

CITY OF SAN CARLOS AND THE SAN CARLOS SUCCESSOR AGENCY
Debt Disclosure Procedure Policy
Effective: May 28, 2019

APPLICABLE CODES AND REGULATIONS:

Section 17 of the Securities Act of 1933 and Section 10(b) of the Securities and Exchange Act of 1934, and regulations adopted by the Securities and Exchange Commission (“SEC”) under those acts, particularly “Rule 10b-5” under the 1934 Act.

PURPOSE:

These Debt Disclosure Procedures (the “Procedures”) memorialize and communicate procedures in connection with obligations, including notes, bonds, loans and other debt obligations, issued by or on behalf of the City of San Carlos and the San Carlos Successor Agency (the “City”), or for which the City supplies material information to potential purchasers of the obligations (such as bonds for Silicon Valley Clean Water), so as to ensure that the City continues to comply with all applicable disclosure obligations and requirements under the federal securities laws.

BACKGROUND:

The City may from time to time issue revenue bonds, notes, loans or other debt obligations or supply material information to potential purchasers of bonds, notes, loans or other debt obligations issued by other entities (such as Silicon Valley Clean Water) (collectively, “Obligations”) in order to fund or refund capital investments, other long-term programs and working capital needs. In offering Obligations to the public, and at other times when the City makes certain reports, the City must comply with the “anti-fraud rules” of federal securities laws. (“Anti-fraud rules” refers to Section 17 of the Securities Act of 1933 and Section 10(b) of the Securities and Exchange Act of 1934, and regulations adopted by the Securities and Exchange Commission under those acts, particularly “Rule 10b-5” under the 1934 Act.)

The core requirement of these rules is that potential investors in Obligations must be provided with all “material” information relating to the offered Obligations. The information provided to investors must not contain any material misstatements, and or omit material information that would be necessary to provide to investors a complete and transparent description of the Obligations and the City’s financial condition. In the context of the sale of securities, a fact is generally considered to be “material” if there is a substantial likelihood that a reasonable investor would consider it to be important in determining whether or not to purchase the securities being offered.

When Obligations are issued to the public, the two central disclosure documents that are prepared are a preliminary official statement (“POS”) and a final official statement (“OS”, and collectively with the POS, “Official Statement”). The Official Statement generally consists of: (i) the forepart that describes the specific transaction including maturity dates, interest rates, redemption provisions, the specific type of financing, the project and other matters particular to the financing; (ii) a section that provides information on the City (the “City Section”); and (iii) various other appendices, including the City’s audited financial report, form of the proposed legal opinion and forms of continuing disclosure undertakings of the City. Investors use the Official Statement as one of their primary resources for making informed investment decisions regarding the Obligations.

DISCLOSURE PROCEDURE:

When the City determines to issue Obligations (or participate in an offering of Obligations being undertaken by another entity), the City Manager requests the involved departments to commence preparation of the portions of the Official Statement (including particularly the City Section) for which they are responsible. While the general format and content of the Official Statement may not normally change substantially from offering to offering, except as necessary to reflect major events, the City Manager and other relevant City staff are responsible for reviewing and preparing or updating the portion of the Official Statement that is within their particular areas of knowledge. Once the draft POS has been substantially updated, the entire draft POS is shared with the City Council for review and input before approval.

Members of the financing team, including Bond and Disclosure Counsel and a municipal advisor (the "Municipal Advisor"), assist staff in determining the materiality of any particular item and in the development of specific language in the City Section. Members of the financing team also assist the City in the development of a "big picture" overview of the City's financial condition, included in the City Section. This overview highlights particular areas of interest. Bond and Disclosure Counsel has a confidential, attorney-client relationship with officials and staff of the City.

The City Manager, Administrative Services Director, or a member of the financing team at the direction thereof, schedules one or more meetings or conference calls with the financing team (which may include City officials, City Attorney, Bond and Disclosure Counsel, the City's Municipal Advisor (and the underwriters of the Obligations, and the underwriters' counsel, if the proposed financing is being undertaken as a negotiated transaction)). New drafts of the forepart of the draft POS and the City Section are then circulated and discussed. Such communications may occur via electronic means rather than by meetings or conference calls. During this part of the process, there is substantial contact among City staff and other members of the financing team to discuss issues that may arise, determine the materiality of particular items and ascertain the prominence in which the items should be disclosed.

Prior to distributing a POS to potential investors, there is typically a formal conference call with City officials involved in the preparation of the POS and members of the financing team (and the underwriters and the underwriters' counsel, if the financing is a negotiated transaction) during which the POS is reviewed in its entirety to obtain final comments and to allow the underwriters (if the proposed financing is being undertaken as a negotiated transaction), to ask questions of the City's senior officials. This is referred to as a "due diligence" meeting.

A substantially final form of the POS is provided to the members of the City Council in advance of approval to afford such members an opportunity to review the POS, ask questions and make comments. The substantially final form of the POS is approved by the City Council, which generally authorizes certain senior staff to make additional corrections, changes and updates to the POS in consultation with the City Attorney and Bond and Disclosure Counsel.

At the time the POS is posted for review by potential investors, senior City officials execute certificates deeming certain portions of the POS complete (except for certain pricing terms) as required by SEC Rule 15c2-12.

Between the posting of the POS for review by potential investors and delivery of the final OS to the underwriter for redelivery to actual investors in the Obligations, any changes and developments will have been incorporated into the POS, including particularly the City Section, if

required. If necessary, to reflect developments following publication of the POS or OS, as applicable, supplements will be prepared and published.

In connection with the closing of the transaction, one or more senior City officials execute certificates stating that certain portions of the OS, as of the date of each OS and as of the date of closing, do not contain any untrue statement of material fact or omit to state any material fact necessary to ensure the statements contained in the OS, in light of the circumstances under which they were made, are not misleading. The City Attorney also provides an opinion letter (generally addressed to the underwriters) advising that information contained in the City Section, as applicable (or specified portions thereof) as of its date did not, and as of the date of the closing, does not contain any untrue statement of a material fact or omitted or omits to state any material fact necessary to ensure the statements therein, in light of the circumstances under which they were made, are not misleading. The City Attorney does not opine to the underwriters or to other third parties as to any financial, statistical, economic or demographic data or forecasts, charts, tables, graphs, estimates, projections, assumptions or expressions of opinion and certain other matters that are customarily excluded. Bond and Disclosure Counsel also provides a negative assurance letter (addressed to the underwriters) with respect to the City Section. Bond and Disclosure Counsel does not give negative assurances to the underwriters or to other third parties as to any financial, statistical, economic or demographic data or forecasts, charts, tables, graphs, estimates, projections, assumptions or expressions of opinion, or information contained in appendices to the OS and certain other matters that are customarily excluded.

CITY SECTION:

The information contained in the City Section is developed by personnel under the direction of the City Manager, with the assistance of the financing team. In certain circumstances, additional officials will be involved, as necessary. The following principles govern the work of the respective staff that contribute information to the City Section:

- City staff members involved in the disclosure process are responsible for being familiar with their responsibilities under federal securities laws as described above.
- City staff involved in the disclosure process should err on the side of raising issues when preparing or reviewing information for disclosure. Officials and staff are encouraged to consult the City Attorney and Bond and Disclosure Counsel if there are questions regarding whether an issue is material or not.
- Care should be taken not to shortcut or eliminate any steps outlined in the Procedures on an ad hoc basis. However, the Procedures are not necessarily intended to be a rigid list of procedural requirements, but instead to provide guidelines for disclosure review. If warranted, based on experience during financings or because of additional SEC pronouncements or other reasons, the City should consider revisions to the Procedures.
- The process of updating the City Section from transaction to transaction should not be viewed as being limited to updating tables and numerical information. While it is not anticipated that there will be major changes in the form and content of the City Section at the time of each update, everyone involved in the process should consider the need for revisions in the form, content and tone of the sections for which they are responsible at the time of each update.
- The City must make sure that the staff involved in the disclosure process is of sufficient seniority such that it is reasonable to believe that, collectively, they are in possession of material information relating to the City, its operations and its finances.

TRAINING:

Periodic training for City staff involved in the preparation of the Official Statement (including the City Section) is coordinated by the finance team and/or the Administrative Services Director. These training sessions are provided to assist staff members involved in identifying relevant disclosure information to be included in the City Section. The training sessions also provide an overview of federal laws relating to disclosure, situations in which disclosure rules apply, the purpose of the Official Statement and the City Section, a description of previous SEC enforcement actions and a discussion of recent developments in the area of municipal disclosure. Attendees at the training sessions are provided the opportunity to ask questions of finance team members, including the City Attorney, concerning disclosure obligations and are encouraged to contact members of the finance team at any time if they have questions.

CONTINUING DISCLOSURE REQUIREMENTS:

In connection with the issuance or execution and delivery of Obligations, the City has entered into (and may in the future enter into) contractual agreements (“Continuing Disclosure Certificates”) to provide its audited financial statements and notice of certain events relating to the Obligations specified in the Continuing Disclosure Certificates. The City must comply with the specific requirements of each Continuing Disclosure Certificate. The City’s Continuing Disclosure Certificates generally require that the annual reports be filed no later than nine months after the end of the City’s fiscal year (currently March 31 of each year, based on a fiscal year ending on June 30), and listed event notices are generally required to be filed within 10 business days of their occurrence.

Specific events that require “listed event” notices are set forth in each particular Continuing Disclosure Certificate. The SEC adopted amendments to SEC Rule 15c2-12, effective February 27, 2019, adding two new listed events, as detailed in **Exhibit A** attached hereto. *Importantly, these new events apply only to Continuing Disclosure Certificates entered into by the City after the February 27, 2019 effective date of the amendments.*

The City shall be responsible for preparing and filing the annual reports and listed event notices required pursuant to the Continuing Disclosure Certificates. Particular care shall be paid to the timely filing of any changes in credit ratings on Obligations (including changes in the credit ratings of insurers of particular Obligations).

In addition, the City Attorney, City Manager, or other City staff will provide written notice to the Administrative Services Director of any default, event of acceleration, termination event, modification of terms (only if material or may reflect financial difficulties), or other similar events (collectively, a “Potentially Reportable Event”) under any agreement or obligation to which the City is a party and that may be a “financial obligation” as discussed below. Such written notice should be provided by the City Attorney to the Administrative Services Director as soon as the City Attorney receives written notice by staff, consultants, or external parties of such event or receives written notice of such event so that the Administrative Services Director can determine, with the assistance of Disclosure Counsel, whether notice of such Potentially Reportable Event is required to be filed on the Electronic Municipal Market Access (EMMA) portal pursuant to the disclosure requirements of SEC Rule 15c2-12. If filing on EMMA is required, the filing is due within 10 business days of such Potentially Reportable Event to comply with the continuing disclosure undertaking for the various debt obligations of the City. *As noted above, the new reporting*

obligations apply only to Continuing Disclosure Certificates entered into by the City after the February 27, 2019 effective date of the amendments to SEC Rule 15c2-12.

For the City's obligations and for those that the City partakes, the City Attorney, City Manager, or other City staff will report to the Administrative Services Director the execution by the City of any agreement or other obligation that might constitute a "financial obligation" for purposes of SEC Rule 15c2-12 and that is entered into after February 27, 2019. Amendments to existing agreements or obligations with "financial obligation" that relate to covenants, events of default, remedies, priority rights, or other similar terms should be reported to the Administrative Services Director as soon as the City Attorney or such other senior staff is receives written notice by City staff, consultants, or external parties of such event or receives a written notice of such amendment requests. Notice to the Administrative Services Director is necessary so that the Administrative Services Director can determine, with the assistance of Disclosure Counsel, whether such agreement or other obligation constitutes a material "financial obligation" for purposes of SEC Rule 15c2-12. If such agreement or other obligation is determined to be a material "financial obligation" or a material amendment to a "financial obligation" described above, notice thereof would be required to be filed on EMMA within 10 business days of execution or incurrence. *As noted above, the new reporting obligations apply only to Continuing Disclosure Certificates entered into by the City after the February 27, 2019 effective date of the amendments to SEC Rule 15c2-12.*

The types of agreements or other obligations that could constitute "financial obligations" and that could need to be reported on EMMA are discussed in the memorandum from Jones Hall, which serves as Bond and disclosure Counsel to the City and the San Carlos Successor Agency, as well as Silicon Valley Clean Water, which is attached hereto as **Exhibit B**.

Exhibit A
Listed Events in SEC Rule 15c2-12

The Administrative Services Director or his or her delegate should review this list routinely to determine whether any event has occurred that may require a filing with EMMA.

For securities subject to SEC Rule 15c2-12, the following events require notice in a timely manner not in excess of ten (10) business days after the occurrence of the event with respect to the applicable securities:

1. Principal and interest payment delinquencies;
2. Non-payment related defaults, if material;
3. Unscheduled draws on debt service reserves reflecting financial difficulties;
4. Unscheduled draws on credit enhancements reflecting financial difficulties;
5. Substitution of credit or liquidity providers, or their failure to perform;
6. Adverse tax opinions, the issuance by the Internal Revenue Service (I.R.S). of proposed or final determinations of taxability, Notices of Proposed Issue or other material notices or determinations with respect to the tax status of the security, or other material events affecting the tax status of the security;
7. Modifications to rights of security holders, if material;
8. Bond calls, if material, and tender offers;
9. Defeasances;
10. Release, substitution, or sale of property securing repayment of the securities, if material
11. Rating changes;
12. Bankruptcy, insolvency, receivership or similar event of the obligated person;
13. Consummation of a merger, consolidation, or acquisition involving an obligated person or the sale of all or substantially all of the assets of the obligated person, other than in the ordinary course of business, the entry into a definitive agreement to undertake such an action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; and
14. Appointment of a successor or additional trustee or the change of name of a trustee, if material.

For continuing disclosure undertakings entered into on or after February 27, 2019, the following events require notice in a timely manner not in excess of ten (10) business days after the occurrence of the event with respect to the applicable securities:

1. Incurrence of a financial obligation of the obligated person, if material, or agreement to covenants, events of default, remedies, priority rights, or other similar terms of a financial obligation of the obligated person, any of which affect security holders, if material; and

2. Default, event of acceleration, termination event, modification of terms, or other similar event under the terms of a financial obligation of the obligated person, any of which reflect financial difficulties.

Exhibit B

**Memorandum Regarding SEC Rule 15c2-12 Amendments from
Jones Hall, A Professional Law Corporation
Bond Counsel and Disclosure Counsel to the City and Successor Agency**

See attached.

Exhibit B

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**RECOMMENDATIONS FOR ISSUERS REGARDING
THE 2019 AMENDMENTS TO RULE 15C2-12**

February 2019

BACKGROUND

Rule 15c2-12 (the “Rule”) of the U.S. Securities and Exchange Commission (the “SEC”), promulgated under the Securities Exchange Act of 1934, requires that before the issuance of municipal securities to investors in a public sale, underwriters must reasonably determine that the issuer and other obligated persons have undertaken to provide certain disclosure information to the Municipal Securities Rulemaking Board (the “MSRB”) through its internet based EMMA system.

This information generally consists of financial and operating data and audited financial statements, which must be filed at least annually, and notices of certain listed events, notice of which must be filed within 10 business days after they occur. The issuer’s undertaking to provide this information is detailed in a continuing disclosure certificate or agreement signed in connection with the issuance of municipal securities.

AMENDMENTS TO THE RULE

In response to concerns that municipal bond investors were not receiving material information regarding private placements or bank loan transactions, the SEC has added two new listed events to the existing 14 listed events:

- (15) incurrence of a financial obligation of the obligated person, if material, or agreement to covenants, events of default, remedies, priority rights or other similar terms of a financial obligation, any of which affect security holders, if material; and
- (16) default, event of acceleration, termination event, modification of terms or other similar events under a financial obligation of an issuer, if any such event reflects financial difficulties.

These new listed events must be included in all continuing disclosure undertakings for transactions closing on or after February 27, 2019 (the “Compliance Date”).

As used in new listed events 15 and 16, a “financial obligation” is (i) a debt obligation; (ii) a derivative instrument entered into in connection with, or pledged as security or a source of payment for, an existing or planned debt obligation; or (iii) a guarantee of (i) or (ii).



Notably, financial obligations are ***not*** (i) municipal securities for which a final official statement is provided to the MSRB, regardless of whether such filing is required under the Rule, provided that a continuing disclosure undertaking is also entered into, or (ii) ordinary financial and operating liabilities incurred in the normal course of business by an issuer.

Therefore, a “financial obligation” is generally the incurrence of debt in a private transaction, without a public offering of securities that would trigger its own continuing disclosure obligations. A “financial obligation” can include short-term and long-term obligations, regardless of whether such obligations are identified as securities, loans, leases or otherwise. Leases that may be considered financial obligations include privately placed certificates of participation and lease financings, but would likely not include operating leases of the issuer.

New listed event 15 applies only applies to financial obligations or covenants entered into after the Compliance Date. Importantly for issuers, there is no requirement to retroactively disclose private placement or bank loan transactions that closed before Compliance Date.

New listed event 16, however, requires the reporting of defaults, events of acceleration, termination events, modification of terms, or other similar events for any financial obligations outstanding, whether entered into before or after a continuing disclosure undertaking entered into on or after Compliance Date. The SEC has noted that it believes that holding an issuer responsible for any of its financial obligations for purposes of new listed event 16, regardless of when it was incurred, should not be overly burdensome since such events are significant in nature, issuers should be aware that such events have occurred, without the need for additional monitoring.

RECOMMENDATIONS FOR ISSUERS

New Continuing Disclosure Undertakings. All continuing disclosure undertakings entered into for transactions closing on or after the Compliance Date need to include new listed event 15 and new listed event 16 in order to comply with the Rule.

Reporting New Financial Obligations. In order to be in a position to file a listed event notice with respect to new listed event 15, issuers should be ready to determine whether or not a future borrowing or other transaction constitutes a “financial obligation,” and if so, determine whether the financial obligation would be material to investors in the issuer’s bonds issued on or after the Compliance Date. If a new financial obligation is determined to be material, a notice must be filed on EMMA within 10 business days of the incurrence of the financial obligation.

Issuers should consider whether they will, as a matter of course, be posting entire transaction documents to EMMA, summaries of the material terms of the documents, or evaluate and decide on a case-by-case basis.

Reporting Events With Respect to Existing Financial Obligations. In order to be in a position to file a listed event notice with respect new listed event 16, issuers should begin examining all of their existing financial obligations, whether or not considered material, and creating a database of such financial obligations. Issuers may also want to identify covenants, events of defaults, remedies, priority rights and other similar terms in an effort to be prepared to easily identify events that may constitute a default, event of acceleration, termination event, modification of terms or other similar event reflecting financial difficulty pursuant to new listed



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event 16. If the issuer determines that such an event has taken place, a notice must be filed on EMMA within 10 business days.

Issuers of municipal securities must be ready to comply with the amendments to the Rule on the Compliance Date, **February 27, 2019**. The attorneys at Jones Hall can assist with any questions related to the amendments to the Rule, or the implementation of policies and procedures to ensure compliance.

Sincerely,

/s/ David T. Fama & James A. Wawrzyniak Jr.

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