion, \$3,005,795, of its unfunded CalPERS side fund liability. This prepayment is recorded on the Statement of Net Position as a Net Pension Asset. Additional payments have been made in subsequent periods and in FY 2012-13, the City prepaid an additional \$950,000 towards its goal of eliminating these existing liabilities and mitigating future pension costs. These pay-down payments are classified under the caption of “Special item” expenditures in the governmental statements of activity for each related year.

In the prior years, the City presented this prepayment as a “Net Pension Asset” on the Government-wide Statement of Net Position. A subsequent review of this treatment and interpretation of the associated standard has resulted in the reversal of this asset recognition and the prior period adjustment noted below. This adjustment impacts government-wide net position but no impact on operational governmental fund and/or cash balances.

Balance at July 1, 2012	\$ 87,071,154
Adjustment of Net Pension Asset	<u>3,749,863</u>
Balance at July 1, 2012, restated	<u><u>\$ 83,321,291</u></u>

In FY 2013-14, the City made a final prepayment of the remaining side fund liabilities, achieving full pay-off for both the safety and miscellaneous plans.

6. Long-Term Obligations

a) Governmental Activities Long-Term Debt

Summary of changes in governmental activities long-term debt for the year ended June 30, 2013 is as follows:

	Balances at July 1, 2012	Additions	Reductions	Balances at June 30, 2013	Due in 1 Year	Due in More Than 1 Year
Certificate of participation	<u>\$ 1,855,000</u>	<u>\$ -</u>	<u>\$ (95,000)</u>	<u>\$ 1,760,000</u>	<u>\$ 95,000</u>	<u>\$ 1,665,000</u>

2004 Refunding Certificate of Participation

On November 1, 1996, the City issued \$2,630,000 principal amount of Certificates of Participation (ABAG 38 COPs). The purpose of the ABAG 38 COPs was to finance the partial purchase of the 5.5 acre Saint William School site for public purposes and uses. During 2004 the City issued \$2,500,000 of 2004 Refunding Certificates of Participation to advance refund \$2,390,000 of outstanding principal on the ABAG 38 Certificates of Participation, set up reserve funds, and to pay related issuance costs. The entire ABAG 38 Certificates of Participation had been paid off by June 30, 2004. This advance refunding was undertaken to reduce total future debt service payments.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

6. Long-Term Obligations

a) Governmental Activities Long-Term Debt, continued

2004 Refunding Certificate of Participation, continued

At June 30, 2013, future debt service requirements for the 2004 Refunding were as follows:

<u>Fiscal Year Ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014	\$ 95,000	\$ 69,956	\$ 164,956
2015	100,000	66,918	166,918
2016	105,000	63,568	168,568
2017	105,000	59,892	164,892
2018	110,000	56,060	166,060
2019 - 2023	635,000	210,755	845,755
2024 - 2028	610,000	66,512	676,512
Total	<u>\$ 1,760,000</u>	<u>\$ 593,661</u>	<u>\$ 2,353,661</u>

b) Non-City Obligations

The following bonds are not reported in the City's financial statements as they are special obligations payable solely from and secured by specific revenue sources as described in the resolutions and official statements of the respective issues. Neither the faith and credit nor the taxing power of the City is pledged for payment of these obligations.

	<u>Balances at July 1, 2012</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balances at June 30, 2013</u>	<u>Due in 1 Year</u>	<u>Due in More Than 1 Year</u>
Raymundo Curb & Gutter	\$ 187,000	\$ -	\$ (17,000)	\$ 170,000	\$ 18,000	\$ 152,000
Avalon Curb & Gutter	34,000	-	(8,000)	26,000	8,000	18,000
Blue Oak Lane	610,000	-	(10,000)	600,000	10,000	590,000
Total	<u>\$ 831,000</u>	<u>\$ -</u>	<u>\$ (35,000)</u>	<u>\$ 796,000</u>	<u>\$ 36,000</u>	<u>\$ 760,000</u>

Raymundo & Avalon Special Assessment Districts

The Raymundo Curb & Gutter Assessment District Improvement Bond was issued on August 3, 2005 to provide financing for the street improvements in that District. The Avalon Drive Curb & Gutter Assessment District Improvement Bond was issued for a similar purpose in 2000. The bonds are payable from a special property tax levied to those residents living within the respective district.

Blue Oak Lane Special Assessment District

On November 5, 2009, Limited Obligation Improvement Bonds were issued for a newly formed Blue Oak Lane Sewer Assessment District (series 2009) to finance the acquisition and construction, by the City, of sanitary sewer improvements serving properties within the subject assessment district. These bonds are issued upon and secured by individual parcel levied assessments to be included in the annual property tax billings annually. The Bonds mature in 2039, were issued in a principal amount of \$662,880 and are subject to semi-annual debt service payments administered by the City.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

7. Compensated Absences Payable

The City's compensated absences at June 30, 2013, were as follows:

	Balances at July 1, 2012	Additions	Reductions	Balances at June 30, 2013	Due in 1 Year	Due in More Than 1 Year
Governmental	\$ 1,434,236	\$ 949,430	\$ (829,156)	\$ 1,554,510	\$ 388,628	\$ 1,165,882
Business-type activities	40,655	44,310	(38,437)	46,528	11,632	34,896
	<u>\$ 1,474,891</u>	<u>\$ 993,740</u>	<u>\$ (867,593)</u>	<u>\$ 1,601,038</u>	<u>\$ 400,260</u>	<u>\$ 1,200,778</u>

8. Net Position/Fund Balances

a) Fund Balances

In the fund financial statements, governmental funds report the following classifications: non-spendable, restricted, committed, assigned, and unassigned. The City Council, as the highest level of decision making authority for the City, can commit fund balances through the adoption of a formal action in accordance with the adoption of its annual Financial Policy. This policy authorizes the City Manager to assign fund balances and has set the budgetary level of control at the Fund and Capital Project level for the governing body and the department level for the City Manager and assignees.

b) Emergency and Operating Reserve

The City Council has established an Emergency and Operating (Emergency) Reserve goal level of 20% of annual operating expenditures has set funds aside accordingly through its annual budgetary actions. These funds would be available for use in such conditions to mitigate negative economic fiscal impacts or State takeaways and can be activated within any one budget cycle through Council action. An economic downturn would entail a projected and/or sudden drop in core revenues (major tax and service revenue loss) of equal to or greater than 5% (including the impact of inflation) and/or a change in economic parameters (such as interest rates, debt service rates, commodity prices, pension rates) that cause a material change in expenditures of 5% or more, or the occurrence of a local natural disaster or unexpected financial claim requiring the immediate use of cash balances of 5% or more, or the occurrence of a local natural disaster or unexpected financial claim requiring the immediate use of cash balances.

In FY 2012-13, in line with budget approval, the City reallocated the pre-established State Budget Stabilization reserve into the aforementioned Emergency reserve. This results in the establishment of one Reserve balance to assist in periods of economic downturn or extraordinary need. The City's FY 2013-14 fiscal plan projects the realization of its 20% reserve goal.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

8. Net Position/Fund Balances, continued

c) Classifications

In the Government-wide Financial Statements, net assets are classified in the following categories:

Invested in Capital Assets, Net of Related Debt – This amount consists of capital assets net of accumulated depreciation and reduced by outstanding debt that attributed to the acquisition, construction, or improvement of the assets.

Restricted Net Assets – This amount is restricted by external creditors, grantors, contributors, or laws or regulations of other governments.

Unrestricted Net Assets – This amount is all net assets that do not meet the definition of “invested in capital assets, net of related debt” or “restricted net assets.”

As prescribed by GASB Statement No. 54, governmental funds report fund balance in classifications based primarily on the extent to which the City is bound to honor constraints on the specific purposes for which amounts in the funds can be spent. As of June 30, 2013, fund balances for government funds are made up of the following;

- *Non-spendable Fund Balance* – includes amounts that are (a) not in spendable form, or (b) legally or contractually required to be maintained intact. The “not in spendable form” criterion includes items that are not expected to be converted to cash, for example: inventories, prepaid amounts, long-term notes receivable and land.
- *Restricted Fund Balance* – includes amounts that can be spent only for the specific purposes stipulated by external resource providers, constitutionally or through enabling legislation. Restrictions may effectively be changed or lifted only with the consent of resource providers.
- *Committed Fund Balance* – includes amounts that can only be used for the specific purposes determined by a formal action of the City’s highest level of decision-making authority, the City Council. Commitments may be modified only by the City taking the same formal action that imposed the constraint originally.
- *Assigned Fund Balance* – comprised of amounts intended to be used by the City for specific purposes that are neither restricted nor committed. Intent is expressed by (a) the City Council or (b) a body (for example: a budget or finance committee) or official to which the City Council has delegated the authority to assign amounts to be used for specific purposes.
- *Unassigned Fund Balance* – conveys the residual classification for the General Fund and includes all amounts not contained in the other classifications. Unassigned amounts are technically available for any purpose.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

8. Net Position/Fund Balances, continued

d) Policies

Order of Utilization

The standard also requires governments to disclose the accounting policies that indicate the order in which restricted, committed, assigned and unassigned amounts are spent.

The City considers restricted amounts to have been spent first when expenditures are incurred and both restricted and unrestricted fund balances are available. Additionally, the City considers committed amounts to have been spent first, assigned amounts to have been spent second, and unassigned amounts to have been spent last when an expenditure is incurred for purposes of which committed, assigned, and unassigned fund balance is available.

In circumstances when an expenditure is made for a purpose for which amounts are available in multiple fund balance classifications, fund balance is generally depleted in the order of restricted, committed, assigned, and unassigned.

Assignment and Commitment Authority

The City Council has approved a financial policy authorizing the City Manager to assign fund balances to facilitate year-end reporting requirements. The City Council, as the highest level of decision making authority for the City, has the ability to commit fund balances through the adoption of a formal policy and/or action. The same action must be taken to modify or rescind the commitment.

e) Fund Balances

Fund balances for all the major and non-major governmental funds as of June 30, 2013 were distributed as follows:

	General	Real Property Proceeds	Capital Projects	Equipment Replacement	In Lieu Park Land	Community Facilities Renewal	Nonmajor Funds	Total
Nonspendable:								
Inventory and prepaids	\$ 36,728	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 36,728
Veteran memorial	12,000	-	-	-	-	-	-	12,000
Total nonspendable	<u>48,728</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>48,728</u>
Restricted:								
Debt service	-	-	-	-	-	-	363,594	363,594
Special revenue programs and projects	-	-	-	-	4,590,390	-	1,872,843	6,463,233
Continuing CIPS	-	-	-	-	-	-	578,837	578,837
Total restricted	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>4,590,390</u>	<u>-</u>	<u>2,815,274</u>	<u>7,405,664</u>
Committed:								
State budget stabilization	-	-	-	-	-	-	-	-
Continuing CIP	-	-	3,046,926	583,434	-	-	-	3,630,360
Total committed	<u>-</u>	<u>-</u>	<u>3,046,926</u>	<u>583,434</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>3,630,360</u>
Assigned:								
Emergency and operating	5,525,000	-	-	-	-	-	-	5,525,000
OPEB	500,000	-	-	-	-	-	-	500,000
PERS Reserve	-	-	-	-	-	-	-	-
Capital projects	-	7,414,894	1,793,117	3,086,854	-	7,165,592	-	19,460,457
Total assignment	<u>6,025,000</u>	<u>7,414,894</u>	<u>1,793,117</u>	<u>3,086,854</u>	<u>-</u>	<u>7,165,592</u>	<u>-</u>	<u>25,485,457</u>
Unassigned	<u>2,428,246</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>2,428,246</u>
Total	<u>\$ 8,501,974</u>	<u>\$ 7,414,894</u>	<u>\$ 4,840,043</u>	<u>\$ 3,670,288</u>	<u>\$ 4,590,390</u>	<u>\$ 7,165,592</u>	<u>\$ 2,815,274</u>	<u>\$ 38,998,455</u>

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

9. Risk Management

a) Bay Cities Joint Powers Insurance Authority

The City is exposed to various risks of loss related to torts; theft of damage to and destruction of assets; errors and omissions; and floods for which the City is insured through Bay Cities Joint Powers Insurance Authority (Bay City).

The City has joined Bay City for general liability, property, errors and omissions, crimes and automobile physical damage coverage in the current year. Bay City is a public agency created in 1986 by and among various municipalities in Northern California to provide a pooled approach to liability insurance pursuant to the California Government Code. It is governed by a Board of Directors comprised of appointed officials from the member entities. The purpose of the pool is to provide various levels of liability coverage, claims administration, and loss control support to member agencies. Annually, each member pays an actuarially determined premium based on a formula which takes into account the prior three years' loss experience, annual payroll, and population.

Bay City provides coverage for its Members in excess of the member's retained limit, or self-insured retention (SIR), up to \$1,000,000 per occurrence. Each Member retains the portion of every loss that falls within their SIR, ranging from \$5,000 to \$500,000. Bay City is also a member of the California Affiliated Risk Management Authorities (CARMA), a risk sharing joint powers authority. When losses exceed the \$1,000,000 per occurrence limit, CARMA provides coverage up to \$29,000,000.

The City self-insures the first \$100,000 of each liability loss. Once the City's deductible is met, Bay Cities becomes responsible for payment of all claims up to the upper limit. During the year ended June 30, 2013, the City contributed \$387,874 for current year coverage.

The City continues to carry excess insurance policy for Workers' Compensation claims through the CSAC Excess Insurance Authority JPA up to the statutory limits and does so using the services of a contracted third-party administrator. The City has a \$250,000 deductible as of June 30, 2013. During the year, the City contributed \$103,216 for current year coverage.

As of June 30, 2013, \$50,000 of revolving funds was held in trust on behalf of the City by the workers' compensation third-party claims administrator. \$55,000 is also being held by Bay Cities in the procurement of liability and claims coverage. The City will receive these funds upon termination of services subject to final withdrawal adjustments.

The Bay City financial statements may be obtained from Bay Cities Joint Powers Insurance Authority, Bickmore / 1750 Creekside Oaks Drive, Suite 200 / Sacramento, CA 95833. CSAC Excess Insurance Authority financial statements may be obtained from CSAC Excess Insurance Authority / 75 Iron Point Circle / Suite 200 / Folsom, CA 956300.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

9. Risk Management, continued

b) Liability for Uninsured Claims

The GASB requires municipalities to record their liability for uninsured claims and to reflect the current portion of this liability as an expenditure in their financial statements. As discussed in the section above, the City has coverage for such claims, but it has retained the risk for the deductible or uninsured portion, of these claims. GASB Statement No. 10, “Financial Reporting for Risk Financing and Related Insurance Issues,” requires that this amount be separately identified and recorded as a liability. Changes in the balances of claims liabilities during the past three years were as follows:

	June 30,		
	2013	2012	2011
Unpaid claims, beginning of year	\$ 2,638,744	\$ 2,407,519	\$ 2,107,901
Incurred claims and changes in estimates	1,047,139	744,540	458,940
Claim payments	(408,379)	(513,315)	(159,322)
Unpaid claims, end of year	\$ 3,277,504	\$ 2,638,744	\$ 2,407,519

In conformance with GASB Statement No. 10, the City obtained an independent actuarial valuation of all outstanding Workers Compensation and Liability claims. The report presented a valuation as of June 30, 2013 and projected values through FY 2014-15. The FY 2012-13 values presented above reflect the estimated present value of open claims as developed in this actuarial report. The estimated amount of claims and judgments due within one year is \$669,896.

10. Self-Funded Reimbursement Dental Plan

The City provides a self-funded reimbursement based dental plan. The City’s contribution for this plan is accounted for in the Dental Reimbursement Fund. The City contributed \$75 per month for each full-time budgeted position. The funds accumulated are used to reimburse full-time salaried employees, council members and their dependents for covered dental claims. There are no administrative charges for this plan. The Dental Reimbursement Fund maintains a positive fund balance of \$157,832 with contributions and reimbursements for the past four fiscal years as follows:

Fiscal year ended June 30,	Contribution Amount	Reimbursement Amount
2009	\$ 96,480	\$ 112,690
2010	92,213	111,342
2011	90,506	106,000
2012	112,254	109,632
2013	114,264	104,711
Total	\$ 505,717	\$ 544,375

The dental plan year commences January 1st of each calendar year. An annual maximum dental reimbursement of \$1,500 is provided for each employee and \$1,000 for each of their dependents. Any remaining balance in the fund for each dental year is carried forward to the following year. In subsequent dental years, the maximum dental coverage for both employees and dependents are increased annually based on the Consumer Price Index but not to exceed 3%.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

11. Pension Plans

California Public Employees' Retirement System Plan

Plan Description

The City contributes to the California Public Employees' Retirement System (CalPERS), an agent multiple-employer public employee defined benefit pension plan. CalPERS provides retirement and disability benefits, annual cost-of-living adjustments and death benefits to plan members and beneficiaries. CalPERS acts as a common investment and administrative agent for participating public entities within the State of California. Benefit provisions and all other requirements are established by State statute and City ordinance. Copies of CalPERS' annual financial report may be obtained from their Executive Office located at 400 P Street, Sacramento, California 95814. Effective with the June 30, 2003 actuarial valuation, CalPERS required that retirement plans with less than 100 members be included in risk pools. These risk pools are cost-sharing multiple-employer defined benefit retirement plans that pool risk. Both the City's safety and miscellaneous retirement plans are included in these risk pools.

Funding Policy

The City's second-tier plans for both its safety and miscellaneous groups providing an alternate level of benefits for newly hired employees. Furthermore, in the current fiscal year, the State of California Assembly Bill 340 (AB 340) created the Public Employees' Pension Reform Act (PEPRA) that implemented new benefit formulas and final compensation period, as well as new contribution requirements for new employees hired on or after January 1, 2013.

Existing active legacy plans carry statutory defined contribution rates, within the benefit levels that the City offers, of 9% of covered salaries for safety employees and 8% for miscellaneous employees. Second-tier plan members will be required by State statute to contribute the full 9% for safety and 7% for miscellaneous. Third-tier employees, for both safety and miscellaneous, hired under AB 340, contribute their full shares defined as 50% of normal cost, a level set by state law for each respective plan and agency.

The City makes up a portion of the contributions required of legacy City employees on their behalf and for their account. On a combined basis, for all plan levels and groups in the current year, this amounted to \$659,375 for the year ended June 30, 2013, as compared to \$790,884 in the prior year.

For legacy employees the City was required to contribute an actuarial determined employer rate of 25.137% for the period from July 1, 2012 through June 30, 2013 of covered payroll for safety employees and 15.178% of annual covered payroll for miscellaneous employees. For second tier plan employees in the same period, the City was required to contribute 20.057% of covered payroll for safety employees and 7.846% of covered payroll for miscellaneous employees. New CalPERS enrollees, as defined under State imposed AB 340 legislation, have estimated employer rates of 11.5% and 6.25% for safety employees and miscellaneous employees, respectively. Contribution rates are established annually and may be amended by CalPERS. Included in the employer contribution rates are the amortization of Side Funds which were created to account for the difference between the funded status of the pool and the funded status of the City plans at the time of joining the risk pool.

The City has paid down the safety side-fund liability using planned designated reserves approximating \$5 million. As of June 30, 2013, the estimated balance of the Side Fund for the public safety plan was reduced to approximately \$155, 000 with miscellaneous fully paid off. In the subsequent period, the City made final and full payment of all side fund liabilities.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

11. Pension Plans, continued

California Public Employees' Retirement System Plan, continued

Annual Pension Cost

For FY 2012-13, the City's annual required employer contributions pension was equal to \$2,023,801 and presented along with other historical contributions as listed below.

Fiscal Year Ended	Annual Pension Cost (APC)		Percentage of APC Contributed	Net Pension Obligation
	Miscellaneous	Safety		
6/30/2011	\$ 1,131,312	\$ 715,110	100%	\$ -
6/30/2012	1,189,791	890,770	100%	-
6/30/2013	1,111,913	911,888	100%	-

A summary of principal assumptions and methods used to determine the annual required contributions is shown below for the cost-sharing multiple-employer defined benefit plan.

Valuation Date	June 30, 2010
Actuarial Cost Method Entry	Age Normal Cost Method
Amortization Method	Level Percent of Payroll
Average Remaining Period	19 Years as of the Valuation Date
Asset Valuation Method	15 Year Smoothed Market
Actuarial Assumptions	
Investment Rate of Return	7.75% (net of administrative expenses)
Projected Salary Increases	3.55% to 14.45% depending on Age, Service, and type of employment
Inflation	3.00%
Payroll Growth	3.25%
Individual Salary Growth	A merit scale varying by duration of employment coupled with an assumed annual inflation growth of 3.00% and an annual production growth of 0.25%.

Funding Status as of the Most Recent Actuarial Date

The City retirement plans for safety and miscellaneous employees are part of the CalPERS risk pool for cities and other government entities that have less than 100 active members. Actuarial valuations performed included other participants within the same risk pool. Therefore, standalone information of the schedule of the funding progress for the City's safety and miscellaneous employee plans is not available or disclosed. With the emergence of new pension standards in FY 2013-14, City specific pension valuations will be developed and disclosed in financial statements accordingly.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

12. Other Post Employment Benefits (OPEB)

Plan Description

The City Retiree Healthcare Plan (Plan) is a single-employer defined benefit healthcare plan administered by the City. The Plan provides healthcare benefits to eligible retirees and their dependents through the CalPERS healthcare program (PEMHCA). Benefit provisions are established and may be amended through agreements and memorandums of understanding between the City, its non-represented employees and the unions representing City employees. The Plan does not issue a financial report.

The City provides a retiree medical contribution using the “5% unequal method,” where the retiree contribution is increased annually until it equals the PEMHCA minimum contribution (\$112 per month for FY 2011-12 and \$115 per month for FY 2012-13). In FY 2011-12, the City’s contribution averaged \$64.59 per month. The City does not provide contributions for retiree dental, vision or life insurance benefits.

City’s Funding Policy

The City continues to pay for retiree healthcare benefits on a pay-as-you go basis. This reporting year the City contributed \$33, 585 for current benefit payments. Retired plan members and their beneficiaries pay the annual premium cost not paid by the employer.

As of June 30, 2013, \$500,000 has been set aside in the General Fund as a reserve with future budgets projected to make increased annual contributions thereafter.

Annual OPEB Cost and Net OPEB Obligation

The City’s annual other post-employment benefit cost (expense) is calculated based on the annual required contribution (ARC) of the employer. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years.

The following table shows the components of the City’s annual OPEB cost for the year, the amount actually contributed to the Plan, and changes in the City’s Net OPEB obligation:

Annual required contribution	\$ 261,000
Interest on net OPEB obligation	34,000
Amortization of net OPEB obligation	(61,000)
Annual OPEB cost (expense)	<u>234,000</u>
Contributions made (including premiums paid)	<u>(33,511)</u>
Increase in net OPEB obligation	200,489
Net OPEB obligation, beginning of year	<u>793,457</u>
Net OPEB obligation, end of year	<u><u>\$ 993,946</u></u>

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

12. Other Post Employment Benefits (OPEB), continued

Annual OPEB Cost and Net OPEB Obligation, continued

The City's annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation for FY 2012-13 and the two preceding fiscal years were as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation	Cumulative OPEB Obligation
6/30/2011	\$ 237,000	10.0%	\$ 212,540	\$ 604,032
6/30/2012	220,000	14.0%	189,422	793,454
6/30/2013	234,000	14.0%	200,489	993,946

Funded Status and Funding Progress

The funded status of the Plan as of June 30, 2011, the Plan's most recent actuarial valuation date, was as follows:

In Thousands

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b)-(a)	Funded Ratio (a)/(b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll (b)-(a)/(c)
6/30/09	\$ -	\$ 1,662	\$ 1,662	0.00%	\$ 10,884	20%
6/30/11	-	2,136	2,136	0.00%	10,369	21%

Actuarial valuations of an ongoing plan involve estimates of the value of expected benefit payments and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan participants) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan participants to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

For the June 30, 2011 actuarial valuation, the entry age normal actuarial cost method was used. The actuarial assumptions included a 4.25% investment rate of return (net of administrative expenses) and a 3% general inflation assumption. The PEMHCA minimum was assumed to annually increase by 4.5%. The UAAL is amortized as a level percentage of projected payrolls over 30 years on a closed basis commencing in 2009.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

13. Contingencies

The City is presently involved in certain matters of litigation that have arisen in the normal course of conducting City business. City management believes, based upon consultation with the City Attorney, that these cases, in the aggregate, are not expected to result in a material adverse financial impact on the City. Additionally, City management believes that the City's insurance programs are reasonably sufficient to cover any potential losses should an unfavorable outcome materialize.

14. Other Information

Joint Powers Agreements

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 of member agencies beyond their representation of the board.

Joint Sewer System Authority (JSSA)

The JSSA, formed in 1968 by a joint exercise of powers among the cities of Palo Alto, Mountain View, and Los Altos, constructed, maintains and operates sewage treatment facilities serving its member cities. The City of Palo Alto acts as administrator for JSSA and bills each member its share of the operating costs. The audited financial statements can be obtained by contacting the City of Palo Alto at P.O. Box 10250, Palo Alto, CA 94303.

North County Library Authority (NCLA)

The NCLA, formed in 1985 by a joint exercise of powers agreement between the City and the Town of Los Altos Hills, provides library services for member residents. The NCLA was created to provide financing for capital improvements and additional services by the public libraries serving the area. Although the City owns the libraries and their sites, the County of Santa Clara (County) is responsible for all library operations. However, since 1985, the NCLA has levied a voter approved special parcel tax to compensate for service reductions due to cutbacks by the County. The special tax has been collected by the County, transferred to the City, on behalf of NCLA, and then transferred back to the County for the specifically requested services provided by the libraries within the NCLA's service area. The City performs administrative and accounting services for NCLA. In 1991, the NCLA issued Special Tax Bonds in the amount of \$3,645,000. The Special Tax Bonds were paid off as of June 30, 2012. In 2010, NCLA successfully passed an updated twenty year parcel tax extending the assessment term to 2030. No new debt was issued in association with this election. The audited financial statements can be obtained by contacting the NCLA at One North San Antonio Road, Los Altos, CA 94022.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

14. Other Information, continued

Joint Powers Agreements, continued

Community Health Awareness Council (CHAC)

CHAC was organized as a joint powers agency between the City of Los Altos, City of Mountain View, Town of Los Altos Hills, Los Altos School District, Mountain View Whisman School District, and Mountain View-Los Altos High School District. CHAC provides prevention and intervention services concentrating on positive alternatives to health abuse and self-destructive behaviors within the communities served. The audited financial statements can be obtained by contacting CHAC at P.O. Box 335, Mountain View, California, 94042.

OPEB Reserves

A review of the City's fund balance assignments will reveal that as of June 30, 2012, \$500,000 in General Fund reserves have been assigned in recognition of existing Post-Retirement Health Actuarial Obligations noted above.

15. Excess Expenditures Over Appropriations

Expenditures exceeded budgeted appropriations in the following funds:

	Budget	Actual	Variance
Debt Service Fund	\$ 167,300	\$ 169,572	\$ (2,272)

16. Proposition 1A Borrowing by the State of California

Under the provisions of Proposition 1A and as part of the FY 2009-10 budget package passed by the California state legislature on July 28, 2009, the State of California borrowed 8% of the amount of property tax revenue, including those property taxes associated with the in-lieu motor vehicle license fee, the triple flip in lieu sales tax, and supplemental property tax, apportioned to cities, counties and special districts (excluding redevelopment agencies). The State is required to repay this borrowing plus interest by June 30, 2013 to those agencies not participating in the loan securitization process. After repayment of this initial borrowing, the California legislature may consider only one additional borrowing within a ten-year period.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

16. Proposition 1A Borrowing by the State of California, continued

Authorized with the FY 2009-10 State budget, the Proposition 1A Securitization Program was instituted by the California Statewide Communities Development Authority ("California Communities"), a joint powers authority sponsored by the California State Association of Counties and the League of California Cities, to enable local governments to sell their Proposition 1A receivables to California Communities. Under the Securitization Program, California Communities simultaneously purchased the Proposition 1A receivables and issued bonds ("Prop 1A Bonds") to provide local agencies with cash proceeds in two equal installments, on January 15, 2010 and May 3, 2010. The purchase price paid to the local agencies equaled 100% of the amount of the property tax reduction. All transaction costs of issuance and interest were paid by the State of California. Participating local agencies have no obligation on the bonds and no credit exposure to the state. The City participated in the securitization program and accordingly property taxes have been recorded in the same manner as if the State had not exercised its rights under Proposition 1A. The receivable sale proceeds were equal to the book value and, as a result, no gain or loss was recorded.

The amount of this borrowing pertaining to the City was \$ 1.08 million.

17. Special Items

On November 30, 2007, the City entered a purchase and sale agreement with the City of Palo Alto to sell the City's share of the Los Altos Treatment Plant (LATP) to the City of Palo Alto for \$6.5 million. In 2010, the third and final regular installment and all collections have been recorded into the Real Property Proceeds Fund. Payments to the City were made net of title and escrow fees and estimated preliminary development costs of \$400,000. In FY 2012-13, this full unused amount, including interest, was paid back in full to the City.

In the current period the City made a further pay-down of its CalPERS side fund liability in the amount of \$950,000 as part of a multi-year plan to reduce pension costs. This amount appears as a special item in the General Fund and is also discussed in the pension disclosure notes above.

18. Developer Agreements

Land Sale/Purchase Agreement

On September 14, 2010 the City approved an Option to Purchase Agreement for the City owned property located at 230 First Street and 400 Main Street for price of \$3.1 million. This was part of a minimum project scope of a two-story building approximating 31,000 square feet. The agreement is contingent upon a series of milestones and feasibility phases. In the current year the City received an additional \$100,000 of initial purchase option payments marking the end of the initial feasibility term. As of year-end, \$500,010 has been collected and these dollars are recorded as revenue in the Real Property Proceeds funds, the balance of which is assigned for future capital projects.

The Government-wide Financial Statements reflect a loss of \$544,576 representing the disposition and write off of the capitalized and un-depreciated value of the City owned physical improvements located at 400 Main Street. This transaction reflects the demolition of said improvements. The ultimate sale of the underlying property is subject to the conditions of the agreement entered into with the developer, which, once met, will trigger the recording and receipt of the sale proceeds. The full sale was realized in early FY 2013-14 as noted in the subsequent events footnote below.

CITY OF LOS ALTOS, CALIFORNIA
NOTES TO THE BASIC FINANCIAL STATEMENTS

Fiscal year ended June 30, 2013

19. Other Commitments

A summary of remaining authorized CIP project balances end of year balances for all City funds by service area follows:

Streets & Roadways	\$ 1,397,558
Pedestrian Safety	1,239,745
Infrastructure & Facilities	701,869
Parks	637,615
Sewer	3,650,223
Technology	793,875
Community Development	61,151
	\$ 8,482,036

20. Prior Period Adjustment

Note 5 above refers to the prior treatment of the City’s CalPERS side-fund pay-down, approximating \$3.7 million, as a “Net Pension Asset” on the Government-wide Statement of Net Position. A subsequent review and interpretation of this classification has negated the need to record this liability payoff as an asset considering the full cash payoff of the amount in question. As such, a prior-period adjustment has been recorded on the Statement of Net Position, effectively reducing the asset and respective net position in the amount of \$3,749,863. This transaction has no cash or fund balance impact on the City’s operational and governmental funds.

21. Subsequent Events

In FY 2013-14, the City finalized the sale option for the property at 230 First Street and 400 Main Street for an agreed upon price of \$3.1 million, less the previously paid option installments recognized in the current and prior years. Escrow closed in early August 2013, resulting in the exchange of title to the buyer, 400 Main Morris Land, LLC. This transaction also triggered the initiation of the private development on the site, as previously approved through the planning and Council action process.

On May 14, 2013, the City adopted the results of an updated Sewer Rate study resulting in a new rate structure model, approximating a 7% per increase per year over the next five years, designed to facilitate the near and long-term capital and operating needs of the Sewer Enterprise Fund. The adoption of the ordinance occurred on July, 9, 2013.

In accordance with accounting standards affecting disclosures of subsequent events, the Company evaluated subsequent events for recognition and disclosure through December 11, 2013, the date which these financial statements were available to be issued. Management concluded that, other than stated above, no material subsequent events have occurred since June 30, 2013 that require recognition or disclosure in the financial statements.